Solicitors Regulation Authority

Review of the Compensation Fund

Report of the Financial Protection Committee's Compensation Fund Review Working Party

April 2009

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EXECUTIVE SUMMARY

The Financial Protection Committee's Compensation Fund Review Working Party has completed its 18 month review of the Compensation Fund under terms of reference agreed by the Committee following consultation with the representative Law Society. Currently public financial protection in respect of solicitors in private practice is afforded through a combination of four arrangements: compulsory professional indemnity insurance; the Compensation Fund; the intervention process (which includes Statutory Trust Account distribution) and Inadequate Professional Services ("IPS") awards. The SRA is responsible for the first three arrangements and the Legal Complaints Service is responsible for IPS awards. This report concentrates on the Compensation Fund but necessarily considers how the Compensation Fund interlocks with the other arrangements.

The Working Party concluded that the underlying principle is client protection. The existing arrangements described in this report already provide a great deal towards a cohesive and complete protection which only needs some adjustment to improve and align it. Anomalies and peculiarities are inevitable in different arrangements that address different needs and total protection under a single scheme is probably an unattainable ideal.

The main recommendations of the Working Party are as follows:

- The Working Party's recommendation that the limit of the grant be increased to £2 million (with discretion) has been implemented in the Compensation Fund Rules 2009 that came into force on 31 March 2009 (see conclusion 6 – page 14).

- The Working Party's recommendations to extend the time limit for applications to the Compensation Fund to 12 months and to retain the discretion to exceed this as appropriate have been implemented in the Compensation Fund Rules 2009 that came into force on 31 March 2009 (see conclusion 7 – page 15).

- From 1 October 2009 the Compensation Fund should not entertain new counsel fee claims. Once the Bar's rules have been changed and contracting between solicitors and Counsel is adopted, claims from Counsel will have an alternative means of redress through the courts (see conclusion 9 – page 16).

- The Compensation Fund reserve should be maintained at a minimum of twice the average annual value of claims over the previous 7 years plus the estimated value of three months recharges (see conclusion 27 – page 36).

- Recharges against the Compensation Fund should be made only for the direct costs of its administration. The wider costs of regulation should be funded from practising certificate income (see conclusion 28 – page 41).

- As part of its review the Working Party has compared the Fund with other jurisdictions' funds and has concluded from the information available that the Fund, combined with professional indemnity and the Statutory Trust Account process, provides equal, if not superior, protection. The Working Party has also considered aspirational criteria produced by the American National Client Protection Organisation (ANCPO) to assist jurisdictions in evaluating their own compensation arrangements' performance. The principal areas where the Fund does not meet the

aspirational criteria relate to governance and the dissemination of information to stake holders (see conclusion 31 – page 48).

- The Working Party concluded that the governance arrangements up until 31 March 2009 were unacceptable as the SRA had responsibility without power and the Society as trustee had power without responsibility. The position has improved since 31 March 2009 because now the SRA Board has clear responsibility for some aspects of the Compensation Fund. The notable exceptions are responsibility for setting contributions (which has been retained by the Council) and investment strategy (which the Board had agreed to delegate to a Law Society Committee). The Working Party recommends that the SRA Board reverse the delegation to the Law Society's Investment Committee. The Working Party is of the view that ultimate responsibility for all aspects of the Compensation Fund should be at arms length from the representative body and should be vested in the SRA Board. This would go some way to addressing the requirements of ANCPO 1.3 and 2.4 as set out paragraph 179 of the main report (see conclusion 32 – page 51).

- From the perspective of clients, aligning the Compensation Fund to the Minimum Terms and Conditions would eliminate most, if not all, of the gaps in client protection. Before any such change could be properly considered, empirical research would be needed to determine the likely cost implications of the change and on that basis an informed decision could be made. The Working Party recommends that this research is carried out (see conclusion 33 – page 56).

Leaving aside the aligning of the Compensation Fund and the Minimum Terms and Conditions, the Working Party concluded that whilst the Compensation Fund could be improved, it had served the public and profession very well and represented the best of the currently available options. The other alternatives were unviable and/or expensive and would involve major changes and risks that would be out of proportion to the problems to be addressed.

The scale of the review was such that inevitably some work remains outstanding and new areas for action have emerged during the course of the review. The key future action points are as follows:

- Complete the review of the provision of information to stakeholders
- Review the new Compensation Fund Rules to assess whether further changes are desirable in the public interest
- Consider how the protection afforded by the three schemes (including the Compensation Fund) will be adapted to accommodate the proposed alternative business structures (ABSs)
- Keep the levels of cover under periodic review
- Investigate the cost and practicality of aligning the Compensation Fund rules with the Minimum Terms and Conditions (MTC)
- Complete the Equality Impact Assessments of the Compensation Fund.

Review of the Compensation Fund

Contents

Foreword

INTRODUCTION

(1) The SRA Board's Financial Protection Committee ("the Committee") was established on 1 April 2007 and took over responsibility for the solicitors' compulsory professional indemnity insurance scheme. Its members are:

Andrew Long -	(Chair) (Solicitor member and member of the SRA Board)
Peter Farthing -	(Solicitor member)
Tony Foster -	(Lay member)
Nick Lord -	(Lay member)
Tim Readman -	(Solicitor member)
Sally Ruthen -	(Solicitor member and member of the SRA Board)
Edward Solomons -	(as of 1 January 2009) (Solicitor member and member of the SRA Board)
Dick Taylor -	(until 31 December 2008) (Solicitor member and member of the SRA Board)
Tim Timson -	(Solicitor member)
Peter Williamson -	(Solicitor member and Chair of the SRA Board)

(2) The Committee was given responsibility for Compensation Fund policy in the summer of 2007 in addition to its responsibility for professional indemnity insurance policy. The Committee determined to carry out a fundamental review of the Compensation Fund split into three distinct areas as follows:

- Protection of the Public
- Financial management
- Operational management

(3) The Committee set up the Compensation Fund Review Working Party ("the Working Party") to carry out the review and to produce a report. The members of the Working Party are:

Peter Farthing - (Chair)
Tony Foster
Andrew Long
Nick Lord
Tim Readman

The members of the Working Party wish to record their gratitude to members of staff who have greatly assisted them in their discussions, and who have contributed greatly to this report.

(4) Following consultation with the representative Law Society, the Committee set the terms of reference for the review as follows.

TERMS OF REFERENCE

Protection of the Public

(5) In undertaking the public protection part of the review the Committee had regard to the relevant SRA key objective:

- ***To protect consumers by ensuring effective professional indemnity and compensation fund arrangements;***

and the relevant SRA strategic outcome:

- ***We will secure effective insurance and compensation arrangements for the profession to protect the consumer in cases of client loss, for example, through negligence, dishonesty or insolvency.***

(6) The agreed terms of reference relating to public protection are as follows:

- To identify gaps in financial protection coverage and establish whether these should be filled by the Compensation Fund.
- To identify variations in financial protection coverage as between the compulsory professional indemnity scheme, the Compensation Fund and repayments from statutory trust funds and consider the extent to which a uniform approach should be adopted so as to remove the variations.
- Review policy, rules and guidelines in relation to provision of adequate public protection.
- Identify and iron out existing weaknesses or conflicts between policy, rules, and their practical application.
- To maintain and build upon existing strengths.
- To review the way in which information about the financial protection arrangements is disseminated to stakeholders.

(7) The Committee also considered certain specific current anomalies and issues as part of the review including:

- Dishonesty hurdle
- Definition of ‘hardship’
- Six month time limit
- Limited Liability Partnerships (LLPs)
- Counsels fees
- Relationship with Qualifying Insurers
- Inadequate Professional Service (IPS) awards
- Lenders costs

Financial management

(8) A number of criticisms of the financial management of the Compensation Fund have been made by the Law Society over several years. In particular it is felt that the forecasting and modelling techniques used in assessing future contribution requirements are crude and inadequate. The perception is that the Fund’s reserves are too high and that it is slow to recover money. There is also the view that the Fund’s administration costs are too high, though this view appears to have been fuelled by the historic Law Society accounting practice under which the Compensation

Fund contributions cover not only the cost of investigating applications and making grants but also management's assessment of the resources engaged in other parts of the SRA (and previously the Law Society's regulatory directorates) in administering and protecting the Fund. These recharged resources include, amongst other things, proportions of the costs of the following: intervention; costs recovery; forensic investigations; fraud intelligence; adjudication; investigation casework; post intervention; finance; archives.

(9) In 2006 there was an over-collection of contributions from the profession due to an error during preparations for the practising certificate renewal exercise. This highlighted significant gaps in financial controls and lack of historical clarity about fund management ownership. The resulting debate helped to clarify the boundaries between the responsibilities of the SRA and the Law Society in management of the fund. Financial management responsibilities sit firmly with the SRA although the Law Society has chosen not to delegate to the SRA the power to set Compensation Fund contribution rates.

(10) The SRA had in any event already concluded that a review of the Compensation Fund was necessary. At its meeting on 18 July 2007 the Law Society Council agreed to accept the SRA recommended Compensation Fund contribution rates on the basis that:

- ***there would be a review by the SRA of a wide range of issues concerning the Compensation Fund and related activities, including the scope for the release of funds from the Statutory Trust Accounts to the Compensation Fund;***

- ***the SRA would consult the Society about the terms of reference of the review and agree them jointly; and***

- ***the SRA would report back to the Council in time for the 2008 decision on the level of contribution to the Compensation Fund.***

(11) The agreed terms of reference relating to financial management are as follows:

- Review the reserving, forecasting and modelling policies used to establish the requirements of the Fund, and in particular whether external actuarial advice should be taken on those issues;
- Review the way in which risk is managed and consider whether risk can be reduced or transferred on a cost effective basis;
- Consider whether there is more that can be done to speed up transfer of monies from statutory trust accounts to the fund;
- Review the cost of administering the fund, including the appropriateness of the current designation of some regulatory activity, as being properly recharged to the Fund;
- Review due diligence, financial monitoring and controls;
- Review the procurement process of intervention agents and identify possible improvements;
- Review the criteria used for interventions.

Operational management

(12) While the operational management of the Compensation Fund is a matter for the SRA Chief Executive and his staff, the Committee wished to be assured that the managerial arrangements in place are appropriate to ensure its effective operation. The

Committee had been provided with an overview from the Director of Client Protection, drawing attention to some historic problems within the Compensation Fund which were being addressed. During the course of the review a piece of work was undertaken involving the restructuring of the Client Protection Directorate and the Compensation Fund. The primary aim of the exercise was to increase the efficiency and effectiveness of the Directorate as a whole. The Committee were kept advised of developments and were given the opportunity to input in broad terms on the proposed changes.

(13) The agreed term of reference relating to operational management is as follows:

- Review the proposed changes to the structure and supporting operational processes of the Client Protection Directorate in terms of the potential gains in effectiveness and efficiency***.***

Legal Services Act 2007 ("the LSA")

(14) As part of the review the Working Party took account of the effects of the LSA and the need to cater for Legal Disciplinary Practices (LDPs). The introduction of LDPs was linked with a move to entity based regulation. As a matter of policy the Committee had to consider how the scope of the protection afforded by the Compensation Fund should be extended to cover practise through the new entities and how Compensation Fund contributions should be calculated in respect of LDPs and other entities.

Benchmarking

(15) To assist the Working Party in its review it was intended to compare the Fund to the arrangements in other jurisdictions and professions both in terms of scope of cover and method of financing. A very helpful survey was carried out by the International Bar Association in 2006. The American National Client Protection Organisation (ANCPO) had produced aspirational criteria to assist jurisdictions in evaluating the performance of their own Client Protection Funds which were of assistance to the Working Party.

REPORT SUMMARY

(16) The report is structured into chapters each dealing with a separate aspect of the review as follows.

(17) **Chapter 1** looks at the scope of the protection afforded to the public through the combination of the compulsory professional indemnity scheme, the Compensation Fund and the statutory trust process. With three different but complementary arrangements there are boundaries, gaps, differences and overlaps and these have been looked at as part of the review. With respect to the Compensation Fund a number of changes were identified that were relatively minor and for the benefit of the public and these have been incorporated in the new Compensation Fund Rules which came into force on 31 March 2009, including:

- an individual whose dealings with a defaulting practitioner have been in a personal capacity and who has suffered or is likely to suffer loss due to a failure to account will be deemed to have suffered hardship

- the maximum grant will be increased from £1 million to £2 million, subject to the power to waive the limit

- the time limit for submitting an application will be increased from 6 months to 12 months.

(18) **Chapter 2** reviews the reserving policy and the recharges made against the Compensation Fund. The Working Party recommends that the Compensation Fund reserve is maintained at 2 times the average annual value of claims plus the estimated value of three months recharges. The recommendation of the Working Party is to make recharges against the Compensation Fund only for the direct costs of its administration and to fund the wider costs of regulation from practising certificate income.

(19) The Working Party concluded that the terms of reference relating to interventions were outside the scope of its terms of reference and should be referred to the Compliance Committee to be taken forward. The term of reference looking at whether there is more that can be done to speed up transfer of monies from statutory trust accounts to the Fund was dealt with as part of the operational management review.

(20) **Chapter 3** reports on the restructuring of the Compensation Fund and statutory trust units into the new integrated Claims Management Unit. The Working Party were pleased to note the progress that had been made and will continue to monitor the operational performance of the Claims Management Unit.

(21) **Chapter 4** sets out the initial work that has been carried out by the Working Party in reviewing the provision of information to stakeholders but the completion of this work is a future action point.

(22) **Chapter 5** looks at benchmarking of the Compensation Fund against compensation arrangements in other jurisdictions. The Working Party has tested the Fund against aspirational criteria set by the American National Client Protection Organisation (ANCPO). The Working Party concluded that, with a few exceptions, the Fund meets or exceeds the aspirational criteria. The key exceptions relate to governance of the Fund and the publication of an annual report.

(23) **Chapter 6** reviews the governance of the Compensation Fund and the effect of the Legal Services Act on those arrangements. The Working Party is of the view that ultimate responsibility for all aspects of the Compensation Fund should be at arms length from the representative body and should be vested in the SRA Board. This is not the case at present as the Council retains the responsibility to set contributions and responsibility for investment strategy has been delegated to the Law Society's Investment Committee, subject to confirmation that such a delegation is possible.

(24) **Chapter 7** examines various alternative ways of providing the protection currently afforded by the Fund. The following options were considered as part of the review:

- Surety bonds
- Insurance - either free standing or by extending the Minimum Terms and Conditions (MTC) of professional indemnity insurance for solicitors to cover all dishonesty by removing the dishonesty exclusion.
- Centralised banking of client money
- Aligning the Compensation Fund to the MTC.

The Working Party concluded that whilst the Compensation Fund could be improved, it had served the public and profession very well and represented the best of the

available options. The alternatives were unviable and/or expensive and out of proportion to the problems to be addressed.

(25) **Chapter 8** notes that in accordance with the SRA's Equality and Diversity Strategy a full range of Equality Impact Assessments are being carried out on the Compensation Fund and these were due to be completed by the end of June 2009.

(26) **Chapter 9** identifies the key action points for the future arising out of the review as follows:

- Complete the review of the provision of information to stakeholders
- Review the new Compensation Fund Rules to assess whether further changes are desirable in the public interest
- Consider how the protection afforded by the three schemes (including the Compensation Fund) will be adapted to accommodate the proposed alternative business structures (ABSs)
- Keep the levels of cover under periodic review
- Investigate the cost and practicality of aligning the Compensation Fund rules with the MTC
- Complete the Equality Impact Assessments of the Compensation Fund.

Chapter 1 - Public Protection
A Review of Policy, Rules and Guidance

INTRODUCTION

1. Currently public financial protection in respect of solicitors in private practice is afforded through a combination of four arrangements: compulsory professional indemnity insurance; the Compensation Fund; the intervention process (which includes Statutory Trust Account distribution) and Inadequate Professional Services ("IPS") awards. Together these provide comprehensive and wide reaching protection that compares very favourably with the protection and compensation offered by other professions and in other jurisdictions.

2. The SRA is responsible for the first three arrangements and the Legal Complaints Service is responsible for IPS awards. The SRA has no control or influence over the making of IPS awards and for this reason IPS awards are outside the scope of this review. The LCS has an entirely separate scheme for handling IPS awards but it interlocks with the professional indemnity arrangements in one respect. Where an IPS award is unsatisfied then the claim is covered by the firm's compulsory professional indemnity insurance. IPS is becoming more important with each rise in the jurisdiction limit (currently £15,000 per claim) and because it is a relatively easy and cheap route for obtaining compensation compared with that obtainable through the courts. When the Office for Legal Complaints comes into operation in 2010 the jurisdiction limit will increase to £30,000.

3. Indemnity insurance provides compulsory minimum cover for any one claim of £2 million (or £3 million for Limited Liability Partnerships and limited companies) for all civil liability arising from private legal practice written on Minimum Terms and Conditions of professional indemnity insurance for solicitors and registered European lawyers in England and Wales ("MTC"). The breadth of cover, and the inability of insurers to avoid cover, are unparalleled in the commercial professional indemnity insurance market. The Compensation Fund may provide grants of up to £2 million to replace money which has either been stolen by a solicitor, or to alleviate hardship or loss suffered by applicants where the solicitor has failed to account for client money in their possession. The Statutory Trust Account process allows for the return to their beneficial owners of funds held by the SRA after intervention.

4. This report sets out the conclusions of the Compensation Fund Working Party ("the Working Party") established by the Financial Protection Committee ("the Committee") to review public protection. The Working Party's tasks were:

    - ***"To review the policy, rules and guidelines in relation to provision of adequate public protection and to identify and address any weaknesses or conflicts between policy, Rules and Guidelines and their practical application.***

    - ***To identify gaps in cover between the compulsory professional indemnity scheme, the Compensation Fund and the statutory trust funds and to consider what if any action is needed to deal with those gaps.***

    - ***To identify variations in the extent to which claimants are compensated as between the compulsory professional indemnity scheme, the Compensation***

Fund and the statutory trust funds and to consider whether a uniform approach should be adopted so as to remove the variations.

- ***To review the role of the Compensation Fund as a Fund of last resort and to examine the practical claims handling issues that arise from having three separate arrangements which together provide client financial protection.***

- ***To carry out a comparison of the Compensation Fund and the arrangements in other jurisdictions and professions both in terms of scope of cover and methods of financing."***

- ***To identify and assess alternative ways of providing the protection currently afforded by the Compensation Fund***

5. During the course of undertaking this review, work has been carried out on amendments to the Solicitors' Indemnity Insurance Rules, new Compensation Fund Rules and new Statutory Trust Rules, to accommodate firm based regulation and the changes to be introduced by the Legal Services Act such as Legal Disciplinary Practices. With the exception of the Statutory Trust Rules, these rules came into force on 31 March 2009. The review of the Compensation Fund Rules and guidelines provided an opportunity to simplify the current rules and guidelines into a single more user friendly document and to propose certain other improvements. The SRA's stated policy was that any changes to take place at this stage would be confined to ones that were relatively minor and for the benefit of the public. The principal changes that were proposed were the subject of consultation with stakeholders.

OVERVIEW OF THE THREE SCHEMES

6. The main principles of the three schemes are summarised in **Annex A**.

Professional Indemnity Insurance

7. The compulsory professional indemnity insurance scheme requires all firms carrying on private practice in England and Wales to have a policy of "qualifying insurance". This provides the public with a good basic level of protection in the event that a firm's negligence or dishonesty results in a civil legal liability to a client who has suffered loss as a result. The scheme is subject to its own rules called the Solicitors' Indemnity Insurance Rules ("SIIR") to which are appended the MTC. Insurers have to offer policies which meet the MTC. A copy of the current MTC is attached as **Annex B**.

8. One of the key elements of the compulsory professional indemnity insurance scheme is the "Assigned Risks Pool" (ARP). The main purposes of the ARP are: to provide financial protection to clients of those firms that practice without having an appropriate policy of Qualifying Insurance; and to leave decisions regarding whether a firm or any solicitor should continue in practice with the SRA rather than the insurance market. The ARP acts as a safety net and provides Qualifying Insurance for a limited period to those firms that find it difficult or impossible to obtain cover from the commercial market. Without this, firms would be forced to close, perhaps as a result of short-term difficulties which had led to problems in obtaining insurance. However, it is essential that firms are covered by the ARP only for a limited period, because it would not be acceptable for those who cannot obtain cover in the commercial market to be protected indefinitely. Firms are allowed to stay in the pool for a maximum of 24 months in any 60 month period. Firms in the ARP are subject to monitoring visits by

the SRA and may have special measures imposed. ARP policies are underwritten by the Qualifying Insurers in proportion to their respective shares of the Qualifying Insurance market in terms of premium income.

9. In the interests of public protection, arrangements have been put in place with Qualifying Insurers to provide cover for claims arising against Firms that have not obtained Qualifying Insurance either from the market or from the ARP.

Compensation Fund

10. The Compensation Fund is a discretionary scheme established under the Solicitors Act 1974, from which a grant may be made to an applicant who has suffered a loss due to a solicitor's dishonesty or to an applicant who has suffered hardship due to a solicitor's failure to account for monies held. The Fund is held by the Law Society and is maintained by contributions from practising solicitors. It is subject to its own rules and to public law principles. The current Compensation Fund Rules and Guidance Notes are set out in **Annex C**. The Rules are in the process of amendment to consolidate the Rules and Compensation Fund guidelines into a single set of rules. The opportunity has been taken to address the specific issues of the time limit for making applications, the hardship test and the limit of the grant. The Compensation Fund Rules 2009 are attached as **Annex D.** Work will begin in 2009 to develop the Rules further in line with the wider requirements of the LSA.

Statutory Trust Accounts

11. This is a process that allows repayment to beneficiaries of money held by a solicitor prior to intervention and now held in trust by the Law Society. The ***Re Ahmed*** case confirmed that the administration of statutory trust accounts is subject to the public law principles of proportionality and reasonableness. It also confirmed the SRA's approach in the exercise of its powers as statutory trustee in the Statutory Trusts Account process. A copy of the judgment is attached at **Annex E**.

ISSUES

12. The issues arising from having three separate arrangements are illustrated at **Annex F**. Broadly, these can be categorised as: the boundaries of each scheme; the gaps (whether intentional or unintentional); the overlaps; and differences. Other issues considered include the impact of the LSA; the difference between the Compensation Fund's Rules and policy and its practice; and the practical claims handling issues that arise from having separate public financial protection arrangements.

ISSUE A – BOUNDARIES OF THE THREE SCHEMES

13. There are intentional boundaries to all three schemes either as a result of deliberately imposed limits, or arising from exclusions.

Professional Indemnity Insurance ("PII") - Boundaries

PII - Minimum Sum

14. The minimum sum insured of £2m for any one claim in the case of a sole practitioner or partnership, or £3m in the case of a relevant recognised body, is an obvious intentional boundary.

15. For 15 years until October 2005 the minimum sum insured had been £1m (plus an additional £0.5m "top-up" in the case of a recognised body such as a limited liability partnership ("LLP") or other incorporated practice). Following a process of review the minimum sum insured was increased to the current levels. This took account of the fact that the Law Society had fallen behind other regulators in this respect, the effect of inflation and the potential size of personal injury awards of the most serious kind.

16. Different levels of cover for a sole practitioner / partnership and a recognised body stem from the historic requirement for "top-up" or "excess layer" insurance for recognised bodies, which was itself a result of the concern expressed by Lord Donaldson of Lymington as Master of the Rolls that there could be a loss of public protection in allowing solicitors to incorporate with limited liability. Having two minimum sums insured can create problems, for example if a partnership with cover of £2m succeeds to a LLP there is no requirement for the partnership to increase cover to £3m. The problems would be removed by having a single minimum sum insured applicable to all firms. This would entail a substantial change in policy after only three years since the last change and this is not something that has been considered as part of this review. It may be a debate for the future once the principles of firm based regulation and the wider implications of the LSA, such as alternative business structures, have become established.

Conclusion 1

In light of the recent review, the Working Party's conclusion is that the minimum sums of indemnity insurance remain appropriate. These minimum sums are regularly reviewed by the Committee.

PII - Aggregation of Claims

17. The MTC allow for aggregation of claims under the "one claim" provision. Until 2004, the MTC defined "one claim" as all claims arising from the same act or omission or from one series of related acts or omissions.

18. This was reviewed in 2004 to deal with the concerns raised by Qualifying Insurers as to the potential for their unlimited financial exposure under the MTC in respect of multiple application of the (then) limit of £1million for any one claim. The clear indications then were that unless something was done to address these concerns there was a real danger that there would be a contraction in the number of Qualifying Insurers which would impact significantly on premium rates. One of the key objectives when setting up the current scheme was to seek to replicate as closely as possible the scope of cover provided by the Solicitors Indemnity Fund whilst ensuring that there were sufficient Qualifying Insurers to create a competitive market. It was important to maintain this delicate balance.

19. As a result of the review, the wording proposed in the case of ***Lloyds TSB General Insurance Holdings Limited and others v Lloyds Bank Group Insurance Co Ltd*** [2003] UK HL 48 (the "Lloyds TSB case") was adopted coupled with the increase in the compulsory limit from £1million to £2million any one claim. The current definition is at clause 2.5 of the MTC (**Annex B**).

20. The question of whether claims can be aggregated will always depend on the individual facts of each case. Where a number of claims are aggregated and the aggregate amount exceeds the limit of cover, the Insurer will tend to argue for

aggregation (and the Insured against), with the result that individual claimants' level of protection is less than the limit of cover. However, if the value of each separate claim is less than, or only slightly above, the level of excess applicable under the policy, the Insurer will tend to argue against aggregation since that will result firstly, in the Insurer not being required to pay out with the burden of paying for each separate claim instead falling on the Insured and secondly, in reducing the amount payable by the Insurer.

Conclusion 2

In light of the review carried out in 2004, the Working Party's conclusion is that the current aggregation provision should remain unchanged at the present time.

PII - Fraud or Dishonesty

21. Fraud or dishonesty is excluded from cover under clause 6.8 of the MTC (**Annex B**). This refers to the acts of a sole principal or all the principals in a firm (which includes a recognised body) since cover must extend to any innocent principal.

22. Claims involving allegations of dishonesty can result in declinature or reservation of cover by Insurers who may attribute knowledge or "blind eye" dishonesty (that is, knowing about the act and doing nothing about it) to all the principals in the firm. In other words every principal in the firm may become tainted by the action of their dishonest partner.

23. In terms of all reasonableness and common sense an exclusion or boundary as to dishonesty is both inevitable and good practice. Each case stands or falls on the particular circumstances and its own merits. Whilst it is reasonable that a solicitor or firm should not be able to insure themselves against their own deliberate dishonesty, the Committee is aware that this exclusion may cause a gap in cover in a particular set of circumstances or at least a delay pending proper investigations by insurers.

24. Some insurers interpret the fraud and dishonesty exclusion very widely and will reject all claims arising from a Firm where dishonesty has been found. For example, in a conveyancing matter a Firm may neglect to attend to the post completion formalities such as registering title and charges with the land registry and paying the stamp duty. The Firm is then the subject of an intervention for dishonesty. Subsequently a claim is received relating to the failure to complete the work. Insurers sometimes erroneously argue that the claim falls within the dishonesty exclusion even though the matter that is the subject of the claim relates to negligence.

25. This is relevant to the differences between the professional indemnity insurance and the Compensation Fund discussed in paragraphs 85 to 87. The Compensation Fund applies a narrower dishonesty test focussing on the particular matter or transaction and can conclude that the matter involves negligence not dishonesty. The claim can then, on the face of it, fall between the two arrangements.

26. Alternative ways of covering claims arising from dishonesty were considered as part of the 2003 review by the Council and the Working Party concluded on balance that no changes are needed for the time being.

Conclusion 3

The Working party's conclusion is that the protection of the public against the dishonesty of solicitors is adequately provided by the current arrangement. The

boundaries of the professional indemnity insurance and the Compensation Fund are not aligned but this does not create a gap in terms of what is covered. There are two different systems for determining dishonesty which can sometimes produce inconsistent results. The only way of determining the position is by legal process.

PII - Private Legal Practice

27. Acts undertaken outside "private legal practice" as defined at clause 8.2 of the MTC (**Annex B**) are not covered by indemnity. Some services such as the provision of financial services work may be provided "either way" - through a solicitor's practice or through a separate business. Add to this non-compliance with the Rules relating to publicity and separate businesses and ambiguity can arise. A separate business that provides "solicitor-like" services but which is not regulated by the SRA does not have the same protection afforded by the indemnity (and/or Compensation Fund) schemes. But if it was, in fact, a solicitor's practice (even though that was not the intention) practising without qualifying insurance, it would fall into the Assigned Risks Pool ("ARP").

28. An example helps to illustrate the point. A Firm of solicitors can run an estate agency as part of its solicitors' practice or as a separate business. Rule 21.05 of the Solicitors' Code of Conduct 2007 requires solicitors to institute safeguards in relation to services such as estate agency delivered through separate businesses. The purpose is to ensure that members of the public are not misled into thinking that a business is regulated by the SRA. One of the requirements is that if the separate business shares premises, office accommodation or reception staff with a firm then the separate business must make it clear to customers that they do not have the protection afforded by the SRA. The question is what happens if, in breach of the code, clients are not given this information. Should the estate agency still be treated as a separate business albeit in breach of the Code of Conduct in which case clients are not protected by the SRA, or should it be treated as a solicitors' Firm practising without compulsory professional indemnity insurance? In the later case clients would be protected by the SRA and the compulsory professional indemnity arrangements through the ARP.

Conclusion 4

There is some blurring of boundaries, for example as to "solicitor like" services or services carried out through a separate business which could lead to confusion for consumers as to what is, and is not, protected. Such problems rarely occur in practice. A further review should take place as firm based regulation and the requirements of the LSA develop.

PII - Eligibility Period

29. Firms that cannot obtain cover from the commercial market, for whatever reason, are eligible to be in the ARP for up to 24 months in any five year period, after which time the firm has two main options, either to obtain qualifying insurance or to close. A firm will not be eligible for a second year if its premium payments are two or more months in arrears at renewal.

30. At the time the current insurance scheme was being established in 1999/2000, the profession strongly supported the establishment of such an arrangement. The 24 month limit reflects the fact that it is essential that firms are covered by the ARP only for a limited period, because of the unacceptability of those firms that cannot obtain cover in the commercial market being protected indefinitely through the safety net provided by the ARP.

31. The numbers of firms covered by the ARP in the last five years (as at 28 January 2009) are as follows:

Indemnity Year	Number of Firms with ARP policy
2004-2005	38
2005-2006	33
2006-2007	33
2007-2008	25
2008-2009	140

The dramatic increase in the number of firms for 2008-2009 was due to a combination of factors including a hardening market, an increase in property related claims and the collapse in income from conveyancing.

Conclusion 5

The Working Party considers that the maximum period that a firm may remain in the ARP is set at the right level. It has taken account of the fact that any extra expenditure incurred by the ARP as a result of having a firm in the pool for a second year, and the number of firms and the claims they attracted against premium, reveals no compelling argument to reduce the period a firm can remain an eligible firm from 24 months to 12 months. Approximately 33% of firms that are in the ARP for a second year are subsequently able to get cover in the market. The Working Party concludes that no change is needed at present.

The Compensation Fund ("CF") - Boundaries

CF - Limit of Grant

32. The limit for grants of £1m (which is inclusive of all interest and costs) is an intentional boundary. This was last reconsidered by Council in 2003 when it was decided to make no change to the level of the maximum grant, so as to balance factors such as public protection, the profession's reputation, and proportionate financial liability for the profession. There is discretion to exceed the limit in exceptional circumstances, and the power to make a further grant in respect of the reasonable costs of an applicant's solicitor or other professional adviser.

33. An example of where the limit was exceeded is the case of a claimant who had been paralysed from the neck down as a result of a road traffic accident. The claimant engaged a solicitor, with the benefit of legal aid, in a personal injury case against the Highway Authority. Settlement of damages was reached and after deductions and interest accrued, the total left was £1.7m of which less than £700,000 was paid to the claimant.

34. The solicitor forged a letter saying the claimant had agreed to him keeping half of his damages as a gift for his hard work. In addition to the damages the solicitor also received costs of £185,000 but did not tell the Legal Services Commission about the settlement.

35. Although the maximum that the Compensation Fund will pay is £1m inclusive of all interest and costs, in this particular case it was decided that the circumstances were truly exceptional and the Compensation Fund paid out in excess of £1.2m. The solicitor was sentenced to a term of imprisonment.

36. A limit of £1m is an obvious difference to the limit of indemnity. The Working Party proposed that the limit be increased to £2m in line with the minimum level of compulsory indemnity cover and that the power of waiver be retained. The SRA consulted on this proposal on 25 April 2008 and a copy of the consultation paper is attached as **Annex G**.

37. Most respondents were in favour of the proposed increase. The Legal Complaints Service were of the view that the greater priority was to expand the scope of the Fund to allow lower level claims rather than to increase the maximum payment the Fund can make. The only outright rejection of the proposal was by the representative Law Society.

Conclusion 6

The Working Party recommendation that the limit of the grant be increased to £2m (with discretion) has been accepted by the Committee and the Board. The change was implemented in the Compensation Fund Rules 2009 that came into force on 31 March 2009.

CF - Time Limit

38. A time limit of 6 months was imposed upon applications to the Compensation Fund, although this period could have been extended if there were exceptional circumstances. The time limit was reviewed in 2003 when it was recommended that it be extended to 12 months. The change was agreed in principle but was not implemented.

39. It is clearly appropriate to have a finite time in which to make an application for redress. Furthermore the Fund needs to be able to calculate and forecast the financial impact each year and to do that needs some idea of the applications it faces. Whilst there have been objections to the 6 month limit (mortgage lenders tend to issue protective claims when they become aware of default by a solicitor), it is a balancing act between having some degree of certainty and not cutting off a route of redress. The Compensation Fund applies a much shorter time limit than limitation periods which apply in litigation (generally 6 years).

40. The Committee consulted on the proposal to increase the limit to 12 months (see **Annex G**). The responses received were divided on this issue. The representative Law Society and two firms were against the proposal for various reasons including that it was not necessary for the purposes of introducing the new regime, it was not justified and inadequate consideration had been given to the cost impacts. The other respondents supported the proposal. The reasons given included that it would provide better protection to vulnerable clients and a period of 12 months was much more reasonable than 6 months.

Conclusion 7

The Working Party's recommendations to extend the time limit for applications to the Compensation Fund to 12 months and to retain the discretion to exceed this as appropriate have been accepted by the Committee and the Board. The change was implemented in the Compensation Fund Rules 2009 that came into force on 31 March 2009.

CF - Hardship Test

41. A hardship test is applied to an application to remedy a loss due to a solicitor's failure to account. No such test is applicable to any claim for loss incurred by reason of dishonesty. Currently there is no method of means testing hardship and the applicant is not required to produce any evidence of hardship but simply has to tick a box. Invariably this test has the effect of excluding institutional lenders, although it is possible for an incorporated entity to demonstrate hardship as the test would be one of fact. On the other hand, the current practice possibly enables many applicants to obtain redress, but who may not pass the test of hardship based on a reasonable objective assessment.

42. As the hardship test is difficult to define and apply it has had little practical impact on applications for grants from the Compensation Fund. Most applications are for small amounts and there is an issue of proportionality in terms of the costs involved in applying a workable hardship test. The Compensation Fund Rules and the guidance tried to define hardship as "material" and it was generally accepted that if a lay applicant confirmed that hardship would be suffered then that assertion was not challenged. The imposition of a hardship test also flew in the face of the Fund's ethos of placing a personal applicant in the position she or he would have been in but for the default of the solicitor.

43. Hardship did not form part of the Council review in 2003. The LSA makes no reference to hardship criteria so any such criteria would have to be contained in the new Compensation Fund Rules. The Committee considered that the opportunity should be taken to address some of the problems with the hardship test. It approved a series of questions to be added to the Compensation Fund application form to establish whether an applicant would suffer hardship if a grant was not paid. Questions that might place an unreasonable burden on the applicant were avoided and they have been tailored to produce a simple positive/negative response. All respondents, with the exception of the Law Society, were supportive of the proposal that an individual whose dealings with a defaulting practitioner had been in a personal capacity and who had suffered or is likely to suffer loss due to a failure to account should be deemed to have suffered hardship.

Conclusion 8

The new hardship test was adopted into the Compensation Fund documentation from April 2008 and it has been incorporated into the new Compensation Fund Rules which came into force on 31 March 2009.

CF - Counsel's Fees

44. Counsel's fees are currently within the boundary of cover. However as part of the 2003 review it was accepted in principle that unpaid Counsel's fees should be excluded from the remit of grants. This was on the basis then that it was inappropriate that a modern regulator be involved in debt collection on behalf of Counsel. It was also felt that it was a matter for Counsel to take the commercial risk if they felt unable to require payment of fees in advance. The change to exclude Counsel's fees was a logical progression to the stance of the Office of Supervision of Solicitors (as it then was) not to regard non payment of Counsel's fees as a conduct issue. However this change has never been implemented.

Conclusion 9

The Committee concluded that it would be appropriate to cease payment of Counsel's fees as all the factors considered in the 2003 review remain relevant. As a result of discussions between the Law Society and the Bar Council the terms of a contract between solicitors and counsel have been agreed. Its introduction requires changes to the Bar's rules. The recommendation of the Working Party is that from1 October 2009 the Compensation Fund should not entertain new counsel fee claims. Once this process has been completed and contracting is adopted, claims from Counsel will have an alternative means of redress through the courts.

CF - Lender's Costs

45. Lender's costs for completion or rectification (in connection with non registration of title) in conveyancing matters (and possibly also other rectification costs) had been treated as being within the boundary of cover despite arguably going beyond the remit of the Fund's cover.

46. The Committee considered that it was difficult to see how these sums are payable where they are not the consequence of a failure to account or of dishonesty, but arise from a breach of contract or from frustration of the retainer. On the other hand, it was unacceptable for such costs simply to be added to a blameless individual borrower's mortgage account without prospect of recovery or challenge.

47. In the light of legal advice, the Committee agreed that, in respect of new applications, such payments should cease from April 2008 until such time as the new Rules were in force.

Conclusion 10

In view of legal advice received regarding grants in respect of rectification costs, the Committee has taken steps to stop future payments for the time being. The new Compensation Fund Rules, that came into force on 31 March 2009, specifically allow the SRA to make grants in respect of the additional reasonable

legal costs to complete outstanding work or to make a grant towards such costs.

Statutory Trust Accounts - Boundaries

48. The Statutory Trust process arises as a result of a resolution to intervene into a practice. Practice funds vest in the Society and are held in separate Statutory Trust Accounts ("STA") with a view to returning monies to those with beneficial entitlement. The process differs from indemnity insurance and the Compensation Fund as it does not of itself offer financial protection. However STA funds are protected whilst held by the Law Society and the investigative nature of the work may identify funds that would otherwise not have been apparent.

49. As the process is primarily concerned with repayment of monies held (which is limited to client money actually held by the firm at point of intervention), there are few boundaries as such. Distribution is dependant on at least some evidence of entitlement being available. There may be a shortfall in the distribution if funds held are insufficient for a full payment to all beneficiaries. The process takes no account of any other losses suffered. Interest is paid, but only what has accrued whilst the money has been held on statutory trust account. Other boundaries are within the terms of the ***Re Ahmed*** judgement, for example proportionality.

50. Responsibility for STA rules and policy has been delegated to the Committee. Rules are in the process of being drafted to consolidate existing practices following powers given under the LSA.

ISSUE B – GAPS BETWEEN THE THREE SCHEMES

51. It is recognised that the complicated nature of the professional indemnity and Compensation Fund schemes and the statutory trust account process, has resulted in gaps between the schemes. Some gaps are deliberate others are not. This may give rise to unforeseen, although not necessarily always undesirable, consequences.

Professional Indemnity Insurance - Gaps

PII - Awards by Regulator

52. Under Clause 1.8 of the MTC, insurance must provide indemnity against any amount paid or payable in accordance with the recommendation of the LCS to the same extent as it indemnifies against civil liability. Such recommendations usually arise out of awards for inadequate professional services ("IPS"). The firm is obliged to pay such an award but in default of such payment, payment must be made by the insurer.

53. The liability of an insurer under this clause is subject to the same exclusions as any other claim under a policy, which means that potentially an insurer could refuse to pay on the grounds of dishonesty. In that event, and despite an award for IPS by the LCS, there could be a gap in cover pending resolution of the issue of dishonesty and in a case where the firm has ceased or the principals are insolvent. More information is provided at paragraphs 103 to 109, where it can be seen that the change to clause 1.8 will provide more clarity.

Conclusion 11

The Working Party is aware of the difficulty and proposes no change at present.

PII - Aggregation

54. The definition of "one claim" in the MTC is open to interpretation and may cause a gap in cover. However, given the Working Party's view as set out at conclusion 2 above, it is considered that this is a risk that has to be tolerated.

PII - The Definition of "Firm"

55. The definition of "firm" in the SIIR may result in gaps. Solicitors (which term includes registered European lawyers and registered foreign lawyers) may practise in a number of different forms including currently, as a sole principal (except registered foreign lawyers) or a partnership, and as a "recognised body" which includes an unlimited company, a limited company and a Limited Liability Partnership ("LLP"). Firms can comprise a combination of these entities e.g. a partnership of recognised bodies, a firm which incorporates part of its practice.

56. The previous changes in the SIIR to permit more than one firm to be insured under a single policy of qualifying insurance and the change to require all the compulsory indemnity insurance in respect of recognised bodies to be on the basis of qualifying insurance addressed some of the gaps that had been identified. However, most members of the public who deal with firms of solicitors are unlikely to appreciate or understand the different practice structures and variations in the level of protection. The LSA allows for new forms of practice and the process of developing the new regulatory framework to allow for firm based regulation is well underway. This is likely to add to the potential for confusion by clients.

57. Section 37 of the Solicitors Act 1974 gives the Society the power to make indemnity rules concerning indemnity against loss arising from claims in respect of any description of civil liability incurred by a solicitor in respect of his or her practice. The power was extended to recognised bodies by section 9 of the Administration of Justice Act 1985. Society has no power to make indemnity rules in respect of an unrecognised body corporate. A known gap created by the wording of the primary legislation is that of an unrecognised body corporate, such as an LLP which has not got recognition and so falls outside the definition of a "firm" under the SIIR. The effect of this is that the unrecognised LLP would fall outside the safety net cover afforded through the ARP.

58. In the future the LSA requires that all legal service bodies must be recognised bodies or recognised sole practitioners. A body requiring recognition will have to apply for this every year (rather than every three years as at present) and so will be required to produce evidence of insurance more regularly. This would mean that it is more difficult for firms to slip through the net. However, this would still not deal with the case of an unrecognised practice that has never been in the system.

59. The SRA has issued a range of consultation papers as part of the process of developing the new regulatory framework to allow firm based regulation and new forms of practice permitted under the LSA including consultation paper 6 which is concerned with client financial protection and was published on the SRA website on 27 February 2008. The Committee took account of the responses received when framing its recommendations to the SRA Board. The recommendations were agreed and the SIIR

will be amended from 31 March 2009 so that the compulsory professional indemnity insurance arrangements will apply to:

- all entities authorised by the SRA,
- any partnership/sole practice that can be authorised only by the SRA, even if it has not obtained recognition by the SRA nor has it been held out as being regulated by the SRA.

60. All other entities and their clients will be outside the protection afforded by the SRA's compulsory professional indemnity arrangements.

Conclusion 12

The Working Party has developed a set of indemnity rules to accommodate firm based regulation and Legal Disciplinary Practices. Further work will be required in preparation for Alternative Business Structures (ABSs) including the development of appropriate amendments to the Solicitors' Indemnity Insurance Rules.

PII - Frustration of Retainer

61. An intervention into a firm may frustrate the retainer with a client. This can result in a solicitor not being able to complete a transaction on behalf of a client resulting in a loss to the client. The question then arises at to whether the loss is caused by negligence or simply as a consequence of the frustration. An example is the purchase of a property where the intervention takes place before completion or registration of title. The client would then incur additional legal costs to complete the purchase. Currently, where the retainer is frustrated due to intervention which prevents planned completion taking place, the claim (for unpaid disbursements in relation to completion) is generally referred to the Fund. If completion took place 6 months or more before the intervention, costs in such cases are initially referred to Insurers.

Conclusion 13

The Working Party proposes no change.

PII - Insolvency of a Qualifying Insurer

62. The insolvency of a Qualifying Insurer could expose a known gap in protection in the event that a claim is made against a firm after its Qualifying Insurer has become insolvent but before the inception of any replacement policy of Qualifying Insurance.

63. The effect of an insolvency event is that the SRA can give notice to the Qualifying Insurer terminating its right to issue policies of Qualifying Insurance. The existing policies remain in place so any claim made prior to the inception of any replacement policy will fall to be dealt with as part of the insolvency or via the Financial Services Compensation Scheme ("FSCS"), subject to the insured firm being eligible for protection by the FSCS. At this point no claim would lie against the Assigned Risks Pool. The same provisions apply to claims arising out of circumstances notified by Insured firms to a Qualifying Insurer prior to insolvency.

64. In the event of a Qualifying Insurer becoming insolvent a firm must put in place Qualifying Insurance with another Qualifying Insurer as soon as reasonably practicable

and in any event within four weeks of the insolvency event. Alternatively, if eligible, the firm can apply to the ARP. The SRA will send a letter to each Firm insured by the insolvent Qualifying Insurer advising them of the insolvency and providing answers to the following questions:

- What steps should Firms be taking now regarding ongoing cover?
- What is the position regarding claims already notified to the insolvent insurer?
- Will Firms qualify for reimbursement from the Financial Services Compensation Scheme?
- Will the Law Society/SRA provide any greater degree of protection?

The letter will also contain contact details of any appointed Administrators.

65. Both the Law Society when setting up the new indemnity scheme, and the SRA subsequently, have adopted the policy that it is not within their remit to provide any greater protection either to firms or their clients against the insolvency of a Qualifying Insurer over and above that available under the FSCS.

Conclusion 14

The Working Party concludes that no action is required at the present time. The incidences of insolvency to date have been rare and appropriate and proportionate provisions are already in place.

66. The Working Party has also considered issues that are not technically gaps but which can cause delay.

PII - Successor Practice Definition

67. The successor practice definition at clause 8.2 of the MTC (**Annex B**) aims to provide a mechanism to identify the correct Insurer to respond to a claim against a ceased firm. The principle is that where a firm ceases as the result of a succession by another firm (e.g. due to a merger, acquisition or absorption) then that successor firm's policy of qualifying insurance should deal with future claims arising from the ceased practice. However, in factually complex or unclear cases there may be difficulty in identifying which, if any, firm is a successor practice. Some cases involve multiple successions where, in the event of a claim against the original practice, it is necessary to establish which is the ultimate successor practice in the chain of succession.

68. A successor practice definition was necessary in order to ensure continuity of cover in a 'claims made' insurance system. Without it many closed firms (and their clients) would not have effective insurance cover. The successor practice definition means that , wherever possible, there is cover with a firm which has a continuing policy. If the successor practice definition was relaxed then (unless client protection was reduced) there would have to be an alternative collective mechanism either through the ARP or funded more generally by the profession.

69. There have been concerns that the successor practice definition makes it very difficult for sole principals to retire. It has been suggested that it can be hard for a sole principal to find a successor practice. Without a successor the cost of going into run-off cover with their own insurer can be substantial and can act as a bar to retirement. In May 2008 a survey by the representative Law Society sought evidence of problems caused by run-off cover costs. Following the survey the Law Society concluded that

there was little hard evidence of a problem. The Law Society is considering issuing guidance to highlight the potential difficulty to firms contemplating closing.

70. It appears therefore that the successor practice principle has worked as intended. Any difficulty is more of a result of a delay (in identifying the insurer on cover) rather than an actual gap in cover. The Qualifying Insurer's Agreement ("QIA") provides a mechanism for resolution of disputes as to whether a claim is properly payable by one insurer or another and in default of agreement the ARP Manager may conduct the claim pending arbitration.

Conclusion 15

The Working Party proposes no change to the definition of "successor practice" at the present time.

The Compensation Fund - Gaps

CF - Hardship

71. An unintentional gap may arise from the application of the hardship test to applications to remedy a loss due to a failure to account as described at paragraphs 41 to 43. A new hardship test has been adopted with effect from April 2008 as referred to in Conclusion 8.

CF - Deliberate Closure

72. The way in which a firm is closed may cause a gap. A closure may be deliberately planned with the intention of avoiding liabilities and obligations. There may then be no files or accounts information available and so no means of investigation obtainable. Ledgers and files may be destroyed and, with deliberate concealment, result in clients being unaware of a problem or the potential for a claim. An intervention by contrast provides some control of the close-down with the intervention agent seeking to ascertain all the information and to contact clients about a possible claim. Increased applications to the Fund arose from such closures, mostly for Counsel or expert fees.

73. Whilst checks could be placed on firms known to be closing to ensure an orderly closure and a form of risk management introduced for those who are closing firms, there would appear to be little remedy to a case of determined malfeasance, other than continued and improved intelligence gathering and sharing (perhaps along the lines of a "traffic light" system).

Conclusion 16

Work continues to improve communication between the SRA, LCS and Insurers. As part of the development of risk-based regulation the Risk Assessment and Designation Centre (RADC) within the Regulation Response Directorate has been created to be the primary gateway for receipt of regulatory information other than confidential intelligence. The Working Party notes the action being taken.

CF - Usual Business

74. Activities falling outside a solicitor's "usual business" can lead to a gap. The dishonesty of, or failure to account by, a solicitor must normally have occurred within the course of a solicitor/client transaction of a kind which is part of the usual business of a solicitor (currently guideline 1(f) (**Annex C**). This is similar to the concept of "private practice" in relation to professional indemnity insurance.

75. "Usual business" is generally meant to refer to any matter where there is a solicitor/client relationship and an underlying transaction. The Working Party has considered various options including:

- tightening the definition to include, for example, a list of generally accepted matters;
- aligning the definition with the "private practice" definition applying in respect of indemnity, so as to exclude work if not done as part of private practice; and
- regarding the definition as a proper boundary and that the principle of "caveat emptor" is a reasonable one to apply in circumstances where a client places money with a solicitor for investment in a "too good to be true" investment scheme.

A great deal of education of the profession has taken place in recent years, for example, in the context of money laundering about the dangers of transferring client funds where there is no genuine underlying transaction.

76. Compensation Fund cover may extend to solicitors not in private practice ("employed solicitors") and solicitors not in practice in England and Wales ("overseas practice"). So it would be difficult to word a unified definition of "usual business" / "private practice". In practical terms the difference between the two definitions has had minimal impact with only one Compensation Fund claim emanating from an overseas solicitor who had happened to have a client account in the UK.

Conclusion 17

The Working Party has considered the definition in the new Compensation Fund Rules which will harmonise the current Rules and their guidelines. "Usual business" will then be linked to a list of persons defined as "defaulting practitioners" and the usual work of their practice. The Compensation Fund has had no claims emanating from employed solicitors and only one claim relating to an overseas solicitor. This is not a significant issue.

CF - Other Issues

77. Other issues that are not technically gaps can cause delay. The predominant issue to date has been the disagreement as to the source of redress between the Fund and Insurers as to the appropriate body to provide cover. This coupled with difficulties of communication and liaison can cause delay and so potentially a temporary gap in cover. Liaison continues to improve communication, referrals and reduce delays.

78. The Qualifying Insurer's Agreement does make some provision for how such problems should be dealt with pending resolution. At present the Fund responds to intervention with emergency payments as an Insurer may take too long to do so. In these circumstances the Compensation Fund becomes a Fund of first resort.

Statutory Trust Accounts ("STA") - Gaps

STA - Shortfall

79. In most cases, usually due to the dishonesty or incompetence of the solicitor, there is a shortfall in the funds available compared with what is due to beneficiaries so the most appropriate method to allocate repayment will be considered. Distribution of monies may follow the presumption in ***Clayton's Case*** that those funds which are deposited with the solicitor first are the funds which are presumed to have been the first to leave the client account (the notion of first-in, first-out). This would mean that the last entries in the client account which are identifiable as still being held would be paid out in full. Otherwise repayment is usually on a pro rata basis (similar to a dividend payment) and if there is a shortfall, it may be possible to claim on the Compensation Fund. Any monies received prior to intervention would form part of the pooled client account which, if in shortfall, would mean a distribution being made in accordance with the general practice of pro rata.

Conclusion 18

The Working Party proposes no change to the principles applied when distributing Statutory Trust monies and these principles have been carried over into the draft new STA Rules.

STA - Evidence

80. Evidence of some sort is required to support a claim for repayment. However it is recognised that the records of an intervened firm are often in a poor and inadequate state. They are usually incomplete with a lack of clear information. This, coupled with an inability to contact clients, will cause a delay between intervention and distribution. The evidence test applied, therefore, is based on a proportionate approach and is dependent upon the actual circumstances and the merits of each case. Insufficient evidence may lead to a gap, in the sense of no repayment. As a matter of good practice (and to avoid speculative or unwarranted claims) there has to be some data upon which to base a distribution. In some cases where there is insufficient information available either from the firm or the client, then there may be a recommendation of no payment.

Conclusion 19

The Working Party proposes no change to the evidential requirements before distributing Statutory Trust monies and these principles have been carried over into the draft new STA Rules.

ISSUE C – DIFFERENCES BETWEEN THE THREE SCHEMES

81. As shown already, the individuality of the indemnity and Compensation Fund schemes, and the Statutory Trust Accounts process, has naturally resulted in differences between them. Some may be inevitable because a different mischief is being addressed. Some may be justifiable. Others, however, may be unnecessary and/or unintended.

Three schemes differences - Limit of Cover

82. From a consumer's point of view the availability and accessibility of redress is important but it is inconsistent that the amount of that redress can vary depending upon the source. Clients who have their money taken by a dishonest sole practitioner will be protected by the Compensation Fund up to the current limit of £1 million, (although that limit can be waived in exceptional circumstances). Clients who suffer the same problems with a partnership will have a claim against the partners and providing there is at least one 'innocent' partner then the claim will fall within the firm's Qualifying Insurance which is subject to a limit of £2 million any one claim. This difference appears to be anomalous, and has now been removed by the increase in the Compensation Fund limit to £2 million – see paragraphs 36and 37.

83. The Working Party's conclusions are set out at conclusions 1 and 6.

Three schemes differences - Hardship

84. The concept of establishing hardship in respect of a claim for redress applies only in respect of a Compensation Fund application relating to a loss due to a failure to account, as provided under S36 (2) (b) of the Solicitors Act 1974. It seems anomalous to impose this "test" just in relation to this limb of an application to the Compensation Fund whereas if the claim fell to be dealt with by the firm's professional indemnity insurance, no such test would apply. The policy has been to place a very low hardship threshold in respect of individual applicants. The Working Party's position is set out at paragraphs 41 to 43.

Three schemes differences - Dishonesty

85. There is a difference in response between the Compensation Fund and indemnity insurance in respect of claims arising from dishonesty. Insurers' interpretation of the definition of dishonesty tends to be wider than that used by the Compensation Fund. The effect of this is that an insurer may reject a claim on the basis that it falls within the dishonesty exclusion in the MTC but the claim will not be regarded as arising from dishonesty for the purposes of the Compensation Fund. For example an insurer may conclude that all principals in a firm were tainted with dishonesty on a "blind eye" basis (in other words, someone knowing there is a risk, or having solid grounds for suspecting that a transaction is improper, but consciously or deliberately deciding to proceed without making the further enquiries that an honest and reasonable person would have made to satisfy themselves as to its propriety).

86. There is also the issue that, for example, dishonesty is determined in different ways in the insurance arena and by the Compensation Fund. In insurance a dispute (including refusal to compensate by insurers) is determined in the courts between the claimant and the insurers; in the Compensation Fund by the adjudication process. Inconsistent findings are possible. For example, insurers may reject a claim stating that it arises out of dishonesty by all principals of the insured firm. The Compensation Fund however may come to a different conclusion on the same claim. Further, recovery by claimants in professional indemnity is on the basis of legal liability as adjudicated in the courts; with all the concomitant strengths and weaknesses of a court based system.

87. The 2003 review by Council concluded that combining cover against dishonesty and negligence in an insurance type arrangement would not be viable. The alternative of dealing with all dishonesty under the remit of the Compensation Fund was considered and rejected. If the Fund took on all such claims the size of the Fund and the

contributions to it would have to be increased many fold. There would also be other resource issues to deal with the increased number of claims, and the cost of administering the Fund would escalate.

88. The Working Party's conclusion is set out at conclusion 3.

Three schemes differences - Evidence or the burden of proof

89. The Statutory Trust Account process requires some evidence, but will entertain less evidence than that required by the Compensation Fund in that the STA process invites the claim in the first place, confident that money is available to be returned. In very rare cases a distribution is made where there is a body of information and a sum of money available even if there is no additional evidence on the basis of proportionality.

90. The Compensation Fund's processes (both in terms of a failure to account application and an application based on dishonesty) are entirely evidence based. The evidence required, however, may differ from case to case depending upon the particular circumstances of the application.

Conclusion 20

The Working Party concludes that no change is necessary. Given the different problems being addressed by the different schemes, the differing evidential requirements are justifiable and proportionate.

Three schemes differences - Aggregation

91. The one claim or series of related acts principle applying to indemnity (paragraphs 17 to 20) does not apply to the Compensation Fund where the limit was £1million (now £2 million) per claimant. This was considered as part of the review by Council in 2003 when the recommendation then was that there should not be a limit per firm. Problematic issues were identified such as the difficulty of assessing how the cumulative nature of grants could be measured (e.g. on a first come-first compensated basis or with a quarantine period to allow all potential claimants to come forward causing delay for early claimants). Aggregation in terms of the Compensation Fund could lead to inequity as if there is a limit per firm many claimants would be compensated to a lesser extent than if there were only a few. Apportionment of compensation amongst claimants would be administratively complex, would lead to appeals and could possibly result in litigation.

Conclusion 21

The Working Party's conclusion is that the current aggregation provision should remain unchanged at the present time.

Three schemes differences - Usual Course of Business and Private Practice

92. Indemnity insurance uses the definition of "private practice" (clause 8.2 of the MTC at **Annex B** and paragraph 27 above) which includes, without limitation, all the professional services provided by a firm including acting as a personal representative, trustee, attorney, notary, licensed insolvency practitioner or in any other role in conjunction with a practice and includes services provided pro bono. The Compensation Fund uses the definition of "usual business" (paragraphs 74 to 76)

which envisages that the dishonesty must have occurred within the course of a solicitor/client transaction of a kind which is part of the usual business of a solicitor.

Three schemes differences - Time Limits

93. There was previously a 6 month time limit in relation to Compensation Fund applications, now increased to 12 months under the new Compensation Fund Rules, no limit in the statutory trust accounts process and the statutory limitations in relation to indemnity insurance claims. The Working Party's conclusion as to the Compensation Fund time limit is set out at conclusion 7.

Three schemes differences - Costs

94. Costs incurred in pursuing a claim are treated differently under the each of the three schemes.

(a) **Compensation Fund** - Under rule 9 of the Compensation Fund Rules the Fund may pay the proper and reasonable costs of an application to the Fund.

(b) **Professional Indemnity Insurance** - In indemnity matters, the costs of pursuing a claim form part of the claim and fall within the minimum sum insured.

(c) **Statutory Trusts** - The STA process simply returns money. The costs of making a claim on the STA are not recoverable.

Conclusion 22

The Working Party concludes that no change is necessary at this point. Although there are differences in how costs are treated, these appear to be justified.

Three schemes differences - Interest

95. The payment and calculation of interest is different under the three arrangements. For Compensation Fund matters a sum in lieu of interest may be paid, but not in every case. When it is payable the Compensation Fund rate is decided by the SRA and is calculated in accordance with the rates prescribed from time to time by the SRA. Generally interest is payable on any grant that is made to the applicant but is not paid on disbursements. Interest on a grant is not subject to tax as it is treated as a gift.

96. STA distributions, where relevant, include interest equivalent to that earned by the funds with the appropriate deduction for withholding tax. The court rate applies to any interest payable in connection with indemnity insurance matters.

Conclusion 23

The Working Party concludes no change in practice is necessary. Although there are differences in how interest is treated, these appear to be justified.

Three schemes differences - Adjudication and Appeals.

97. Decisions relating to the exercise of the discretion of the Compensation Fund, the determination of entitlement to Statutory Trust Funds and the distribution of Statutory Trust Funds are susceptible to judicial review. It is essential then that a clear and transparent decision making process which demonstrates the separate consideration of Compensation Fund and Statutory Trust issues should be in place. One of the most important reasons for this is that the Compensation Fund will more often than not be a beneficiary through its right of subrogation against the Statutory Trust and so could itself apply for judicial review of the decision made by the Statutory Trust managers. Currently adjudicators dealing with STA issues do not adjudicate on Compensation Fund applications.

98. The STA process allows for decision making to be delegated to the office but all decisions are currently made by a nominated adjudicator selected from a team of adjudicators (or Statutory Trust Panel if the value is over £500,000 (subject to conditions). There is a right of appeal provided certain criteria are met (an amount in dispute of over £5,000; the first instance decision based upon lack of evidence and merit; if the decision was not made by the Statutory Trusts Panel). Until October 2008 there had been no appeals as matters tend to be resolved by negotiation. An appeal has now been notified by a sole principal of an intervened into firm where the principal had been struck off for dishonesty. There can be no appeal against the basis or scheme of distribution.

99. Depending upon its value a decision maker within the office will decide on an application to the Compensation Fund. A Panel will consider: any claim over £100,000; any rejected claim over £10,000; any matter that is likely to be judicially reviewed or raises a matter of policy. There is no right of appeal. If a caseworker feels that there is some likelihood of rejection they will disclose that fact and the reasoning to the applicant who may comment so the Panel will have the opportunity to take those comments into account. The Fund tries to put the applicant in the same position as if there was no intervention. This differs from the STA process.

100. Both the Compensation Fund and the STA process allow for a decision to be reconsidered if new information is provided. In an STA matter, an amended decision can of course impact upon the whole distribution and so it is not merely the applicant's interests at issue.

101. In indemnity matters, if a claim is not satisfied then the claimant can seek a resolution of the claim through the civil courts.

ISSUE D – OVERLAPS BETWEEN THE THREE SCHEMES

102. Overlaps between the schemes exist. Whilst these are less of a public protection issue than gaps, overlaps have the potential to cause confusion and duplication and can slow down the process of claim handling. Overlaps primarily arise between professional indemnity and the Compensation Fund, for example the concept of consequential loss, and proof of claim. Under the new Compensation Fund Rules, costs will be split into three areas: litigation for the purposes of mitigating losses; application costs; and failure to complete.

Conclusion 24

In an ideal world a comprehensive scheme of redress would have been designed. In reality the four arrangements have been developed at different times to meet different needs and inevitably there are overlaps and gaps, but these do not lead to serious problems.

ISSUE E – OTHER MATTERS OF COVERAGE

Inadequate Professional Services

103. IPS is intended to recognise and compensate for poor service, rather than to provide damages for negligence. IPS usually manifests itself as, amongst other things, unreasonable delay or inaccurate or incomplete information given to the client. If the Legal Complaints Service ("LCS") finds a client has received poor service from his/her solicitor, it can tell the solicitor, amongst other things, to pay compensation for distress and inconvenience. The compensation limit for IPS awards was increased on 1 January 2006 from £5,000 to £15,000. The LCS categorises poor service on a scale from "modest" (where the poor service has had a limited effect) through to "extremely serious" (where the poor service has severely affected the client's wellbeing, possibly over a long period of time or with permanent effects).

104. The LCS regard distress and inconvenience as the harmful effect that poor service from a solicitor can have on the client's general wellbeing. "Distress" includes worry, concern, embarrassment, anxiety, disappointment and loss of reasonable expectations. "Inconvenience" refers to the time and effort a client has spent on a complaint that would not have been necessary if their solicitor's service had been adequate. Inconvenience can also arise from the poor service itself. Compensation for distress and inconvenience is intended to be a tangible acknowledgement of regret for the "emotional" consequences for the client.

105. 'Consequential loss' is a term well understood in law and in the Working Party's view means 'loss indirectly flowing from a breach of contract or of duty which is recoverable at law or in equity'. There can be no doubt that liability for such loss is a form of civil liability and so is covered by the MTC. A problem has arisen because the LCS and its predecessors have adopted the term 'consequential loss' to cover elements of its awards for IPS which are not normally recoverable at law or in equity. For example, the LCS sometimes includes in IPS awards compensation for distress, inconvenience, hurt feelings and delay. Awards of damages of these types are rarely made by the Courts, and are usually confined to certain types of breaches of contracts of employment, or breaches of contracts to provide enjoyable holidays. A court would not regard such losses as flowing from a solicitor's breach of professional duty.

106. Qualifying Insurers object to meeting IPS awards consisting of, or containing elements of, consequential loss in the sense used by the LCS. Their objection is on the ground that as those elements would not be awarded by a Court, they do not constitute a species of civil liability, which is what is covered by the MTC. The answer to that objection is that clause 1.8 of the MTC requires the insurer to meet any award by, among others, the LCS, and so the insurer must meet an LCS award even if it contains elements of compensation which would not be awarded by a Court, subject only to the permitted exclusions set out in the MTC.

107. Some solicitors deal promptly with a decision to award compensation and either pay or refer the matter to their Qualifying Insurer. Sometimes, however, solicitors do not

comply, whether due to an inability, or an unwillingness, to pay. In that event the LCS or the client may also refer the issue direct to the Qualifying Insurer as a claim covered by clause 1.8 of the MTC. Where a firm defaults on payment of an IPS award which falls within the excess the claimant has the right to serve notice on the relevant Qualifying Insurer to make good the default. The interpretation of this clause has been reluctantly accepted by the Qualifying Insurers. Amongst other things, Qualifying Insurers have previously attempted to argue that:

- clause 1.8 does not extend to an award by the LCS;

- the MTC do not cover costs reduction and directions made by an adjudicator for a solicitor to pay the LCS's costs; and

- if there is a refusal to pay an office award of IPS which necessitates the matter going to the Solicitors Disciplinary Tribunal for the purpose of enforcing the LCS award, then clause 1.8 does not come into effect until that decision. If this was correct the process would require change because it would be unacceptable for clients not to receive compensation for such a length of time.

108. Other IPS issues for Qualifying Insurers include:

- the trigger point for the purposes of a "claim", although it has been agreed recently that the earliest trigger should be any complaint made by the client to the firm directly, seeking compensation, before any contact with the LCS. Not every complaint amounts to a claim;

- what constitutes "loss", "breach" or "causation" arising from civil liability, and the statutory limitation period. However clause 1.8 recognises that civil liability can arise from a variety of mechanisms;

- distress and inconvenience - insurers do not consider this to be a proper claim arising from civil liability as a court will rarely give compensation for distress and inconvenience; and

- blurred awards that cross over with indemnity. This could lead to "double recovery" and compensation should not be awarded for the same financial effects twice. This has largely been addressed by improved and earlier communication between the LCS and Insurers. The question of some form of "full and final settlement letter" has also been looked at both in 2005 by what was then the Compliance Board and again in discussion between the Legal Complaints Service and insurers when it was accepted that "full and final settlement", however worded, would not prevent a client from making a conduct complaint.

109. From October 2008 clause 1.8 of the MTC has been changed as follows:

"Award by ~~legal ombudsman~~ regulatory authority

The insurance must indemnify each Insured against any amount paid or payable in accordance with the recommendation of the Legal Services Ombudsman, the Legal Complaints Service or any other regulatory authority to the same extent as it indemnifies the Insured against civil liability".

The Working Party's view is set out at conclusion 11.

Firm Based Regulation

110. The Working Party has considered how the various schemes should be modified to accommodate firm based regulation and the introduction of Legal Disciplinary Practices ("LDPs") under the LSA. The Working Party considered whether the protection afforded by the compulsory professional indemnity scheme and the Compensation Fund should be aligned, particularly where solicitors are practising through entities not authorised by the SRA. The Working Party considered the extent to which the SRA should act as "default regulator" in order to protect the public interest. In this context acting as "default regulator" means providing the public with some degree of financial protection in circumstances where a regulated individual (e.g. a solicitor or registered European lawyer) practises through an unrecognised entity. The Working Party decided that the benefits of a uniform approach should take second place to the objective of protecting the public.

111. The approach adopted with respect to the professional indemnity scheme is set out in paragraphs 55 to 60. In summary the SIIR were amended, from 31 March 2009, so that the compulsory professional indemnity insurance arrangements now apply to:

- all entities authorised by the SRA,
- any partnership/sole practice that can be authorised only by the SRA, even if it has not obtained recognition by the SRA nor has it been held out as being regulated by the SRA.

All other entities and their clients are outside the protection afforded of the SRA's compulsory professional indemnity arrangements.

112. The Working Party also considered the extent to which the protection afforded by the Compensation Fund should extend to the new entities. The cover provided by the Compensation Fund is in respect of the acts or defaults of persons in whatever capacity they might practise whereas the cover afforded by the compulsory professional indemnity scheme relates only to "private practice" and is based on firms.

113. The Working Party felt that for the time being at least, the current scope of the Compensation Fund should be maintained and adapted to accommodate the new entities. The starting point was to agree that the object of the Fund as set out in the Compensation Fund Rules 2009 ***'is to replace client money which a defaulting practitioner or a defaulting practitioner's employee or manager has misappropriated or otherwise failed to account for,"*** where "***defaulting practitioner***" means:

(a) ***a solicitor in respect of whose act or default, or in respect of whose employee's act or default, an application for a grant is made;***

(b) a registered European lawyer in respect of whose act or default, or in respect of whose employee's act or default, an application for a grant is made;

(c) a recognised body in respect of whose act or default, or in respect of whose manager's or employee's act or default, an application for a grant is made; or

(d) a registered foreign lawyer who is a manager of a partnership, limited liability partnership or company together with a solicitor, a registered European lawyer or a recognised body, and in respect of whose act or default or in respect of whose employee's act or default, an application for a grant is made….;

114. The Working Party went on to consider the extent to which cover by the Fund should be restricted in relation to individual defaulting practitioners practising through various

entities. Following consultation the Working Party recommended that the carve-out from cover should be limited to the new situation where solicitors are practising in firms authorised not by the SRA but by another approved regulator. In these circumstances it was felt appropriate that clients should be protected by whatever compensation arrangements are provided by the other approved regulator.

115. In the same way the Working Party recommended that the Compensation Fund should extend to an individual authorised by another regulator practising through a firm recognised by the SRA. The new Compensation Rules make it clear that under firm based regulation, the SRA's Compensation Fund is available to deal with applications relating to the default by any individual within any SRA recognised firm. This is in keeping with the spirit of firm based regulation and will provide clarity for clients.

ISSUE F – COMPENSATION FUND - MISMATCH BETWEEN GUIDELINES, POLICY AND PRACTICE

116. For the best of reasons in terms of protecting the public, inconsistencies have existed between the Compensation Fund's policy/guidelines and the practice actually adopted. The review has highlighted a number of such mismatches. The new Rules will resolve some of these issues. Examples are given below

Fund of last resort

117. The Fund is a discretionary fund and was often referred to as a fund of "last resort". However, in the public interest the Fund acts as fund of "first resort" in almost all cases, and always in emergencies when instant funding is required, for example, to complete a house purchase.

Hardship

118. The hardship test (referred to in paragraphs 41 to 43 above) applies to 'failure to account' applications. The test applied was found to be inadequate and was based on self certification using a tick box. This mismatch has been addressed in the short term by an amendment to the Compensation Fund application form and in the longer term by appropriate provisions in the new Compensation Fund Rules.

ISSUE G – CLAIMS HANDLING ISSUES

119. In the context of the Compensation Fund and statutory trust accounts, a single, high level claims handling process has been created for the Client Protection Unit with the aim of an efficient, fast and cohesive mechanism to compensate or return funds to the client as quickly as possible by the most appropriate route. The possibility of conflict between the Compensation Fund and statutory trusts accounts has been considered and it is believed that this can be avoided whilst there are two possible sources of payment and separation of decision making. Further information is set out in Chapter 3.

Conclusion 25

The Working Party proposes no further action. It receives regular updates upon claims of interest and continues to monitor these.

CONCLUSION

Conclusion 26

The underlying principle is client protection. The existing schemes described in this report already provide a great deal towards a cohesive and complete protection which only needs some adjustment to improve and align it. Anomalies and peculiarities are inevitable in different schemes that address different needs and total protection under a single scheme is probably an unattainable ideal.

Chapter 2 – Financial Management

INTRODUCTION

120. A number of criticisms of the financial management of the Compensation Fund have been made by the Law Society over several years. In particular it is felt that the forecasting and modelling techniques used in assessing future contribution requirements are crude and inadequate. The perception is that the Fund's reserves are too high and that it is slow to recover money. There is also the view that the Fund's administration costs are too high, though this view appears to have been fuelled by the historic Law Society accounting practice under which the Compensation Fund contributions cover not only the cost of investigating applications and making grants but also management's assessment of the resources engaged in other parts of the SRA (and previously the Law Society's regulatory directorates) in administering and protecting the Fund.

121. The Law Society has delegated responsibility for the financial management of the Fund to the SRA although the Law Society has chosen not to delegate to the SRA the power to set Compensation Fund contribution rates.

FORECASTING AND MODELLING

122. As part of undertaking this review, modelling of the Compensation Fund has been developed based on an analysis of historic data. Previously risk had been determined, to a great extent, by utilising the experience and knowledge of staff in investigation and intelligence functions to determine potential trends in future default.

123. Forecasting has been based upon cash flow projections carried out in the Finance function and contribution proposals have been made by negotiating a balance between cash flow predictions and the assessed risk to the Fund's solvency.

124. There is no precise methodology for forecasting claims against the Fund. Information which is currently used to forecast future claims has two sources:

- historic intervention trends - (volumes of intervention by type)
- work in progress within the Compensation Fund - (active files in the office or in abeyance awaiting information)

125. A range of information is held from which more sophisticated forecasts could be developed. However, achieving the capability to identify trends from information received and investigation/decision making processes to specific claims outcomes is highly dependent on significant development of the SRA's computer systems. This cannot be achieved in the short term. The Working Party agreed that it would be most desirable for this development work to be completed.

126. Two further current sources of information will be used to support future claims forecasting:

- Live Interventions List - (includes agent information, any potential account shortfall, the volume of live files and ledger information where available)
- Interventions List – (details of potential interventions including size and location of firms, potential grounds for intervention and their current stage in the process)

127. The Working Party has considered whether additional benefit can be achieved by using external analysts to predict the impact of claims and economic trends in support of contribution setting. Prior to 2001 the Law Society used actuaries to provide external advice on contribution setting. In 2001 the Society's Audit Committee decided not to continue this arrangement on grounds that it did not demonstrate adequate cost benefit. The Working Party believe that the Audit Committee's decision was correct. The report did not provide any analysis of risks in relation to contribution setting and its recommendation, to establish a reserve of two year's claims (£75 million) was not accepted.

128. As part of review the Working Party obtained advice from Marsh (who are the Committee's appointed indemnity insurance advisers) on the value of using actuaries to support forecasting and modelling. Marsh confirmed that both the cost and effectiveness of actuarial input is dependent upon the quality of available information. Although actuaries are used to using poor data this substantially reduces the accuracy, and therefore value, of their findings. The Working Party concluded that actuarial advice will not provide any more certainty than can be achieved through existing forecasting methods.

RESERVING POLICY

129. The primary purpose of maintaining a reserve in the Compensation Fund account is to make sure that there is adequate money available to pay all grants from the fund authorised during any 12 month practising year.

130. The Working Party applied the following principles when considering the target minimum level of reserve which should be maintained:

- **Public protection will be maintained**
  - No grant will be refused, reduced or delayed because money is not available from the fund.

- **Excessive demands upon contribution payers will be minimised**
  - Substantial year on year changes to contribution levels must be avoided.
  - Payment of a second contribution during any practising year must be avoided.

Base calculation for reserve setting

131. As the starting point the Working Party recommended the following base calculation:

- ***Average grants paid*** – the average annual grant payment total over the last 7 years; ***plus***

- ***Three months estimated recharges*** - to cover the cost of recharging to the Compensation Fund between the end of September and the end of December.

The Working Party then considered three options for setting the minimum reserve based on 1, 1½ and 2 times the average grants paid.

Setting the minimum reserve at the average grants paid

132. One option is to maintain the reserve at a level which provides basic protection to clients. This option is considered to be unacceptable by the Working Party because it provides inadequate protection against the risk of having to collect supplementary contributions during the practising year (with associated costs), and the risk of delaying payments to clients.

133. Based upon the current profile of claims and recharges, setting the minimum reserve at the average grants paid results in a target minimum reserve of £16 million broken down as follows:

£13 million - to cover larger than expected grants during the year;
£3 million - to cover recharge costs to year end.
£16 million

134. The Working Party did not support this option. It risks payments to clients being delayed because of the need to call upon the profession for a second contribution in the practising year. From the profession's point of view, maintaining a low reserve will sustain the pattern of substantial year on year changes in contributions which has been evident over the last 20 years. The Working Party's view is that this is unacceptable in all but the most extreme circumstances.

Setting the minimum reserve at 1½ times average grants paid

135. A partial move towards smoothing the impact upon contributions which would result from allowing some reserve to be held with the purpose of limiting the impact of fluctuations in grants paid.

136. Based upon the current profile of claims and recharges, setting the minimum reserve at 1½ times average grants paid results in a target minimum reserve of £22.5 million broken down as follows:

£13 million - to cover larger than expected grants during the year;
£6.5 million - to smooth the impact on contributions of recovering from growth in claims;
£3 million - to cover recharge costs to year end.
£22.5 million

Setting the minimum reserve at twice average grants paid

137. Applying the principles stated in paragraph 130 the Working Party recommends that the policy should be to target maintaining the reserve at twice the average annual value of grants paid plus the cost of three months recharges. Based upon the current profile of claims and recharges this gives a target minimum reserve of £29 million broken down as follows:

£13 million - to cover larger than expected grants during the year;
£13 million - to smooth the impact on contributions of recovering from growth in claims;
£3 million - to cover recharge costs to year end.
£29 million

Financial impact

138. A model based upon grants paid over a 7 year period between 2001 and 2007 was used to compare the impact of the alternative reserving policies. This period was chosen because it reflected a cycle where grants paid in individual years had been both high and low. The maximum grants value in the period was £20 million and the minimum £9.47 million.

139. Over the 7 year period the model produced the following results for annual contributions:

- **Reserve set using 1 times average claims**:
  Lowest contribution £184; highest contribution £400; range £216.
  Total contributions over the 7 years: £1,954

- **Reserve set using 1.5 times average claims**:
  Lowest contribution £240; highest contribution £370; range £130.
  Total contributions over the 7 years: £1,950

- **Reserve set using 2 times average claims**:
  Lowest contribution £260; highest contribution £280; range £20.
  Total contributions over the 7 years: £1,920

140. What this demonstrates is that with a 1 times multiplier there is considerable volatility in the contribution levels over the 7 years. This volatility can be significantly reduced by using a 1.5 times multiplier and be almost eliminated by moving to a 2 times multiplier.

141. The model shows the impact of smoothing contributions over a period of time despite significant fluctuations in grants paid. The issue is the extent to which smoothing is applied to contributions. Total contributions paid over the seven year period are approximately the same for each of the multiplier options. For example, over 7 years with a 1 times multiplier the total amount payable is £1,954 with little smoothing whereas with a 2 times multiplier volatility is removed and the total amount payable is hardly affected at £1,920.

Relationship between the reserve and contribution setting

142. Maintenance of the reserve is one consideration which must be taken into account when setting the annual contribution. Further items included in calculation of contributions are:

- analysis of the economic climate
- the estimated value of claims looking forward over a 3 year period
- estimated transfers from statutory trust accounts
- interest received
- recharges against the Compensation Fund

Conclusion 27

The recommendation of the Working party is to maintain the Compensation Fund reserve at a minimum of twice the average annual value of claims over the previous 7 years plus the estimated value of three months recharges.

RECHARGING AGAINST THE COMPENSATION FUND

143. The practice of recharging certain regulatory costs to the Compensation Fund, as permitted by section 36A of the Solicitors Act 1974, has been reviewed by the Working Party. Ultimate responsibility for setting the Compensation Fund contribution currently sits with Council. The Working Party's recommended policy is to recharge to the Compensation Fund only those costs which directly relate to its administration.

144. For many years, the Law Society's policy has been that a percentage of the operational costs of delivering regulation should be recharged to the Compensation Fund. There is a monthly transfer from the Compensation Fund into the operating accounts which is based upon a percentage of the costs incurred by business functions during the period. Examples of recharges which do not relate specifically to administration of the fund are shown below.

Description	Basis of recharge
Interventions Team	34%
Cost Recovery Team	54%
Forensic Investigation	70%
Fraud Intelligence	60%
Legal Fees - Intervention	100%
Investigation Casework Team	45%
Statutory trusts distribution	60%

145. When considering annual Compensation Fund contribution setting comments have frequently been made in Council about the level of contributions set and the recharges made for administration of the fund.

In particular:

"The cost of the Compensation Fund contribution is too high"

"The costs charged to the Compensation Fund are disproportionate to the sums paid in grants"

146. Internal audit, when reviewing the recharges in 2006, raised concerns about the subjectivity of recharging the cost of functions for which the impact upon the Compensation Fund cannot be measured. They accepted that there was provision within the Act for making recharges but recommended that a review should be undertaken.

147. In carrying out the initial review of recharging in 2007 the Working Party agreed with the views expressed from Council and recommended that only those costs directly attributable to administration of the fund should be recharged.

148. Using the current policy, estimated recharges against the Compensation Fund in 2009 will be approximately £14.9 million of which £2.3 million relates to the direct cost of Compensation Fund administration. All other recharges relate to either interventions or a percentage of the cost for carrying out a range of regulatory functions which may influence reduction of claims against the Fund.

149. Provisions currently exist in Section 36A of the Solicitors Act for these recharges to be made. The Legal Services Act 2007 extends the provisions to include the full costs of interventions.

The relevant subsections of the 2007 Act are:

36A Compensation funds:

(8) A compensation fund may be applied by the Society for the purposes mentioned in subsection (9) (in addition to the making of grants in respect of compensation claims).

(9) The purposes are:

(a) payment of premiums on insurance policies effected under subsection (6);

(b) repayment of money borrowed by the Society for the purposes of the fund and payment of interest on any money so borrowed;

(c) payment of any other costs, charges or expenses incurred by the Society in establishing, maintaining, protecting administering or applying the fund;

(d) payment of any costs, charges or expenses incurred by the Society in exercising its powers under Part 2 of Schedule 1;[1]

(e) payment of any costs or damages incurred by the Society, its employees or agents as a result of proceedings against it or them for any act or omission of its or theirs in good faith and in the exercise or purported exercise of such powers.

Recharging principles

150. The Working Party has agreed principles which it believes should be applied when considering the appropriate level of recharges.

These are that:

- recharges against the Compensation Fund should only be made for those activities which can directly be attributed to its operation and protection;
- the cost of regulatory functions which do not exist primarily to protect the Compensation Fund should be funded by the profession as a whole rather than from targeted contributions from those who hold clients' money.

151. In establishing the principles the primary concerns were that:

- no clear evidence exists to demonstrate what percentage of the wider functions of regulation reduce calls upon the Compensation Fund;
- none of the wider functions of regulation currently recharged to the fund would cease or be reduced if the Compensation Fund did not exist.

[1] Part 2 of Schedule 1 of the Solicitors Act 1974 provides intervention powers.

For example:

- Sixty percent of the cost of the Fraud Intelligence Team is currently recharged to the Compensation Fund. Analysis of risk indicators has shown that only a very small percentage of initial intelligence gathered and processed by the SRA will lead to reduced cost to the Compensation Fund. A precise value cannot be applied to this.

- Seventy percent of the cost of the Forensic Investigations Unit is currently charged to the Compensation Fund. Such investigations can lead to some form of action but only a very small percentage lead to interventions resulting in claims. There is no precise measure for this.

152. Both these functions are used by the SRA to regulate, and both would operate if the Compensation Fund did not exist. There is no method by which to accurately determine how much of the cost of these functions should be charged to the Compensation Fund. If there was this would be likely to change annually adding complexity to the financial planning process.

Recharging the cost of Compensation Fund administration - recommended policy

153. Applying the principles stated in paragraph 150 the Working party recommends that the policy should be to recharge to the Compensation Fund only the costs of its administration. The Compensation Fund exists to protect clients from loss and it is therefore entirely appropriate that the direct costs of maintaining it are borne by solicitors who hold client money.

154. The effect of this would be to reduce the recharge against the fund from £14.9 million to £2.3 million. This would substantially reduce the annual cost of the full individual contribution to the Compensation Fund. The difference, £12.6 million, would need to be collected from the practising certificate (PC) fee. The impact of this is shown in paragraphs 161 to 163 of this report.

155. By applying the Working Party's policy recommendation the Council will be responding positively to the concerns highlighted in paragraph 145 which have in the past been raised at its meetings. This will also remove the issue of subjectivity outlined in paragraph 146 which has been raised by the Society's Auditors in relation to how much is recharged against wider regulation functions.

Recharging for administration and intervention costs – not recommended

156. An alternative approach would be to recharge the direct costs plus those costs which are clearly supported by statute and can be accurately accounted for. The Legal Services Act makes provision for all intervention costs to be recharged to the Compensation Fund. Previously recharges could only be made where interventions were carried out on grounds of dishonesty.

157. The effect of this would be to reduce the recharge against the fund from £14.9 million to £6.5 million. This would be reflected in a reduction in the annual cost of the full individual contribution to the Compensation Fund. The difference, £8.4 million, would need to be collected from the PC fee. The impact of this is shown in paragraphs 161

to 163 of this report.

158. The Working Party spent some time trying to identify a suitable alternative to the recommended policy. This option is presented because it represents the middle ground in terms of financial adjustments and it is possible to reconcile intervention costs in the accounts; but the logic of its inclusion in relation to protection of the Compensation Fund is flawed. Intervention does not, in many cases lead to a call upon the Compensation Fund. In 2008 45% of interventions have been on grounds of dishonesty (37% in 2007), not all interventions on grounds of dishonesty lead to claims, and the number and value of claims made in relation to interventions on other grounds are relatively low.

Maintaining the existing policy position – not recommended

159. It would be possible to maintain the existing level of recharges against the Compensation Fund.

Possible grounds for this could be that:

- it is considered appropriate to target the wider cost of regulation at solicitors who hold client money.
- it is beneficial to recharge the cost of a wider range of regulation functions to the Compensation Fund to avoid increasing the PC fee.

160. The Working Party does not support this option because it does not comply with either of the recharging principles. Additionally this would make no progress towards responding to concerns which have previously been raised by Council or mitigate the concerns of the Law Society's auditors.

Financial impact

161. The recharge to the Compensation Fund contains the costs of operating a significant percentage of the SRA. Any reduction in recharges to the Compensation Fund will need to be reflected by an increase in the practising certificate fee. Currently statistics show that the equivalent of approximately 52,000 full Compensation Fund contributions and the equivalent of approximately 103,000 full practising certificate fees are paid in the year. This means that for every reduction in Compensation Fund contribution of £1 the Practising Certificate fee will increase by 51 pence.

Table 1: Allocation of Compensation Fund (CF) contributions and of Practising Certificate (PC) fees resulting from the recommended policy and alternative options in this paper.

	Recharging criteria	Individual Full CF Contribution	Increase in Individual Full PC fee
Recommended policy	**Direct costs of CF administration only**	**£43**	**£122**
Alternative policy option	Direct costs + interventions	£125	£81
Current policy	Maintain existing recharge	£260	£0

162. Table 1 shows that by implementing the recommended policy a solicitor who currently pays both the full Compensation Fund contribution and full PC fee will be charged a total of £165. This is a reduction of £95 from the £260 Compensation Fund contribution paid under current application of recharges. By transferring costs to the PC fee, the wider cost of regulation has been shared across a larger group than those who contribute to the Compensation Fund.

163. Table 1 also shows that by continuing to apply current recharging policy the impact upon individual Compensation Fund contributions is substantial before any consideration is given to the amount of grants which might be paid during a practising year. It is this inflation of contributions through recharges which often leads to contentious debate when contributions are set annually. In making its recommendation the SRA Board's intention is to make the methodology underpinning contribution setting both transparent and supportable.

Conclusion 28

The recommendation of the Working Party is to make recharges against the Compensation Fund only for the direct costs of its administration. The wider costs of regulation should be funded from practising certificate income.

Using stop loss insurance to protect the fund

164. Marsh have given advice on the suitability and cost of purchasing catastrophe cover for the Compensation Fund. They have provided a guide to what might be achievable based upon limited information available. A brief description of the analysis from Marsh is attached at **Annex H**.

165. The advice from Marsh was that the terms available would not be attractive and the benefits would be limited. Marsh's assessment was that the prospect of a viable scheme was poor and currently difficult to justify economically for a scheme which could be effectively funded through contributions. The Working Party does not recommend that this option is explored further.

Chapter 3 – Operational Management

INTRODUCTION

Claims management structure

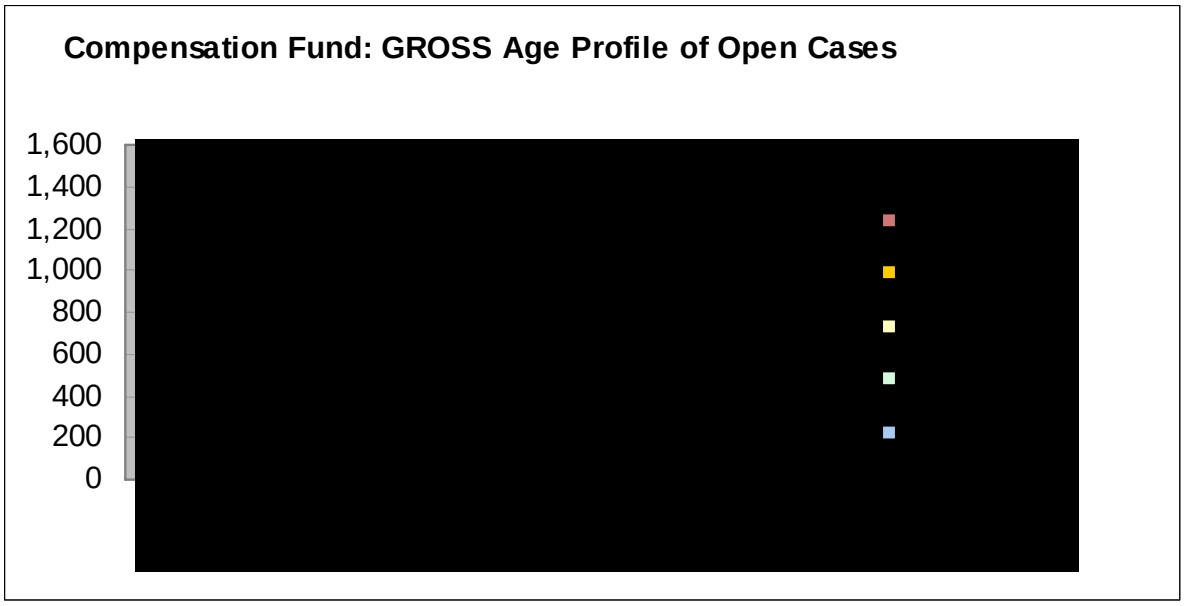
166. Prior to 2008, applications to the Compensation Fund and under the statutory trusts process were handled independently within the SRA. All client financial protection was brought together into a single Client Protection Directorate. This enabled a process of restructuring to be undertaken contemporaneously with this review. The aim was to integrate the two strands into one process thereby increasing the overall efficiency and effectiveness of claims handling. The new Claims Management Unit will be the single point of entry for applications for redress and its remit is to ensure that clients receive funds, by way of a grant from the Compensation Fund or by access to funds held on trust to which they have beneficial entitlement, in the shortest possible time frame.

167. To ensure timely redress, existing working processes and job roles have been revised; the multi-layered and multi-skilled structure comprises a mix of Level 1 Claims Investigators (new entrants covering the more straightforward and simple matters) and Level 2 Claims Investigators (more experienced caseworkers dealing with the moderate and complex matters). The Claims Management business unit also includes the Directorate Support Unit, a multi-skilled team providing administration, financial and secretarial support to all units within the Client Protection Directorate.

Claims management process and performance measurement

168. The new structure allows experienced investigators to focus on more complex and aged matters that require greater technical expertise and time to progress. Whilst the receipt of new matters has not changed significantly, the age profile information shown in the **Chart 1** demonstrates claims are progressing faster than previously seen and that the majority of work in progress is less than 6 months old.

Chart 1



169. It is the responsibility of Team Managers to ensure that there are robust resource planning and risk management processes in place and that interventions are allocated at an early stage. Background information for each intervention is collated in advance of claims being received into the unit and enables Team Managers to predict resource requirements for progressing matters expeditiously once received. A new "Early Warning System" is currently being developed (project manager appointed December 2008), with a view to bringing together information from all areas of the business in one place to further support Team Managers in their resource planning going forward.

170. Claims Advisors undertake pre and post investigation assessments and provide feedback on individual development needs and review the technical aspects of the work undertaken by the Claims Investigators. Additionally, the Claims Advisors are on hand to provide guidance throughout the investigation process to the team.

171. To ensure a fair distribution of work and to provide the basis for individual and team performance management, a work-study programme has been undertaken and its recommendations have been implemented.

172. Complexity weightings are applied to files and allocated to Investigators who have capacity. As well as providing a throughput target, the system promotes development by affording a degree of flexibility for the Claims Investigators by allowing them some freedom to specialise or vary the type of investigation undertaken.

173. Regular management information is produced and reported to stakeholders.

Conclusion 29

The Working Party are pleased to note the progress that has been made and will continue to monitor the operational performance of the Claims Management Unit.

Chapter 4 – Provision of information to stakeholders

174. The Working Party has given initial consideration to the way in which information about the Compensation Fund is communicated to stake holders. Draft 'frequently asked questions and answers' aimed at potential applicants were reviewed but are yet to be finalised. The restructuring of the Claims Management Unit involved a fundamental review of the claims handling process which may affect the information to be provided to applicants. The Working Party noted that the SRA website had been relaunched and suggested that the Compensation Fund should have its own home page or separate site (as does the Financial Services Compensation Scheme). In either case a site index with hyperlinks was necessary.

175. The Working Party also identified the need to review the way in which the Compensation Fund reports to its stakeholders but has not undertaken this task to date.

Conclusion 30

The completion of the review of the provision of information to stakeholders is a future action point.

Chapter 5 – Benchmarking

INTRODUCTION

176. As part of its review the Working Party has undertaken a comparison of the Compensation Fund based on information from a variety of sources. In 2006 the International Bar Association ('IBA') carried out a comprehensive survey of client compensation arrangements in member jurisdictions which the Working Party felt was sufficient for its purposes. A copy of that survey is attached as **Annex I**. In addition a limited survey has been carried out as part of this review to check the up to date position (see **Annex J**). The IBA survey report suggests various standards for client compensation schemes based on the standards set by the American National Client Protection Organisation ('ANCPO').

177. The Working Party considered the ANCPO's aspirational criteria produced to assist jurisdictions in evaluating their own compensation arrangements' performance. A copy of the standards is attached as **Annex K**. ANCPO identify four fundamental building blocks for any fund striving for excellence:

    (1) An organisational structure that secures the Fund's independence;
    (2) Steady, secure and adequate funding;
    (3) Accessibility; and
    (4) Responsiveness to the need.

ASSESSMENT AGAINST ASPIRATIONAL CRITERIA

178. A summary of the aspirational criteria with commentary relating to the Compensation Fund is attached as **Annex L**. The Working Party concluded that, with a few exceptions, the Fund meets or exceeds the aspirational criteria.

179. The key areas where the Fund may not, either now or in future, meet the aspirational criteria are as follows:

ANCPO 1.3 **The Fund shall constitute a trust separate and independent from any other fund or entity of the Court, bar association, law society or government agency.**

The trust is vested in the Society. Clearly this does not effect the separation that ANCPO propose.

ANCPO 2.4 **The [funding] assessment should not be halted, suspended, or reduced because the Fund has a positive balance. To the contrary, a substantial reserve should be sought, as interest income will help the Fund meet the need in times of large or numerous claims.**

Whilst contributions have in the past varied markedly from year to year, an annual contribution of some sort has always been collected. The recommendation is that a substantial reserve should be maintained. Whilst this has been true in the past, there is pressure to reduce the reserve.

ANCPO 3.2 **The Fund should issue and publish an annual report. Quarterly or semi-annual news releases should be done as well, even in the absence of high volume activity.**

The Fund does not produce a stand alone report but it is included in the Law Society's annual report and accounts. This will be looked at as part of the review of the way information is disseminated to stakeholders.

ANCPO 4.2 **Limitations on the payment of awards – whether per claim, per claimant, per year or in the aggregate against any one lawyer – are not to be favoured. Every opportunity should be sought to eliminate such limitations on the Trustees' discretion to pay awards.**

There is no limit as to the amount that may be paid out as against any solicitor or claimant as the Fund deals with applications, on a claim by claim basis, with a limit of £2 million per claim but extendable in exceptional cases.

Conclusion 31

As part of its review the Working Party has compared the Fund with other jurisdictions' funds and has concluded from the information available that the Fund, combined with professional indemnity and the Statutory Trust Account process, provides equal, if not superior, protection.

The Working Party has also considered aspirational criteria produced by the American National Client Protection Organisation (ANCPO) to assist jurisdictions in evaluating their own compensation arrangements' performance. The principal areas where the Fund does not meet the aspirational criteria relate to governance and the dissemination of information to stake holders.

Chapter 6 – Compensation Fund Governance

INTRODUCTION

180. Until 31 March 2009 the key provisions relating to the Compensation Fund were to be found in section 36 and schedule 2 of the Solicitors Act 1974 ("the Act"). Paragraphs 1 and 3 of Schedule 2 refers to the trust status of the Fund as follows:

> ***1. The fund shall be maintained and administered by the Society and shall be held by the Society on trust for the purposes provided for in section 36 and this Schedule.***
>
> ***3. The Society may invest in securities in which the trustees are authorised by law to invest trust funds in their hands any money which forms part of the fund.***

181. The important point to note is that it was the corporate Law Society that held the fund on trust and it was the corporate Law Society (rather than the Council or the Council members) that was the trustee. The Council was empowered to act on behalf of the Society in maintaining and administering the Fund by virtue of section 80 of the Act, and could delegate its functions in accordance with section 79.

182. With effect from 31 March 2009 section 36 and schedule 2 were replaced by new sections 36 and 36A. The new sections are enabling provisions which give the Society the power to make rules relating to all aspects of the Compensation Fund. New Compensation Fund Rules came into force on the same day. The equivalent provision is to be found in subsections (1) and (5) of schedule 36A as follows:

> ***(1) Compensation Rules may require or authorise the Society to establish or maintain a fund or funds ("compensation funds") for the purpose of making grants in respect of compensation claims.***
>
> ***(5) The Society may invest any money which forms part of a compensation fund in any investments in which trustees may invest under the general power of investment in section 3 of the Trustee Act 2000 (as restricted by sections 4 and 5 of that Act).***

183. Although there is no mention of the fund being held by the Society ***'***on trust', the power to invest the fund is equivalent to that trustees have under the Trustee Act 2000. Sections 79 and 80 of the Act have also been amended with effect from 31 March 2009. The amended section 79 provides:

> ***(1) The Council may arrange for any function of the Council…..to be exercised by -.***
>
> ***(a) a committee of the Council,***
> ***(b) a sub-committee of such a committee,***
> ***(c) a body corporate which is established for the purpose of providing services to the Council (or to a committee of the Council) and is a wholly owned subsidiary of the Society, or***
> ***(d) an individual (whether or not a member of the Society's staff).***

184. In this context the SRA Board is '***a committee of the Council***' and the Financial Protection Committee is '***a sub-committee of such a committee***'. Subsection (2)

enables the SRA Board to arrange for the discharge of a delegated function by one of its committees or by an individual.

(2) Where by virtue of subsection (1) any function may be discharged by a committee, the committee may arrange for the discharge of the function by -.

(a) a sub-committee of that committee,
(b) a body corporate which is established for the purpose of providing services to the Council (or to a committee of the Council) and is a wholly owned subsidiary of the Society, or
(c) an individual (whether or not a member of the Society's staff).

185. A committee of the SRA Board may also include or consist of individuals other than members of the SRA Board (subsection (10)).

DELEGATION

186. The powers of the Council delegated to the SRA Board are set out in the General Regulations 2008. The main terms of reference of the Solicitors Regulation Authority Board relating to the Compensation Fund are -

(11) Subject to (15), to make Compensation Fund Rules and to deal with all other matters relating to the Compensation Fund, including the financial management of that Fund.

(12) To deal with all matters relating to monies held on statutory trust following intervention, including the authorisation of the transfer of funds held on statutory trust to the Compensation Fund subject to rights of subrogation.

(14) Subject to (11) and (15), to exercise the powers of the Society and of the Council under all primary and secondary legislation on all matters within its terms of reference.

(15) To set and amend from time to time the level of fees and charges payable by any person or body in relation to the discharge of its functions, with the exception of setting annual contributions and any special levy payable to the Compensation Fund under paragraph 2 of Schedule 2 to the Act.

(16) To set, implement and review policy on matters within its terms of reference.

187. In turn the SRA Board has delegated certain responsibilities for the Compensation Fund to its Financial Protection Committee as follows:

a) To advise the Board of the Solicitors Regulation Authority (SRA) on all policy, technical and operational matters relating to the Compensation Fund ……..

c) To advise the Board of the SRA on all policy, technical and operational matters relating to the …… Solicitors' Compensation Fund Rules.

d) To advise the Board of the SRA on the setting of Compensation Fund contributions.

188. At its meeting on 26 February 2009 the SRA Board agreed to the delegation of responsibility for the investment strategy relating to the Compensation Fund and

Statutory Trust Accounts to the Law Society's Investment Committee subject to confirmation that such a delegation was possible and subject both to the Financial Protection Committee being represented on the Investment Committee and being able to set parameters with regard to, for example, liquidity requirements. The Financial Protection Committee was authorised to satisfy itself as to how the latter requirements might best be achieved.

189. The membership of the Investment Committee is currently, the Chief Executive, the Group Finance Director and the Chief Executive, SRA. The Working Party does not consider that a body consisting of two senior staff members of the representative body and one senior staff member of the SRA can properly be regarded as a committee of the SRA Board. Even if as a matter of constitutional practice it is, the Working Party does not regard its membership as appropriate. It should include members of the SRA Board and/or the Financial Protection Committee. Further the interests of the SRA should not be in the minority (as they are in the body as it is currently composed).

190. To summarise the position as from 31 March 2009:

Function	Responsibility	Delegation
1 Making the Compensation Fund Rules, subject to concurrence.	SRA Board	Advising the SRA Board delegated to Financial Protection Committee
2 Compensation Fund Policy	SRA Board	Advising the SRA Board delegated to Financial Protection Committee
3 Management and administration of the Compensation Fund	SRA Board	Advising the SRA Board delegated to Financial Protection Committee
4 Setting of Compensation Fund contributions	Council	Advising the Council delegated to the SRA Board, and by the Board to the Financial Protection Committee
5 Compensation Fund investment strategy	SRA Board / Law Society Investment Committee	Delegation to Law Society's Investment Committee (subject to confirmation that this is possible)

Conclusion 32

The Working Party concluded that the governance arrangements up until 31 March 2009 were unacceptable as the SRA had responsibility without power and the Society as trustee had power without responsibility. The position has improved since 31 March 2009 because now the SRA Board has clear responsibility for some aspects of the Compensation Fund. The notable exceptions are responsibility for setting contributions (which has been retained by the Council) and investment strategy (which the Board had agreed to delegate to a Law Society Committee). The Working Party recommends that the SRA Board reverse the delegation to the Law Society's Investment Committee. The Working Party is of the view that ultimate responsibility for all aspects of the Compensation Fund should be at arms length from the representative body and should be vested in the SRA Board. This would go some way to addressing the requirements of ANCPO 1.3 and 2.4 as set out paragraph 179.

Chapter 7 – Alternatives to the current Compensation Fund

INTRODUCTION

191. As the Committee was charged with undertaking a fundamental review of the Compensation Fund one of the tasks for the review was ***"to identify and assess alternative ways of providing the protection currently afforded by the Compensation Fund"***. This is not on the basis that the Compensation Fund needs to be replaced but rather that it is appropriate as part of any fundamental review.

192. One of the concerns raised by sole practitioners in the past has been the difference in the protection afforded by the Compensation Fund and the compulsory professional indemnity scheme in respect of claims arising from a principal's dishonesty. In 1990/1, consideration was given to the merger of the Compensation Fund with the Solicitors Indemnity Fund (SIF). The aim was to remove anomalies between the cover offered by the two funds in particular, claims met by SIF where there was an honest partner who qualified for indemnity and those claims met by the Compensation Fund where a sole practitioner was dishonest or, in the case of a partnership, all partners were dishonest. The review considered the differences between the funds, the method of finance and nature of claims that may be paid. The pros and cons were reviewed including the need to seek a change to the Solicitors Act 1974 to enable a merger. It was determined not to proceed with this.

193. The Working Party considered the following options:

- Surety bonds or capital adequacy requirements
- Insurance - either free standing or by extending the Minimum Terms and Conditions (MTC) of professional indemnity insurance for solicitors to cover all dishonesty by removing the dishonest exclusion.
- Centralised banking of client money
- Aligning the Compensation Fund to the MTC.

POSSIBLE ALTERNATIVES TO THE COMPENSATION FUND

Surety bonds

194. At present there is no statutory authority to require the profession to take out bonds to ensure client protection. There would need to be an extension of section 37 Solicitors Act 1974 (the indemnity section) or the introduction of other legislation in place. To achieve this, the Legal Services Board would first need to be convinced that such a move was in the interests of consumers or at the very least not going to adversely affect their interests.

195. Bonds are generally backed by insurance. There is therefore a risk that, as with extending the MTC to include all dishonesty, an insurer might refuse to renew cover where the risk is deemed to be unacceptable, perhaps due to a substantial claim having been paid out. To maintain public protection there would need to be a mechanism to deal with the situation of where a claim arises against a firm that is found not to have a current surety bond or sufficient capital adequacy. This could mean that it would still be necessary to maintain a Compensation Fund to deal with claims in such circumstances.

196. The administration and maintenance of a bond may also present problems. It is likely the amount of a bond will be linked to the nature and value of work undertaken by a firm. If the work changes to a higher risk area or values increase the value of the bond may become inadequate and could create a similar situation as referred to above where a financial protection fallback position is necessary.

197. It would be necessary to consider what type and size of practice would need to be bonded or to demonstrate capital adequacy. Claims on the Compensation Fund rarely involve firms with more than three principals, so it would make sense to limit the requirements to small firms. However, sole practitioners and smaller firms may struggle to afford the premiums or may not have the required assets available. Premiums are likely to be high and certainly more than current contributions to the Compensation Fund, making it restrictive.

198. An approach was made to Marsh to explore the potential of surety bonds both in terms of adequacy of cover and the cost to the individual firms in order to draw a comparison with the cover and associated cost of cover currently afforded by the Compensation Fund. Their response was as follows:

> ***"Unfortunately, I cannot get any interest from the surety market for this. Underwriters believe the requirement you have requested would be classified as a financial guarantee (which is restricted under their reinsurance treaties) and they also don't like the fact they would be looking to bond only small firms (of up to 3 partners). Neither of these issues make this an attractive proposition."***

Insurance

199. Removing the dishonesty exclusion from the MTC would have the effect of bringing within the compulsory professional indemnity scheme all claims involving dishonesty arising from private practice. This is likely to be fiercely resisted by insurers due to the moral hazard and it would make it harder for small firms to obtain Qualifying Insurance outside the Assigned Risks Pool.

200. As an alternative to extending the MTC fidelity insurance could be sought for the benefit of clients to provide cover for the claims currently dealt with by the Compensation Fund. However it is unlikely that this type of insurance would be attractive to insurers. Even if it was, the insurer may refuse further cover if the risk is considered to be too onerous or it has been caught by major claims. Whether this could be achieved by extending cover under existing insurance arrangements or by way of a separate policy may be considered to be academic in terms of the potential to refuse cover.

201. If insurers were willing to provide cover under the MTC for all dishonesty then one of the key issues would be the cost to the profession. Premiums would be likely to rise dramatically for some firms which could spell financial disaster for sole practitioners and the smaller firm. Initial views from Ray Brown at Marsh were as follows:

> ***"We confirm in the past we have briefly considered the likelihood of extending the Minimum Terms and Conditions for PI cover to include dishonesty of sole practitioners but concluded it would be impractical to do so without inhibiting the ability of sole practitioners to obtain PI cover.***
>
> ***As you know, for other firms dishonesty cover is provided subject to the existence of innocent partners.***

In addition, consideration was given to a requirement that sole practitioners (or firms) take out some other form of dishonesty insurance such as Fidelity or Surety and again it was concluded this was not possible to mandate with any prospect of universal success.

My own view is that the Compensation Fund is the most appropriate vehicle to provide this particular client protection. At this moment in time commercial insurers would not be receptive to providing additional dishonesty cover for firms where there was no robust infrastructure and supervision around the handling of client funds and the feeling that activity in this area is of considerable concern."

202. The ability of the Compensation Fund to react quickly has many benefits to the public and profession. First, the client suffers little or no disruption, second, the loss is contained saving thousands of pounds in interest and costs and third, perhaps most importantly, it is instrumental in maintaining / restoring faith in the profession.

203. It has been suggested that the Compensation Fund be retained simply to make emergency payments which could be reclaimed from insurers. However that could be quite problematical as the Compensation Fund makes the payments reliant on the intervention agent's view that a claim would fall within the ambit of the Compensation Fund and that all necessary evidence is present. At that stage the Compensation Fund has not made any investigation itself. It may be much more difficult to persuade an insurer and therefore some risk exists as to whether the Compensation Fund will be able to recover the payment.

Centralised banking

204. A further alternative might be to operate central banking on behalf of the profession. The client funds of all firms would be held centrally by the SRA (or other regulator?). However, it is unlikely the profession would warm to such an idea as the practical difficulties for them and indeed the financial administrators are likely to be many. Any such proposals go beyond boundaries of this review.

205. In France client moneys are held in a centralised fund called the Carpa with lawyers having access through the banking system. The system has provided security for lawyers and their clients and the scheme is backed by insurance. However, it should be noted that French avocats are not involved in the transfer of real estate so the volume and scale of transactions will be much smaller than in England and Wales.

206. Any move towards centralised banking would involve significant changes to the way firms have operated to date and nature and scale of the problems being addressed do not warrant such a radical solution if, indeed, it is a solution. It would not work as an effective way of preventing the theft of client money unless the centralised bank made detailed enquiries into every transaction.

Aligning the Compensation Fund to the MTC

207. Aligning the Compensation Fund with the MTC would undoubtedly increase the cost of running the Fund. Although a detailed study has not been undertaken, any increase to the cost would probably be in the areas of special damages, consequential loss and legal costs with claims being paid on a full indemnity basis including interest at judgment rates, rather than increases due to a change in value of paid capital losses. The reason for this is that, in relation to the type of capital losses which fall within the ambit of the Compensation Fund, if the loss is proven, it would usually result in a grant

being paid in the full amount. Having said that, it is within present discretion to reduce or refuse grants, but the instances of that happening are quite rare.

208. The discretion to reduce / reject tends to occur mainly in relation to claims based on investment fraud where the applicant is himself the author of his own misfortune. An insurer might argue contributory negligence so there may not, in real terms, be very much difference, if any, to the outcome of this scenario if the Compensation Fund and MTC were to be aligned.

209. As stated above, the probable increase in cost is likely to be in relation to the additional or consequential losses. If the Compensation Fund dealt with these in similar manner to an insurer, without its discretion, these claims are likely to be paid. Legal costs may be argued but going to taxation will mean additional cost and could be deemed disproportionate in certain cases resulting in an increase in payments under this head.

210. Difficulties may arise in the early stages in forecasting possible levels of claim payments which would affect contribution setting. This position is likely to change after the first year or so through emerging trends.

211. The Compensation Fund would be likely to see a dramatic change in the nature and value of such claims including for example, loss of earnings and other losses generally dealt with by insurers and currently outside the Compensation Fund's remit. The outcome of a MTC aligned Compensation Fund is likely to mean additional cost, not just in terms of payments from the Fund but also in terms of administrative costs, additional staffing needed to undertake what is likely to be an increased case load and other knock on costs which would have to be passed on to the profession which would necessitate an increase in contributions.

212. There are a number of disadvantages to adopting the MTC approach. The most obvious is the additional cost to the profession. This could mean a significant increase in the contributions which may prove to be detrimental to certain of the profession and thus meet with resistance. The SRA would have no discretion as to what may be paid / refused. Values of claims are likely to increase, particularly in respect of costs as the Compensation Fund would no longer be able to invoke its guidelines. This in turn would result in an increase in grants. The scope of claims would increase with new heads of claim being admitted for example, distress and inconvenience again leading to more payments.

213. On the positive side, the Compensation Fund would be more transparent with applicants having a clearer idea of what they should expect from it, particularly with discretion removed. Any gaps between the Compensation Fund and insurance disappear.

Conclusion 33

From the perspective of clients, aligning the Compensation Fund to the Minimum Terms and Conditions would eliminate most, if not all, of the gaps in client protection. Before any such change could be properly considered, empirical research would be needed to determine the likely cost implications of the change and on that basis an informed decision could be made. The Working Party recommends that this research is carried out.

CONCLUSION

Conclusion 34

Leaving aside the aligning of the Compensation Fund and the MTC, the Working Party concluded that whilst the Compensation Fund could be improved, it had served the public and profession very well and represented the best of the currently available options. The other alternatives were unviable and/or expensive and would involve major changes and risks that would be out of proportion to the problems to be addressed.

Chapter 8 – Equality and diversity

214. The Working party noted that in accordance with the SRA's Equality and Diversity Strategy a full range of Equality Impact Assessments were being carried out on the Compensation Fund and these were due to be completed by the end of June 2009.

Chapter 9 – Future action points

215. The scale of the review was such that inevitably some work remains outstanding and new areas for action have emerged during the course of the review. The key future action points are as follows:

- Complete the review of the provision of information to stakeholders
- Review the new Compensation Fund Rules to assess whether further changes are desirable in the public interest
- Consider how the protection afforded by the three schemes (including the Compensation Fund) will be adapted to accommodate the proposed alternative business structures (ABSs)
- Keep the levels of cover under periodic review
- Investigate the cost and practicality of aligning the Compensation Fund rules with the MTC
- Complete the Equality Impact Assessments of the Compensation Fund

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Date: April 2009

THE THREE SCHEMES - AN OVERVIEW

Professional Indemnity Insurance

The key provisions are:

- Compulsory minimum cover of £2 million (or £3 million) for all civil liability arising from private legal practice. In addition, defence costs are covered without financial limit;
- Unpaid inadequate professional service awards, and unpaid claims falling within the excess, are included in the cover;
- The Minimum Terms and Conditions override inconsistent policy terms;
- Dishonesty cover is provided to innocent principals, but not to any individual dishonest principal or employee of the firm. If all the principals of the firm have been dishonest then the claim falls to be dealt with by the Compensation Fund;
- If a firm ceases without successor practice then the policy is automatically extended by 6 years to provide run-off cover;
- Qualifying Insurers are prohibited from avoiding or repudiating the insurance on any ground including non-disclosure, misrepresentation and failure to pay premium;
- There are only limited permitted exclusions relating to matters unconnected with the work of private practice, such as employment, partnership disputes, or trading debts.

The Compensation Fund

The key provisions are:

- grants can be made of up to £1m to replace money which has either been stolen by a solicitor, or to alleviate hardship or loss suffered by applicants where the solicitor has failed to account for client money in their possession;
- grants may also be made to a solicitor who has suffered loss because of liability to clients as a result of default of his partner or employee;
- a loan can be made
- grants can include an applicant's new solicitor's costs of carrying out work which the original solicitor failed to do, and the legal costs of making the application to the Compensation Fund;
- an application may fail if it is made outside the time limit of 6 months or if the applicant does not prove the claim;

- a grant may be limited or refused if fault on the part of the applicant is found;

- a sum in lieu of interest can be paid.

Statutory Trust Accounts

Some of the fundamental principles of the process are set out here:

- In cases where the intervention agent appointed by the SRA is unable to return the funds to their beneficial owners, or is instructed not to do so because of insufficient monies to allow for payment of full entitlement, the funds are transferred to the Society (on behalf of the SRA) to hold in trust;

- The SRA attempts to identify who has beneficial entitlement to the funds (which includes the Compensation Fund under its rights of subrogation). It makes contact with the beneficiaries with an invitation to claim, and distributes the funds accordingly. Distribution is decided through an adjudication process;

- Distribution may only be a proportion of what the beneficiaries are entitled to due to a shortfall client account;

- The evidence to support a distribution need not be conclusive for a distribution to be made and the SRA is proactive, rather than reactive, in that it seeks out and invites claims from potential beneficiaries;

- In contrast to indemnity and the Compensation Fund, the funds are client monies held in trust, and not third party funds. Distribution involves only the funds held plus interest, and does not take account of any other losses suffered;

- Interest is paid upon monies held;

- No time limit applies.

Solicitors Regulation Authority

Minimum Terms and Conditions of Professional Indemnity Insurance for Solicitors Registered In England and Wales

2008

Contents

Minimum Terms and Conditions of Professional Indemnity Insurance for Solicitors and Registered European Lawyers in England and Wales

1 Scope of cover

1.1 Civil liability

The insurance must indemnify each Insured against civil liability to the extent that it arises from Private Legal Practice in connection with the Firm's Practice, provided that a Claim in respect of such liability:

(a) is first made against an Insured during the Period of Insurance; or

(b) is made against an Insured during or after the Period of Insurance and arising from Circumstances first notified to the Insurer during the Period of Insurance.

1.2 Defence Costs

The insurance must also indemnify the Insured against Defence Costs in relation to:

(a) any Claim referred to in clause 1.1, 1.4 or 1.6; or

(b) any Circumstances first notified to the Insurer during the Period of Insurance; or

(c) any investigation, inquiry or disciplinary proceeding during or after the Period of Insurance arising from any Claim referred to in clause 1.1, 1.4 or 1.6 or from Circumstances first notified to the Insurer during the Period of Insurance.

1.3 The Insured

For the purposes of the cover contemplated by clause 1.1, the Insured must include:

(a) the Firm; and

(b) each service, administration, trustee or nominee company owned as at the date of occurrence of relevant Circumstances by the Firm and/or the Principals of the Firm; and

(c) each Principal, each former Principal and each person who becomes a Principal during the Period of Insurance of the Firm or a company referred to in paragraph (b); and

(d) each Employee, each former Employee and each person who becomes during the Period of Insurance an Employee of the Firm or a company referred to in paragraph (b); and

(e) the estate or legal personal representative of any deceased or legally incapacitated person referred to in paragraph (c) or (d).

1.4 Prior Practice

The insurance must indemnify each Insured against civil liability to the extent that it arises from Private Legal Practice in connection with a Prior Practice, provided that a Claim in respect of such liability is first made against an Insured:

(a) during the Period of Insurance; or

(b) during or after the Period of Insurance and arising from Circumstances first notified to the Insurer during the Period of Insurance.

1.5 The Insured - Prior Practice

For the purposes of the cover contemplated by clause 1.4, the Insured must include:

(a) each Partnership or Recognised Body which, or sole practitioner who, carried on the Prior Practice; and

(b) each service, administration, trustee or nominee company owned as at the date of occurrence of relevant Circumstances by the Partnership or Recognised Body which, or sole practitioner who, carried on the Prior Practice and/or the Principals of such Partnership or Recognised Body; and

(c) each Principal and former Principal of each Partnership or Recognised Body referred to in paragraph (a) or company referred to in paragraph (b); and

(d) each Employee and former Employee of the Partnership, Recognised Body or sole practitioner referred to in paragraph (a) or company referred to in paragraph (b); and

(e) the estate or legal personal representative of any deceased or legally incapacitated sole practitioner referred to in paragraph (a) or person referred to in paragraph (c) or (d).

1.6 Successor Practice

The insurance must indemnify each Insured against civil liability to the extent that it arises from Private Legal Practice in connection with a Successor Practice to the Firm's Practice (where succession is as a result of one or more separate mergers, acquisitions, absorptions or other transitions), provided that a Claim in respect of such liability is first made against an Insured:

(a) during the Period of Insurance; or

(b) during or after the Period of Insurance and arising from Circumstances first notified to the Insurer during the Period of Insurance.

1.7 The Insured - Successor Practice

For the purposes of the cover contemplated by clause 1.6, the Insured must include:

(a) each Partnership or Recognised Body which, or sole practitioner who, carries on the Successor Practice during the Period of Insurance; and

(b) each service, administration, trustee or nominee company owned as at the date of occurrence of relevant Circumstances by the Partnership or Recognised Body which, or sole practitioner who, carries on the Successor Practice and/or the Principals of such Partnership or Recognised Body; and

(c) each Principal, each former Principal and each person who becomes during the Period of Insurance a Principal of any Partnership or Recognised Body referred to in paragraph (a) or company referred to in paragraph (b); and

(d) each Employee, each former Employee and each person who becomes during the Period of Insurance an Employee of the Partnership, Recognised Body or sole practitioner referred to in paragraph (a) or company referred to in paragraph (b); and

(e) the estate or legal personal representative of any deceased or legally incapacitated sole practitioner referred to in paragraph (a) or person referred to in paragraph (c) or (d).

1.8 Award by regulatory authority

The insurance must indemnify each Insured against any amount paid or payable in accordance with the recommendation of the Legal Services Ombudsman, the Legal Complaints Service or any other regulatory authority to the same extent as it indemnifies the Insured against civil liability.

2 Limit of insurance cover

2.1 Any one Claim

The Sum Insured for any one Claim (exclusive of Defence Costs) must be, where the Firm is a Relevant Recognised Body, at least £3 million, and in all other cases, at least £2 million.

2.2 No limit on Defence Costs

There must be no monetary limit on the cover for Defence Costs.

2.3 Proportionate limit on Defence Costs

Notwithstanding clauses 2.1 and 2.2, the insurance may provide that liability for Defence Costs in relation to a Claim which exceeds the Sum Insured is limited to the proportion that the Sum Insured bears to the total amount paid or payable to dispose of the Claim.

2.4 No other limit

The insurance must not limit liability to any monetary amount (whether by way of an aggregate limit or otherwise) except as contemplated by clauses 2.1 and 2.3.

2.5 One Claim

The insurance may provide that, when considering what may be regarded as one Claim for the purposes of the limits contemplated by clauses 2.1 and 2.3:

(a) all Claims against any one or more Insured arising from:

(i) one act or omission;

(ii) one series of related acts or omissions;

(iii) the same act or omission in a series of related matters or transactions;

(iv) similar acts or omissions in a series of related matters or transactions

and

(b) all Claims against one or more Insured arising from one matter or transaction

will be regarded as one Claim.

2.6 Multiple underwriters

2.6.1 The insurance may be underwritten by more than one insurer, each of which must be a Qualifying Insurer, provided that the insurance may provide that the Insurer shall be severally liable only for its respective proportion of liability in accordance with the terms of the insurance.

2.6.2 Where the insurance is underwritten jointly by more than one insurer:

(a) the insurance must state which Qualifying Insurer shall be the Lead Insurer; and

(b) in addition to any proportionate limit on Defence Costs in accordance with clause 2.3, the insurance may provide that each Insurer's liability for Defence Costs is further limited to the extent or the proportion of that Insurer's liability (if any) in relation to the relevant Claim.

[Note: under clause 2.6 of the Qualifying Insurer's Agreement, a Policy may be issued on an excess of loss basis only in the layers set out in that clause.]

3 Excesses

3.1 The Excess

The insurance may be subject to an Excess of such monetary amount and on such terms as the Insurer and the Firm agree. Subject to clause 3.4, the Excess may be 'self-insured' or partly or wholly insured without regard to these minimum terms and conditions.

3.2 No deductibles

The insurance must provide that the Excess does not reduce the limit of liability contemplated by clause 2.1.

3.3 Excess not to apply to Defence Costs

The Excess must not apply to Defence Costs.

3.4 Funding of the Excess

The insurance must provide that, if an Insured fails to pay to a Claimant any amount which is within the Excess within 30 days of it becoming due for payment, the Claimant may give notice of the Insured's default to the Insurer, whereupon the Insurer is liable to remedy the default on the Insured's behalf. The insurance may provide that any amount paid by the Insurer to remedy such a default erodes the Sum Insured.

3.5 One Claim

The insurance may provide for multiple Claims to be treated as one Claim for the purposes of an Excess contemplated by clause 3.1 on such terms as the Firm and the Insurer agree.

3.6 Excess layers

In the case of insurance written on an excess of loss basis, there shall be no Excess except in relation to the primary layer.

4 Special conditions

4.1 No avoidance or repudiation

The insurance must provide that the Insurer is not entitled to avoid or repudiate the insurance on any grounds whatsoever including, without limitation, non-disclosure or misrepresentation, whether fraudulent or not.

4.2 No adjustment or denial

The insurance must provide that the Insurer is not entitled to reduce or deny its liability under the insurance on any grounds whatsoever including, without limitation, any breach of any term or condition of the insurance, except to the extent that one of the exclusions contemplated by clause 6 applies.

4.3 No cancellation

The insurance must provide that it cannot be cancelled other than if (and with effect from the date upon which):

(a) the Firm's Practice is merged into a Successor Practice, provided that there is insurance complying with these minimum terms and conditions in relation to that Successor Practice; or

(b) replacement insurance complying with these minimum terms and conditions commences, but only where, in the case of insurance not provided wholly or partly by the Assigned Risks Pool, the replacement insurance is not provided wholly or partly by the Assigned Risks Pool.

Cancellation must not affect the rights and obligations of the parties accrued under the insurance prior to the date of cancellation.

4.4 No set-off

The insurance must provide that any amount payable by the Insurer to indemnify an Insured against civil liability to a Claimant will be paid only to the Claimant, or at the Claimant's direction, and that the Insurer is not entitled to set-off against any such amount any payment due to it by any Insured including, without limitation, any payment of premium or to reimburse the Insurer.

4.5 No 'other insurance' provision

The insurance must not provide that the liability of the Insurer is reduced or excluded by reason of the existence or availability of any other insurance other than as contemplated by clause 6.1. For the avoidance of doubt, this requirement is not intended to affect any right of the Insurer to claim contribution from any other insurer which is also liable to indemnify any Insured.

4.6 No retroactive date

The insurance must not exclude or limit the liability of the Insurer in respect of Claims arising from incidents, occurrences, facts, matters, acts and/or omissions which occurred prior to a specified date.

4.7 Successor Practice - 'double insurance'

The insurance may provide that, if the Firm's Practice is succeeded during the Period of Insurance and, as a result, a situation of 'double insurance' exists between two or more insurers of the Successor Practice, contribution between insurers is to be determined in accordance with the relative numbers of Principals of the owners of the constituent Practices immediately prior to succession.

4.8 Advancement of Defence Costs

The insurance must provide that the Insurer will meet Defence Costs as and when they are incurred, including Defence Costs incurred on behalf of an Insured who is alleged to have committed or condoned dishonesty or a fraudulent act or omission, provided that the Insurer is not liable for Defence Costs incurred on behalf of that Insured after the earlier of:

(a) that Insured admitting to the Insurer the commission or condoning of such dishonesty, act or omission; or

(b) a court or other judicial body finding that that Insured was in fact guilty of such dishonesty, act or omission.

4.9 Resolution of disputes

The insurance must provide that, if there is a dispute as to whether a Practice is a Successor Practice for the purposes of clauses 1.4, 1.6 or 5.3, the Insured and the Insurer will take all reasonable steps (including, if appropriate, referring the dispute to arbitration) to resolve the dispute in conjunction with any related dispute between any other party which has insurance complying with these minimum terms and conditions and that party's insurer.

4.10 Conduct of a Claim pending dispute resolution

The insurance must provide that, pending resolution of any coverage dispute and without prejudice to any issue in dispute, the Insurer will, if so directed by the Law Society of England and Wales, conduct any Claim, advance Defence Costs and, if appropriate, compromise and pay the Claim. If the Society is satisfied that:

(a) the party requesting the direction has taken all reasonable steps to resolve the dispute with the other party/ies; and

(b) there is a reasonable prospect that the coverage dispute will be resolved or determined in the Insured's favour; and

(c) it is fair and equitable in all the circumstances for such direction to be given;

it may in its absolute discretion make such a direction.

4.11 Minimum terms and conditions to prevail

The insurance must provide that:

(a) the insurance is to be construed or rectified so as to comply with the requirements of these minimum terms and conditions; and

(b) any provision which is inconsistent with these minimum terms and conditions is to be severed or rectified to comply.

4.12 Period of Insurance

The Period of Insurance must not expire prior to 30 September 2009.

5 Run-off cover

5.1 Cessation of the Firm's Practice

The insurance must provide that, if the Firm's Practice ceases during or on expiry of the Period of Insurance and the Firm has not obtained succeeding insurance in compliance with these minimum terms and conditions (a **Cessation**), the insurance will provide run-off cover.

5.2 Scope of run-off cover

The run-off cover referred to in clause 5.1 must indemnify each Insured in accordance with clauses 1.1 to 1.8 (but subject to the limits, exclusions and conditions of the insurance which are in accordance with these minimum terms and conditions) on the basis that the Period of Insurance extends for an additional six years (ending on the sixth anniversary of the date upon which, but for this requirement, it would have ended).

5.3 Succession

The insurance must provide that run-off cover is not activated if there is a Successor Practice to the ceased Practice, provided that there is insurance complying with these minimum terms and conditions in relation to that Successor Practice.

5.4 Suspended Practices

The insurance must provide that, where run-off cover has been activated in accordance with this clause 5, but where the Firm's Practice restarts, the Insurer may (but shall not be obliged to) cancel such run-off cover, on such terms as may be agreed, provided that:

(a) there is insurance complying with these minimum terms and conditions in relation to that Firm in force on the date of cancellation;

(b) the Qualifying Insurer providing such insurance confirms in writing to the Firm and the Insurer (if different) that:

(i) it is providing insurance complying with these minimum terms and conditions in relation to that Firm for the then current Indemnity Period; and

(ii) it is doing so on the basis that the Firm's Practice is regarded as being a continuation of the Firm's Practice prior to Cessation and that accordingly it is liable for Claims against the Firm arising from incidents, occurrences, facts, matters, acts and/or omissions which occurred prior to Cessation.

6 Exclusions

The insurance must not exclude or limit the liability of the Insurer except to the extent that any Claim or related Defence Costs arise from the matters set out in this clause 6.

6.1 Prior cover

Any Claim in respect of which the Insured is entitled to be indemnified by the Solicitors Indemnity Fund (**SIF**) or under a professional indemnity insurance contract for a period earlier than the Period of Insurance, whether by reason of notification of Circumstances to SIF or under the earlier contract or otherwise.

6.2 Death or bodily injury

Any liability of any Insured for causing or contributing to death or bodily injury, except that the insurance must nonetheless cover liability for psychological injury or emotional distress which arises from a breach of duty in the performance of (or failure to perform) legal work.

6.3 Property damage

Any liability of any Insured for causing or contributing to damage to, or destruction or physical loss of, any property (other than property in the care, custody or control of any Insured in connection with the Firm's Practice and not occupied or used in the course of the Firm's Practice), except that the insurance must nonetheless cover liability for such damage, destruction or loss which arises from breach of duty in the performance of (or failure to perform) legal work.

6.4 Partnership disputes

Any actual or alleged breach of the Firm's Partnership or shareholder agreement or arrangements, including any equivalent agreement or arrangement where the Firm is a limited liability partnership or a company without a share capital.

6.5 Employment breaches, discrimination, etc.

Wrongful dismissal, repudiation or breach of an employment contract or arrangement, termination of a training contract, harassment, discrimination or like conduct in relation to any Partnership or shareholder agreement or arrangement or the equivalent where the Firm is a limited liability partnership or a company without a share capital, or in relation to any employment or training agreement or arrangement.

6.6 Debts and trading liabilities

Any:

(a) trading or personal debt of any Insured; or

(b) breach by any Insured of the terms of any contract or arrangement for the supply to, or use by, any Insured of goods or services in the course of the Firm's Practice; or

(c) guarantee, indemnity or undertaking by any particular Insured in connection with the provision of finance, property, assistance or other benefit or advantage directly or indirectly to that Insured.

6.7 Fines, penalties, etc

Any:

(a) fine or penalty; or

(b) award of punitive, exemplary or like damages under the law of the United States of America or Canada, other than in respect of defamation; or

(c) order or agreement to pay the costs of a complainant, regulator, investigator or prosecutor of any professional conduct complaint against, or investigation into the professional conduct of, any Insured.

6.8 Fraud or dishonesty

The insurance may exclude liability of the Insurer to indemnify any particular person to the extent that any civil liability or related Defence Costs arise from dishonesty or a fraudulent act or omission committed or condoned by that person, except that:

(a) the insurance must nonetheless cover each other Insured; and

(b) the insurance must provide that no dishonesty, act or omission will be imputed to a body corporate unless it was committed or condoned by, in the case of a company, all directors of that company, or, in the case of a limited liability partnership, all members of that limited liability partnership.

6.9 Directors' or officers' liability

The insurance may exclude liability of the Insurer to indemnify any natural person in their capacity as a director or officer of a body corporate (other than a Recognised Body or a service, administration, trustee or nominee company referred to in clauses 1.3(b), 1.5(b) or 1.7(b)) except that:

(a) the insurance must nonetheless cover any liability of that person which arises from a breach of duty in the performance of (or failure to perform) legal work; and

(b) the insurance must nonetheless cover each other Insured against any vicarious or joint liability.

6.10 War and Terrorism, and Asbestos

The Insurance may exclude, by way of an exclusion or endorsement, liability of the Insurer to indemnify any Insured in respect of, or in any way in connection with:

(a) terrorism, war or other hostilities; and/or

(b) asbestos, or any actual or alleged asbestos-related injury or damage involving the use, presence, existence, detection, removal, elimination or avoidance of asbestos or exposure to asbestos,

provided that any such exclusion or endorsement does not exclude or limit any liability of the Insurer to indemnify any Insured against civil liability or related Defence Costs arising from any actual or alleged breach of duty in the performance of (or failure to perform) legal work or failure to discharge or fulfil any duty incidental to the Firm's Practice or to the conduct of Private Legal Practice.

7 General conditions

7.1 As agreed

The insurance may contain such general conditions as are agreed between the Insurer and the Firm, but the insurance must provide that the special conditions required by clause 4 prevail to the extent of any inconsistency.

7.2 Reimbursement

The insurance may provide that each Insured who:

(a) committed; or

(b) condoned (whether knowingly or recklessly):

(i) non-disclosure or misrepresentation; or

(ii) any breach of the terms or conditions of the insurance; or

(iii) dishonesty or any fraudulent act or omission,

will reimburse the Insurer to the extent that is just and equitable having regard to the prejudice caused to the Insurer's interests by such non-disclosure, misrepresentation, breach, dishonesty, act or omission, provided that no Insured shall be required to make any such reimbursement to the extent that any such breach of the terms or conditions of the insurance was in order to comply with any applicable rules or codes laid down from time to time by the Council of the Law Society of England and Wales, or in the Law Society publication ***Your Clients - Your Business***, as amended from time to time.

The insurance must provide that no non-disclosure, misrepresentation, breach, dishonesty, act or omission will be imputed to a body corporate unless it was committed or condoned by, in the case of a company, all directors of that company, or, in the case of a limited liability partnership, all members of that limited liability partnership. The insurance must provide further that any right of reimbursement contemplated by this clause 7.2 against any person referred to in clauses 1.3(d), 1.5(d) or 1.7(d) (or against the estate or legal personal representative of any such person if they die or become legally incapacitated) is limited to the extent that is just and equitable having regard to the prejudice caused to the Insurer's interests by that person having committed or condoned (whether knowingly or recklessly) dishonesty or any fraudulent act or omission.

7.3 Reimbursement of Defence Costs

The insurance may provide that each Insured will reimburse the Insurer for Defence Costs advanced on that Insured's behalf which the Insurer is not ultimately liable to pay.

7.4 Reimbursement of the Excess

The insurance may provide for those persons who are at any time during the Period of Insurance Principals of the Firm, together with, in relation to a sole practitioner, any person held out as a partner of that practitioner, to reimburse the Insurer for any Excess paid by the Insurer on an Insured's behalf. The Sum Insured must be reinstated to the extent of reimbursement of any amount which eroded it as contemplated by clause 3.4.

7.5 Reimbursement of moneys paid pending dispute resolution

The insurance may provide that each Insured will reimburse the Insurer following resolution of any coverage dispute for any amount paid by the Insurer on that Insured's behalf which, on the basis of the resolution of the dispute, the Insurer is not ultimately liable to pay.

7.6 Withholding assets or entitlements

The insurance may require the Firm to account to the Insurer for any asset or entitlement of any person who committed or condoned any dishonesty or fraudulent act or omission, provided that the Firm is legally entitled to withhold that asset or entitlement from that person.

7.7 Premium

The premium may be calculated on such basis as the Insurer determines and the Firm accepts including, without limitation, a basis which recognises Claims history, categories of work performed by the Firm, numbers of Principals and Employees, revenue derived from the Firm's Practice and other risk factors determined by the Insurer.

7.8 Co-operation and assistance

The insurance (except in the case of an ARP Policy) must provide that, if the ARP Manager is appointed to conduct any Claim, each Insured will give the ARP Manager and any investigators or solicitors appointed by it all information and documents they reasonably require, and full co-operation and assistance in the investigation, defence, settlement, avoidance or reduction of any actual or possible Claim or any related proceeding.

8 Definitions and interpretation

8.1 General

In these minimum terms and conditions, unless the context otherwise requires:

(a) the singular includes the plural, and vice versa; and

(b) the male gender includes the female and neuter genders; and

(c) person includes a body corporate; and

(d) a reference to a partnership does not include a limited liability partnership which is a body corporate; and

(e) a reference to a director includes a member of a limited liability partnership; and

(f) headings are merely descriptive and not an aid to interpretation; and

(g) words and expressions which begin with a capital letter in these minimum terms and conditions have the meaning set out in this clause 8; and

(h) words and expressions in these minimum terms and conditions are to be construed consistently with the same or similar words or expressions in the Solicitors' Indemnity Insurance Rules 2008**.**

8.2 Defined terms

In these minimum terms and conditions:

Circumstances means an incident, occurrence, fact, matter, act or omission which may give rise to a Claim in respect of civil liability

Claim means a demand for, or an assertion of a right to, civil compensation or civil damages or an intimation of an intention to seek such compensation or damages. For these purposes, an obligation on a Firm and/or any Insured to remedy a breach of the Solicitors' Accounts Rules 1998 (as amended from time to time), or any rules which replace the Solicitors' Accounts Rules 1998 in whole or in part, shall be treated as a Claim, and the obligation to remedy such breach shall be treated as a civil liability for the purposes of clause 1, whether or not any person makes a demand for, or an assertion of a right to, civil compensation or civil damages or an intimation of an intention to seek such compensation or damages as a result of such breach.

Claimant means a person or entity which has made or may make a Claim including a Claim for contribution or indemnity.

Defence Costs means legal costs and disbursements and investigative and related expenses reasonably and necessarily incurred with the consent of the Insurer in:

(a) defending any proceedings relating to a Claim; or

(b) conducting any proceedings for indemnity, contribution or recovery relating to a Claim; or

(c) investigating, reducing, avoiding or compromising any actual or potential Claim; or

(d) acting for any Insured in connection with any investigation, inquiry or disciplinary proceeding.

Defence Costs do not include any internal or overhead expenses of the Firm or the Insurer or the cost of any Insured's time.

Employee means any person other than a Principal:

(a) employed or otherwise engaged in the Firm's Practice (including under a contract for services) including, without limitation, as a solicitor, lawyer, trainee solicitor or lawyer, consultant, associate, locum tenens, agent, appointed person (as defined in the Solicitors' Indemnity Insurance Rules 2008), office or clerical staff member or otherwise;

(b) seconded to work in the Firm's Practice; or

(c) seconded by the Firm to work elsewhere.

Employee does not include any person who is engaged by the Firm under a contract for services in respect of any work where that person is required, whether under the Solicitors' Indemnity Insurance Rules 2008 or under the rules of any other professional body, to take out or to be insured under separate professional indemnity insurance in respect of that work.

Excess means the first amount of a Claim which is not covered by the insurance.

The Firm means:

(a) the Partnership (as constituted as at commencement of the Period of Insurance) or Recognised Body which, or sole practitioner who, contracted with the Insurer to provide this insurance; and

(b) the Partnership referred to in paragraph (a) as constituted from time to time, whether prior to or during the Period of Insurance.

Firm's Practice means:

(a) the legal Practice carried on by the Firm as at the commencement of the Period of Insurance; and

(b) the continuous legal Practice preceding and succeeding the Practice referred to in paragraph (a) (irrespective of changes in ownership of the Practice or in the composition of any Partnership which owns or owned the Practice).

Insured means each person and entity named or described as a person to whom the insurance extends and includes, without limitation, those referred to in clause 1.3 and, in relation to Prior and Successor Practices respectively, those referred to in clauses 1.5 and 1.7.

Insurer means the underwriter(s) of the insurance.

Lead Insurer means the insurer named as such in the contract of insurance, or, if no Lead Insurer is named as such, the first-named insurer on the relevant certificate of insurance

Partnership means an unincorporated Firm, and does not mean a Firm incorporated as a limited liability partnership, and Partner means a partner in an unincorporated Firm

Period of Insurance means the period for which the insurance operates.

Principal means, in relation to:

(a) a Recognised Body or other body corporate which is a company - each director or officer of that body and any person held out as a director or officer; and

(b) a Recognised Body which is a limited liability partnership - each member of that body; and

(c) a Partnership - each Partner of that Firm and any person held out as a Partner (and where a Recognised Body is a Partner - each director and officer of that body and each person held out as a director or officer, if the body is a company; and each member of that body if the body is a limited liability partnership); and

(d) a sole practitioner - that practitioner.

Prior Practice means each Practice to which the Firm's Practice is ultimately a Successor Practice by way of one or more mergers, acquisitions, absorptions or other transitions.

Private Legal Practice means the provision of services in private Practice as a solicitor or Registered European Lawyer including, without limitation:

(a) providing such services in England, Wales or anywhere in the world, whether alone or with other lawyers in a Partnership permitted for practice in England and Wales by rule 12 of the Solicitors' Code of Conduct 2007; and

(b) the provision of such services as a secondee of the Firm; and

(c) any Insured acting as an executor, trustee, attorney, notary, insolvency practitioner or other personal appointment; and

(d) the provision of such services by any Employee.

Private Legal Practice does not include practising as an Employee of an employer other than a solicitor, a Registered European Lawyer, a Partnership permitted for practice in England and Wales by rule 12 of the Solicitors' Code of Conduct 2007, or a Recognised Body.

Relevant Recognised Body means a Recognised Body other than:

(a) an unlimited company, or an oversea company whose members' liability for the company's debts is not limited by its constitution or by the law of its country of incorporation; or

(b) a nominee company only, holding assets for clients of another Practice; and

(i) it can act only as agent for the other Practice; and

(ii) all the individuals who are Principals of the Recognised Body are also Principals of the other Practice; and

(iii) any fee or other income arising out of the Recognised Body accrues to the benefit of the other Practice.

Recognised Body means a body corporate for the time being recognised under Section 9 of the ***Administration of Justice Act*** 1985.

Successor Practice means a Practice identified in this definition as 'B', where:

(a) 'A' is the Practice to which B succeeds; and

(b) 'A's owner' is the owner of A immediately prior to transition; and

(c) 'B's owner' is the owner of B immediately following transition; and

(d) 'transition' means merger, acquisition, absorption or other transition which results in A no longer being carried on as a discrete legal Practice.

B is a Successor Practice to A where:

(i) B is or was held out, expressly or by implication, by B's owner as being the successor of A or as incorporating A, whether such holding out is contained in notepaper, business cards, form of electronic communications, publications, promotional material or otherwise, or is contained in any statement or declaration by B's owner to any regulatory or taxation authority; and/or

(ii) (where A's owner was a sole practitioner and the transition occurred on or before 31 August 2000) - the sole practitioner is a Principal of B's owner; and/or

(iii) (where A's owner was a sole practitioner and the transition occurred on or after 1 September 2000) - the sole practitioner is a Principal or Employee of B's owner; and/or

(iv) (where A's owner was a Recognised Body) - that body is a Principal of B's owner; and/or

(v) (where A's owner was a Partnership) - the majority of the Principals of A's owner have become Principals of B's owner; and/or

(vi) (where A's owner was a Partnership and the majority of Principals of A's owner did not become Principals of the owner of another legal Practice as a result of the transition) - one or more of the Principals of A's owner have become Principals of B's owner and:

(A) B is carried on under the same name as A or a name which substantially incorporates the name of A (or a substantial part of the name of A); and/or

(B) B is carried on from the same premises as A; and/or

(C) the owner of B acquired the goodwill and/or assets of A; and/or

(D) the owner of B assumed the liabilities of A; and/or

(E) the majority of staff employed by A's owner became employees of B's owner.

Notwithstanding the foregoing, B is not a Successor Practice to A under paragraph (ii), (iii), (iv) (v) or (vi) if another Practice is or was held out by the owner of that other Practice as the successor of A or as incorporating A, provided that there is insurance complying with these minimum terms and conditions in relation to that other Practice..

Sum Insured means the aggregate limit of liability of each Insurer under the insurance.

Solicitors' Compensation Fund Rules 1995

Client Protection Directorate

Statutory authority, rules and guidelines

The Law Society's Compensation Fund is maintained pursuant to Section 36 of the Solicitors Act 1974. The object of the Fund is to enable the Society to make grants to those persons who have suffered loss by reason of the dishonesty of a solicitor, or his employee, or to an applicant who has suffered hardship as a consequence of a failure by a solicitor to account for money.

Section 36(2) provides as follows:-

> "Where the Council are satisfied –
>
> (a) that a person has suffered or is likely to suffer loss in consequence of dishonesty on the part of a solicitor, or of an employee of a solicitor, in connection with that solicitor's practice or purported practice or in connection with any trust of which that solicitor is or formerly was a trustee; or
>
> (b) that a person has suffered or is likely to suffer hardship in consequence of failure on the part of a solicitor to account for money which has come to his hands in connection with his practice or purported practice or in connection with any trust of which he is or formerly was a trustee; or
>
> (c) that a solicitor has suffered or is likely to suffer loss or hardship by reason of his liability to any of his firm's clients in consequence of some act or default of any of his partners or employees in circumstances where but for the liability of that solicitor a grant might have been made out of the Compensation Fund to some other person;
>
> the Society may make a grant out of the Compensation Fund for the purpose of relieving that loss or hardship."

Section 36(8) provides as follows:-

> "The Council may make Rules about the Compensation Fund and the procedure for making grants from it."

The administration of the Compensation Fund is presently subject to the Solicitors' Compensation Fund Rules 1995 which provides as follows:-

Solicitors' Compensation Fund Rules 1995

Rules dated 26 January 1995 made by the Council of the Law Society under Section 36(8) of the Solicitors Act 1974 and section 9 of the Administration of Justice Act 1985.

1 Interpretation

(a) In these Rules:

"the Act" means the Solicitors Act 1974.

"applicant" means a person or persons applying for a grant out of the Compensation Fund under section 36 of the Act, Schedule 2 paragraph 6 of the Administration of Justice Act 1985 or Schedule 14 paragraph 6 of the Courts & Legal Services Act 1990.

"**defaulting practitioner**" means:

(i) a solicitor in respect of whose act or default, or in respect of whose employee's act or default, an application for a grant is made;

(ia) a registered European lawyer in respect of whose act or default, or in respect of whose employee's act or default, an application for a grant is made;

(ii) a recognised body in respect of whose act or default, or in respect of whose officer's or employee's act or default, an application for a grant is made; or

(iii) a registered foreign lawyer who is practising in partnership with a solicitor or a registered European lawyer, and in respect of whose act or default or in respect of whose employee's act or default, an application for a grant is made;

and the expressions "defaulting solicitor", "defaulting registered European lawyer", "defaulting recognised body" and "defaulting registered foreign lawyer" shall be construed accordingly.

"recognised body" has the meaning assigned by section 9 of the Administration of Justice Act 1985;

"registered European lawyer" means an individual registered with the Law Society under regulation 17 of the European Communities (Lawyer's Practice) Regulations 2000: and

"registered foreign lawyer" has the meaning assigned by section 89 of the Courts & Legal Services Act 1990.

(b) Other expressions in these Rules have the meaning assigned to them by the Act.

(c) The Interpretation Act 1978 applies to these Rules as it applies to an Act of Parliament.

2. Grants in respect of persons not authorised to practise

(a) A grant may be made in respect of a defaulting solicitor even if the defaulting solicitor had no practising certificate in force or was suspended

from practice at the date of the relevant act or default provided that the Council is reasonably satisfied that the applicant was unaware of the absence of a practising certificate or of the suspension.

(aa) A grant may be made in respect of a defaulting registered European lawyer even if, at the date of the relevant act or default, the registration of that lawyer in the Society's register of European lawyers was suspended or was cancelled under regulation 8 of the European Lawyers Registration Regulations 2000 due to non-renewal provided that the Council is satisfied that the applicant was unaware of the suspension or cancellation.

(b) A grant may be made in respect of a defaulting recognised body even if the recognition of that body had expired by effluxion of time under Rule 18 of the Solicitors' Incorporated Practice Rules 1988 on or before the date of the relevant act or default provided that the Council is reasonably satisfied that the applicant was unaware of such expiry.

(c) A grant may be made in respect of a defaulting registered foreign lawyer even if, at the date of the relevant act or default, the registration of that lawyer in the register of foreign lawyers was suspended or was cancelled under Schedule 14 paragraph 3(4)(a) of the Courts & Legal Services Act 1990 due to non-renewal provided that the Council is reasonably satisfied that the applicant was unaware of the suspension or cancellation.

3. Grants to practitioners

No grant shall be made

(i) under section 36(2)(c) of the Act to any solicitor, or

(ii) under section 36(2)(c) of the Act to any registered European lawyer, or

(iii) under Schedule 14 paragraph 6(1)(c) of the Courts & Legal Services Act 1990 to any registered foreign lawyer, or

(iv) under Schedule 2 paragraph 6(2)(c) of the Administration of Justice Act 1985 to any solicitor, registered European lawyer, recognised body or registered foreign lawyer, or to any other individual or body corporate permitted under the Solicitor's Incorporated Practice Rules to be a member of a recognised body,

unless the Council is satisfied that no other means of making good the loss is available and that he or she is fitted by reason of conduct, age and experience (or in the case of a recognised body or other body corporate it is fitted by reason of the conduct, age and experience of its officers and employees) to receive such a grant.

4. Foreign lawyers

(a) If a registered European lawyer is exempted from contributing to the Compensation Fund under the Solicitors' Compensation Fund (Foreign Lawyers' Contributions) Rules 1991 on the basis of completely equivalent cover under home state rules, no grant shall be made:

(i) under section 36(2)(a) of the Act in respect of any act or default of the registered European lawyer or his or her employee unless, in the case of an employee, the employee is:

(A) a solicitor, or

(B) the employee of a partnership which includes at least one person who is not exempted on the basis of that provision;

(ii) under section 36(2)(b) of the Act in respect of any act or default of the registered European lawyer; or

(iii) under section 36(2)(c) of the Act to the registered European lawyer.

(b) No grant shall be made under section 36 of the Act in respect of any act or default of a registered European lawyer, or the employee or partner of a registered European lawyer, where such act or default took place outside the United Kingdom, unless the Council is satisfied that the act or default was, or was closely connected with, the act or default of a solicitor, or that the act or default was closely connected with the registered European lawyer's practice in the United Kingdom.

(c) No grant shall be made under Schedule 14 paragraph 6(1) of the Courts & Legal Services Act 1990 in respect of the act or default of a registered foreign lawyer, or of the employee or partner of a registered foreign lawyer, where such act or default took place outside England and Wales, unless the Council is satisfied that the act or default was, or was closely connected with, the act or default of a solicitor, or that the act or default was closely connected with practice in England and Wales.

5. Application form

Every applicant shall complete and deliver to the Society an application in such form as may from time to time be prescribed by the Society.

6. Time limits

Every application shall be delivered to the Society within six months after the loss, or likelihood of loss, or failure to account, as the case may be, first came, or reasonably should have come, to the knowledge of the applicant. The Council may extend this period if satisfied that there are exceptional circumstances which justify the extension of the time limit.

7. Documentation in support

The Council may require an application to be supported by a statutory declaration and accompanied by any relevant documents and shall cause such enquiries to be made in relation to the application as it sees fit. Failure to provide documentation or information requested or to co-operate fully in the

Council's enquiries may be taken into account when the application is considered.

8. Other remedies

The Council may, before deciding whether or not to make a grant, require the pursuit of any civil remedy which may be available in respect of the loss, the making of a formal complaint to the Police in respect of any dishonesty on the part of the defaulting practitioner or may require the assistance of an applicant in the taking of any disciplinary action against the defaulting practitioner.

9. Costs for submitting applications

Where a grant is made, the Council may consider an application for a further grant in respect of the reasonable costs properly incurred by the applicant with either his solicitor or other professional adviser, provided that such costs were incurred wholly, exclusively and necessarily in connection with the preparation, submission and proof of the application. If, in the view of the Council, such costs were not reasonably or properly incurred then the Council may decline to pay some or all of those costs.

10. Interest

The Council may consider an application for a supplementary grant by way of a sum in lieu of lost interest on a principal grant. Such interest will normally be calculated in accordance with the rates prescribed from time to time by the Council for Compensation Fund applications and will normally be calculated from the day the loss which was the subject of the principal grant was incurred, up to the next working day after the despatch of the grant cheque.

11. Discretion to limit grant

In relation to any loss sustained, or any sum of money which came under the control of a defaulting practitioner, after 10th June 1993, the Council will refuse to authorise a grant of an amount which would result in sums exceeding £1,000,000.00 (inclusive of all costs and interest) being paid to or on behalf of an applicant from either the Compensation Fund or the Solicitors Indemnity Fund or both together in respect of any individual transaction or matter.

12 Assisting in recovering money

An applicant to whom a grant has been made may be required to prove, on behalf of the Society, in any insolvency and/or winding-up of the defaulting practitioner and also to comply with all proper or reasonable requirements of the Council in the exercise of subrogated rights under section 36(4) of the Act.

13. Refusal of an application

If the Council refuses to make a grant of either the whole or part of the amount applied for then the Council shall cause the applicant to be informed in writing of the reasons for the decision.

14. Notice to defaulting practitioner

(a) The Council shall not make a grant unless a letter has been sent:

  (i) to the defaulting solicitor at his or her last known correspondence address or to any solicitors or other lawyers instructed by him or her;

(ia) to the defaulting registered European lawyer at his or her last known correspondence address or to any solicitors or other lawyers instructed by him or her, as well as to the appropriate regulatory body for the defaulting registered European lawyer within his or her home jurisdiction or jurisdictions, whether in Europe or elsewhere;

(ii) to the defaulting recognised body at its registered office as last communicated to the Council or the Society under the Solicitors' Incorporated Practice Rules 1988 (or any Rules for the time being replacing those Rules); or

(iii) to the defaulting registered foreign lawyer at his or her last known correspondence address or to any solicitors or other lawyers instructed by him or her as well as to the appropriate regulatory body for the defaulting registered foreign lawyer within his or her home jurisdiction or jurisdictions.

informing him/her or it of the nature and value of the application and not less than eight days have elapsed since the date of such letter.

(b) If by reason of death, insolvency or other disability, proper notification under sub-paragraphs (a)(i), (ia) or (iii) of this rule cannot be given to a defaulting practitioner then such notice may be given to a Personal Representative, Trustee in Bankruptcy or any other person who the Society is satisfied acts for or on behalf of the defaulter and/or his or her Estate.

(c) Where the defaulting practitioner is a recognised body and it appears to the Society that any letter sent under (a)(ii) above will not come to the attention of the recognised body (or any officer or employee thereof) then the letter may be sent to the liquidator and/or receiver of the recognised body or to any other person for the time being accountable for the affairs of the recognised body.

(d) If it appears to the Society that any letters sent under sub-paragraphs (a)(i) to (iii) of this rule will not come to the attention of the defaulting practitioner or any other person on his or her behalf, then the Council may make a grant notwithstanding failure to comply with the provisions of this Rule.

15. Notice of requirements

Any requirement of the Council or the Society under these Rules may be communicated by a notice in writing.

16. Guidelines

When exercising the discretion conferred upon it by Section 36(2) of the Act, Schedule 2 paragraph 6(2) of the Administration of Justice Act 1985 and Schedule 14 paragraph 6(1) of the Courts and Legal Services Act 1990, the Council may take into consideration the Guidelines contained in the Schedule to these Rules and decisions of the Council, and any other guidelines that the Council may approve, although these guidelines and decisions shall not fetter the Council's discretion.

17. Waivers

The Council may waive any of the provisions of these Rules excepting Rule 14.

18. Repeal and commencement

These Rules shall come into operation on 1 March 1995, whereupon the Solicitors' Compensation Fund Rules 1975 (as amended) shall cease to have effect save in respect of applications submitted before that date.

Solicitors' compensation fund rules 1995 [Schedule]

Guidelines

These guidelines form part of the Solicitors Compensation Fund Rules 1995 made by the Council on 26 January 1995, although were subject to amendment by the Council on 18 July 1996 and 25 February 2004.

In these guidelines, reference to a solicitor shall include registered European lawyers; registered foreign lawyers practising in partnership with a solicitor or a registered European lawyer; and recognised bodies.

1. General Principles

(a) The basic object of the Fund is to replace "clients' money" misappropriated by a solicitor or his or her employee(s), but, although an applicant for a grant must be a person who has suffered loss through the actions of the solicitor, he or she need not necessarily be or have been the solicitor's client.

(b) A grant out of the Fund is made wholly at the discretion of the Council of the Law Society. No person has a right to a grant enforceable at law, but the intention of the Council is to seek to administer the Fund in an even-handed and consistent manner.

(c) The Fund is administered as a fund of last resort. This means that a grant may be limited or refused to an applicant where the loss is an insured risk or where the loss is capable of being made good by recourse to another person.

(d) The burden of satisfying the Council that a loss has been suffered within the ambit of the Fund rests with each applicant, but the Society will give guidance and, so far as possible, for the purpose of the application, allow the applicant reasonable access to records under the Society's control or to which the Society has access.

(e) A grant may be made out of the Fund to a solicitor applicant, usually by way of a loan, in circumstances where a loss within the ambit of the Fund has been suffered by reason of misappropriation of clients' money by his or her partner or employee or where he or she is the purchaser of a practice from a defaulting solicitor, provided that the application is not tainted with the default. Exceptionally, such a grant may be made even though the applicant may be entitled to indemnity under the Solicitors' Indemnity Fund and without prejudice to that indemnity.

(f) The Council normally require that the “dishonesty" or '"failure to account” referred to in Section 36(2)(a) and (b) of the Solicitors Act 1974 must have occurred within the course of a solicitor/client transaction of a kind which is part of the usual business of a solicitor.

2 Losses which cannot be the subject of a grant

Certain losses are outside the ambit of the Fund because the Council has no power to make a grant. Examples are:-

(a) losses arising as a result of misappropriation of money by a solicitor outside his or her practice as such or by a solicitor's employee acting outside the scope of his or her employment;

(b) losses arising solely by reason of professional negligence by a solicitor;

(c) losses arising by reason of the failure of a solicitor to satisfy a money judgment against him or her where the facts of the judgment would not otherwise give rise to a claim on the Compensation Fund;

(d) losses where the Council is satisfied that either no evidence of dishonesty is available or, where in the case of failure to account, an applicant is not suffering material hardship.

3. Losses in respect of which a grant may not be made

Notwithstanding the statutory provisions of section 36, there are certain losses in respect of which it is not normally the practice of the Council to make a grant. Examples are: -

(a) losses which result from, but do not form part of any misappropriation of, or failure to account for, money or money's worth. This is subject to certain exceptions, e.g. legal costs incurred in applying for a grant and interest on the amount of the grant.

(b) the application is tainted with the applicant's own dishonesty.

(c) the applicant has contributed to his, her or its loss as a result of his/her or its activities, omissions or behaviour either before, during or after the transaction giving rise to the application or thereafter.

(d) in the case of an applicant who is a member of a profession, or is engaged in trade or business or performs a function, where the loss arises in connection with that profession or in the course of that trade, business or function, and there is evidence that the applicant and/or the applicant's servants or agents contributed to the loss by failing to exercise a reasonable standard of care.

(e) the loss amounts to a claim for contractually agreed interest between the applicant and the solicitor. Where, following the authorisation of a principal grant, the Council makes a supplementary grant for a sum in lieu of lost interest, the sum is calculated at rates which may from time to time be prescribed by the Council.

(f) the Society was not notified of the applicant's loss within six months of the date upon which the loss first came or ought to have come to the applicant's knowledge, and there are no exceptional circumstances which, in the opinion of the Council, justify the delay (see Rule 6 of the Solicitors' Compensation Fund Rules);

(g) the application is based on the failure by a solicitor to comply with an undertaking. The Fund does not generally underwrite a solicitor's undertaking. Failure on the part of a solicitor to comply with an undertaking is a matter of misconduct which may be the subject of a complaint to the Office for the Supervision of Solicitors, but does not of

itself entitle the recipient to make a successful application for a grant out of the Fund.

An application may, however, be considered favourably if it can be shown that an undertaking was given in the course of the solicitor's usual business as a solicitor acting on behalf of a client, that the recipient acted reasonably in accepting the undertaking and placing reliance on the solicitor in his or her capacity as such and that:

(i) the undertaking was given with dishonest intent for the purpose of procuring money or money's worth, or

(ii) the undertaking, although not given with dishonest intent, Is subsequently dishonestly not performed by the solicitor for the purpose of procuring money or money's worth.

The Council does not consider the giving of an undertaking in circumstances which amount to the solicitor giving a bare guarantee either of his or her personal liabilities or the financial obligations and liabilities of a client or third party to form part of the usual business of a solicitor, and such an undertaking would therefore not normally be regarded as having been given within the course of a solicitor/client transaction.

(h) the loss occurred in relation to an overseas partnership of which all solicitor partners are exempt from other provisions of Rules 12 and 13 of the Solicitors Overseas Practice Rules 1990 by virtue of Rules 12(6) and 13(6), and the loss did not occur as a result of a solicitors dishonesty.

(i) the application is by the Legal Services Commission for loss occasioned through making regular payments under the Commission's contracting schemes for civil and/or criminal work.

4. Requirements to be satisfied

Every applicant for a grant out of the Compensation Fund must satisfy the Council:-

(a) that he, she or it has suffered or is likely to suffer actual loss of money or money's worth;

(b) that such loss has been occasioned by (i) the dishonesty of a solicitor (or his or her employee) acting in the course of his or her practice as such or in connection with a Trust of which the solicitor was at the material time, a professional Trustee or (ii) the failure of a solicitor (or his or her employee) to account for money received in the course of his or her practice or in connection with a Trust of which the solicitor was, at the material time, a professional Trustee;

(c) that any alleged dishonesty is evidenced either by the conviction of the solicitor (or his or her employee), or by a finding of fraud in a civil action, or by evidence leading to an inevitable presumption of theft. Where an application is based on failing to account, the application must be supported by sufficient documentation to substantiate that a failure to account has occurred and that the applicant is suffering or is likely to suffer hardship; and

(d) that the loss is not reasonably recoverable from any other source.

5. Interim grants

In an application where it appears that there is severe hardship, the Council may make an interim grant before the full investigation of the whole application has been completed and without the full application being admitted. However, the Council must be satisfied that there has been a loss of an amount at least equal to that to be paid out by way of an interim grant.

6. Claims where the defaulting solicitor is or was in partnership

(a) Losses caused by the dishonesty of a partner or employee will normally be recoverable from the Solicitors' Indemnity Fund, or after 31 August 2000 from the firm's insurer under the Solicitors' Indemnity Insurance Rules. The Council may, however, make a grant to an applicant in respect of part of his or her claim which is not covered by the Indemnity Fund or by the firm's insurance, e.g. where the remaining partners are unable to settle all or part of the claim from their own resources.

(b) Accordingly, applicants should proceed with a claim against the remaining partners who, in turn, will make a claim against the Indemnity Fund, or after 31 August 2000 under the firm's insurance. Where there is doubt as to whether a claim should be met from the Indemnity Fund or the Compensation Fund, the Society endeavours to make suitable arrangements with Solicitors' Indemnity Fund Limited to ensure that claims are paid promptly.

7. Institution of civil proceedings

In some cases the Council may require an applicant to institute civil proceedings including, where appropriate, insolvency proceedings against the solicitor in respect of the loss suffered. The purpose of the proceedings may be to recover all or part of the alleged loss or to quantify precisely the amount of such loss. No applicant should institute proceedings unless and until the written consent of the Society has been obtained and the question of who is to be responsible for the costs has been decided, otherwise any application for a grant in respect of such costs may be rejected by the Council.

8. Prosecution of dishonest solicitors

In all appropriate cases, the applicant will be expected to assist the Police in connection with enquiries into the commission of any criminal offence by the solicitor in respect of the alleged acts giving rise to the application. However, the Council may consider an application for a grant notwithstanding that a defaulting solicitor has not been convicted of any such offence nor has been the subject of a finding of dishonesty by the Solicitors' Disciplinary Tribunal.

9. Personal liabilities of a solicitor

The Council will not normally make a grant in respect of the personal or trading debts or liabilities of a solicitor or a solicitor's firm or where the monies form part of a commercial transaction or business venture between the applicant and the solicitor outside the normal solicitor/client relationship.

10. Applicant's own behaviour

When considering any application, the Council takes into account the conduct of the applicant and/or the applicant's servants or agents both before and after the loss was sustained. If the Council, in the exercise of its discretion, considers an applicant and/or an applicant's servants or agents to have inter alia contributed to the circumstances of the loss, or to have failed to submit an application for a grant within a reasonable time (see also Rule 6 of the Solicitors' Compensation Fund Rules), or to have failed to pursue an application diligently, then the application may be rejected in its entirety or the amount of any grant substantially reduced.

11. Deduction from grants

(a) The Council may deduct from any grant the costs that would have been due to the solicitor provided that the work had been properly completed so that the applicant will not be in a better position by reason of a grant than he or she would otherwise have been in. A deduction in respect of notional costs may be made by the Council notwithstanding the fact that the defaulting solicitor may not have held a practising certificate at all material times. If a defaulting solicitor did the work so badly, or did not complete it, with the result that the applicant has had to instruct another solicitor to carry out or finish the work, then a grant may be made for the additional reasonable costs incurred by the applicant.

(b) The Council will normally seek to deduct from any grant all monies already recovered by an applicant and monies which either will be or should have been recovered. For example, if an application is for a sum of £10,000 but an applicant has already recovered, from whatever source, a sum of £2,000, the Council will normally seek to base any grant on the balance of £8,000. This principle will usually apply even when an applicant believes that he is receiving re-payments at a contractually agreed rate, but where the solicitor has, in fact, actually misappropriated the money advanced and is, for example, making re-payments in lieu of interest in an effort to allay suspicion.

12. Payment of interest on claims

In appropriate cases, the Council will consider an application for a supplementary grant in lieu of lost interest on the amount of the grant from the date of the loss (see Rule 10 of the Solicitors' Compensation Fund Rules). If paid, interest will normally be calculated at those rates prescribed from time to time by the Council which take into account that a grant is a gift and is therefore not subject to tax.

13. Payment of costs of application

The Council has the power to make a further grant in respect of the reasonable costs of an applicant's solicitor or other professional adviser relating to a claim where a grant is authorised (see Rule 9 of the Solicitors' Compensation Fund Rules). The Council may not, however, be prepared to make such a further grant or may grant less than the full costs if it is of the opinion that all or part of the costs should not have been incurred, or might have been saved by an earlier approach to the Society, or is of the view that the costs incurred are unreasonable or excessive.

14. Multi-profession frauds

In an application where the loss has been sustained as a result of the combined activities of more than one profession, (e.g. a solicitor conspires with an accountant or surveyor, or a dishonest solicitor is assisted by a negligent accountant or valuer) the Council will normally consider how each contributing factor affected the applicant's loss. The Council will normally endeavour to base any grant on its assessment of that portion of the loss primarily attributable to the acts of the solicitor as opposed to that portion which is primarily attributable to the acts or omissions of the other professional parties, or to other factors. The Council may decide to make a grant on a pro-rata basis in accordance with its assessment of the importance of each contributing factor in the loss, or may reject an application in its entirety if it is of the opinion that the loss was primarily due to other factors rather than the solicitor's dishonesty.

15. Normal maximum payout

For any loss sustained, or any sum of money that came into the possession of a defaulting solicitor, subsequent to 10 June 1993, it is the Council's policy not to authorise a grant with regard to any individual transaction which would result in an aggregate sum exceeding £1,000,000, inclusive of all interest and costs, being paid from a combination of the Compensation Fund and the Solicitors Indemnity Fund or the Compensation Fund solely.

16. Rejection of claim

The most common ground for rejection of an application is that it does not come within the Compensation Fund's statutory framework. When the Council refuse or are unable to make a grant, the applicant will be informed in writing of the reason for this decision. The fact that an application has been rejected does not prevent a further application being submitted, or the rejected application being re-considered, provided that substantial new relevant evidence, information or submissions are produced in support of the new application or the request for re-consideration.

Solicitors' Compensation Fund Rules 2009

Rules dated 31 March 2009 commencing 31 March 2009 made by the Solicitors Regulation Authority Board under sections 36, 36A, 79 and 80 of the Solicitors Act 1974 and section 9 of the Administration of Justice Act 1985,

with the concurrence of the Master of the Rolls under section 9 of the Administration of Justice Act 1985 and article 4 of the Legal Services Act 2007 (Commencement No. 4, Transitory and Transitional Provisions and Appointed Day) Order 2009

and the concurrence of the Lord Chancellor under paragraph 16 of Schedule 22 to the Legal Services Act 2007 and article 4 of the Legal Services Act 2007 (Commencement No. 4, Transitory and Transitional Provisions and Appointed Day) Order 2009.

1. Interpretation

(1) In these rules:

"the Act" means the Solicitors Act 1974;

"applicant" means a person or persons applying for a grant out of the Compensation Fund under rule 3 of these rules;

"appointed representative" means the personal representative of a deceased defaulting practitioner; the trustee of a bankrupt defaulting practitioner; the administrator of an insolvent defaulting practitioner, or other duly appointed representative of a defaulting practitioner;

"approved regulator" means a body listed in paragraph 1 of Schedule 4 to the Legal Services Act 2007 (whether or not that paragraph has been brought into force), or designated as an approved regulator by an order under paragraph 17 of that Schedule,

and reference to the SRA as an approved regulator means the SRA carrying out regulatory functions assigned to the Law Society as an approved regulator;

"defaulting practitioner" means:

(a) a solicitor in respect of whose act or default, or in respect of whose employee's act or default, an application for a grant is made;

(b) a registered European lawyer in respect of whose act or default, or in respect of whose employee's act or default, an application for a grant is made;

(c) a recognised body in respect of whose act or default, or in respect of whose manager's or employee's act or default, an application for a grant is made; or

(d) a registered foreign lawyer who is a manager of a partnership, limited liability partnership or company together with a solicitor, a registered European lawyer or a recognised body, and in respect of whose act or default or in respect of whose employee's act or default, an application for a grant is made;

and the expressions "defaulting solicitor", "defaulting registered European lawyer", "defaulting recognised body" and "defaulting registered foreign lawyer" shall be construed accordingly;

"exempt European lawyer" has the meaning assigned in rule 24 of the Solicitor's Code of Conduct 2007;

“manager” means a partner in a partnership, a member of a limited liability partnership or a director of a company, as defined in rule 24 of the Solicitor's Code of Conduct 2007;

“recognised body” has the meaning assigned by section 9 of the Administration of Justice Act 1985;

“registered European lawyer” means an individual registered with the SRA under regulation 17 of the European Communities (Lawyer’s Practice) Regulations 2000;

“registered foreign lawyer” has the meaning assigned by section 89 of the Courts and Legal Services Act 1990 and-

“SRA” means the Solicitors Regulation Authority.

(2) Other expressions in these rules have the meaning assigned to them by the Act.

(3) The Interpretation Act 1978 applies to these rules as it applies to an Act of Parliament.

2. Maintenance of and contributions to the Fund

(1) The Law Society (“the Society”) shall establish and maintain the fund called the Solicitors' Compensation Fund ("the Fund") for making grants in respect of compensation claims.

(2) Every solicitor, registered European lawyer, registered foreign lawyer and recognised body shall make contributions to the Fund in such amounts, at such times and in such circumstances, as may be prescribed from time to time by the Council of the Law Society. Any unpaid contributions may be recovered as a debt due to the Society.

(3) Paragraph (2) shall not apply to a solicitor, registered European lawyer or registered foreign lawyer who is a Crown Prosecutor.

(4) The Society may invest any money which forms part of the Fund in any investments in which trustees may invest under the general power of investment in section 3 of the Trustee Act 2000 (as restricted by sections 4 and 5 of that Act).

(5) The Society may insure with authorised insurers, in relation to the Fund, for such purposes and on such terms as it considers appropriate.

(6) The Society may

(a) borrow for the purposes of the Fund;

(b) charge investments which form part of the Fund as security for borrowing by the Society for the purposes of the Fund.

(7) The Fund may be applied by the SRA for the following purposes (in addition to the making of grants in respect of compensation claims):

(a) payment of premiums on insurance policies effected under paragraph (5);

(b) repayment of money borrowed by the Society for the purposes of the Fund and payment of interest on any money so borrowed under paragraph (6);

(c) payment of any other costs, charges or expenses incurred by the Society in establishing, maintaining, protecting, administering or applying the Fund;

(d) payment of any costs, charges or expenses incurred by the SRA in exercising its powers under Part 2 of Schedule 1 to the Act (intervention powers);

(e) payment of any costs or damages incurred by the Society, the SRA, their employees or agents as a result of proceedings against any or either of them for any act or omission of its or theirs in good faith and in the exercise or purported exercise of such powers.

3. Grants which may be made from the Fund

The object of the Fund is to replace client money which a defaulting practitioner or a defaulting practitioner's employee or manager has misappropriated or otherwise failed to account for. The applicant need not necessarily be or have been the defaulting practitioner's client.

(1) A grant out of the Fund is made wholly at the discretion of the SRA. No person has a right to a grant enforceable at law.

(2) For any grant to be made out of the Fund, an applicant must satisfy the SRA that:

(a) he has suffered or is likely to suffer loss in consequence of the dishonesty of a defaulting practitioner or the employee or manager of a defaulting practitioner or

(b) he has suffered or is likely to suffer loss and hardship in consequence of a failure to account for money which has come into the hands of a defaulting practitioner or the employee or manager of a defaulting practitioner, which may include the failure by a defaulting practitioner to complete work for which he was paid,

in the course of a transaction of a kind which is part of the usual business of the persons listed in rule 1 (1) (a) to (d).

(3) For the purposes of paragraph (2)(b):

(a) an individual whose dealings with the defaulting practitioner have been in a personal capacity and who has suffered or is likely to suffer loss due to a failure to account shall be deemed to have suffered hardship; and

(b) a body corporate, or an individual whose dealings with the defaulting practitioner have been in a business capacity and who has suffered or is likely to suffer loss due to a failure to account must provide evidence to satisfy the SRA that it, he or she (the body or individual) has suffered or is likely to suffer hardship.

(4) A grant may, at the sole discretion of the SRA, be made as an interim measure.

4. Grants in respect of persons in default of regulatory requirements

(1) A grant may be made in respect of a defaulting solicitor even if the defaulting solicitor had no practising certificate in force at the date of the relevant act or default provided that the SRA is reasonably satisfied that the applicant was unaware of the absence of a valid practising certificate.

(2) A grant may be made in respect of a defaulting registered European lawyer even if, at the date of the relevant act or default, the registration of that lawyer in the SRA's register of European lawyers was suspended or was cancelled under regulation 8 of the European Lawyers Registration Regulations 2000 due to non-renewal provided that the SRA is reasonably satisfied that the applicant was unaware of the suspension or cancellation.

(3) A grant may be made in respect of a defaulting recognised body even if the recognition of that body had expired for non-renewal under regulation 8.3 of the Solicitors' Recognised Bodies Regulations 2007 on or before the date of the relevant act or default provided that the SRA is reasonably satisfied that the applicant was unaware of such revocation.

(4) A grant may be made in respect of a defaulting registered foreign lawyer even if, at the date of the relevant act or default, the registration of that lawyer in the register of foreign lawyers was suspended, or was cancelled under Schedule 14 paragraph 3(4)(a) of the Courts and Legal Services Act 1990 due to non-renewal, provided that the SRA is reasonably satisfied that the applicant was unaware of the suspension or cancellation.

5. Grants to practitioners

(1) A grant may be made to a defaulting practitioner who or which has suffered or is likely to suffer loss by reason of his, her or its liability to any client in consequence of some act or default of:

(a) in the case of a defaulting solicitor, registered European lawyer or registered foreign lawyer, any of his or her employees or any fellow manager;

(b) in the case of a defaulting recognised body, any of its managers or employees or any fellow manager,

in circumstances where but for the liability of that defaulting practitioner a grant might have been made from the Fund to some other person.

(2) No grant shall be made under paragraph (1) unless the SRA is satisfied that no other means of making good the loss is available and that the defaulting practitioner is or in the case of a recognised body are fit and proper to receive a grant.

(3) A grant under paragraph (1) shall normally be made by way of a loan and shall be repayable by the recipient at the time and upon such terms as shall be specified by the SRA.

(4) In the case of a defaulting recognised body, such grant may be payable to one or more of the managers of the defaulting recognised body. If a loan is made to more than one manager, they shall be jointly and severally liable for the repayment of the loan to the Society.

6. Foreign lawyers

(1) If a registered European lawyer is exempted from contributing to the Fund on the basis that he or she has completely equivalent cover under home state rules, no grant shall be made:

(a) in respect of any act or default of the registered European lawyer or his or her employee unless, in the case of an employee, the employee is:

(i) a solicitor, or

(ii) the employee of a partnership which includes at least one person who or which contributes to the Fund; or

(b) under rule 5 to the registered European lawyer.

(2) No grant shall be made in respect of any act or default of a registered European lawyer or an exempt European lawyer, or the employee of a registered European lawyer, where such act or default took place outside the United Kingdom, unless the SRA is satisfied that the act or default was, or was closely connected with, the act or default of a solicitor or the employee of a solicitor, or that the act or default was closely connected with the registered European lawyer's practice in the United Kingdom.

(3) No grant shall be made in respect of the act or default of a registered foreign lawyer, or of the employee of a registered foreign lawyer, where such act or default took place outside England and Wales, unless the SRA is satisfied that the act or default was, or was closely connected with, the act or default of a solicitor or the employee of a solicitor, or that the act or default was closely connected with practice in England and Wales.

7. Losses outside the remit of the Fund

A grant will not be made in respect of the following:

(a) Losses arising solely by reason of professional negligence by a defaulting practitioner, or the employee or manager of a defaulting practitioner.

(b) Losses which are the personal debts of a defaulting practitioner and where the facts would not otherwise give rise to a claim on the Fund.

(c) The loss results from, but does not form part of, any misappropriation of, or failure to account for, money or money's worth.

(d) The loss results from the trading debts or liabilities of the defaulting practitioner.

(e) The loss amounts to a claim for contractually agreed interest between the applicant and the defaulting practitioner.

(f) The SRA was not notified of the applicant's loss in accordance with rule 10.

(g) The loss occurred in relation to an overseas partnership which does not fall within rule 15, 27(1)(c) or (2)(b) of the Solicitors' Code of Conduct 2007, unless:

(i) the loss occurred as a result of a solicitor's dishonesty, or

(ii) the loss occurred as a result of failure to account by a solicitor acting as a named trustee.

(h) The application is by the Legal Services Commission for loss occasioned through making regular payments under the Commission's contracting schemes for civil and/or criminal work.

8. Undertakings

A grant in respect of a failure by a defaulting practitioner to comply with an undertaking will be considered if it can be shown that the undertaking was given in the course of the defaulting practitioner's usual business acting on behalf of a client, that the recipient acted reasonably in accepting the undertaking and placing reliance on the undertaking and that:

(i) the undertaking was given with dishonest intent for the purpose of procuring money or money's worth, or

(ii) the undertaking, although not given with dishonest intent, is subsequently dishonestly not performed for the purpose of procuring money or money's worth.

The SRA does not consider the giving of an undertaking in circumstances which amount to the giving of a bare guarantee of the defaulting practitioner's personal liabilities, or the financial obligations and liabilities of a client or third party, to form part of the usual business of a solicitor or other legal practitioner.

9. Multi-party and multi-profession issues

(1) Where the loss has been sustained as a result of the combined activities of more than one party, (e.g. a defaulting practitioner conspires with an accountant or surveyor, or is assisted by a negligent accountant or valuer) the SRA will consider the role of each contributing factor in causing the applicant's loss. The SRA will base any grant on its assessment of that portion of the loss primarily attributable to the acts of the defaulting practitioner as opposed to that portion which is primarily attributable to the acts or omissions of the other parties, or to other factors. The SRA may decide to make a grant on a pro-rata basis in accordance with its assessment of the importance of each contributing factor in the loss, or may reject an application in its entirety if it is of the opinion that the loss was primarily due to other factors rather than the defaulting practitioner's dishonesty.

(2) When a solicitor, registered European lawyer or registered foreign lawyer is practising as the manager or employee of a body authorised not by the SRA but by another approved regulator, the SRA will not consider any claim in respect of that individual's act or default, or his or her employee's act or default.

(3) When an individual authorised not by the SRA but by another approved regulator is practising as the manager or employee of a recognised body, the SRA will in its discretion consider a claim in respect of that individual's act or default.

10. Applications: form and time limit

Every application must be delivered to the SRA, in such form as may from time to time be prescribed by the SRA, within twelve months after the loss, or likelihood of loss, or failure to account, as the case may be, first came, or reasonably should have come, to the knowledge of the applicant. The SRA may extend this period if satisfied that there are circumstances which justify the extension of the time limit.

11. Documentation in support

The burden of proving a claim rests with the applicant who must provide such documentation as may be required by the SRA including when requested, a statement of truth. Failure to provide such documentation or to co-operate with the SRA will be taken into account when determining the merits of the application.

12. Exhausting other remedies

(1) A grant may be refused or limited where the loss or part of the loss is an insured risk or where the loss is capable of being made good by some other means.

(2) The SRA may, before deciding whether to make a grant, require the applicant:

(a) to pursue any civil remedy which may be available to the applicant in respect of the loss,

(b) to commence insolvency proceedings,

(c) to make a formal complaint to the Police in respect of any dishonesty on the part of the defaulting practitioner or

(d) to assist in the taking of any action against the defaulting practitioner.

(3) In the absolute discretion of the SRA, a grant may be made before requiring the applicant to resort to other means of recovery.

13. Notice to defaulting practitioner

(1) The SRA shall not make a grant unless:

(a) a communication has been sent to the defaulting practitioner at his, her or its last known correspondence address or to his, her or its appointed representative informing the defaulting practitioner of the nature and value of the application; and

(b) not less than eight days have elapsed since the date of receipt of such communication, which shall be regarded as the day following the date of the communication.

(2) If it appears to the SRA that any communication sent under paragraph (1) will not come to the attention of the defaulting practitioner or his, her or its appointed representative, then the SRA may make a grant notwithstanding failure to comply with the provisions of this rule.

14. Costs

(1) **Litigation**

Where an applicant intends to or has already instituted proceedings for recovery of his loss and wishes to apply for a grant in respect of the costs of the proceedings, the SRA will only consider such costs where:

(a) they can be shown to be proportionate to the loss and the amount likely to be recovered, or

(b) the proceedings were necessary for the making of an application to the Fund.

(2) **Application costs**

Where a grant is made, the SRA may consider an application for a further grant in respect of the reasonable costs properly incurred by the applicant with either his solicitor or other professional adviser, provided that such costs were incurred wholly, necessarily and exclusively in connection with the preparation, submission and proof of the application.

(3) **Costs where the defaulting practitioner has failed to complete work**

If the defaulting practitioner did not complete the work for which he was paid, a failure to account shall be deemed to have arisen within the meaning of rule 3(2)(b) of these rules. In such circumstances, the SRA may consider making a grant in respect of the additional reasonable legal costs incurred by the applicant in completing the outstanding work or a grant by way of contribution towards those costs.

15. Interest

(1) The SRA may consider an application for a supplementary grant by way of a sum in lieu of lost interest on a principal grant. Such interest will be calculated in accordance with the rates prescribed from time to time by the SRA. This will normally be calculated from the day the loss which was the subject of the principal grant was incurred, up to the next working day after payment of the principal grant. Such payment will take into account that a grant is a gift and is therefore not subject to tax.

(2) Where the application for the principal grant is in respect of a failure to redeem a mortgage, the SRA may also make a grant in respect of the additional interest accrued to the mortgage account as a result of the defaulting practitioner's failure to redeem.

16. Maximum grant

Subject to rule 23, the maximum grant that may be made is £2million.

17. Recovery and subrogation

Where a grant is made otherwise than by way of loan or if by way of a loan repayment of the loan is waived or otherwise the borrower has failed to repay part or all of the loan, the Society shall be subrogated to the rights and remedies of the person to whom or on whose behalf the grant is made (the recipient) to the extent of the amount of the grant. In such event the recipient shall if required by the SRA whether before or after the making of a grant and upon the SRA giving to the recipient a sufficient indemnity against costs, prove in any insolvency and/or winding-up of the defaulting practitioner and sue for recovery of the loss in the name of the recipient but on behalf of the Society. The recipient shall also comply with all proper and reasonable requirements of the SRA for the purpose of giving effect to the Society's rights and shall permit the SRA to have conduct of such proceedings.

18. Reduction in grants

Where an applicant or the applicant's servant or agent has contributed to the loss as a result of his, her or its activities, omissions or behaviour whether before, during or after the event giving rise to the application, the SRA may, in the exercise of discretion and to the extent that such activity, omission or behaviour has contributed to the loss, reduce the amount of any grant that may be authorised or reject the application in its entirety.

19. Deduction from grants

(1) The SRA may deduct from any grant the costs that would have been legally due to the defaulting practitioner so that the applicant will not be in a better position by reason of a grant than he, she or it would otherwise have been in.

(2) The SRA may within its discretion deduct from any grant all monies already recovered by an applicant and monies which either will be or should have been recovered.

20. Refusal of an application

(1) If the SRA refuses to make a grant of either the whole or part of the amount applied for, the applicant will be informed in writing of the reasons for the decision.

(2) The fact that an application has been rejected does not prevent a further application being submitted provided that substantial new relevant evidence, information or submissions are produced in support of the new application.

21. Appeals

Should the applicant wish to appeal against refusal of an application, written notice of intention to appeal must be delivered to the SRA within thirty days of the date of receipt of the decision, which shall be regarded as the day following the date of the written communication of the decision. Such notice must be accompanied by details of the grounds of appeal together with any additional evidence in support.

22. Notice of requirements

Any requirement of the SRA under these rules will be communicated in writing.

23. Waivers

The SRA may waive any of the provisions of these rules except rules 13 and 20 to 24.

24. Repeals and commencement

(1) These rules shall come into operation on [1 March 2009], whereupon

(a) the Solicitors' Compensation Fund Rules 1995 shall cease to have effect save in respect of applications submitted before that date, which shall continue to be subject to the 1995 rules; and

(b) the Solicitors' Compensation Fund (Foreign Lawyers' Contributions) Rules 1991 shall cease to have effect.

(2) On [1 July 2009] rule 4 shall be amended as follows:

(a) in paragraph (2):

(i) delete "cancelled under regulation 8 of the European Lawyers Registration Regulations 2000" and substitute "revoked under regulation 9.2(a)(ii) of the SRA Practising Regulations [2009]"; and

(ii) delete "suspension or cancellation" and substitute "suspension or revocation";

(b) in paragraph (3):

(i) delete "had expired for non-renewal under regulation 8.3" and substitute "was suspended or was revoked under regulation 9(c)"; and

(ii) delete "expiry" and substitute "suspension or revocation"; and

(c) in paragraph (4):

(i) delete "cancelled under Schedule 14 paragraph 3(4)(a) of the Courts and Legal Services Act 1990" and substitute "revoked under regulation 9.2(a)(ii) of the SRA Practising Regulations [2009]"; and

(ii) delete "suspension or cancellation" and substitute "suspension or revocation".

ANNEX D

England and Wales High Court (Chancery Division) Decisions

Neutral Citation Number: [2006] EWHC 480 (Ch)

Neutral Citation No: [2006] EWHC 480 (Ch)

IN THE HIGH COURT OF JUSTICE
CHANCERY DIVISION

Royal Courts of Justice
Strand
London WC2A 2LL

March 14 2006

B e f o r e :

MR JUSTICE LAWRENCE COLLINS

In the Matter of the interventions into the solicitors' practices known as Ahmed & Co, Biebuyck Solicitors, Dixon & Co and the practices of Mr Zoi

and

In the Matter of Sections 35 and 36 and Schedules 1 and 2 of The Solicitors Act 1974

and

In the Matter of the Law Society Compensation Fund Rules 1995

Mr Timothy Dutton QC, Mr John Nicholls and Miss Abigail Doggett (instructed by Russell-Cooke) appeared for the Law Society in its role as Statutory Trustee
Miss Patricia Robertson (instructed by Field Fisher Waterhouse) appeared for the Law Society in its role as Trustee of the Compensation Fund.

HTML VERSION OF JUDGMENT

Mr Justice Lawrence Collins:

I The Law Society and its powers of intervention

1. The Law Society is a corporate body which represents the solicitors of England and Wales. The Law Society's regulatory functions under the Solicitors Act 1974 ("the 1974 Act") are exercisable against solicitors regardless of whether or not those solicitors are members of the Law Society, and are exercised by the Law Society as a public body and in the public interest.

2. Under section 35 of the 1974 Act, the Law Society has power to intervene into solicitors' practices. Every year, there are between 50 and 100 such interventions. The grounds for an intervention are set out in Part I of Schedule 1 to the 1974 Act. Typically, interventions will occur when the Council of the Law Society has reason to suspect dishonesty on the part of the solicitor concerned (or his employees) or where there has been failure by the solicitor to comply with the Solicitors' Accounts Rules 1998. Interventions are also necessary in other circumstances, such as when a solicitor is incapacitated by age or illness, is made bankrupt, is imprisoned, has been struck off or suspended from practice, abandons his practice, is practising uncertificated, has previously been the subject of an intervention on grounds of suspected dishonesty and within 18 months is found practising as a sole solicitor, or when the personal representative of a deceased solicitor practising alone prior to death is guilty of undue delay in connection with the solicitor's practice.

3. The powers exercisable on intervention are set out in Part II of Schedule 1 to the 1974 Act. By paragraph 5(1) the court may, on the application of the Law Society, order that no payment shall be made without the leave of the court by any person of any money held on behalf of the solicitor or his firm. By paragraph 6:

> "(1) … if the Council pass a resolution to the effect that any sums of money to which this paragraph applies, and the right to recover or receive them, shall vest in the Society, all such sums shall vest accordingly (whether they were received by the person holding them before or after the Council's resolution) and shall be held by the Society on trust to exercise in relation to them the powers conferred by this Part of this Schedule and subject thereto upon trust for the persons beneficially entitled to them.
>
> (2) This paragraph applies...
>
> (a) where the powers conferred by this paragraph are exercisable by virtue of paragraph 1, to all sums of money held by or on behalf of the solicitor or his firm in connection with his practice or with any trust of which he is or formerly was a trustee;
>
> (b) where they are exercisable by virtue of paragraph 2, to all sums of money in any client account; and
>
> (c) where they are exercisable by virtue of paragraph 3, to all sums of money held by or on behalf of the

> solicitor or his firm in connection with the trust or other matter to which the complaint relates."

4. By paragraph 9, the Law Society may require production of the solicitor's practice documents. The powers to vest monies in the Law Society and to obtain possession of practice documents can be exercised in combination: ***Sritharan v Law Socie***ty [2005] EWCA Civ 476, [2005] 1 WLR 2708, at [46].

5. If the Law Society takes possession of any sum of money to which paragraph 6 applies, it must pay it into a special account in the name of the Law Society or in the name of a person it has nominated on its behalf or in a client account of a solicitor nominated on its behalf. The monies in the hands of the nominated person or solicitor are held on trust on the same terms as the Law Society holds it on trust, that is (paragraph 7(1))

> "on trust to exercise in relation to them the powers conferred by [Part II of Schedule 1] and subject thereto on trust for the persons beneficially entitled to them".

6. These powers are exercisable notwithstanding any lien on the money or documents concerned or any right to their possession: paragraph 12.

7. Under paragraph 13, the costs incurred by the Law Society for the purposes of Schedule 1, including the costs of any person exercising the powers in Part II of Schedule 1 on behalf of the Law Society, are to be paid by the solicitor (or his personal representatives, if appropriate) and are recoverable as a debt owing to the Law Society.

8. By paragraph 16 of Schedule 1: "The Society may do all things which are reasonably necessary for the purpose of facilitating the exercise of its powers under this Schedule." This is an ancillary power which is confined to facilitating the exercise of the express powers conferred by the Schedule: ***Rose v Dodd*** [2005] EWCA Civ 957, at [29]; see also ***Dooley v Law Society***, November 27, 2001, unreptd, at [13].

9. Intervention does not give the Law Society the power to take over the practice and to carry it on or to close it down. The Law Society does not become the administrator of the practice, nor a receiver or manager. The focus of the legislation is on precautionary and preventive powers. The ownership of the assets (apart from practice monies) and the goodwill of the practice remain with the solicitor and can be disposed of notwithstanding the intervention; but the solicitor's practising certificate is automatically suspended under section 15(1A) of the Act where the intervention is on grounds of suspected dishonesty or breach of the Solicitors' Accounts Rules or the solicitor has been committed to prison: ***Rose v Dodd*** [2005] EWCA Civ 957 at [24], [27].

10. The right to recover sums due from former clients to the solicitor remains vested in the solicitor. The solicitor alone can commence and pursue recovery proceedings, and the Law Society has no duty to pursue such proceedings. But any recovery effected by the solicitor would vest automatically in the Law Society subject to the statutory trust: ***Dooley v. Law Society***, ***supra***, at [9], [10].

11. The Law Society is required to serve on the solicitor or his firm, and on any other person having possession of sums of money to which paragraph 6 applies, a certified copy of the Council's resolution and a notice prohibiting payment out of any such sums of money: paragraph 6(3). A payment out at a time when such payment is prohibited by a notice by a person on whom the notice has been served constitutes an offence: paragraph 6(6).

12. The intervention process is compliant with Article 1 of the First Protocol to the European Convention on Human Rights, in that, although it does constitute an interference with a solicitor's peaceful enjoyment of his property, the interference is necessary in proper cases in the public interest: ***Holder v The Law Society*** [2003] EWCA Civ 39, [2003] 1 WLR 1059.

II The Compensation Fund

13. The Compensation Fund is established under section 36 of the 1974 Act, funded by annual contributions paid by practising solicitors (Schedule 2, paragraphs 2 and 6(a)), out of which grants may be made by the Law Society for the purpose of relieving loss or hardship caused by dishonesty or failure to account. The Compensation Fund is not a legal entity, and the fund is held and administered by the Law Society.

14. Such a fund was first established under the Solicitors Act 1941, the purpose being then to relieve or mitigate losses sustained by any person in consequence of dishonesty on the part of a solicitor.

15. The Council of the Law Society may make a grant out of the Compensation Fund where it is satisfied that:

    (1) a person has suffered or is likely to suffer loss in consequence of dishonesty on the part of a solicitor, or of an employee of a solicitor, in connection with the solicitor's practice or purported practice or in connection with any trust of which that solicitor is or formerly was a trustee; or

    (2) a person has suffered or is likely to suffer hardship in consequence of failure on the part of a solicitor to account for money which has come into his hands in connection with his practice or purported practice or in connection with any trust of which he is or formerly was a trustee; or

    (3) a solicitor has suffered or is likely to suffer loss or hardship by reason of his liability to any of his or his firm's clients in consequence of some act or default of any of his partners or employees in circumstances where but for the liability of that solicitor a grant might have been made out of the Compensation Fund to some other person.

16. The purpose of the grant must be to relieve the loss or hardship of which the Council was satisfied in order to consider making the grant. It is possible for the Compensation Fund to make a grant under (c) above in the form of a loan: section 36(3). The Council has to give reasons for a refusal of a grant: section 36(7).

17. The Compensation Fund Rules 1995, together with the guidelines published by the Law Society, give an indication of how the Law Society is likely to exercise its discretion when faced with an application for a grant. In particular:

    (1) Applications should be delivered to the Law Society within 6 months after the loss or likelihood of loss or failure to account first came or reasonably should have come to the knowledge of the applicant. This period of time can be extended in exceptional circumstances by the Council: Rule 6.

    (2) The Compensation Fund is reliant upon the applicant for full and frank disclosure of all material dealings between the applicant and the solicitor in cases where the solicitor's records are so bad that it is very difficult for the Law Society to establish with any degree of certainty what the state of the account was between the applicant and the solicitor. The Council may require an application to be supported by a statutory declaration and accompanied by any relevant documents. The failure to provide such documentation or co-operate with the Council's enquiries may be taken into account when consideration is given to the application: Rule 7.

(3) The Council may require an applicant to pursue an alternative civil remedy prior to the making of a grant; Rule 8. The Fund is a fund of last resort and grants may be refused where the loss is an insured loss or is capable of being made good by recourse to another person: Guideline 1(c). The Council does not usually make a grant where the application is based on the failure of a solicitor to comply with an undertaking. The purpose of the Fund is not to underwrite solicitors' undertakings: Guideline (3)(g).

(4) There is a cap of £1,000,000 on any grant made out of the Compensation Fund in respect of any individual transaction or matter: Rule 11.

(5) Where a grant is made, the Council may also consider an application for a further grant in respect of the reasonable costs properly incurred by the applicant with either his solicitor or other professional adviser exclusively and necessarily in connection with the preparation, submission and proof of the application: Rule 9.

(6) Where a grant is made, the Council may also consider an application for a further grant in lieu of lost interest on the principal grant. Such interest is normally calculated in accordance with rates prescribed from time to time by the Council: Rule 10.

(7) It is possible for the Council to make a payment of an interim grant, in cases of severe hardship, prior to completion of full investigation of the entire application, but only if it is satisfied that loss of an amount at least equal to the amount paid out by way of interim grant has been suffered: Guideline 5.

18. Paragraph 1 of Schedule 2 provides that the Compensation Fund is held on trust by the Law Society, "for the purposes" set out in section 36 of the Act and in Schedule 2.

19. In ***R v Law Society***, ***ex p Mortgage Express*** [1997] 2 All ER 348 Lord Bingham CJ said (at 359) that the Law Society would be in breach of trust were it to make a grant out of the Compensation Fund when the statutory criteria set out in section 36(2) were not satisfied. But it is clear from that decision that the trust is not an ordinary private law trust, but is a fund in relation to which (once the applicant qualifies for a grant) the Law Society has to exercise discretion or judgment in accordance with public law principles. Lord Bingham CJ said (at 360):

> "Any discretion … must be exercised reasonably, fairly, in good faith, so far as possible consistently and with regard to the objects of the legislation. But there is nothing to prevent the Law Society formulating and following policies which satisfy these criteria, provided they do not fetter their discretion by applying such policies inflexibly and without recognising that exceptional cases may call for exceptional exercises of discretion."

20. Applicants do not have a right to compensation which they are entitled to enforce; all they have is a right to seek a favourable exercise of discretion: ibid. See also ***R v Law Society, ex p Reigate Projects Ltd*** [1993] 1 WLR 1531, at 1543-1544; ***R v Law Society, ex p Ingman Foods Oy Ab*** [1997] 2 All ER 666; ***R v The Law Society, ex. p. Nielsen***, December 3, 1998, unreptd.; ***The Mortgage Corporation v Law Society***, December 15, 2000, unreptd. at [13], [14].

21. The powers of intervention on grounds of "reason to suspect dishonesty" enable the Law Society to exercise control over those solicitors whose conduct might give rise to claims against the Compensation Fund, claims which ultimately have to be met by the profession as a whole: ***Sritharan v Law Society*** [2005] EWCA Civ 476, [2005] 1 WLR 2708 at [18]; ***Pine v Law Society*** [2002] EWCA Civ 175, [2002] 1 WLR 2189 at [12].

22. The Compensation Fund pays the cost of interventions where the ground for intervention is reason to suspect dishonesty: Schedule 2, paragraph 7(e). This is

because interventions on grounds of dishonesty are in the interests of the profession as a whole, in that they may prevent further dishonesty on the part of the intervened in solicitor, which would, otherwise, result in further claims on the Compensation Fund from the victims of that dishonesty: ***Law Society v KPMG Peat Marwick*** [2000] 1 All ER 515, affd [2000] 1 WLR 1921. A consequence of the Law Society's exercise of its two basic powers of intervention (document possession and money vesting), in suspected dishonesty cases, is protection of the Compensation Fund.

23. To the extent that the Compensation Fund has made a grant to a person entitled to client account monies, it will be subrogated under section 36(4) to the right to receive any money that person would have received from the Law Society. Such recoveries will then be carried back to the credit of the Compensation Fund pursuant to Schedule 2, paragraph 6(f).

24. In practice, the Compensation Fund is subrogated to a significant number (in some cases, the overwhelming majority) of such persons' rights to such money in any given intervention. This is because, following an intervention, a significant number of persons usually make claims upon, and receive grants from, the Compensation Fund.

III The problem and the applications to the court

25. The same factors that prompt the Law Society to intervene into a practice frequently make the Law Society's task following intervention extremely difficult. In particular, it is often the case upon intervention that the solicitor's records (such as accounting records, client files and client ledgers) are in disarray, incomplete, or sometimes partially or completely non-existent, whether through dishonesty, incompetence, incapacity, abandonment or otherwise. Such problems may be long standing.

26. Moreover, there are often significant discrepancies between the sums of money recovered following an intervention and the money that should have been present in the solicitor's client accounts. In cases where there are such shortfalls, the Law Society must then determine how best to deal with the shortfall, in terms of distributions to be made of the funds recovered on intervention.

27. A solicitor stands in a fiduciary relationship to his clients: ***Nocton v Lord Ashburton*** [1914] AC 932; ***Moody v Cox & Hatt*** [1917] 2 Ch 71; ***Brown v IR***C [1965] AC 244; ***Boardman v Phipps*** [1967] 2 AC 4***6; Clark Boyce v Mouat*** [1994] 1 AC 428; ***Bristol & West Building Society v Mothew*** [1998] Ch 1; ***Hilton v Barker Booth & Eastwood*** [2005] UKHL 8, [2005] 1 WLR 567. Money on client account has often been said to be held on trust for the client: ***In re a Solicitor*** [1952] Ch 328; ***Target Holdings Ltd v Redfern*** [1996] 1 AC 421, 436; ***Twinsectra Ltd v Yardley*** [2002] UKHL 12, [2002] 2 AC 164, at [12] where Lord Hoffmann said: "Money on a solicitor's account is held on trust. The only question is the terms of that trust."

28. The solicitor's duties are underpinned by a regulatory regime whereby (a) the Solicitors' Accounts Rules require client money to be held in separate client bank accounts, prescribe the records which must be kept and the circumstances in which the solicitor is permitted to draw on client money and guard against the mixing of client money and office money; (b) clients have the right to apply to court (inter alia) for delivery of a cash account, a list of money held for the client and payment over of that money: CPR, r 67.2.

29. In intervention cases, the Law Society frequently inherits a disordered and chaotic situation, and must seek to understand, as best it can, such records as there are with the available resources it has, in order to distribute the monies it has removed from a solicitor's control to the clients or other persons who appear to the Law Society in all of these circumstances to be entitled to it.

30. It emerged, in the course of proceedings by Mr Halley against the Law Society (***Halley v Law Society*** [2003] EWCA Civ 97, [2003] WTLR 845), that there might have been inadvertent breaches of trust by the Law Society in its dealing with money vested in it upon intervention. In particular, the Law Society became concerned that insufficient efforts had been made pro-actively to identify, contact and account to clients (and others) for whom money was held. On intervention, current clients were generally told that there had been an intervention and who the intervening agent was, and told to apply to the Compensation Fund if they considered that they were owed monies (i.e. rather than being repaid money held for them in trust). The concentration upon current clients and the reactive nature of the process of expecting clients to apply to the Compensation Fund meant that there had been apparent failures to contact or account to clients for whom the solicitor had been holding money. There was also concern about the transfers being made into the Compensation Fund from money which was held on statutory trust in purported exercise of the Compensation Fund's rights of subrogation. As a result a continuing review was instigated.

31. It was found that in some dishonesty intervention cases (usually where there was a shortfall on client account) the money received from the intervention agents was paid direct into the Compensation Fund without waiting for aggregate grants from the Compensation Fund to exceed the amount received, probably because it was assumed that grants would in due course exceed that amount. In addition, funds in long-standing statutory trust accounts had been transferred into the Compensation Fund as part of a concern to clear old balances held.

32. As a result of detailed investigations a total of £2.7 million was in June 2004 repaid by the Compensation Fund to be held on statutory trust. The money represented repayment of erroneous transfers into the Compensation Fund since February 1999.

33. Subsequently the intervention processes have been reviewed and improved, and there has been a detailed analysis of all the trust accounts which the Law Society holds in order to ensure that so far as possible beneficiaries were accounted to where they could be identified and traced, and there has been put in place a system of evidence gathering to enable to Law Society to discharge its duties as statutory trustee.

34. Detailed instructions to intervention agents were issued and revised from time to time.

35. As a result of the new processes, instead of beneficiaries being required unnecessarily to apply to the Compensation Fund, intervention agents and/or the Law Society have been able to distribute funds to beneficiaries where the client account has been reconciled and verified as intact, and almost £15.8 million was distributed in this way in relation to interventions effected between April 2002 and April 2004.

36. But there are significant problems relating to client accounts which impact on the ability of the Law Society to identify and trace beneficiaries and distribute funds. For example (i) there may be a shortfall of funds on client account; (ii) there may be no proper records detailing amounts held or on whose behalf they are held (since dishonest solicitors sometimes deliberately destroy all records); (iii) documents, files or other records may be missing; (iv) there may be a lack of accounting material to enable the Law Society to reconcile the accounts at the date of intervention or subsequently; (v) there may be false accounting entries concealing misappropriation, and, consequently, the beneficiaries; (vi) books may purport to balance but the solicitor's "clients" who have been providing funds to the solicitor may themselves be involved in fraud, money laundering, theft or false accounting and may not be the true beneficial owners of the funds; (vii) the intervened solicitor may not cooperate; (viii) the firm's staff may not cooperate because they have not been paid; and (ix) there may be a generally chaotic situation, involving angry and upset clients, utilities being cut off and equipment being repossessed.

37. These problems make it difficult, and sometimes impossible, for the Law Society as statutory trustee to establish who is beneficially entitled to the funds on client account.

38. Where there are problems, some clients will receive in effect their full beneficial entitlement by way of payments from the Compensation Fund, and in those cases the Compensation Fund has rights of subrogation under section 36(4) of the 1974 Act, and as a consequence distribution may be possible to the Compensation Fund (like any other beneficiary) from money held on statutory trust. But before any money can be paid to the Compensation Fund it is necessary to determine how much of that money belonged to the recipient of the grant.

39. The consequence is that there are the following problems. In the past when clients came forward to claim funds, unless the accounts were clearly intact, they were generally told to apply to the Compensation Fund, whereas in fact they were entitled to their share of the money held on statutory trust and should not have had to apply to the discretionary Compensation Fund. As a result it is possible that clients who were entitled to money but were refused a discretionary grant would have been left uncompensated (e.g. as a result of the expiry of the time limit for applications to the Compensation Fund).

40. As a consequence of what is described as the aggregated basis, excessive sums were transferred from the statutory trust to the Compensation Fund. For example a client may have been paid 100% by the Compensation Fund, in a case where the client account was deficient by 50%, and yet the whole amount was transferred to the Compensation Fund from the statutory trust where the amount payable from the money held on statutory trust to the client would only have been 50%. The problem would be compounded if only some of the clients had been paid by the Compensation Fund. In addition the Compensation Fund was wrongly treated as having a subrogated claim in respect of interest and costs paid to the client.

41. It is accepted that the approach was mistaken. Section 36 of the 1974 Act does give the Compensation Fund a right of subrogation, in respect of the full amount of the grants made, but in exercising that right the Compensation Fund can have no greater claim against the client account than the client would have had. The client would only be entitled to recover from the client account his or her remaining share of the monies in that account and such interest as has accrued on that share (not any shortfall, nor interest on the shortfall). Further, the client could not claim against the client account for the costs of making a claim on the Compensation Fund (which the Compensation Fund reimburses in exercise of its discretion).

42. Where the statutory trust account is incomplete, the Law Society now recognises that, before making any distribution (including pursuant to a right of subrogation) the Law Society as trustee needs to have, so far as possible, identified precisely whose money has been lost or, where this has not been possible, to have arrived at a proper scheme of distribution for the remaining trust funds.

43. As a result of these problems, the Law Society has reviewed and rewritten intervention agent's instructions. It has established a new unit, the Post Intervention Unit ("PIU"), to ensure that clients are properly accounted to for their funds, and to correct past errors. The Law Society has separated decision making in relation to Compensation Fund grants and decisions about payments from monies held on statutory trust to the Compensation Fund. It has investigated possible overpayments to the Compensation Fund from statutory trusts, resulting in repayments of almost £3 million. The PIU has created a template to record all relevant information in respect of each statutory trust to enable an informed decision to be made by the Law Society as statutory trustee about distribution. The template acts as a guide to Law Society officers to enable them methodically to acquire all relevant evidence in relation to each statutory trust.

44. Very few people appear to have complained that they have not received what they would have been entitled to, and only two cases have been brought before the High Court of which the Society is aware, in respect of the Law Society's conduct under paragraph 6, post intervention. The first involved an unsuccessful claim by a broker involved in dishonesty: ***Halley v Law Society*** [2003] EWCA Civ 97, [2003] WTLR 845. The second involved proceedings brought by the Law Society for directions, and again the court was not critical of the Law Society: ***Law Society v Soulimov***, May 27, 2002, unreported. Two cases were also pursued by claimants arising from an intervention into a firm called J.R. Sierzant & Co, but the amounts involved totalled less than £10,000 and the matters were dealt with in the County Court.

45. Because of the difficulties inherent in identifying persons entitled to any given amount of money, no payments have been made to the Compensation Fund by way of subrogation since 2001, except in cases where the client account was intact (or what is known as a top up grant was made) and therefore full distribution was possible. As at November 30, 2004, the total sums amounted to some £44 million. There were over 950 statutory trust accounts, although some of them were very small, and 85% of the funds were held in 161 of the accounts. By October 31, 2005 the amount locked up in the statutory trusts had increased to £52.55 million (of which 35% represent funds to which the Compensation Fund might be entitled by way of subrogation). It is undesirable for the Compensation Fund and the profession to have uncertainty, not least because this may affect the size of the Compensation Fund and the level of contributions which may be required from the profession in each year to maintain it.

46. The Law Society has applied to the court for directions relating to the exercise of its powers as statutory trustee, and in particular as to whether its duties are the same as those of a trustee under a private trust, or are affected by the statutory nature of the trust and its status in public law. The court plainly has jurisdiction. If the trust is to be treated as a private law trust the court obviously has jurisdiction to lend assistance in the form of guidance concerning specific questions that arise in the execution of the trust, and in particular whether some proposed action is within the trustees' powers, or is a proper exercise of the trustees' powers.

47. Should the Law Society be exercising public statutory functions under statutory trusts and not private law trusts, then the Law Society brings these matters before the court in order to demonstrate how it has been reaching decisions to date and resolving difficulties to date and how it would propose to do so going forward. If statutory power to seek directions were required (which I do not think it is) paragraph 16 of Schedule 1 would provide it.

IV The applications and the issues

A. Four test cases

48. In order to check how the newly designed processes were operating and to identify any issues arising, the template system was tested by reference to a sample group of 60 statutory trusts, arising from 60 different interventions. From this sample of 60, four specific cases were identified to bring before the court because they raise particular problematic issues.

(1) Ahmed & Co

49. Mr Sheikh Rahim Ahmed practised in Wembley. His practice involved a large amount of immigration work. An inspection of Mr Ahmed's books of accounts and documents began in October 2000. Mr Ahmed told the Forensic Investigation Unit that he was practising alone, not in partnership, with eleven members of staff.

50. The Law Society's Compliance Board Adjudication Panel ('the Panel') resolved to intervene into Ahmed & Co on December 20, 2001 and intervention notices were served on January 3, 2002. The intervention was on grounds of (a) suspected dishonesty on the part of Mr Ahmed and (b) failure to comply with the Solicitors' Accounts Rules and/or the Solicitors' Practice Rules.

51. The Panel's resolution included a resolution under paragraph 6. The sum of £75,662.03 was frozen in the general client account and designated deposit accounts held by Ahmed & Co.

52. When compared with other interventions, the accounting records of Ahmed & Co were, in fact, very good. The amounts shown as due in the solicitor's accounting records tallied with the amounts recovered from the Ahmed & Co bank accounts. The accounts were up to date to the end of December 2001, a few days before the intervention, and when updated they reconciled. On the basis of all the available information, there did not appear to be any deficit.

53. The Compensation Fund paid out grants to a substantial number of Ahmed & Co former clients and/or others beneficially entitled to money in the client accounts. Its subrogated claims amounted to about £38,000 (inclusive of interest), which was paid to it on December 22, 2004.

54. As a result of such good records and, most importantly, the fact that there was not a shortfall in funds as at the date of intervention, the Law Society decided that it was possible, in this case, to distribute to those entitled whom it was possible to locate and contact. Just over £10,000 of the trust fund remains undistributed.

55. The Part 8 Claim in respect of this intervention was issued on January 17, 2005 with the Court's permission without any defendants.

56. Mr Ahmed was served several times at different addresses with the claim form and evidence in support of the claim. The papers first served on Mr Ahmed at 54 High Road, Willesden Green, under cover of a letter dated January 19, 2005, were returned. Service was effected at a different address found in Law Society records, 48 Hazel Road, London, by letter dated July 1, 2005. Nothing was heard from Mr Ahmed. However, Mr Ahmed and others involved in the firm have been struck off the Roll of Solicitors.

(2) Biebuyck Solicitors

57. Anthony Biebuyck had been a sole practitioner since 1993, practising in Chelmsford. He had a general practice, for the purposes of which he employed 14 staff, including an assistant solicitor.

58. There was an inspection of Mr Biebuyck's books of account and other documents carried out in August 2002. Following this, the Law Society intervened into Biebuyck Solicitors on grounds of (a) suspected dishonesty and (b) failure to comply with the Solicitors' Accounts Rules. The Professional Regulation Adjudication Panel's resolution included a resolution under paragraph 6. Intervention notices dated 14th October 2002 were served on Barclays Bank Plc and the Royal Bank of Scotland.

59. £180,267.54 was frozen in the practice's general client accounts on October 15, 2002. A further £32,547.71 was recovered after the intervention.

60. Mr Biebuyck was struck off the Roll of Solicitors on October 30, 2003.

61. The records were up to date to 2 months before the intervention, but the client accounts were not intact at the time of the intervention. Not all of the money that should have been in the accounts was present, and many of the client files were

missing, hampering attempts to understand and reconcile, if at all possible, the discrepancies. The shortfall identified is the sum of £130,311.83. There are some examples of ledger debit entries for some clients, which if netted off would lessen the shortfall.

62. The Compensation Fund has submitted subrogated claims to £364,100.13 principal. This sum is clearly well above the amount of money (just over £200,000) currently held by the Law Society, highlighting the deficit existing in this case. It is also an indicator that the majority of persons potentially entitled to funds have probably made a claim on and received a grant from the Compensation Fund (which is now subrogated to their entitlements).

63. The possibility was contemplated of an interim distribution of the sum of £166,050.56 to the Compensation Fund from the funds, which sum must on any view (that is, on the basis that the existing uncertainties are resolved unfavourably as far as its potential entitlement is concerned) be due to the Compensation Fund. In this case, it has not yet, in fact, been made.

64. The Part 8 Claim in respect of this intervention was issued on January 17, 2005 with the Court's permission without any defendants.

65. Mr Biebuyck was served, under cover of a letter dated January 19, 2005, with the claim form and evidence in support, and replied by e-mail on January 20, 2005 confirming that, whilst he was willing to help if he could, he did not want to be represented in the proceedings.

(3) Dixon & Co

66. Anne Christine Dixon had a general practice as a sole practitioner in Oxford Street, London. She also practised in partnership under the name of Dixon Emberton. However, this partnership was not the subject of an intervention.

67. An inspection of Ms Dixon's books of accounts and other documents was commenced in November 2001. Ms Dixon told the Forensic Investigation Unit that she had been practising alone since 1987 and that she had been severely affected by the death of her partner and office colleague and, as a result, had allowed matters relating to the proper running of her practice to drift.

68. The sole ground for intervention into Dixon & Co was failure to comply with the Solicitors' Accounts Rules. The Professional Regulation Adjudication Panel also resolved that all monies within paragraph 6(2)(a) would be vested in the Law Society. Intervention notices were served dated March 5, 2002, and sums totalling £31,120.75 were recovered from the Dixon & Co general client accounts.

69. The records were written up to six days before the intervention, and the practice bookkeeper then wrote them up to the intervention date. The client accounts were not intact at the time of the intervention. In fact, a considerable shortfall in funds has been identified, in the order of £251,000. Corresponding with this shortfall is a very large debit balance in the name of one client, a Mr H, who was sued to judgment by the Law Society for the money he was overpaid from the Dixon & Co client accounts. However, whilst a judgment has been obtained, Mr H has declared himself bankrupt and there do not currently appear to be any assets against which the judgment can effectively be enforced.

70. After the intervention, Ms Dixon remitted to the Law Society sums totalling £14,563 to seek to reduce the shortfall in funds somewhat. The shortfall identified takes into account these additional sums.

71. The Compensation Fund has submitted subrogated claims amounting to £288,275.74 principal. A sum that is clearly substantially more than the funds (£45,683.75) available for distribution. This does indicate that many persons have made claims against the Compensation Fund and that the Compensation Fund grants have, in many cases, alleviated the problems of the deficient client accounts for the client/person entitled to the funds in the account, leaving the Compensation Fund to bear the loss (in that it is unable, through its subrogated claims, to recover all of the money it has paid out by way of grants).

72. However, some discrepancies appeared, in the course of investigation, between the Compensation Fund's subrogated claims as calculated by the Compensation Fund itself and as calculated by the Law Society in its capacity under paragraph 6. These discrepancies have been the subject of ongoing investigation and resolution.

73. The Part 8 claim form for this claim was issued, without defendants with the permission of the court, on July 4, 2005.

74. Ms Dixon was served with a copy of the claim form and accompanying evidence in support under cover of letter dated July 5, 2005. Ms Dixon responded with some comments on the evidence on July 14, 2005. She indicated that she did not wish to be joined to these proceedings, but indicated that she may write again with further comments.

(4) Zoi & Co/Lancaster Bailey

75. Farooq Zoi practised under the name of Zoi & Co and under the name of Lancaster Bailey in Plaistow and Edgware Road. He had previously operated in partnership, but at the time of the intervention was a sole practitioner. His was a general practice employing 20 un-admitted staff.

76. The Law Society carried out an inspection into Mr Zoi's books of accounts and other documents between October 2000 and June 2001. The Professional Regulation Adjudication Panel resolved to intervene into any practices or the remainder of any practices, which Mr Zoi conducted as a principal, on the grounds of (a) suspected dishonesty and (b) failure to comply with the Solicitors' Accounts Rules. The resolution included a resolution under paragraph 6.

77. An intervention notice dated June 14, 2002 was served on Barclays Bank and a total sum of £37,002.47 was frozen in the client accounts of Lancaster Bailey and Zoi & Co.

78. The accounting records recovered at the time of the intervention were (compared with the other three cases) very unreliable. They were significantly out-of-date and much of the underlying material, such as client files, was missing. The accounts had only been written up to 18 months before the intervention, and it was not possible to reconcile the accounts from the client ledger list.

79. However, once served with these proceedings, Mr Zoi produced a client ledger list for May 2002, the month before the intervention, which appeared to reconcile to the bank statements for that month. The additional material has been the subject of analysis by the accounting department working for Russell-Cooke, the solicitors for the Law Society, albeit with an element of caution given the manner in which the additional material was produced.

80. The Compensation Fund has thus far made subrogated claims amounting to £21,669.40, and there are some applications made for grants to be paid out of the Fund still pending.

81. The new information produced by Mr Zoi does not alter the approach in his case. It may result, subject to further verification if possible, in additional sums being distributed to other clients, if they can be located, shown in the client ledger list for May 2002 produced by Mr Zoi. The amount remaining undistributed, even if the information can be verified and relied upon, will be £6,075.11.

82. The claim form for this case was issued, again without defendants but with the permission of the Court, on July 4, 2005.

83. Mr Zoi was served by way of letter dated July 5, 2005 with the claim form and supporting evidence. He has been involved in proceedings with the Law Society, appearing at the Solicitors Disciplinary Tribunal in August 2005. He confirmed by way of e-mail dated July 26, 2005 that he does not wish to be joined to the proceedings.

B. The issues

84. The Law Society has identified the following issues:

(1) What, on a proper construction, is the nature of any obligations imposed upon or powers vested in the Law Society under section 35 and paragraph 6? The Law Society's submission is that references to trusts in paragraph 6 should be construed as references to statutory public law trusts, as opposed to private law trusts.

(2) If considered to be a private law trustee, is the Law Society entitled to take into account the issue of proportionality, as between cost incurred and results achieved, when identifying beneficial entitlement and beneficiaries of the trust funds vested in it under paragraph 6, and in discharging any obligation as a private law trustee to identify, ascertain and contact beneficiaries of the trust?

(3) Is the Law Society entitled to verify accounting records from a sample of client files, as opposed to every client file that has been uplifted at the time of intervention, the sample being selected on a case by case basis, reasonably and proportionately appropriate to the facts of each particular case?

(4) Where it is not reasonably and proportionately possible to reconcile and verify the client account monies with a client ledger list or lists as at the date of intervention, may the Law Society compile a best list of entitlement to the funds (known as "the Best List") from the material (including accounts records, primary accounts material such as bank statements, client files, client ledger lists and Compensation Fund information) reasonably and proportionately available to it?

(5) May the Law Society net off debit and credit ledgers in the name of the same client, so that that client's entitlement, if any, to the funds vested in the Law Society is calculated using the aggregate balance over all of his or her ledgers, where the Law Society has taken reasonable and proportionate steps to verify that the debit ledger represents money withdrawn from the client account for or on behalf of the client whose name appears on the ledger?

(6) May the Law Society re-allocate transactions posted to a suspense ledger to named ledgers where, following reasonable and proportionate inquiries into those transactions, there is sufficient information, applying a reasonable and proportionate approach, to indicate that it is correct to do so?

(7) May the Law Society rely on the balances shown on ledgers and the debit postings made to those ledgers, save where there is evidence which puts the Law Society on notice that particular balances may be wrong and that particular debit postings may not be reliable as an indication of the solicitor's use of a particular client's money? If so, the Law Society then need only conduct reasonable and proportionate enquiries, before coming to a view as to what is to be regarded as the

correct balance on any particular ledger. Where there is evidence that a debit transaction out of the client account was made for or on behalf of the client or with the client's money, to whose ledger the debit was posted, should that debit posting remain posted to the ledger, notwithstanding the fact that the debit was or may have been unauthorised by the client?

(8) May the Law Society, in its capacity as statutory trustee under paragraph 6, rely on the verification exercise carried out by the Compensation Fund, to identify what subrogated claims the Compensation Fund has to the funds vested in the Law Society under paragraph 6, and only investigate such claims where the amount of any particular claim exceeds that which the Law Society, in its capacity under paragraph 6, believed, prior to intimation of the claim by the Compensation Fund, could be claimed in respect of that particular client?

(9) Where there is no evidence of a bill, or other written notification of the costs incurred, having been sent to the client or paying party, are sums of money on a client ledger, which might represent payments made on account of costs or be equivalent to the costs incurred on behalf of that client, to be held for the client and not for the solicitor? In determining whether the sums of money should be held for the client or the solicitor, need the Law Society only conduct reasonable and proportionate enquiries?

(10) May the Law Society determine entitlement to the funds vested in it, having regard to any shortfall in the client account(s) at the date of intervention, and the most reasonable and proportionate manner of allocating the shortfall as between all of the clients who had money deposited in the client account(s) prior to the intervention, taking note of principles of private trust law governing allocation of deficiencies in trust funds?

(11) Is the Law Society's advertising campaign, which has regard to section 27 of the Trustee Act 1925, a rational approach in seeking to determine entitlement to funds vested in the Law Society under paragraph 6, alternatively, if held to be a private law trustee, is it a proper discharge of the Law Society's obligation to ascertain beneficial entitlement to the trust funds?

(12) Should the Law Society make reasonable and proportionate attempts to contact persons entitled to the funds vested in the Law Society under paragraph 6, including a current general approach, but without fettering discretion, and dependent upon the given facts, of contacting persons with an apparent entitlement over about £75 where current contact details are known or considering tracing persons with a ledger balance over £500 where current contact details are not known?

(13) May the Law Society retain, from the undistributed surplus of funds, money as reimbursement for its costs incurred properly and reasonably in determining entitlement to the funds and effecting a distribution of the funds to those entitled thereto?

85. Accordingly, the Law Society seeks a number of orders and declarations in relation to these interventions, which include (depending on the problems encountered in relation to each of the practices):

(1) An order approving the process adopted by the Law Society to create a best list of beneficiaries of the trust and their entitlements to trust money ("the Best List") as a proper discharge of its obligation as a trustee to ascertain the beneficiaries of its trust.

(2) An order directing that the Law Society may in creating the Best List, in the cases of clients with both verified credit and debit balances, net the same off against each other.

(3) An order approving the process adopted by the Law Society to create the list of beneficiaries of the trust (including the process of verification of a sample of client files as opposed to every single client file) as a proper discharge of its obligation as a trustee to ascertain the beneficiaries of its trust.

(4) A declaration as to the beneficial entitlement of the solicitor to trust money on account of unbilled work carried out for some of the clients whose ledgers are included in the Best List.

(5) An order approving that distribution to the beneficiaries of the trust be approached based on the Best List of beneficiaries and their respective entitlements to trust money.

(6) An order approving that distribution to the Compensation Fund be approached based on its subrogated rights to trust money as set out in the Law Society's distribution list.

(7) Given that there is a shortfall in trust money as compared to the entitlement to trust money recorded in the Best List, an order approving distribution, allocating the identified shortfall on a pro rata basis, to all beneficiaries, including the Compensation Fund by way of subrogation, without retention of any trust money or other security, save for the undertaking given by each claimant to repay any overpayment of trust money made to the claimant, as set out in the claim form filled in by the claimant.

(8) An order approving an approach to distribution to the Compensation Fund based on its subrogated rights to trust money and, in so far as is necessary, the determination of the existence and/or extent of those subrogated rights.

(9) An order approving the process adopted by the Law Society to contact and obtain information from beneficiaries, in order to distribute to them their share of the trust money, as a proper discharge of its obligation as a trustee to notify beneficiaries of the trust and to seek to make a distribution of trust money to them.

(10) An order approving distribution (without retention of any trust money or other security, save for the undertaking given by each claimant to repay any overpayment of trust money made to the claimant, as set out in the claim form filled in by the claimant) in which the trust money is allocated between all beneficiaries, including the Compensation Fund by way of subrogation, on a last in last out basis applying the rule in ***Clayton's Case***, and in which, in the absence of evidence identifying all of the beneficiaries to the trust money on the foregoing basis, all those beneficiaries identified recover their full entitlement to trust money.

(11) An order directing that any money remaining, after a distribution to beneficiaries has been effected so far as is reasonably possible, can be retained by the Law Society as reimbursement for its costs and expenses in administering the trust.

86. The Law Society accepts that, if the court holds that the Law Society, whilst bound by statutory duties, is not a private law trustee, there may be no need to continue to determine the majority of the other matters. But the Law Society submits that it would still be necessary or desirable to consider the specific issues arising in these test cases for the following reasons: (a) given the complexity of the points in issue, the Law Society needs to be confident that the court has considered its approach; (b) consideration of these matters should serve to demonstrate to the court some of the very considerable difficulties encountered by the Law Society in administering these funds, even where, as in the test cases, very considerable resources have been devoted to them and reinforce the points made in support of the Law Society's primary submission that there are difficulties inherent in construing paragraph 6 as creating private law trusts; (c) consideration of these matters enables the court to

have a factual matrix against which to make the decision as to how best to construe paragraph 6.

87. In summary the Law Society in its capacity as statutory trustee argues that the trust is subject to public law for these reasons. First, monies held on trust under paragraph 6 are expressly subject to the powers conferred by Part II of Schedule 1, and the fact that the trust may be subject to such powers is inconsistent with a private trust. Second, the Law Society's position as statutory trustee is analogous to that of a trustee in bankruptcy in that a trust is created in circumstances where there is often financial chaos and the trustee has no idea who all the beneficiaries are or how the trust will be divided. Third, the expression "trust" is not a term of art and its meaning depends on the context. Fourth, it would be highly inconvenient if the trust were a private law trust: it might fail for uncertainty of beneficiaries; it might fail for evidential uncertainty owing to the often uncertain or incomplete nature of the solicitors' records in these cases. Consequently, paragraph 6 creates two stages. Stage one creates a statutory purpose trust whereby monies are held to exercise in relation to them the powers conferred by Schedule 1, including determining entitlement to the funds. Stage two creates a secondary statutory trust for those who have been determined to be entitled in stage one.

88. In its capacity as trustee of the Compensation Fund, the Law Society puts forward for the assistance of the court the contrary arguments. They are in summary these: the fact that a trust does not fulfil all the traditional criteria does not mean that it is not a private law trust. The relevant feature of a trust is that there is a separation of legal title and beneficial interest. The fact that the interest cannot be ascertained until claims are established and verified does not prevent the court from recognising the trust. Parliament would not have intended that private law trust duties over client account monies should be converted to public law duties on intervention. This is further confirmed by the absence of any express obligation to distribute or power to recover costs. If it had been intended to remove the pre-existing private trust there would be clear wording to that effect. The legislative history provides no evidence that Parliament intended to impose a public law trust. A private trust analysis is not unworkable. Proportionality is relevant in private law. Conceptual and evidential uncertainty relate solely to express trusts. There is no absolute need to inform beneficiaries of claims. It would be sufficient for the statutory trustee to take out insurance in respect of any liability from late-emerging beneficiaries or alternatively to provide undertakings to replace any overpayment. The statutory trustee's duty to act reasonably and proportionately would be fulfilled in these circumstances by the compilation of a Best List.

V The paragraph 6 trust

89. The Solicitors Act 1974 was a consolidating Act. The wording now contained in Section 35 and Schedule 1 was first introduced in the Solicitors (Amendment) Act 1974, section 8 and Schedule 1.

90. The origins of the intervention jurisdiction were in the Solicitors Act 1941, by which the Compensation Fund was established. The Compensation Fund was established to make discretionary grants in dishonesty cases, and by section 2(2) it was to be "held by the Society in trust for the purposes" provided in section 2 and the First Schedule, and any rules made under section 2. The power to intervene was confined to dishonesty cases, and to a power to require production of documents and a power to ask the court to prohibit payments by the solicitor's bank without the court's permission: Schedule 1, paragraphs 4 and 5.

91. The power to intervene was subsequently extended to cases where a solicitor had been struck off or suspended: Solicitors (Amendment) Act 1956, section 9. No provision was made by that Act for the funding of interventions on this ground.

92. Those provisions were consolidated in the Solicitors Act 1957, which by sections 31 and 32 introduced separate Schedules for intervention (Schedule 1) and the Compensation Fund (Schedule 2). Schedule 1, paragraph 7, provided for the Law Society to apply to the court for an order prohibiting payments from bank accounts of the solicitor or his firm. By Schedule 2, paragraph 1, the Compensation Fund was to be held on trust by the Law Society, and by paragraph 7(e), it was provided that the costs of interventions on the grounds of dishonesty should (as before) be borne by the Compensation Fund.

93. The Solicitors Act 1965 extended the circumstances in which the intervention powers could be exercised (to encompass also undue delay, bankruptcy etc, and deceased solicitors' practices in certain circumstances). It also extended the nature of the powers, giving the Law Society for the first time a power to resolve to take control of monies: all the powers were set out in Schedule 1 which was substituted for Schedule 1 to the 1957 Act.

94. Schedule 1 to the 1965 Act enabled the Law Society to require production of documents and (for the first time) to take control of monies:

(1) By paragraph 7, the court was given the power, on the application of the Law Society, to order that no payment be made by a bank from any account in the name of the solicitor or his firm without leave of the court.

(2) By paragraph 10, the Law Society was given the new power, exercisable on a resolution of the Council, to take control of all sums of money due from the solicitor to clients, or held by the solicitor for clients, or subject to a trust of which the solicitor was trustee.

(3) By paragraph 12, the Law Society was able to pay such monies into special accounts and "may operate on, and otherwise deal with, such special …accounts as the solicitor or his firm might have operated on, or otherwise dealt with, the said banking account."

(4) By paragraph 13(1), the Law Society was able to serve a notice on the solicitor or other persons directing the transfer of monies in accordance with the directions of the Society "provided that …no such directions shall be given by the Society except with the approval of the person to whom the said moneys belong, being in the case of a trust the trustee, and, where the solicitor is the sole trustee or a co-trustee thereof only with one or more of his partners, clerks or servants, the person beneficially entitled to such moneys". By paragraph 13(2), the Law Society was given express power to apply to the Court for directions "where the Society is unable to ascertain the person to whom the said monies belong or where the Society otherwise thinks it expedient so to do."

(5) By paragraph 17, the Law Society was given express power to make regulations with respect to the procedure to be followed in giving effect to the provisions of, inter alia, paragraphs 10, 12 and 13(1), and with respect to any matters incidental, ancillary or supplemental to those provisions.

95. The Solicitors (Amendment) Act 1974 replaced the existing powers, by repealing section 31 of the 1957 Act, the substituted Schedule 1 thereto and the relevant provisions of the 1965 Act. In Schedule 1 the 1974 Act set out both the circumstances in which the powers could be exercised (which were extended to include failure to comply with accounts rules or indemnity rules) and also the powers themselves. There was no change to the position whereby the Compensation Fund continued to fund dishonesty interventions. The Solicitors (Amendment) Act 1974, Schedule 1, paragraph 6(1) (which is reproduced in the 1974 Act, Schedule 1, paragraph 6(1)) introduced the trust concept for the first time in the context of interventions.

96. A review of the potentially admissible materials from 1973-4 (including minutes of the relevant Standing Committee) has revealed nothing that sheds light on the meaning of the word "trust" in paragraph 6 of Schedule 1 to the 1974 Act (or on that word in the Solicitors (Amendment) Act 1974)).

97. There are a number of differences between the trust created by the Act under Section 36 and Schedule 2 and that created under Section 35 and Schedule 1.

98. First, paragraph 3 of Schedule 2 contains a specific power to invest the Compensation Fund. There is no such specific power in relation to the trusts created under paragraph 6. I accept the Law Society's point that this is consistent with the view that the Compensation Fund is a trust fund which it is expected that the Law Society will hold onto, maintain and administer, as paragraph 1 of Schedule 2 states, and from which grants will be made from time to time in the exercise of the Law Society's discretion: but the trusts created by paragraph 6 are expected to be transient, short term trusts, in respect of which it is envisaged that the Law Society will distribute the funds to those entitled to it as soon as it is in a position to do so following the intervention.

99. Second, there is provision made for the Law Society to protect itself against too many claimants against the Compensation Fund. Paragraph 5 of Schedule 2 permits the Compensation Fund to insure the Fund for such purposes and on such terms as the Council may deem expedient. In fact, this has not been done since it would prove to be too expensive. There is no such provision made in respect of the funds vested in the Law Society under paragraph 6. There is no explicit guidance in the Act as to how the Law Society should handle a situation, following intervention, when the client accounts prove to be deficient and there are insufficient funds to meet all of the claims made (notwithstanding the fact that this is, unfortunately, a very common situation).

100. Third, grants are made out of the Compensation Fund according to the exercise of its discretion, which it exercises specifically and explicitly to compensate the most deserving of applicants: cf ***R v Law Society, ex p Mortgage Express*** [1997] 2 All ER 348, 360. By contrast, on an intervention, the Law Society holds the money on trust for the purpose of the exercise of its powers, and according to the beneficial interests in it. "It has no general discretion to pay it to the most deserving of beneficiaries": ***Halley v Law Society*** [2003] EWCA Civ. 97, [2003] WTLR 845, at [41].

101. The wording of the trust created by Schedule 2 is more obviously in line with the creation of a statutory purpose trust than that of the wording of the trust created by paragraph 6. Paragraph 1 of Schedule 2 states "the fund … shall be held by the Society on trust for the purposes provided for in Section 36 and this Schedule", whereas paragraph 6 states "all such sums…shall be held … on trust to exercise in relation to them the powers conferred by this Part of this Schedule and subject thereto upon trust for the persons beneficially entitled to them."

102. If the paragraph 6 trust were a private law trust, then it would import the duties of a private law trustee. Those duties would include the following: first, a trustee has to ascertain the identity of the beneficiaries, and to ascertain their beneficial entitlement. Second, a trustee is obliged to inform a beneficiary of full age and capacity of his interest in and rights under the trust: ***Lewin on Trusts*** (17th ed. 2000, Mowbray et al), para 23-03. Third, a trustee is obliged to give beneficiaries a full and accurate record of the stewardship and management of the trust, and is required to keep and render proper, clear and accurate financial accounts: ***Lewin on Trusts***, para 23-05. Fourth, a trustee has to distribute to the correct beneficiaries of a trust fund, and that obligation is a strict obligation: ***Lewin on Trusts***, para 26-03. This principle is onerous and places a trustee in a demanding position, in terms of correctly distributing to the right beneficiaries of the trust.

103. The Law Society argues that in practice the imposition of private law trust principles on the Law Society might render the scheme created by Schedule 1 unworkable. The reality is that the Law Society is in a fundamentally different position from that of a private law trustee. When (unlike a private law trustee) the Law Society is required to try to reconstruct from (often extremely poor or possibly fraudulent) records who might be entitled to the client account monies, and how much of the monies those persons might be entitled to receive in any distribution, it is unworkable to impose upon the Law Society a strict obligation to distribute to the "right" beneficiaries only. Such a conclusion overlooks the reality that seeking to ascertain who are the "right" beneficiaries involves numerous decisions and the exercise of discretion on the part of the Law Society. Normally a trustee would be under a duty to look to trust records which would ordinarily exist in a private law trust to inform the trustee about the state of the trust, the identity of the trust property and trust beneficiaries etc. The Law Society is in a very different position. It must look to the solicitors' accounting records, but it must do so in a situation where the very reason why it has become a trustee of the client account monies, in the first place, is usually linked to some deficiency in those accounting records. If the Law Society is not able to take those decisions, and exercise its discretion, in a manner which will only be overturned if it has acted in an irrational and unreasonable manner etc, it becomes almost impossible to administer the funds vested in it upon each intervention. To obtain any kind of certainty, the Law Society may well have to burden the court with frequent applications for directions and approval of the decisions it had taken or was proposing to take.

104. I am satisfied that the Law Society's position, that its duties in relation to the paragraph 6 trust are grounded in public law, is correct. This is so for the following reasons.

105. There is no doubt that the duties of the Law Society in relation to the Compensation Fund are duties grounded in public law. Grants are made out of the Compensation Fund according to the exercise of its discretion, which it exercises specifically and explicitly to compensate the most deserving of applicants: cf ***R v Law Society, ex p Mortgage Express*** [1997] 2 All ER 348, 360. The wording of the trust created by Schedule 2 is more obviously in line with the creation of a statutory purpose trust than that of the wording of the trust created by paragraph 6. Paragraph 1 of Schedule 2 states "the fund … shall be held by the Society on trust for the purposes provided for in Section 36 and this Schedule."

106. In ***Law Society v Soulimov***, May 27, 2002, unreported, it was assumed that paragraph 6 involved a private law trust. Mr Soulimov demanded payment of money (which he alleged was his) from the client account vested in the Law Society following intervention into Mr Simms' practice. The Law Society was concerned as to the propriety of paying the money out, because of the quality of the evidence it had, and commenced an application for directions from the court, as a private law trustee would. In the application, the Law Society took a neutral role and surrendered its discretion to the court. In that case the primary question now before the court was not the subject of argument.

107. In regulating the profession, the Law Society performs a public duty: ***Law Society v KPMG Peat Marwick*** [2000] 1 All ER 515, [33], affd [2000] 1 WLR 1921 at [16], [19] and [23]. In ***Swain v Law Society*** [1983] 1 AC 598, at 607-608, Lord Diplock said that the Law Society has both a private capacity and a public capacity. When acting in its private capacity it was subject to private law, but

> "It is quite otherwise when the Society is acting in its public capacity .. The Council in exercising its powers under the Act to make rules and regulations and the Society in discharging functions vested in it by the Act … are acting in a public capacity and what they do in that capacity is governed by public law; and although the legal consequences of doing it may result in creating rights enforceable in private law, those rights are not necessarily the same as those that

> would flow in private law from doing a similar act otherwise than in the exercise of statutory powers" (at 608)

108. Similarly Lightman J said in ***Law Society v Dooley***, ***supra***, at [12] that the approach of the Law Society – namely, to allow the solicitor supervised access to these documents for the purposes of the solicitor recovering unpaid costs due to him at the time of the intervention (notwithstanding the fact that the costs of such supervision might make costs recovery economically unattractive or unviable) - reflected a fair and reasonable balance in accord with the Law Society's public law duties as a public body to protect the interests of the solicitor's former clients.

109. The starting point is the construction of paragraph 6 in Schedule 1. The wording does not give an answer, and, as has been seen there is no relevant legislative history. But Parliament must be taken to have known that the Law Society might well be acquiring depleted funds, that it might not know where the beneficial interest lay, and might not know who the potential beneficiaries might be. The Law Society had to look to the solicitor's accounting records, in a situation where the very reason why it has become a trustee of the client account monies, in the first place, would often be linked to some deficiency in those accounting records.

110. The use of the word "trust" does not conclude the matter. The word "trust" is defined in the Act as follows (at section 87(1)): " 'trust' includes an implied or constructive trust and a trust where the trustee has a beneficial interest in the trust property, and also includes the duties incident to the office of a personal representative, and 'trustee' shall be construed accordingly." This definition is not exhaustive and is of no assistance in relation to the present question. The same word "trust" is used in both Schedule 2 and Schedule 1 to impose different obligations on the Law Society and "trusts" of differing natures, which indicates that the word is not a term of art, but means different things even within the same Act.

111. There is no doubt that when the word "trust" is used in a statute it does not necessarily mean a classic private trust. Thus in ***Tito v Waddell (No. 2)*** [1977] 1 Ch 106 the relevant Ordinance described the resident commissioner as being paid compensation to hold on trust on behalf of the former owner or owners of a native or natives of the colony subject to such directions as the Secretary of State may from time to time give. Sir Robert Megarry V-C said (at 211) that, when the word "trust" was used one has to look to see whether in the circumstances of the case, a sufficient intention to create a true trust is manifested: "One cannot seize upon the word 'trust' and say that this shows that there must therefore be a true trust" (at 227).

112. In ***Ayerst v C& K (Construction) Ltd*** [1976] AC 167 it was held that an order winding up a company divested the company of the beneficial ownership of its assets for the purposes of its unrelieved losses and capital allowances being used by a successor company. In the context of the question whether the company still retained legal ownership of its assets, Lord Diplock discussed the analogous position of the assets of a bankrupt, the legal title to which vests in the trustee in bankruptcy. Lord Diplock referred (at 178) to the example of a trustee in bankruptcy as a "trust" imposed by statute which clearly did not have all the indicia of a private law trust. One of the reasons for this was that, in the course of administration of the bankrupt's estate, prior to the submission of all the proofs from the creditors of the bankrupt, the trustee had no way of knowing all of the beneficiaries for whom he was administering the estate, and the shares in which he would distribute the estate. Lord Diplock went on to say that the label "statutory trust" can be understood as characterising a trust that does not bear all the indicia of a trust as would be recognised by a Court of Chancery apart from the statute. He said (at 180) that all that may be meant by the use of the word "trust" was giving property the essential characteristic which distinguishes trust property from other property; namely, it cannot be used or disposed of by the legal owner for his own benefit but must be used or disposed of for the benefit of others.

113. Accordingly, it does not follow that, when the word "trust" is used, that brings with it the full range of trust obligations attendant upon a traditional private law trust, particularly so when the trust is imposed by statute and is in the context of the exercise of a public function. The meaning of a word depends on its context. Thus in ***Brooks v Brooks*** [1996] AC 375, where the question was the meaning of the word "settlement" in the Matrimonial Causes Act 1973. Lord Nicholls said (at 391): "In English law 'settlement' is not a term of art, with one specific and precise meaning. Its meaning depends on the context in which it is being used."

114. In my judgment the background to the need for the powers and the structure of Part II of Schedule 1 make it clear that the paragraph 6 trust was not intended to be, and could not have been intended to be, an ordinary private law trust. The Law Society inherits, like a trustee in bankruptcy, a situation not of its own making including records which are often in a chaotic state, in which it does not know initially where all the funds lie, and then, having recovered the funds, does not know who the claimants to the funds are. It has, nonetheless, to determine entitlement to the funds and distribute to those identified as claimants to the funds. It would be difficult if the Law Society were, in that context, to be burdened with overly excessive or onerous duties as a private law trustee under paragraph 6. I accept the Law Society's submission that the trust created under paragraph 6 can be labelled a statutory trust. Similarly, the term "beneficiaries" can be used, in the sense of statutory beneficiaries entitled under paragraph 6 to a share of the funds vested in the Law Society (as opposed to beneficiaries of a private law trust).

115. This approach is also supported by the consideration that the Law Society needs to be able to act efficiently in circumstances where there may be many clients involved (***cf. R v Takeover Panel, ex p Datafin plc*** [1987] 1 QB 815, 840), and it is not likely that it could have been envisaged that the Law Society would constantly be applying to the court for directions of the kind sought in this case.

116. Such an interpretation would also avoid the danger that the trust might be void. Were the trust under paragraph 6 a private law trust it would be a fixed trust, and not a discretionary one. A fixed trust with conceptual and/or evidential uncertainty is a void trust, and a fixed trust is only valid if it is possible to draw up a complete list of the beneficiaries at the time of distribution: ***Lewin on Trusts***, para 4-30. I accept that it is by no means certain that failure to identify the clients would make such a private law trust invalid, and certainly a court would do everything it could to find it valid, but it would be an odd interpretation of paragraph 6 to allow it to result in a situation where it is possible that some trusts were valid, because of the good level of accounting records maintained by the solicitor prior to intervention, and others (those, often in fact, where intervention was required the most) were void for evidential uncertainty. The only way in which to ensure that all of the trusts created under paragraph 6 are valid, no matter how bad is the level of evidence as to beneficiaries, is to recognise that the trust created under paragraph 6 is not a trust subject to the usual rules, such as evidential certainty, imposed upon such fixed private trusts.

117. I consider that the analogy of liquidators and trustees in bankruptcy is an apt one. They inherit the company's or individual's affairs when they are financially in a mess and, very often, there is a deficit between the available assets and the total potential claims for a share in the assets. The purpose of their appointment is to wind up the company's or individual's affairs and distribute such assets, as are recovered and available, to the creditors. Similarly, the Law Society intervenes and, in some, limited, senses, winds up the practice that is the subject of the intervention. It is not an administrator, but it is terminating the practice of the individual solicitor, at least so far as it relates to historic client matters. It inherits a situation, often, financially in a mess where there is a deficit between the funds in the client accounts and the potential claims to those funds and it, too, has to distribute the monies it recovers to identified claimants.

118. Consequently, I do not consider that in exercising the power under paragraph 6 the Council of the Law Society is effecting an assignment of the trusts constituted by the client accounts, such as it was in the hands of the solicitor. It is legally divesting the solicitor of legal ownership of the funds and vesting the same in the Law Society, and also creating a new trust upon which the funds are to be held. The solicitor did not hold the funds on trust to exercise in relation to them the powers conferred by Part II of Schedule 1. On the other hand, paragraph 6 specifically provides that the funds are to be held on trust to exercise in relation to them the powers conferred by Part II of Schedule 1, and only subject thereto on trust for the persons beneficially entitled to them.

119. This solution effectively involves two forms of statutory trust. A statutory purpose trust first arises whereby the monies are held to exercise in relation to them the powers conferred by Schedule 1, which includes the ancillary power in paragraph 16. The statutory purpose trust must include the purpose of determining who are beneficially entitled to the funds in order that the funds can be held for those who are entitled to them. A second statutory trust arises under paragraph 6, namely, for the persons beneficially entitled to the funds.

120. The Law Society therefore has a statutory power to determine who is entitled to the funds under paragraph 6. That does not mean that it has a discretion as to who is beneficially entitled: ***cf Roy v Kensington and Chelsea and Westminster Family Practitioner Committee*** [1992] 1 AC 624; ***Trustees of the Dennis Rye Pension Fund v Sheffield City Council*** [1998] 1 WLR 840; ***Steed v Secretary of State for the Home Departmen***t [2000] 1 WLR 1169. In taking steps to determine who is beneficially entitled, it must exercise the power in a way that is bona fide, rational, reasonable, takes into account relevant considerations and does not take into account irrelevant considerations. The exercise of the power would be subject to review on public law grounds. So also the statutory power to distribute must be exercised in accordance with public law principles.

121. The Law Society accepts that private law trust principles and the claims of the clients to the monies prior to the intervention would be relevant: ***cf R v Tower Hamlets LBC, ex p Chetnik Developments Ltd*** [1988] AC 858, 882, per Lord Goff of Chieveley. The Law Society, in exercising its power rationally and reasonably, would need to take into account and give due weight to principles of trust law in, for example, arriving at a Best List of whom it reasonably considers to be, on the available information, the most probable persons entitled to the fund vested in itself.

VI Other matters

122. Accordingly most of the other questions which the Law Society has brought before the court do not, strictly, arise for determination. I have set out the relevant material on these questions in an appendix to this judgment, together with my views on the approach which the Law Society has taken. But there are three matters with which I should deal at this point.

A Unbilled costs

123. The first relates to the position of unbilled costs. I am satisfied that the Law Society is right to proceed on the basis that where there is no evidence of a bill, or other written notification of the costs incurred, having been sent to the client or paying party, sums of money on a client ledger, which might represent payments made on account of costs or be equivalent to the costs incurred on behalf of that client, are to be held for the client and not for the solicitor. In determining whether the sums of money should be held for the client or the solicitor, the Law Society need only conduct reasonable and proportionate enquiries.

124. It is common for clients to pay solicitors money on account of the solicitors' costs or on account of unpaid professional disbursements. This money is client money and, as such, has to be held in a client account: Solicitors' Accounts Rules ("SAR 98"), r.13 and the notes thereto, and r.19(4). One of the fundamental principles of the SAR 98 is that client money is kept separate from office money, which belongs to the solicitor; see SAR 98, r.1(b), r.13(c), r.19(1)(a)(i).

125. In order for money to be transferred properly from a solicitor's client account to office account, certain procedures have to be followed, as laid down in the SAR 98. Under rule 19(2), the solicitor must first give or send a bill of costs or other written notification of the costs incurred to the client or to the paying in party, whenever he properly requires payment of his fees. Once that has been done, the money then becomes office money and must be transferred out of the client account within 14 days: see r. 19(3). Consequently it has been held that a solicitor cannot transfer small, old balances existing on client ledgers to his office account without raising a proper bill prior to the transfer: ***Doggett v Law Society***, February 21, 2000, unreported.

126. These are provisions of the SAR 98 that are often breached by solicitors who are then subject to intervention. It is not uncommon for solicitors who are the subject of inspections and/or interventions to have made round sum withdrawals on account of costs generally without reference to precise figures as should be contained in a proper bill of costs. Such round sum withdrawals are prohibited: note (x) to r. 19.

127. The Compensation Fund operates a policy whereby it may deduct, from any grant it makes to an applicant, the costs that would have been due to the solicitor provided that the work had been properly completed, so that the applicant is not in a better position by reason of a grant than he would otherwise have been. This is so, even if the intervened in solicitor did not hold a practising certificate at all material times: Guideline 11(a). It can mean there are situations in which the Compensation Fund makes a grant to an individual of less than the balance shown under the name of the individual on the Best List, having calculated itself what the likely costs of the work done by the intervened in solicitor on behalf of the applicant would have been. This leaves a small residual balance on the client's ledger, the beneficial entitlement to which the Law Society, in its capacity as statutory trustee, must determine.

128. While it is justifiable for the Compensation Fund, in the exercise of its discretion, to choose not to award a grant which includes sums of money, which it considers equivalent to the amount of work the solicitor concerned had carried out on behalf of the applicant, the Law Society is determining existing entitlement to the funds at the date of intervention.

129. I accept the Law Society's submission that the Law Society should treat money on a client ledger as held for the client and not for the solicitor. To do so would not undermine the solicitor's entitlement to be paid for work he has done and for fees properly incurred, should there be any. This is a personal remedy as between the solicitor and the client. It (and the lien which it triggers) is a separate question to that of entitlement to the money physically sitting in the client account at the date of intervention, subsequently vested in the Law Society.

130. The Law Society is mindful of the fact that the solicitor who has been the subject of an intervention may well have a considerable interest in being able to recover costs properly due to him, but in respect of which he has not been able, prior to the intervention, to bill his respective clients. To ensure that the interference with the solicitor's property is as little as is reasonably possible, the Law Society usually agrees to allow the solicitor supervised access to the files in order that he may take steps to recover costs due to him. The Law Society is entitled to do so, even though the costs of providing supervision of the solicitor (recoverable from the solicitor himself under paragraph 13 of Schedule 1) may render costs recovery by the solicitor economically unviable***: Dooley v Law Society***, ***supra***, at [11]-[12].

B Distribution in cases of deficiency

131. The second question to which I shall refer is the application of the Rule in ***Clayton's Case*** where there is a deficiency. I accept that the Law Society may determine entitlement to the funds vested in it, having regard to any shortfall in client account at the date of intervention, and the most reasonable and proportionate manner of allocating the shortfall as between all of the clients who had money deposited in client account prior to the intervention, taking note of principles of private trust law governing allocation of deficiencies in trust funds.

132. It is very common for there to be a deficit between the amount of money recorded as supposedly in client account at the time of the intervention and the amount of money that is, in fact, there and becomes vested in the Law Society. This may arise as a result of debit balances, representing the fact that sums of money have been spent on behalf of other clients who did not have money in the client account at the time the money was withdrawn on their behalf. Alternatively, the solicitor may have been dishonest and withdrawn money, to which he was not entitled, for himself or others and either posted such withdrawals dishonestly to named clients, or not bothered posting the withdrawals to any ledger. Alternatively, the solicitor may have failed properly or accurately to record withdrawals made from the client accounts for some time prior to the intervention.

133. The rule in ***Clayton's Case*** is still treated as the starting point: ***Lewin on Trusts***, para 41-52. Under that rule, those funds which are deposited with the solicitor first are the funds which are presumed to have been the first to leave the client account. However, it takes only a very small counterweight to displace the rule in ***Clayton's Case***: ***Russell-Cooke Trust Co v Prentis*** [2002] EWHC 2227 Ch, [2003] 2 All ER 478 at [55]. It is commonly recognised that a pari passu solution, in which all of the beneficiaries share the loss pro rata in accordance with the proportion of their beneficial entitlement to the fund as a whole, is the usual solution: ***Commerzbank Aktiengesellschaft v IMB Morgan Plc*** [2004] EWHC 2771 (Ch), [2005] 1 Lloyd's Rep. 298 at [47] and [48]. This solution was adopted in ***Barlow Clowes International Ltd (in Liquidation) v Vaughan*** [1992] 4 All ER 22.

134. In most intervention cases, there will be a counterweight. Payments into solicitors' general client accounts do not generally get paid out in the same sequence. Nor would any of the clients of the solicitor expect them to. Some clients' money sits in solicitors' accounts for some time, for example, if paid in as a payment on account of costs in ongoing litigation. Other money comes in and goes out again in a short space of time, for example, the purchase money remitted by a mortgage company to complete a conveyancing transaction. In ***Russell-Cooke Trust Co v Prentis*** Lindsay J said (at [58]) that he considered the pari passu approach to be the system least unfairly distributing loss on an account that should have been dealt with in accordance with SAR 98.

135. Accordingly, the pro rata approach is, in most cases, likely to be the most appropriate approach, simply because of the very nature of a solicitor's general client account. In addition, attempting to allocate a deficit on the basis of the "first in first out" rule would also be extremely impracticable. The evidence is that it is difficult enough, given the commonly found levels of available evidence, to reconstruct the accounts as at the date of the intervention with sufficient accuracy. The following problems arise in the application of the "first in first out" rule:

136. It would require the identification of all of the misappropriations from the client account. This would, itself, not necessarily be straightforward. Ledger balances which are in debit at the time of the intervention are an obvious place to start, but they are not the only possible source of misappropriations. There may have been unauthorised or improper withdrawals from the client account which were posted to a ledger sufficiently in credit, so that the net effect was that the credit on that ledger was reduced as opposed to creating a negative debit balance. The only way in which

those misappropriations could possibly be identified is if the Law Society went behind all the ledgers in credit, checking every transaction that had been posted to that ledger.

137. Even if all of the misappropriations from the client account could be successfully identified, then, in order to allocate them on a "first in first out" rule, a reconciliation of the account would be necessary as at the date of each misappropriation, together with a list of dates on which all of the funds present in the reconciled account had been deposited. The difficulties in achieving reconciliation at the time of the intervention demonstrate how difficult, time-consuming and expensive such a process would be. Equally, the further back in time the reconciliations go, the less evidence there may well be from which a reconciled account could be drawn up, and the greater chance that attempting to chase down evidence from missing files etc. would produce inconclusive or no results.

138. Assuming misappropriations could be successfully identified and reconciliations effected at each of the relevant dates, it may well be that the client's money presumed to have been used under the "first in first out" rule would have subsequently been used in a legitimate transaction. The rule in ***Clayton's Case*** is only an evidential presumption, rebuttable by contrary evidence. It would be incredibly onerous, and most likely not possible, to attempt to undo all of the legitimate withdrawals that took place after a misappropriation on the basis of an evidential presumption that money legitimately withdrawn for a client had earlier been presumed withdrawn under the rule.

C Costs reimbursement from undistributable sums

139. The third issue is whether, as it proposes, the Law Society may reimburse itself for costs out of undistributable sums. The relevant sums arise because there may be historic balances, which have remained on ledgers for long periods of time without any further movement on the ledger. There may be clients for whom up-to-date contact details are not available and who do not come forward in response to advertisement. There may be small sums for which any further work would be completely disproportionate to the amounts of money involved. These small sums, when added together over numerous interventions, amount to significant amounts of money.

140. The Law Society is proposing to retain the undistributable sums as reimbursement of the Law Society's properly incurred costs in determining entitlement to the funds and taking steps to distribute the funds to those it has determined to be entitled thereto. Costs would only be reimbursed from property that would not otherwise be distributed to clients, those clients not being reasonably and proportionately identifiable or contactable.

141. In addition, the Law Society has offered an undertaking to repay money retained as reimbursement to late-emerging beneficiaries. The undertaking would be limited to the total sum of money it had received as reimbursement for its costs. It would also be limited to a period of one year. The limitation of one year has been chosen in order that the Law Society may have some certainty after a reasonable period of time, in order to be able to know what financial liabilities it has going forwards, and rule out contingent liabilities going forward after a period of time has elapsed.

142. This would present no problem if the Law Society were a private law trustee, since it would be entitled to be indemnified out of the trust property for all expenses and costs incurred in connection with the performance of its duties: ***Lewin on Trusts***, paras 21-03–21-03E; Trustee Act 2000, section 31(1).

143. But if a public body is to levy a charge, there must be clear statutory authority to that effect: ***Attorney-General v Wiltshire Dairies Limited*** (1921) 37 TLR 884, affd (1922) 38

TLR 781, HL. Consequently, a public body charged with a public duty may not charge for carrying out the duty without specific statutory authority: Goff and Jones, ***Law of Restitution***, 6th ed. 2002, paras 10-019 – 10-024; ***Woolwich Building Society v IRC*** [1993] A.C. 70 at 155 per Lord Keith (dissenting), and 164-165 per Lord Goff of Chieveley. The authority must be express or arise by necessary implication: ***R v Richmond upon Thames London Borough Council, ex p McCarthy & Stone (Developments) Ltd*** [1992] 2 AC 48, at 74, per Lord Lowry. See also ***R v Greater Manchester Police Authority, ex p Century Motors (Farnworth) L***td, March 24, 1998, unreported.; ***R v Liverpool City Council, ex parte Barry*** [2001] EWCA Civ 384.

144. With some hesitation I have come to the conclusion that the Law Society is entitled to make the deduction from the undistributable funds. The fact that the relevant funds are undistributable is not relevant to the existence of the power, although it does mean that it is unlikely that there will be any prejudice to anyone if it should turn out that, contrary to my view, the Law Society has no power to deduct its costs. My reasons are these.

145. The essential question is whether, in the absence of an express power, there is any necessary implication that there is such a power. Against such an implication are the express provisions for costs. First, paragraph 13 of Schedule 1 provides that the solicitor is responsible for the costs, but the solicitor may have disappeared, and/or be bankrupt, and/or simply be unable to raise sufficient money to pay the costs. Second, the effect of paragraph 7(e) of Schedule 2 is that the Law Society's costs in dishonesty interventions are payable out of the Compensation Fund (about one-third of interventions). Nevertheless I consider that there is the necessary implication because although, in fact, the Law Society has sufficient funds to carry out the intervention exercise, it is not publicly funded and it might be possible to envisage cases in which it could not carry out the intervention exercise unless it could be satisfied that the costs would be met. The potential sources of recovery from the intervened in solicitor and the Compensation Fund should not preclude the Law Society being reimbursed out of money that will not otherwise be distributed, particularly if it may be that, in a given intervention, recovery under paragraph 13 is theoretical only and will not result, in reality, in recovery of all or part of the costs incurred. I do not consider that the ancillary power in paragraph 16 is a safe basis for reimbursement, but I do accept the alternative submission that the power to reimburse can derived from the general principle that where a person seeks to enforce a claim to an equitable interest in property, the court has a discretion to require as a condition of giving effect to that equitable interest that an allowance be made for costs incurred in connection with the administration of the property: ***cf Re Berkeley Applegate*** [1989] Ch 32.

146. I should record my gratitude to counsel and solicitors for the excellent and extremely thorough presentation of this interesting matter.

147. I will hear submissions of the form of the order.

Appendix

A1. I will set out in this Appendix the contentions of the Law Society in relation to the subsidiary matters which do not strictly arise for decision in the light of the ruling that the Law Society's duties are not those of a private law trustee, together with in each case my view of the procedure adopted or proposed to be adopted.

A. Verification of accounting records from a sample of client files

A2. The Law Society first seeks to reconcile such accounting records as it has following the intervention. Under rule 32(7) of the Solicitors' Accounts Rules ("SAR 98"), solicitors are obliged every five weeks (a) to compare the balance on the client

cash accounts with the balances shown on statements and passbooks (after allowing for unpresented items) of all general client accounts and separate designated client accounts, (b) as at the same date to prepare a listing of all of the balances shown by the client ledger accounts of the liabilities to clients and compare the total of those with the balance on the client cash account, and (c) to prepare a reconciliation statement which must show the cause of any difference in these comparisons. Although the strict obligation is to effect a reconciliation once every five weeks, the notes to the accounting rules strongly recommend writing up (and effecting a reconciliation of) the accounting records weekly, even in the smallest of practices, and daily in the case of larger firms.

A3. The current balance on each client ledger account must always be shown or be readily ascertainable from the solicitor's records: r.32(5).

A4. Often, when the Law Society intervenes, the solicitor has not been complying with these obligations and the Law Society must carry out its own reconciliation to ascertain whether or not the sums recorded in the solicitor's records, as held by the solicitor for each client, amount to the total the bank has recorded as deposited in the bank account(s). Even where there has been compliance, the records may not be up to date at the date of the intervention and may need to be brought up to date prior to effecting a reconciliation at the date of the intervention.

A5. In Ahmed & Co, Mr Ahmed's accounts were up to date as at the end of December 2001, a few days prior to the intervention and, when updated to the date of the intervention, they reconciled. Biebuyck Solicitors' records were up to date as at August 30, 2002, two months prior to the intervention, and also reconciled. Dixon & Co's records were also written up, six days prior to the intervention. The practice bookkeeper, upon request by the intervention agent, then wrote the records up to the date of the intervention. In the case of Mr Zoi's practices, at the time of the Law Society's first evidence, it appeared that the accounts had been written up to September 30, 2000 pre-dating the intervention (in June 2002) by over a year and a half. It was not possible to reconcile the accounts, from that client ledger list, as at the date of the intervention. Mr Zoi subsequently produced a client ledger list for May 2002, the month prior to the intervention, which appears to reconcile to the bank statements for that month.

A6. The Law Society proceeds to verify, if possible, the accounting records which are present. Verification involves looking at underlying client files in order to ascertain whether or not the client ledgers accurately reflect transactions that have taken place in relation to a particular client or matter.

A7. Some form of exercise of verification is important given that some solicitors who are the subject of interventions are known to falsify entries on ledgers in order to make the client ledgers reconcile with the amounts of money held in the solicitors' client bank accounts. When faced with an investigation into their accounts and records (often a precursor to an intervention), solicitors have been known to falsify records in order to eliminate discrepancies and achieve a reconciliation.

A8. But the number of files a solicitor holds is usually very considerable. It includes "dead" files concerning matters closed a long time prior to the intervention. In theory, it would be possible for a solicitor to falsify the client ledgers to make a ledger balance appear to be a nil balance and, therefore, a finished matter, when it was not in fact so. The only – and wholly impracticable – way in which the Law Society could know for certain that all of the seemingly finished matters were indeed finished is if it were to revisit all of the files relating to finished matters, and not just the files relating to live matters. Live matters are usually the focus of an intervention, because the client is more likely to be affected by the intervention.

A9. If the Law Society were required in all cases to examine all of the files a solicitor holds, it would make the process of intervention vastly more expensive and time-

consuming than it already is. The Law Society has adopted the approach of examining a sample of client files in order to verify reasonably and proportionately, if possible, the accounting records. By way of example, in Ahmed & Co, 10% of live client files were examined by the intervention agent. The sample represented client balances amounting to more than 50% of the funds held on trust under paragraph 6. The sample tallied with the accounting records, strongly suggesting that such records were accurate.

A10. The verification undertaken varies according to the circumstances of the individual case. For example, in Biebuyck Solicitors, the intervention agents had identified unusually large billing and, therefore, wished to examine more closely the reasonableness of billing in general. To do so, they examined dead files with a nil balance on the client ledger, as well as files relating to live matters, in order to examine the reasonableness of the billing of those cases and to identify any cases in which the client's ledger had gone into debit historically and the reasons for the client's ledger being allowed to go into debit.

A11. This reconciliation procedure reflects the procedure which the solicitor should have been following in any event, had he been complying with SAR 98. It is in line with private trust law requiring trustees to acquaint themselves with the trust and to read and consider the trust records. I accept, therefore, that it is a rational approach for a public body exercising public statutory functions to adopt, as well as being a proper discharge of a private law trustee's obligation to acquaint itself with its trust.

B Compiling a "Best List" of entitlement to the funds

A12. In the case of Ahmed & Co, the sample of files examined verified the accounting records, which was a relatively unusual case. It is possible in an intervention for there to be insufficient files to verify, as in the practices of Mr Zoi. It is also often the case that there are concerns when the files are examined, in relation to the accuracy of the accounting records, as in Biebuyck Solicitors.

A13. The initial reconciliation exercise, even if successful, may also throw up doubts because of the presence of debit ledger entries. Under SAR 98, r. 22(7), money held for a client in a designated client account must not be used for payments for another client. Under rule 22(6), a solicitor may make a payment in respect of a particular client out of a general client account even if no money or insufficient money is held for that client in the solicitor's general client accounts, so long as sufficient money is held for that client in a designated client account and the appropriate transfer is made immediately from the designated client account to the general client account.

A14. Overdrawn client ledgers (arising from debit ledger entries) suggest that withdrawals have been made from the client account, in breach of SAR 98, over and above the amount that that particular client had deposited in the client account, and that, therefore, another client's money has been withdrawn and used. Rule 1(d) states that solicitors must use each client's money for that client's matters only. Overdrawn ledgers suggest strongly that the client account is not intact and that there is insufficient money in the bank account to meet the claims of clients who have deposited money with the solicitor.

A15. The notes to SAR 98, r.32(7) also state that, when effecting a reconciliation, solicitors should not use the credits of one client against the debits of another, when checking whether the total client liabilities tally with the amount recorded as deposited in the client bank account. This is described as improper since it fails to show up the shortage. The initial reconciliations achieved in Biebuyck Solicitors and Dixon & Co only tally with the bank statements because the credits of one client are used against the debits of another client so that the net position is shown. This, superficially, conceals the shortage in trust funds. The shortage is revealed when a list of all of the ledgers in credit (ignoring the ledgers in debit) is compared with the available trust funds. The ledgers in credit represent potential beneficiaries of the trust funds and

their respective claims on the trust funds and this should be compared to the trust funds available for distribution. This has been done in both Biebuyck Solicitors and Dixon & Co and the shortage has been exposed.

A16. Although a reconciliation, in which debit ledger balances are used against credit ledger balances and the net position alone is compared against the bank balance of the client account(s), is limited in that, without more, it would conceal the extent of any shortfall on the account, it does, it is submitted, have some value: if a reconciliation can be achieved on that basis, it does suggest that the solicitor has recorded all of the withdrawals made out of the client account accurately, even if those withdrawals should not have been made since a client did not have the requisite money in the client account to permit a withdrawal in his name. It is always possible that a solicitor could have forged such postings in order to achieve a reconciliation, but, in the absence of evidence to suggest that that is so, and given that interventions can occur where the solicitor has been incompetent (for example, by permitting withdrawals in the name of a client when there was insufficient money in the client account to do so) but not dishonest, a reconciliation which demonstrates that the withdrawals have all, or mainly all, been accurately recorded by the solicitor is a useful starting point in the investigation into the entitlement to the funds.

A17. In cases such as Biebuyck Solicitors, Dixon & Co, or the practices of Mr Zoi, the Law Society must then proceed to consider how best it can arrive at a list of beneficiaries and beneficial entitlement to the trust funds.

A18. It does so by identifying the most up–to-date list that it can find of client ledger balances. If no list of ledger balances can be found, then alternative sources could be used, such as the list of applicants for a grant from the Compensation Fund or a list of current clients. The Law Society's agents then review such accounting information as there is (both primary and secondary such as solicitor's vouchers, solicitor's bank reconciliations, cheque book stubs, paying in books and bank statements) to see if the identified list can be updated by, for example, reposting un-presented items back to ledgers, or identifying unidentified transactions and posting them to the specific client to whose matter they related (this involves writing to third parties, such as banks, for details about unidentified transactions posted to suspense accounts).

A19. Compensation Fund information comes from all of the applications made to the Compensation Fund. In relation to those that are withdrawn, it is possible that they are withdrawn because, when the solicitor was notified of the intention to award a grant under Rule 14 of the Compensation Fund Rules, he made a direct payment to the applicant, obviating the need for a grant to be made from the Compensation Fund. If the direct payment made was made in respect of funds which were in the client account at the date of the intervention, the solicitor will then expect to be entitled to receive a share in the distribution based on an entitlement to those funds.

A20. The inherent difficulty in compiling a Best List is similar to that encountered in verification. It is theoretically possible to investigate further, in terms of investigating all of the nil balances and their underlying dead files. The client ledger balances represent, in some cases, months or years of different transactions in relation to a matter. It would theoretically be possible, but, again, obviously completely impracticable, for the Law Society to re-visit every single one of those transactions to see if what is entered on the ledgers accurately represents the transaction that took place, as recorded in the client file.

A21. Were the Law Society required to carry out such an activity, the costs in terms of time and finance would, again, be very substantially increased from the considerable level which they already reach. Interventions would, in all probability, become a wholly unmanageable burden for the Law Society.

A22. It is far from certain that such an exhaustive exercise would produce better results. Many of the dead files may date back considerably and further information

from the client may be difficult to obtain, given the lapse in time. The files themselves may appear to tell a different story to the accounting records because the files were not kept properly or have missing information. It may not be possible to find up-to-date contact details for third parties, such as clients, from whom additional information may be required to make sense of the files and/or of individual transactions that took place many months or years previously.

A23. Generally, a trustee does not have to look into all of the historic trust records to see if there might have been some misfeasance by a previous trustee: ***Lewin on Trusts***, para 12-58. Whilst the Law Society does not have to suspect dishonesty in relation to every ledger automatically, the difficulty it faces is that it is intervening in situations where the very reason why it is intervening might be sufficient to give a normal private law trustee grounds for investigating historic transactions concerning the trust. Often, the Law Society is on notice that the ledgers cannot necessarily be trusted or taken at face value and that there may well be errors in the trust accounts, such as they are, either through incompetence or dishonesty: ***Law Society v Soulimov***, May 27, 2002, unreported, at [71].

A24. I accept that the decision to compile a Best List and the manner in which it is compiled by the Law Society, in situations where reconciliation and verification are not possible on the available evidence, is a rational approach for a public body to adopt in exercising public statutory functions in determining entitlement to funds vested in it under paragraph 6. It is both reasonable and proportionate in the context of a body with finite resources exercising statutory powers given to it by Parliament in the interests of the public at large. If the Law Society were a private law trustee, such an approach would be a proper discharge of its obligation to ascertain beneficial entitlement to the trust funds.

C Ability to net off debit and credit ledgers

A25. It is normal for clients to instruct solicitors on various matters and to remit to the solicitor different amounts of money in relation to each separate matter. Under SAR 98, r. 29 the Council of the Law Society may publish guidance with the concurrence of the Master of the Rolls to assist solicitors in complying with SAR 98. The guidance is in SAR 98, Appendix 3. Paragraph 2.4 of the guidance states that ledger accounts should include the name of the client and contain a heading providing a description of the matter or transaction concerned. This means that it is common for the same client to have several ledgers headed with different matters, should that client have instructed the solicitor on more than one matter.

A26. If a client has a ledger balance which is in debit, this prima facie suggests that money was withdrawn on behalf of the client and for his benefit when the client had not deposited sufficient funds with the solicitor in relation to that matter for the withdrawal to be permissible. The client has effectively received an unauthorised windfall of funds that were not his.

A27. The loss of such a withdrawal is borne by the remainder of the clients who had deposited money in the client account, unless the client, in whose favour the withdrawal was made, had deposited other money in the client account in respect of other matters which had not been withdrawn at the time of the intervention. Such deposits would be represented by ledger balances in the same client's name but headed with the description of other matters, which were in credit at the time of the intervention.

A28. Such examples have arisen in these cases and the Law Society proposes to net off the ledger balances in credit and those in debit in the same client's name relating to different matters, since, then, the loss to the client account arising as a result of the debit balance will be borne solely by the client for whose benefit the withdrawal was made, as opposed to being borne by all of the other clients who did not receive any benefit from the withdrawal.

A29. The netting off approach can be said to be accepted implicitly by SAR 98. Rule 22(5) only prohibits the paying out of money from a general client account in relation to a particular client if the money to be paid out exceeds the money held on behalf of that client in all the solicitor's general client accounts. There is no requirement for the money not to exceed the money deposited by that client in respect of that particular matter. The solicitor must simply be aware of the total of all of the money deposited by that client in his general client accounts, and ensure that money paid out on behalf of that client does not exceed that total.

A30. Netting off is different to adjusting ledger balances by posting back to those ledgers sums that should not have been debited from them, e.g. because of post-intervention receipts correcting mistakes made earlier or because of un-presented cheques, or by reducing ledger balances to reflect sums which should have been debited from them, e.g. because of transactions going out of the client account posted to a suspense ledger that should have been properly posted to the client's ledger. Netting off occurs once the ledger balances have been finalised, so far as possible, and occurs in respect of ledgers that are in relation to different matters, so that, when receiving a share in the distribution of the funds, each client's entitlement to such a distribution is based on his aggregate position across all his ledgers, at the date of intervention.

A31. In clear-cut cases, there may seem to be no problem with the above approach. However, as is repeatedly the problem for the Law Society in the intervention context, it is possible that a debit balance under a client's name is not a genuine debit balance or that the money withdrawn from the client account, although posted to that client's ledger, was not used for that client's benefit. In some cases, it is not possible to be satisfied either way on the evidence.

A32. It is in that context that the Law Society does what is reasonably and proportionately possible in investigating the debit balance before proposing to net it off against credit balances in the same client's name.

A33. In the absence of any evidence (or any reasonably and proportionately sufficient evidence) suggesting a ledger balance is wrong, it takes the ledger balances at face value as genuinely representing withdrawals made on behalf of the named client for the amount recorded on the ledger.

A34. By way of example, in Biebuyck Solicitors five debit ledgers have been identified in the name of five persons who also are named on ledgers with credit balances. The five balances are for the following amounts: -£623.10, -£451, -£205, -£100, -£36. These are relatively small balances. The point of principle is important because, in some cases, very large balances may be involved. In any event, over numerous interventions, the amount of money affected by this point of principle will be significant.

A35. The corresponding balances under the same names which are in credit are, respectively, £623.10, £1085.80, £80, £151 and £36. If netting off were to take place on all of the above, the shortfall in funds in Biebuyck solicitors would be lessened by the sum of £1,290.10. The benefit of this lessening in the overall shortfall would be shared by all of those entitled to the funds, since the general shortfall is to be allocated on a pro rata basis between all.

A36. Verification of the debit balances involves finding the files for those clients and those matters. This is what will happen in the case of these five ledger entries. If they are all successfully found, they can be examined. Should there be nothing on the file, which suggests that the sums debited from that client's ledger should not have been, then the debit ledger balance is usually considered to be verified. This is the general approach. It is difficult and undesirable to fashion an absolute, automatic approach from which there is never any variation, since each case and even each ledger entry involves different facts and may require further investigation.

A37. I accept that the netting off approach is a rational approach for the Law Society to adopt in exercising public statutory functions in determining entitlement to funds vested in it under paragraph 6. If the Law Society were a private law trustee, it would be a proper discharge of the Law Society's obligation to ascertain beneficial entitlement to the trust.

D Re-allocating postings from a suspense ledger to named ledgers

A38. Suspense ledgers are not (generally) supposed to be used by solicitors, although they are relatively common in accounts of solicitors who are the subject of an intervention. SAR 98, r. 32(16) states that suspense client ledger accounts may be used only when the solicitor can justify their use; for instance, for temporary use on receipt of an unidentified payment, if time is needed to establish the nature of the payment or the identity of the client. Frequently, the suspense ledgers in the accounts of solicitors who are the subjects of an intervention have been used for long periods of time, the solicitor writing transactions to the ledger, instead of properly attributing the transaction and writing it to a properly named client ledger.

A39. Credit transactions, that is, transactions comprising money coming into the general client account, will, if they remain unnamed, be for the benefit of all of the named clients recorded as having money deposited in that general client account. The money coming into the general client account, in real cash terms, swells the money available in that account and, assuming that that account has an overall deficit (as is often the case), lessens the deficit to be borne by all the named clients.

A40. However, the Law Society does not presume that these credit transactions cannot be allocated, and, instead, attempts to identify the person for whose benefit money was being deposited in the account. The Law Society seeks, if reasonably possible, to identify the transaction and re-post it to a named ledger, either existing at the time of the intervention or (if there is none already existing) created by the accountants working on the accounts on behalf of the Law Society.

A41. Likewise, debit transactions are investigated, when they have been posted to suspense ledgers. If such transactions remained unnamed, and therefore unallocated, they will be a loss that falls on all of the clients who are recorded as having deposited money in the client accounts. It may be that this remains the case, even if the transaction can be identified. However, if identified in the name of a client with an existing credit balance on a ledger relating to that specific matter, then the debit transaction can be posted back to that ledger, thereby reducing the credit balance; or, if the ledger relates to another matter (see the principles discussed in the previous section), then the debit transaction can be netted off against that credit balance and, thereby, borne by that client alone.

A42. Again, in clear-cut cases there may seem to be no difficulty with that approach and, at times, there is enough accounting material for the accountants to be confident about the re-allocation of transactions posted to a suspense ledger, from that ledger, to a named ledger. The issue arises where there is an absence of information and a need to decide the level of information to justify, acting in a reasonable and proportionate manner, a decision to re-allocate or not re-allocate transactions from suspense ledgers.

A43. By way of example, there was a suspense ledger in Dixon & Co with a balance of -£2,283.75. This balance represented a transfer from the Dixon & Co client account to the office account effected by Ms Dixon without attribution to any particular named client. Ms Dixon provided information to the Law Society stating that the transfer was on account of costs whilst she was away and that she knew one transfer was in relation to Mr B and one in relation to Mr and Mrs H. She believed that there should be a bill on the respective files.

A44. Both of these clients had ledgers which were in credit: Mr and Mrs H in the sum of £547.49 and Mr B in the sum of £421.87. No file could be found for Mr and Mrs H and it was not possible to contact them. Mr B's file, which was found, suggested that the costs had already been paid.

A45. Ms Dixon, subsequently, informed Russell-Cooke on November 7, 2005, that the Mr and Mrs H matter may have been taken over by Dixon Emberton. A request has been made of that firm for the file and a response is awaited. Mr B was contacted by Russell-Cooke and said that he had no recollection on the issue of costs and had no records. Ms Dixon, in her letter of November 7 2005, also said that there were two Mr B matters and, therefore, there should be two bills. Only one file has been found, and it may be that the costs were due and/or bill was raised on the other matter, in respect of which no file has been found.

A46. The Law Society has reached a decision on the currently available evidence, in these two cases, that this level of evidence is not sufficient to warrant reallocating the debit postings from the suspense ledger to the respective ledgers of Mr and Mrs H and Mr B.

A47. The point of principle is that of proportionality in setting the level of evidence on which the Law Society can properly act in re-allocating transfers posted to suspense ledgers and in setting the level of inquiries which the Law Society should make into transactions posted to suspense ledgers.

A48. I accept that this is a rational approach for the Law Society to adopt in exercising public statutory functions to determine entitlement to funds vested in it under paragraph 6. If it were a private law trustee, it would be a proper discharge of its obligation to ascertain beneficial entitlement to the trust funds.

E Reliance on posting of debits to a specific ledger by a defaulting solicitor

A49. It is not uncommon for a solicitor who is the subject of an inspection and an intervention to create postings in his accounting records. It is also possible that entries may be wrong through human error and not dishonesty.

A50. Unlike common private law trusts, a solicitor's general client accounts may be dealing with numerous transactions each day, with money coming into and out of the account, all having to be accurately recorded.

A51. Whilst a private law trustee should always investigate prior misfeasance by his predecessors, should he become aware of it, the context in which the Law Society inherits the client accounts is such that it is possible in most cases to question whether or not the ledger balances as at the date of the intervention are 100% accurate.

A52. However, to have to go behind all of the ledger postings as a matter of course, because of the context in which the Law Society is intervening, would impose an extraordinarily onerous burden on the Law Society in terms of time, money and human resources. The Law Society's position is that, if reasonably sufficient specific evidence emerges in the course of the intervention to cast doubt on a particular posting or postings, it will do all that it reasonably and proportionately can to investigate the posting and to rectify it should it emerge with reasonable certainty that it is wrong.

A53. The Compensation Fund has, in some cases, made grants to individuals based on the information then available as to the amounts deposited in the client account by that individual. As the investigation has continued, it has become clear that the Best List compiled by the efforts of the Law Society and its agents, in its capacity under

paragraph 6, varies from the basis on which the Compensation Fund made a particular grant or grants.

A54. Moreover, it has been known for a solicitor to certify that money lent to him in his personal capacity was "client funds" in order to deceive the Compensation Fund into making grants to the lenders, on the basis that those lenders were individuals who had suffered loss or hardship as a result of the solicitor's dishonesty or failure to account for the client money in his hands: ***Holder v Law Society*** [2002] EWHC 1559, [2003] 1 WLR 1059, at [13] to [15].

A55. Insofar as these discrepancies have emerged, the Law Society has taken or will take all reasonable and proportionate steps to investigate and to seek to ascertain the cause of the discrepancy. The Law Society does not propose to apply a fixed threshold to its investigations; in other words, there should be no fixed minimum amount of discrepancy, less than which no investigation will be carried out. It would be very difficult to set a fixed threshold, given the manner in which each individual discrepancy depends on its own individual facts. However, the guiding principle in all investigations is what is reasonable and proportionate in that set of facts.

A56. By way of example, various discrepancies arose in Dixon & Co, several of which have been resolved since these proceedings were commenced.

A57. The remaining discrepancies, those of Mr R as executor of Mr H, a discrepancy of £4,824.62, of Mrs P, a discrepancy of £208.75, of Mrs C, a discrepancy of £944.97 and of Mr W, a discrepancy of £250, all relate to one issue: where there is evidence that points to a solicitor removing a client's money from the client account, albeit in an unauthorised manner, whether the loss of that money from that client account should be borne by the individual client (or the Compensation Fund by way of subrogation in this case) or pro rata amongst all clients. All of the discrepancies concern transfers of money on account of costs from the client account to the office account, when there was no bill, or it appears that there was no bill, sent to the client. This could also be characterised as an allocation of loss question.

A58. Mrs P made an application to the Compensation Fund for a grant representing funds which she had paid into the client account on account of costs, amounting to £1,007.50. A total of £767.95 had been transferred by Ms Dixon from her client account to the office account on account of costs and posted to Mrs P's ledger. The Compensation Fund could find evidence of only one bill having been sent to the client for the sum of £558.12. It took the view that there was no evidence of bills for £150 and £58.75 having been raised to justify the transfers on October 31, 2000 posted to Mrs P's ledger.

A59. Accordingly, the Compensation Fund made a principal grant of £449.38, being the sum originally remitted to Ms Dixon less the sum of £558.12 properly billed. The Compensation Fund then asserted a claim by way of subrogation to the full amount of the grant of £449.38.

A60. The ledger shows Mrs P as entitled to receive £240.63, since the ledger also reflects the (possibly) unauthorised transfers out of the client account on account of costs in the sums of £150 and £58.75 on October 31, 2000.

A61. The question arises as to whether the Compensation Fund should receive a distribution of the funds based on the higher figure of £449.38, monies which it says should have been in the account had the solicitor complied with SAR 98, or the lower figure of £240.63, the amount which the Law Society, in its capacity as trustee under paragraph 6, believes was left in the client account at the date of intervention in the name of Mrs P.

A62. The Law Society, in its capacity as trustee under paragraph 6, conducted further investigations and examined the underlying materials that might shed light on the veracity of the debit postings to the client ledger. In essence, the ledger card shows the transfers out of the client account to the office account on account of costs. The file shows nothing of use either way. The relevant bank statements show that there were transfers from the client account to the office account on the relevant days, albeit not in the precise amounts listed above, but this is not surprising, since it is common for solicitors to make one transfer from the client account to the office account which include several clients' costs all in one go.

A63. On the basis of the investigations carried out, it would appear that the sums of money were transferred out of the client account to the office account and, therefore, lost from the client account. The Law Society, in its capacity as trustee under paragraph 6, is concerned solely with establishing and determining entitlement to funds in the solicitor's client account at the date of intervention. This is a question of tracing so far as is possible on the evidence and identifying the location and movement of funds. If there is evidence that a particular client's funds were removed from the solicitor's account on a particular day, albeit that such removal might have been unauthorised, the Law Society is of the view that it is reasonable to allocate that loss of money from the client account to that particular client.

A64. The Law Society is reliant upon the postings made by the defaulting solicitor and there is a valid concern that those postings, in certain cases, may not be accurate but may be self-serving, for example, in the case of a solicitor taking randomly from the client account and posting to unrelated ledgers where he or she thinks the misappropriations will be least noticed. A measure of reliance on the solicitor is inevitable, since very often the only tools which the Law Society has, with which to identify entitlement to the funds vested in it, are whatever accounts and records the solicitor kept. The decision of how to allocate loss is not a decision as between the loss falling on the innocent client and the loss falling on the defaulting solicitor, where the presumption may well be that the solicitor should bear the loss, but it is a decision between innocent clients. Should the ledger not be relied upon and the posting of debited costs be reversed, this would increase the loss falling on other clients of the solicitor.

A65. On the available information in Mrs P's case, since there is evidence that the transfers took place out of the client account, and there is nothing to suggest that they were not transfers effected on account of costs incurred on her behalf, it may be that the Law Society should rely on the current ledger balance for Mrs P and the debits that have been made to that ledger. On the other hand, it may well be considered necessary to ascertain some positive evidence (as opposed to the absence of any contrary evidence) suggesting that the transfer was effected on account of actual costs incurred on Mrs P's behalf (albeit unbilled), so that the transfer is evidenced as referable to something related to the client, justifying the allocation of the loss of money from the client account to that particular client. In Mrs P's case, a review of the file has shown that work has been done on Mrs P's matter, which indicates costs were incurred on her behalf, albeit it is not clear if they were billed properly so as to be debited in accordance with SAR 98. It is possible that further information could be obtained from Mrs P or Ms Dixon. However, the costs involved in doing so, given the costs already incurred in investigating what is a discrepancy of £208.75, may well be disproportionate. If so, and the debit postings of costs that might not have been billed are reversed, this increases the general shortfall in the client account at the time of the intervention by £208.75, which will be borne pro rata, see below, by all the clients on the Best List. As a general policy, the Law Society favours the first solution, namely, reliance on the current ledger balance, given the absence of evidence to suggest that it was wrong.

A66. The Law Society in its capacity as trustee under paragraph 6 submits that the same approach must be adopted where the costs debited exceed what is considered by the Compensation Fund to be reasonable for the work in progress. The

Compensation Fund in making a discretionary grant will assess what it considers to be a reasonable value for the work in progress being carried out by the solicitor and deduct that from any grant that it makes. In the case of Mr R as executor of Mr H, mentioned above, where a discrepancy remains between the Compensation Fund and the Law Society in its capacity as trustee under paragraph 6, the Compensation Fund came to the view that whilst £12,036.77 incl. VAT had been deducted from the client ledger on account of costs, incurred in the course of the administration of the estate, only one bill had been rendered in the sum of £2,131.50. However, rather than award a grant based on the difference between those two figures, the Compensation Fund commissioned an informal assessment as to the value of the work done by Ms Dixon on behalf of the estate. The value of the work was assessed at £7,212.15 inclusive of VAT and the Compensation Fund made a grant for the difference between the value of the work and the actual sums deducted from the client ledger. The difference between £12,036.77 and £7,212.15 is £4,824.62.

A67. The Compensation Fund has asserted a claim by way of subrogation for the amount of £4,824.62 granted, in addition to the balance remaining on client account of £11,852.45. Since the sums deducted from the client account on behalf of the solicitor's costs incurred on behalf of that client are a loss to that particular client, even if unauthorised, then it must follow that it is still a loss to that particular client, even if the sums deducted were too high and could have been the subject of assessment. Whilst it is right that the Compensation Fund, in the exercise of its discretion, can take such matters into account in deciding what level of grant it will award in its discretion, the Law Society, in its capacity under Paragraph 6, is concerned to identify and determine entitlement to a specific fund of money existing at the date of intervention, applying principles of tracing. All that concerns the Law Society in identifying entitlement is the movement and identity of funds deposited by clients in the client account.

A68. Were it to be said that the Law Society, in its capacity as trustee under paragraph 6, had to take into account what the reasonable value of the work done by a solicitor for a client was, this would require the Law Society to conduct informal assessments into that value, which, as can be seen from the Compensation Fund records referred to above, are by no means necessarily simple or cheap inquiries. There may be situations, as in the case of Mr R, where the Compensation Fund has already carried out such an inquiry, upon which perhaps reliance could be placed. However, the principle, if a correct principle, which the Law Society, in its capacity as trustee under paragraph 6 contends it is not, would have to be applied in all situations, including those where the Compensation Fund has not been involved and has not conducted its own inquiry into what might have been a reasonable cost for the work done by the solicitor on behalf of the client.

A69. The usual form of discrepancy concerns situations where the Compensation Fund's view of the subrogatable element of its grant exceeds the adjusted and updated ledger balance of the client (in the Best List) to which the Compensation Fund is subrogated. It is also the case that the subrogatable element of the Compensation Fund's grant may be less than the ledger balance. It is common for there not to be an exact match. The Law Society would not generally investigate differences where the Compensation Fund grant was less than the ledger balance. However, in the case of Biebuyck Solicitors, the Compensation Fund has raised a specific example of this where the Compensation Fund grant is less than the amount of the ledger in the name of Mr F, and it believes that the client ledger may overstate the client's entitlement to funds at the date of the intervention.

A70. This is a highly fact sensitive area, which needs to be considered on a case by case basis. The general approach of the Law Society is to (i) rely on ledgers save where there is evidence to suggest the ledger balance might be wrong, (ii) conduct reasonable and proportionate inquiries into differences over what should be the correct ledger balance (and this would be done whether the beneficiary pointing out the discrepancy was the Compensation Fund or a non-Law Society beneficiary, and

discrepancies include those that arise when a non-Law Society beneficiary emerges claiming an entitlement to funds when he or she is not recorded even as having a ledger in the records held by the Law Society), and (iii) treat deductions from the client account as losses of a particular client's money where there is reasonably and proportionately sufficient evidence to indicate that the transfers were made in relation to that client, in respect of that client's money, albeit unauthorised.

A71. I accept that this is a rational approach for the Law Society to adopt in exercising its public statutory functions to determine entitlement to funds vested in it under paragraph 6. If it were a private law trustee, it would be a proper discharge of the Law Society's obligation to ascertain beneficial entitlement to the trust funds.

F Reliance on Compensation Fund verification exercise

A72. In order for the Compensation Fund to exercise its right (under section 36(4) of the Act) of subrogation to the rights of a recipient of a grant from the Compensation Fund to the funds vested in the Law Society under paragraph 6, it must identify how much money it believes that recipient had in the client accounts of the relevant solicitor at the time of the intervention and, therefore, how much of the money vested in the Law Society at the time of the intervention belonged to the recipient of the grant.

A73. Grants made by the Compensation Fund are also made in respect of items, such as lost interest, the costs of instructing new solicitors to rectify work badly done or to complete work incompletely done by the original solicitor, the costs of instructing solicitors or other professionals to prepare the application to the Compensation Fund or certain compensatory items such as penalties for late payment of stamp duty.

A74. Each composite grant has to be broken down into all its elements. A subrogated claim will only be maintained in respect of the sum or sums that represent money the Compensation Fund believed, at the time of making the grant, to be money which the applicant should have had in the solicitor's client accounts at the time of the intervention.

A75. In order to identify this element of the grant, the Compensation Fund staff carry out a verification exercise.

A76. The Law Society is mindful of the need to ensure that the Compensation Fund is treated no differently – neither worse nor more favourably – than any other person entitled to a share of the funds vested in the Law Society under paragraph 6. As other non-Law Society persons do, so must the Compensation Fund submit a claim form verifying the number of subrogated claims it is making to any funds vested in the Law Society under paragraph 6.

A77. When considering how far the Law Society, in its capacity under paragraph 6, should re-verify the claims submitted by the Compensation Fund, it is important to bear in mind that the Compensation Fund is itself a trust and the administrators of the Compensation Fund will have had to carry out their own checks upon receipt of an application for a grant, to satisfy themselves of the basis on which an application was being made to the Fund.

A78. There are times when the Compensation Fund has access to better, different or just more evidence relating to entitlement to the money in the client accounts at the time of intervention and, as such, is a useful source of information in compiling the Best List.

A79. The Compensation Fund is part of the Law Society's regulatory arm. Both the funds within paragraph 6 and those administered by the Compensation Fund are subject to the same statutory framework, in the context of the Law Society exercising

the public function given to it by Parliament to regulate the solicitors' profession. To require the Law Society, in its capacity as trustee under paragraph 6, automatically to re-consider everything done by the Compensation Fund staff, when there is nothing to suggest that there is any need to do so, would be unnecessary duplication, and render the Law Society's exercise of its statutory powers far more onerous.

A80. The Law Society has adopted the approach whereby it relies on the claims submitted to it by the Compensation Fund and does not seek to go behind the verification exercise carried out by the Law Society's staff who administer the Compensation Fund, save where it, in its capacity as trustee under paragraph 6, has conflicting evidence which suggests that the Compensation Fund's assessment of how much money a particular client should have had in the client account at the time of intervention cannot be relied upon or might be questioned.

A81. In the practices of Mr Zoi, such is the state of evidence available to the Law Society from the solicitor's own records that, in respect of some of the claims submitted by the Compensation Fund to the trust fund, it has to rely entirely on the Compensation Fund. It has no evidence to suggest that the Compensation Fund might be wrong or inaccurate in any respect in its analysis of the subrogated claims it can properly maintain to the funds, save for the further investigation now being carried out in Zoi & Co in light of further evidence.

A82. I accept that the reliance upon the Compensation Fund's record of its verified claims by way of subrogation to funds vested in the Law Society, save where a claim exceeds that which the client, to whose claim the Compensation Fund is subrogated, is a rational approach for the Law Society to adopt in the exercise of its public statutory functions in determining entitlement to funds vested in it under paragraph 6. If it were a private law trustee, it would be a proper discharge of its obligation to ascertain beneficial entitlement to the trust funds.

G Entitlement in respect of unbilled costs

A83. I have dealt in the judgment with the principles relating to unbilled costs, and I set out here the Law Society's evidence.

A84. In each of the cases now before the court, where this issue has arisen, the solicitor concerned has been contacted. But these are all cases in which the solicitor is interested neither (i) in ascertaining current entitlement to the sums of money concerned, in terms of helping to identify whether or not a bill exists and has been sent to the client already, rendering the money office money under SAR 1998, r. 19(2) nor (ii) in recovering the costs himself.

A85. In seeking to ascertain whether or not there has been a bill, or written notification, prepared and/or sent to the client, in the absence of assistance from the solicitor concerned, the Law Society has to decide how far it should look to see if it is possible to establish evidence either way. Investigations - involving looking for files that may not exist, looking through the files that do exist or are found, for information that may not be recorded in that file, trying to contact clients or third parties when no addresses or up-to-date addresses and/or contact details for those persons are available and/or the individual concerned may not be able to recall whether or not a proper bill, or written notification of costs incurred, was sent - can be extremely onerous in terms of time and financial expense, with far from sure prospects of success or certainty.

A86. A line has to be drawn which is both reasonable and proportionate and which makes sense in the context of a body with finite resources exercising statutory powers given to it by Parliament in the interests of the public at large. The Law Society has done and will do what it reasonably and proportionately can to ascertain whether or not a bill has been sent in the cases that have arisen and, on the basis of

the available evidence, will reach a decision as to whether the matter was properly billed.

A87. By way of example, in Biebuyck Solicitors, the Compensation Fund refused Miss M a grant on the basis that the balance of £20.75 on her ledger was in respect of work carried out by the solicitor. The grant awarded to Mr S was reduced by £616.88 to reflect the costs incurred by Mr Biebuyck. This balance remains on Mr S's ledger once the Compensation Fund has been paid its entitlement to the funds based on its subrogated claim of £23,000, the amount of the grant which it gave to Mr S.

A88. Neither of the files showed any evidence which might assist on the question of whether or not a bill or written notification had been sent to the client or paying party. Mr Biebuyck has said he is not asserting any claim to the funds held by the Law Society based on costs due to him. Responses are awaited from Mr S and Miss M and, should any be forthcoming, they will be considered prior to distribution.

A89. As far as Miss M is concerned, subject to any response from her or further information provided by her, there is insufficient evidence to say that the balance on her ledger is office monies. It will be treated as client account monies held for her.

A90. The Compensation Fund has shed some further light on the deduction on account of costs it made in the case of Mr S. The matter related to the release of a charge held by Mr S, where the Compensation Fund were of the view that the chargor was to pay the legal costs. The sum of £616.88 was paid over and above the amount required to release the charge, which the Compensation Fund considered to be evidence that the chargor must have been notified of the legal costs incurred as being £616.88. SAR 1998, r. 19(2), does allow for written notification of the costs incurred to be sent or given to the paying party as opposed to the client, and this may be a case where, even without evidence of a bill having been raised and sent, rule 19(2) can be considered to have been complied with and the balance of £616.88 should be treated as having been office money at the time of the intervention.

A91. The question of unbilled costs arises in respect of ledgers where there has been no Compensation Fund involvement. For example, in Biebuyck Solicitors, the ledger of Mr G shows a credit balance of £115. However, Mr G has returned a claim form stating that his claim was settled and that no money was owing to him and that Mr Biebuyck had deducted his fees from his claim. Notwithstanding the fact that Mr Biebuyck appears not to be attempting to assert any claim to such monies, in the light of Mr G's comments, the Law Society takes the view that it is reasonable and proportionate to treat the balance of £115 as office money at the time of the intervention.

H Allocation of a deficit in trust funds

A92. I have dealt in the judgment with the legal aspects of distribution where there are deficits, and I set out here the Law Society's evidence.

A93. The Law Society does not presume that the most applicable evidential presumptive rule will be the pro rata rule. The case of the practices of Mr Zoi is an unusual case, but a good example of a case in which the accountants reconstructing the solicitor's accounts identified a situation in which the rule in Clayton's Case would be more apt on the specific facts of that case.

A94. From an analysis of the bank statements immediately prior to the intervention date, it became clear that one of Mr Zoi's client accounts (the one with the largest amount of money in) had gone overdrawn shortly before the intervention. Once an account is overdrawn, the money that had been deposited therein has been dissipated and, should the account go back into credit at a later date, the credit balance is clearly created by new money and not the money which was originally

deposited in the account (unless it can be shown that the "new money" represents the traceable proceeds of the money originally deposited in the account and then dissipated): ***Bishopsgate Investment Management Ltd v Homan*** [1995] 1 WLR 31.

A95. The fact that the client account had become overdrawn less than a month prior to the intervention gave the accountants a much narrower window to survey and in which to assess all the payments coming in and out of the client account in those few days. It was also thought to render consideration of deposits made into the account prior to the point in time at which it became overdrawn more or less academic.

A96. Moreover, it became clear from the bank statements that a substantial proportion of the trust funds had been paid into the client account just 3 days prior to the intervention, and that there had only been one relatively small payment out of the account after that receipt. The sum of £19,300 was received from PKP French solicitors on behalf of Mr M on June 11, 2002, 3 days prior to the intervention on June 14, 2002. On June 14, 2002 a cheque in the sum of £1,770 was paid out from the client account. Compensation Fund information revealed that it was paid out on behalf of Mr M. There were no payments out of the client account other than this one payment after receipt of the sum of £19,300. Thus, clearly, the sum of £17,530 remained in the account of the money paid in on behalf of Mr M.

A97. The application of a last in-last out rule does seem more appropriate in this case, and, on that basis, the sum of £17,480 will be paid to the Compensation Fund, since it paid a grant to Mr M for this amount on account of the monies deposited in the Zoi & Co client account at the date of intervention. The balance of £50 may be paid to Mr M, subject to the investigation concerning the sum of money paid to Mr A by the Compensation Fund, which was also supposed to relate to the sum of money received on behalf of Mr M.

A98. The remaining funds in the Zoi & Co client account will also be dealt with on a last in-last out basis; however, this is the subject of some further investigation, as a result of recent information provided by Mr Zoi which might shed a little more light on sums that were previously unidentifiable.

A99. I accept that the Law Society's approach of determining entitlement to the funds vested in it, having regard to any deficiencies in the client account at the date of the intervention, and the private trust law principles of allocating deficiencies between beneficiaries to deficient mixed trust fund, is a rational approach. If it were a private law trustee, I would have approved the pro rata method of allocating loss in Biebuyck Solicitors and Dixon & Co and the application of the rule in ***Clayton's Case*** in Zoi & Co.

I Advertisement

A100. In cases where private law trustees are concerned as to whether or not they have sufficiently identified all of the beneficiaries of their trust, they can obtain some protection under section 27 of the Trustee Act 1925 by giving notice by advertisement in the Gazette. This provision only applies to trustees for sale of personal property as opposed to all trustees of personal property. The Law Society is a trustee of personal property, but not a trustee for sale of personal property.

A101. The Law Society has carried out an advertising campaign which mirrors the requirements of section 27. Advertisements have been placed both in the Gazette and in newspapers circulating in the area where the majority of the solicitor's known clients were located; this being the best equivalent to land comprising the trust property, as provided for in section 27.

A102. In all of these cases, the advertisements have been repeated in a manner which would not have been required under section 27. This has been part of doing

everything possible in the context of these test cases and goes beyond what the Law Society would consider, in general, to be proportionate. It has served to highlight how, even deploying unrestricted resources and imposing no limit upon the steps taken in the name of proportionality, results may not be forthcoming. In general, the advertisements have produced only a handful of responses at best.

A103. I accept that the use of the advertising campaign is a factor to be taken into account in demonstrating that the Law Society has adopted a rational approach to its exercise of its power to determine entitlement to the funds vested in it under Paragraph 6 or, if it were a private law trustee, in demonstrating that the decisions reached by the Law Society could be approved as a proper discharge of the Law Society's obligation to ascertain beneficial entitlement to the trust funds.

J Contacting persons entitled to funds: £75 limit

A104. The Law Society adopts various methods for contacting persons who might be entitled to a share in the funds. Advertising, described above, serves not only as a mechanism of identifying entitlement for the Law Society as a result of any information that it obtains following the advertising campaign, but also as a method of alerting those who have been identified as entitled to a share in the funds to the possible existence of their rights to claim against the funds.

A105. All clients with live matters should have already been contacted by the intervention agent at the date of intervention. The Law Society has now adopted an approach of only writing again to those clients with ledgers recording over £75 in the client account at the date of intervention.

A106. The cost of the steps which are involved in writing to a client, where up-to-date contact details are known, and then processing any response and making any payment that might be due once the response has been processed are estimated by the Law Society to be on average £233. These costs will be increased where the file has to be requested from Law Society archives, or from a solicitor to whom it was released, in order that contact details can be obtained.

A107. Substantial costs will already have been incurred in reconciling the accounts, verifying them if possible, compiling a Best List and resolving all of the uncertainties arising as a result of compiling that Best List, ascertaining any shortfall, deciding how to allocate that shortfall and advertising. All of these costs have to be incurred before it can be determined to what any one client who deposited money in the general client account might be entitled and, therefore, before the stage is reached when a client can be written to.

A108. Moreover, in cases of shortfall, a client may have a ledger balance in credit with the sum of £75 but, if loss is allocated on a pro rata basis, his or her entitlement to funds may be considerably less. For example, in Dixon & Co, a client such as Miss D who has a ledger balance of £70.50 will only be entitled to £10.64 out of the funds vested in the Law Society and a client such as Miss M who has a ledger balance of £84.52 will only be entitled to £12.75 out of those funds. To incur, say, between £82 and £233 worth of costs, on top of substantial costs that have already been incurred, in order to be able to effect a distribution of £10.74 or £12.75 is, in the Law Society's view, disproportionate. In many cases, it may not be known, until the letter is written and sent, whether or not the contact details are up–to-date for the client. If not up-to-date, the costs of tracing that client will increase the costs of distribution of whatever sums that client is entitled to, and the costs of sending the letter will have been incurred with no success in effecting a distribution.

A109. In the case of Biebuck Solicitors, Mr S made an application to the Compensation Fund for a grant of £50, but was rejected since he could not

demonstrate hardship as a consequence of the failure of Biebuyck Solicitors to account for money to him.

A110. On the basis that Mr S had a ledger in credit for the sum of £50, the amount he would receive on a pro rata distribution of the funds would be in the order of £30, given the shortfall in the client account at the date of the intervention. The Compensation Fund has said that it has Mr S's address as at April 24, 2003, but that address dates back over two and a half years and it may no longer be up–to-date. The only way in which the Law Society would know whether or not it is, would be if a letter were sent, by which time the costs (which would certainly exceed £30) would have been incurred, possibly in vain.

A111. In these circumstances the Law Society submits that it is rational (i) for the Law Society to apply, as a general current approach, a limit of £75 on a client ledger, less than which it will not write again to clients in addition to the letter that should have been written at the time of the intervention, whilst (ii) recognising that there may always be particular cases which merit not following the general approach. If it were a private law trustee, that would be a proper discharge of its obligation to contact beneficiaries and inform them of the trust.

A112. If a client comes forward, perhaps in response to the earlier letter written by the intervention agent or having seen the advertisement or having contacted the Compensation Fund, and requests distribution of what he or she is entitled to, the Law Society is likely to effect a distribution, even though the costs incurred in doing so may exceed the amount being distributed. This also means that, should the client come forward and approach the Compensation Fund seeking a grant from the Compensation Fund, he or she could be referred on to the Law Society, in its capacity as trustee under paragraph 6.

A113. Where contact details or up-to-date contact details are not available for clients who might be entitled to substantial amounts, the Law Society considers the use of tracing agents. In the Law Society's experience, the effectiveness of using tracing agents has not been high, and is extremely dependent on the amount of information available for the client being traced. The amount of money invested in tracing also affects the effectiveness of the tracing exercise, and the amount of money that can be spent proportionately and reasonably is directly affected by the value of the ledger balance. A guideline level of £500 has been adopted now above which tracing will be considered by the Law Society. A flexible approach has been adopted so that, in Dixon & Co, where the shortfall was considerable, the level of £500 was applied as referable to the amount to be distributed to those entitled as opposed to their ledger balances.

A114. I accept that this is a rational approach.

K Disputes between beneficiaries

A115. There may be situations where proper determination of entitlement is outside the bounds of what it can achieve from the material available to it e.g. the solicitor's books and records and accounting materials. Entitlement may well depend on factual and evidential matters in dispute between two would-be beneficiaries. The name on a client ledger list may not always reveal what dealings there may have been with the entitlement to the money recorded on that ledger. In such a situation, the Law Society may ask for directions as trustee.

L Distribution

A116. Many balances left on client ledgers are small balances and swiftly dwarfed by the costs even of locating the client file, finding a current address for the client and writing to the client in an attempt to notify the client of the trust and the existence of

his or her possible claim to a share in the trust funds. These costs are increased where, as often is the case, repeat letters have to be sent to the client chasing the client for a response to the initial letter and/or attempts have to be made to find an up-to-date contact address for the client by means of tracing agents if necessary.

A117. Ordinarily, a private law trustee would exert a right to reimbursement for the expenses incurred in administering the trust, recoverable from the trust fund itself: Trustee Act 2000, section 31(1). Exercising the right to reimbursement against the trust fund itself, in the case of a private law trustee, acts as natural barrier to carrying out exhaustive disproportionate attempts to locate and contact beneficiaries who have disappeared. Since the Law Society's own funds are being expended in determining beneficial entitlement to these trusts and effecting a distribution, the natural barrier against disproportionate enquiries into the whereabouts of beneficiaries is not present, albeit that the Law Society does not have inexhaustible funds and is funded by the profession itself.

A118. The Law Society is mindful of the desirability of ensuring speedy distribution to those who have been determined as entitled to funds. To that end, the Law Society has formulated an approach of interim distribution, which involves distributing to an identified person the minimum to which on any view he must be entitled, even were outstanding matters resolved eventually by the Law Society wholly contrary to the interests of that particular person.

A119. Although interim distributions will only take place where the Law Society is confident of the minimum entitlement of the person to whom it is proposing to effect an interim distribution, it is possible for there to be others entitled to the funds of whom the Law Society is unaware, given, for example, the fact that investigations are ongoing at the time of an interim distribution. Accordingly, recipients of an interim distribution will usually be asked to give undertakings to repay any amount, subsequently determined to have been overpaid in the interim distribution. The reality is that the most common recipient of an interim distribution is likely to be the Compensation Fund, since the Compensation Fund is often entitled to the largest proportion of the funds, by way of subrogation. Whereas, for the purposes of the interim distribution, resolving uncertainties against a particular individual (e.g. presuming that that individual bears the entire shortfall in funds by himself) would often eliminate the entitlement of an individual who was not the Compensation Fund, this is often not so for the Compensation Fund, because of the size of its entitlement.

A120. Where there is evidence of potential discrepancies between additional information (more likely than not provided by the Compensation Fund) and the ledger balances held by the Law Society in its capacity as trustee under paragraph 6, and whilst investigation into those discrepancies is ongoing, the balance that reflects the least favourable distribution as far as concerns the recipient of the interim distribution will be used in calculating the distribution. To calculate entitlement based on a possible higher ledger balance for the recipient would risk overpaying. It may be correct to calculate the overall claims to funds using the higher ledger balance in order that the potential overall claim is as high as possible, whilst the calculation of the entitlement of the individual to a share in the funds is calculated using the lower of the two possible ledger balances to reduce the risk of overpayment. The principles on which interim distributions are to be made is the subject of discussion between the Compensation Fund and the Law Society. In the case of Biebuyck Solicitors, Mrs N was the beneficiary of a trust; from evidence supplied by the trustee the balance of the trust funds at the time of the intervention should have been £194,000, but the Best List indicated a ledger balance of £164,000. The shortfall of £30,000 indicates misappropriation, or at least erroneous debits. Whilst further investigation is ongoing, the most prudent course would be to calculate an interim distribution using the higher value of her ledger for calculation of the total potential claims on the funds so that that figure is in the order of £370,000 as opposed to £340,000, whilst using the lower balance to calculate the Compensation Fund's entitlement to funds by way of subrogation to her ledger, so that that figure is in the order of £164,000 as opposed to

£194,000. An alternative would be to rely on the lower balance for both the calculation of the total potential claims on the funds, and, therefore, the shortfall, and for the Compensation Fund's entitlement to funds by way of subrogation to that ledger balance.

A121. The standard claim form used to date has included an undertaking in the following form:

> "I hereby formally confirm that I am entitled to the sum claimed and acknowledge that any payment I receive will be made in reliance upon my confirmation.
>
> In the event that it transpires that I am not entitled to all or part of any sum paid to me, I undertake to return that sum to The Law Society within seven days of notification."

A122. The intention has been for undertakings to be given in both the interim and final distribution contexts. This standard form is not limited in terms of time.

A123. The Law Society has considered whether to ask, as an extreme precaution, for an undertaking from persons to whom distribution is effected, even if the Law Society is held only to be amenable to judicial review. The undertaking would guard against the remote possibility of judicial review of the Law Society's determination as to entitlement. However, the Law Society regards guarding against such a remote possibility in this way (save in unusual cases) as unattractive and unlikely to achieve a better or fairer solution overall than not seeking the undertaking, and paying the wronged person who emerges later claiming an entitlement to funds.

A124. I see no objection to the Law Society effecting distribution to those it has determined are entitled or identified as entitled, without any further retention or other security save for that which has been mentioned above.

M Retention of the undistributed sums as reimbursement of the Law Society's properly incurred costs in determining entitlement to the funds and effecting distribution of the funds

A125. I have dealt with this in principle in the judgment. I set out here the Law Society's evidence.

A126. In Zoi & Co, once all the funds have been distributed to those who can be identified as entitled to a share in the funds, there will remain an unidentified surplus of £6,075.11, and it is possible that that unidentified surplus may be greater. This unidentified surplus is unidentified in the sense of there not even being names of clients to whom the funds might be payable.

A127. In Dixon & Co, potential entitlement to the funds far exceeds the funds. The shortfall in Dixon & Co in the client account at the time of the intervention was considerable and calculated at the time of the Law Society's original evidence as £250,181.31. Therefore, any undistributed surplus in this case would not arise as a result of an inability to identify those entitled to the funds. It might well arise, though, when distribution is effected. Clients may well have moved since the intervention in March 2002 and there may be no up-to-date address or contact details for some clients. Other clients have a ledger balance under £75 in credit and no further attempts would be made to contact them for the reasons explained above, given the considerable costs involved, the extremely small amounts that would be distributable to them and the amount of work that has already been done in Dixon & Co in compiling a Best List and in notifying clients by way of advertisement etc. In Dixon & Co the agent has confirmed that all clients whose files were uplifted at the time of the intervention were written to, regardless of whether their matter was a finished or

current matter. The number of ledgers with balances under £75 are 28, with balances ranging from £3.50 to £70.50 and a total value of £1,106.45. Bearing in mind the amount of shortfall in the Dixon & Co client account at the time of the intervention, this is in fact only £160.39 of the funds to be distributed in Dixon & Co. This would be the undistributable surplus in Dixon & Co solely attributable to the application of limit of £75 under which no further letter would be sent to the client. Moreover, if any of the clients with one of the small balances in credit approached the Law Society, perhaps in response to the advertisement, or the letter from the intervention agent, or information from the Compensation Fund, their entitlement would be likely to be distributed to them, thereby reducing the undistributed surplus.

A128. On the current available evidence, the amount of money which will remain undistributed on ledgers over £75, as a result of the absence of contact details or response from the person entitled to the funds is estimated to be £1,122.92.

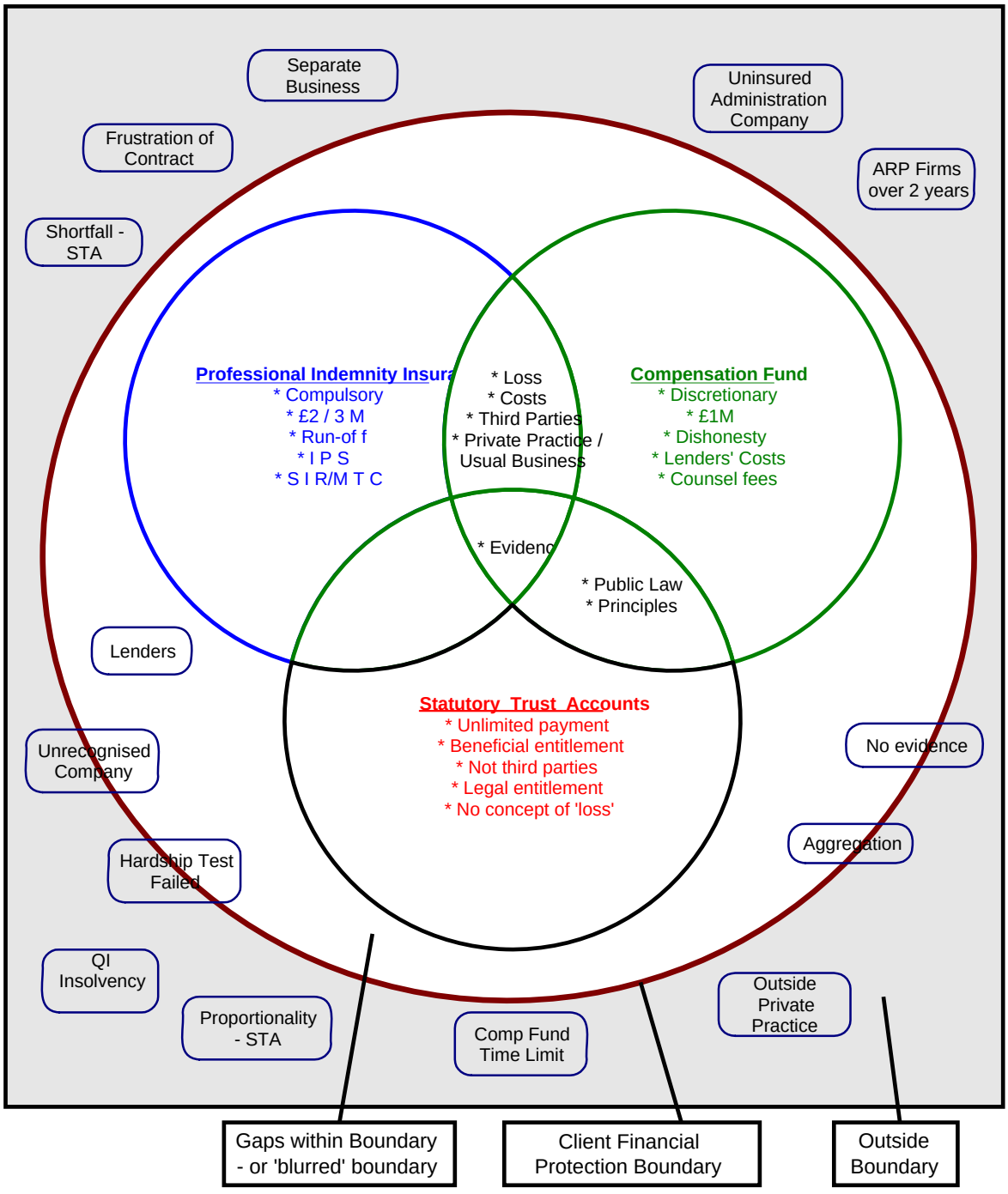
A129. The Law Society has recovered its costs of intervention from solicitors in approximately 6 to 10 cases each year; for example, in 2004, having incurred the sum of £5,086,591 in intervention costs, the Law Society recovered £960,681.

A130. In some cases, such as Ahmed & Co and Zoi, all reasonably and proportionately identifiable and contactable beneficiaries have received the most they were recorded as entitled to at the time of the intervention in the solicitor's records. In Ahmed & Co, the practice monies were intact and, therefore, all those who could reasonably and proportionately be found received all that they were recorded as entitled to at the time of the intervention. In Zoi, once all reasonably and proportionately identifiable and locatable persons have received that to which they appear to be entitled there remains a surplus for which there are no known beneficiaries.

A131. However, in other cases, such as Dixon & Co and Biebuyck Solicitors, the practice monies were not intact and there was a shortfall at the time of the intervention. In determining entitlement, the Law Society has considered and taken into account private law trust methods of allocating deficiencies in trust funds as between beneficiaries of a mixed fund, and arrived, in both, at a pro rata method of allocation of loss. The entitlement of individuals to the funds in the Law Society's hands is their pro rata entitlement. Once they receive their pro rata entitlement, those persons will have received their full entitlement to the funds in the Law Society's hands. Although this is the case, if it transpires that there is a surplus after distribution in such cases, an alternative way of dealing with the surplus might be to distribute a second amount to those who have already participated in the initial distribution, pro rata to the amount they are recorded as having deposited with the solicitor at the time of the intervention.

A132. The disadvantages of this approach are that to do so may well be, in some cases, disproportionate, given the small amounts of surplus there may be and the costs of effecting a second distribution. Dixon & Co is a good example of this. More importantly, in dealing with any surplus, there need to be safeguards to protect any late-emerging persons, who have been identified by the Law Society as entitled to the money, but who were not reasonably and proportionately contactable by the Law Society at the time of the initial distribution. It would be far harder to ensure that a late-emerging person would be paid his entitlement, if the surplus (which was not distributed in the initial distribution) were distributed in a second wave of distribution to those who had received their entitlement already in the initial distribution. If the surplus is used to reimburse the Law Society for its costs incurred under paragraph 6, that could be underwritten by an undertaking given by the Law Society to repay the relevant amount of money to such a late-emerging person. The Law Society considers that such an undertaking should be confined (i) to one year and (ii) to those who had been previously identified as entitled to a share of the funds but were not traceable or contactable by the Law Society at the time of distribution.

ANNEX E


Separate Business
Uninsured Administration Company
Frustration of Contract
ARP Firms over 2 years
Shortfall - STA
Professional Indemnity Insura
* Compulsory
* £2 / 3 M
* Run-of f
* I P S
* S I R/M T C
* Loss
* Costs
* Third Parties
* Private Practice / Usual Business
Compensation Fund
* Discretionary
* £1M
* Dishonesty
* Lenders' Costs
* Counsel fees
* Evidenc
* Public Law
* Principles
Lenders
Statutory Trust Accounts
* Unlimited payment
* Beneficial entitlement
* Not third parties
* Legal entitlement
* No concept of 'loss'
Unrecognised Company
No evidence
Aggregation
Hardship Test Failed
QI Insolvency
Proportionality - STA
Comp Fund Time Limit
Outside Private Practice
Gaps within Boundary - or 'blurred' boundary
Client Financial Protection Boundary
Outside Boundary

Legal Services Act: New forms of practice and regulation

Consultation paper 10

Compensation Fund

25 April 2008

Table of contents

1. Introduction

1. The Solicitors Regulation Authority (SRA) maintains a Compensation Fund for the purposes of making grants to persons who have suffered loss by reason of the dishonesty of a solicitor and to applicants who have suffered hardship as a consequence of a failure by a solicitor to account for money. Grants are made at the discretion of the SRA.

2. Currently the key provisions relating to the Compensation Fund are to be found in section 36 and schedule 2 of the Solicitors Act 1974 (“the Act”). Section 36 sets out the requirement to maintain a Compensation Fund, the scope of the Fund and the power to make Rules about the Fund and about the procedure for making grants from it. The collection of contributions and the administration of the Fund are dealt with in Schedule 2.

3. The procedures for making and processing applications are set out in the Compensation Fund Rules 1995. Attached to the Rules are guidelines which decision makers may take into account when exercising the SRA’s discretion.

4. One of the changes to be introduced by the Legal Services Act 2007 (LSA) is the repeal of section 36 and schedule 2 and the introduction of new sections 36 and 36A. The new sections are enabling provisions which give the Society (in practice the SRA) the power to make rules relating to all aspects of the Compensation Fund. This means that the new rules must include the relevant provisions currently in section 36 and schedule 2 and they must come into effect upon the commencement date to avoid a hiatus.

5. In the new sections 36 and 36A there is no longer any reference to dishonesty or hardship. The SRA could have taken the opportunity to totally rewrite the rules and to extend the scope of the Fund. However, it is important to get the new rules in place, including any process of concurrence and/or approval, by 1 March 2009, so as to be in time for the implementation of Legal Disciplinary Practices, firm-based regulation of partnerships and other changes in the SRA's rule-making powers. It is therefore considered appropriate that any changes to take place now will be confined to ones that are relatively minor and for the benefit of the public. It is unlikely that major changes will be proposed until the Legal Services Board is up and running and the new approval process is in place.

6. The current rules and guidelines are attached as Annex 1 and the proposed new rules as Annex 2.

2. Proposed changes

General changes

7. The implementation of the LSA and the need to restructure the rules has provided the opportunity to simplify the provisions currently set out in the 1995

rules and guidelines with a view to making them more user friendly. In particular, it is not intended at this stage to have separate guidelines. Whilst the new legislation provides for guidelines, it is considered to be better that all the relevant provisions are set out in one document, rather than two as is the present case, and that they are written in more consumer friendly language. Some of the current guidelines should more properly be treated as rules, and have been adapted as such. Others in effect merely repeat the rules and have been deleted.

Hardship

8. Under the current provisions of the Act grants can be made (a) in the event of dishonesty, or (b) where a failure to account has occurred and hardship arises as a result. The hardship test broadly has the effect of separating out applications from private individuals from those from institutional applicants such as banks and building societies. This is because it is difficult for such a financial institution to show that it has suffered hardship. It has been a long established policy of the Fund that for private individuals the hurdle to be overcome is very low.

9. Whilst the LSA will substitute a new section 36 of the Solicitors Act which no longer refers to dishonesty or hardship, the draft new rules have retained these terms. The reasons for this are (i) to maintain, by and large, the status quo for reasons set out in paragraph 5, and (ii) to maintain the focus of the protection afforded by the Fund on individual applicants acting in their personal capacity. That is not to say that the Fund considers that a body corporate or other business could not suffer hardship. The main change introduced in the draft new rules is to formalise the low hurdle for private individuals. Rule 3 provides that an individual applicant whose dealings with the defaulting practitioner were in a private capacity will be deemed to have suffered hardship. This is not a significant change in the way in which the Fund has been operating in practice but it will provide transparency. A business client, whether an individual, partnership or body corporate, will have to demonstrate hardship.

Maximum grant

10. Under the present rules, the Fund limits grants to £1 million for any one claim. There is power to waive this limit if the circumstances justify it. It is believed that the limit has been waived on just one occasion. This was an exceptional case involving the defrauding of a paraplegic of a large part of his award of damages. The current limit was set about 14 years ago at a time when the limit of

indemnity under the compulsory professional indemnity scheme was £1 million per claim. With effect from 2005 the minimum level of indemnity was increased to £2 million any one claim for sole practitioners and partnerships and to £3 million for limited companies and limited liability partnerships.

11. Over the last 14 years the value of property and the level of damages for personal injury have increased considerably and an increase in the level of the maximum grant is long overdue. It is therefore proposed that the Compensation Fund limit should be increased to £2 million in line with minimum level of compulsory indemnity cover (see Rule 16) and that the power of waiver be retained.

Time limit

12. The current rules state that an application must be submitted within six months of the date that the loss, or the possibility of loss, first came to the applicant's knowledge and that failure to comply could result in the applicant being penalised. It is often difficult for a full application to be put together within this time scale not least because following an intervention into a firm, it may take some time to clarify the financial position of the firm. Another factor is that applicants are often in the position of having to piece together information where files and papers are missing. It is therefore considered that the six month period is too short.

13. To overcome these problems it is proposed to extend the time limit to twelve months (see Rule 10). This should not raise any financial issues and will allow an applicant more time to collate evidence thus the applicant will be in a position to submit a complete application making it easier for the Fund's staff to investigate the claim.

Rectification costs

14. The Compensation Fund has for very many years dealt with applications for reimbursement of additional costs incurred by an applicant for the completion of work that the applicant's solicitor has been paid for but has not carried out. This type of claim often relates to a conveyancing matter where the post completion formalities were outstanding at the time the firm was the subject of an intervention by the SRA. The client of the intervened firm is placed in the position of having to instruct a new firm to complete the work. In some cases the mortgage lender instructs its solicitors to complete the work and passes the rectification cost onto the borrower.

15. This type of grant has not been specifically expressed in the Compensation Fund Rules to date so the opportunity has been taken to address this by the insertion of a new Rule 14.3. The average annual cost of this type of grant is around £120,000 which is not expected to change significantly following the introduction of this Rule.

Fund of last resort

16. In the current guidelines it is stated at general principle 1 (c) that the Fund is administered as a fund of last resort. This implies that before making any grant the Fund will require applicants to exhaust other civil remedies. Whilst in many

17. cases this is indeed how the fund operates there are occasions where, in the public interest, the Fund acts as a fund of first resort.

18. Examples of where the Fund acts as a fund of first resort include:

    (1) Following an intervention by the SRA into a conyeyancing practice the Compensation Fund makes emergency funds available to the practice in the form of loans to enable the completion of urgent property transactions. This minimises the disruption to clients and also the size of any potential claims on the Fund.

    (2) In circumstances where there is complex theft of client money resulting in intervention and uncertainty as to whether claims should fall to the firm's indemnity insurer or the Compensation Fund, the Fund has dealt with claims pending the outcome of an investigation to establish where claims should properly lie.

    (3) The Compensation Fund will provide immediate funding where there is an urgent need such as a defaulting solicitor's client facing the threat of bankruptcy or facing the repossession of property due to the failure of the solicitor to redeem a mortgage.

19. In the draft new Rules the reference to fund of last resort has been replaced by a new Rule 12 - "Exhausting other remedies" – which more accurately reflects the true position.

3. Questions

1. Do you agree that an individual whose dealings with a defaulting practitioner have been in a personal capacity and who has suffered or is likely to suffer loss due to a failure to account should be deemed to have suffered hardship? (Rule 3)

2. Do you agree that the maximum grant should be increased from £1 million to £2 million, subject to the power to waiver the limit? (Rules 16 and 22)

3. Do you agree that the time limit for submitting an application should be increased from 6 months to 12 months? (Rule 10)

4. Do you consider that grants in respect of rectification costs should be specifically expressed in the Rules? (Rule 14(3))

5. Do you consider that the wording of Rule 12 more accurately describes the true nature of the Fund rather than the phrase "Fund of last resort"?

Please give reasons for your answers.

4. How to respond

For information on how to respond, please visit our website.

- Go to www.consultations.sra.org.uk.
- Select **Compensation Fund**.
- Click **How to respond**.
- Alternatively, go to www.sra.org.uk/consultations/798.article#respond.

Time limits

The deadline for responses is **6 June 2008**, except that for comments on Question 2 (raising the limit for grants to £2 million), the deadline is extended to **20 June 2008**.

Annex 1

[Draft] Solicitors' Compensation Fund Rules ~~1995~~ [2009]

Rules dated ~~26 January 1995~~ [1 March 2009] commencing [1 March 2009] made by the ~~Council of the Law Society~~ Solicitors Regulation Authority Board under ~~Section 36(8)~~ sections 36, 36A and 79 of the Solicitors Act 1974 and section 9 of the Administration of Justice Act 1985, with the concurrence of the Master of the Rolls under section 9 of the Administration of Justice Act 1985 and the concurrence of the Lord Chancellor under paragraph 16 of Schedule 22 to the Legal Services Act 2007.

1. Interpretation

~~(a)~~(1) In these ~~Rules~~ rules:

"the Act" means the Solicitors Act 1974;

"applicant" means a person or persons applying for a grant out of the Compensation Fund under ~~section 36 of the Act, Schedule 2 paragraph 6 of the Administration of Justice Act 1985 or Schedule 14 paragraph 6 of the Courts & Legal Services Act 1990~~ rule 3 of these rules;

"appointed representative" means the personal representative of a deceased defaulting practitioner; the trustee of a bankrupt defaulting practitioner; the administrator of an insolvent defaulting practitioner, or other duly appointed representative of a defaulting practitioner;

"compensation claim" means a claim in respect of a loss for which a grant may be made under these rules;

"defaulting practitioner" means:

~~(i)~~(a) a solicitor in respect of whose act or default, or in respect of whose employee's act or default, an application for a grant is made;

~~(ia)~~(b) a registered European lawyer in respect of whose act or default, or in respect of whose employee's act or default, an application for a grant is made;

~~(ii)~~(c) a recognised body in respect of whose act or default, or in respect of whose ~~officer's~~ manager's or employee's act or default ~~(in the case pf a company), or in respect of whose member's act or default (in the case of a limited liability partnership)~~, an application for a grant is made; or

~~(iii)~~(d) a registered foreign lawyer who is ~~practising in~~ a manager of a partnership, limited liability partnership or company together with a solicitor ~~or a~~, a registered European lawyer or a recognised body, and in respect of whose act or default or in respect of whose employee's act or default, an application for a grant is made;

and the expressions "defaulting solicitor", "defaulting registered European lawyer", "defaulting recognised body" and "defaulting registered foreign lawyer" shall be construed accordingly;

"exempt European lawyer" has the meaning assigned in rule 24 of the Solicitor's Code of Conduct 2007;

"manager" means a partner in a partnership, a member of a limited liability partnership or a director of a company, as defined in rule 24 of the Solicitor's Code of Conduct 2007;

"recognised body" has the meaning assigned by section 9 of the Administration of Justice Act 1985;

"registered European lawyer" means an individual registered with the ~~Law Society~~ SRA under regulation 17 of the European Communities (Lawyer's Practice) Regulations 2000; ~~and~~

"registered foreign lawyer" has the meaning assigned by section 89 of the Courts and Legal Services Act 1990;

"SRA" means the Solicitors Regulation Authority; and

when referring to a practitioner, applicant or other person which is a body rather than an individual, words denoting the masculine or feminine gender (such as "he or she" or "who") also include the neuter ("it" or "which").

~~(b)~~(2) Other expressions in these ~~Rules~~ rules have the meaning assigned to them by the Act.

~~(c)~~(3) The Interpretation Act 1978 applies to these ~~Rules~~ rules as it applies to an Act of Parliament.

2. Maintenance of and contributions to the Fund

(1) The Law Society ("the Society") shall establish and maintain the fund called the Solicitors' Compensation Fund ("the Fund") for making grants in respect of compensation claims.

~~Guideline 1. General principles~~

~~Guideline 1(a)~~

(2) Every solicitor, registered European lawyer, registered foreign lawyer and recognised body shall make contributions to the compensation fund at such times and in such circumstances, as may be prescribed from time to time by the SRA. Any unpaid contributions may be recovered as a debt due to the Society.

(3) Paragraph (2) shall not apply to a solicitor, registered European lawyer or registered foreign lawyer who is a Crown Prosecutor.

(4) The Society may invest any money which forms part of the Fund in any investments in which trustees may invest under the general power of investment in section 3 of the Trustee Act 2000 (as restricted by sections 4 and 5 of that Act).

(5) The Society may insure with authorised insurers, in relation to the Fund, for such purposes and on such terms as it considers appropriate.

(6) The Society may

(a) borrow for the purposes of the Fund;

(b) charge investments which form part of the Fund as security for borrowing by the Society for the purposes of the Fund.

(7) The Fund may be applied by the SRA for the following purposes (in addition to the making of grants in respect of compensation claims):

(a) payment of premiums on insurance policies effected under paragraph (5);

(b) repayment of money borrowed by the Society for the purposes of the Fund and payment of interest on any money so borrowed under paragraph (6);

(c) payment of any other costs, charges or expenses incurred by the Society in establishing, maintaining, protecting, administering or applying the Fund;

(d) payment of any costs, charges or expenses incurred by the SRA in exercising its powers under Part II of Schedule 1 to the Act (intervention powers);

(e) payment of any costs or damages incurred by the SRA, its employees or agents as a result of proceedings against it or them for any act or omission of its or theirs in good faith and in the exercise or purported exercise of such powers.

3. Grants which may be made from the Fund

Guideline 1. General principles

Guideline 1(a)

The basic object of the Fund is to replace "clients' money" misappropriated by a solicitor or his or her employee(s), but, although an client money which a defaulting practitioner or a defaulting practitioner's employee or manager has misappropriated or otherwise failed to account for. applicant for a grant must be a person who has suffered loss through the actions of the solicitor, he or she The applicant need not necessarily be or have been the defaulting practitioner's client.

Guideline 1(b)

(1) A grant out of the Fund is made wholly at the discretion of the Council of the Law Society SRA. No person has a right to a grant enforceable at law, but the intention of the Council is to seek to administer the Fund in an even-handed and consistent manner.

(2) For any grant to be made out of the Fund, an applicant must satisfy the SRA that:

(a) he has suffered or is likely to suffer loss in consequence of the dishonesty of a defaulting practitioner or the employee or manager of a defaulting practitioner or

(b) he has suffered or is likely to suffer loss and hardship in consequence of a failure to account for money which has come into the hands of a defaulting practitioner or the employee or manager of a defaulting practitioner, which may include the failure by a defaulting practitioner to complete work for which he was paid,

in the course of a transaction of a kind which is part of the usual business of the persons listed in rule 1(1) (a), (b), (c) and (d).

~~***Guideline 1(f)***~~

~~The Council normally require that the "dishonesty" or '"failure to account" referred to in Section 36(2)(a) and (b) of the Solicitors Act 1974 must have occurred within the course of a solicitor/client transaction of a kind which is part of the usual business of a solicitor.~~

(3) For the purposes of paragraph (2)(b):

(a) an individual whose dealings with the defaulting practitioner have been in a personal capacity and who has suffered or is likely to suffer loss due to a failure to account shall be deemed to have suffered hardship; and

(b) a body corporate, or an individual whose dealings with the defaulting practitioner have been in a business capacity, and who has suffered or is likely to suffer loss due to a failure to account must provide evidence to satisfy the SRA that the body or individual has suffered or is likely to suffer hardship.

~~***Guideline 5. Interim grants***~~

~~In an application where it appears that there is severe hardship, the Council may make an interim grant before the full investigation of the whole application has been completed and without the full application being admitted. However, the Council must be satisfied that there has been a loss of an amount at least equal to that to be paid out by way of an interim grant.~~

(4) A grant may, at the sole discretion of the SRA, be made as an interim measure.

~~***Guideline 6. Claims where the defaulting solicitor is or was in partnership***~~

~~(a) Losses caused by the dishonesty of a partner or employee will normally be recoverable from the Solicitors' Indemnity Fund, or after 31 August 2000 from the firm's insurer under the Solicitors' Indemnity Insurance Rules. The Council may, however, make a grant to an applicant in respect of part of his or her claim which is not covered by the Indemnity Fund or by the firm's insurance,~~

~~e.g. where the remaining partners are unable to settle all or part of the claim from their own resources.~~

~~(b) Accordingly, applicants should proceed with a claim against the remaining partners who, in turn, will make a claim against the Indemnity Fund, or after 31 August 2000 under the firm's insurance. Where there is doubt as to whether a claim should be met from the Indemnity Fund or the Compensation Fund, the Society endeavours to make suitable arrangements with Solicitors' Indemnity Fund Limited to ensure that claims are paid promptly.~~

~~2.~~ 4. Grants in respect of persons not authorised to practise

~~(a)~~(1) A grant may be made in respect of a defaulting solicitor even if the defaulting solicitor had no practising certificate in force ~~or was suspended from practice~~ at the date of the relevant act or default provided that the ~~Council~~ SRA is reasonably satisfied that the applicant was unaware of the absence of a valid practising certificate ~~or of the suspension~~.

~~(aa)~~(2) A grant may be made in respect of a defaulting registered European lawyer even if, at the date of the relevant act or default, the registration of that lawyer in the ~~Society's~~ SRA's register of European lawyers was suspended or was cancelled under regulation 8 of the European Lawyers Registration Regulations 2000 due to non-renewal provided that the ~~Council~~ SRA is satisfied that the applicant was unaware of the suspension or cancellation.

~~(b)~~(3) A grant may be made in respect of a defaulting recognised body even if the recognition of that body had expired for non-renewal under regulation ~~7.1 of the Recognised Bodies Regulations [2005]~~ 8.3 of the Solicitors' Recognised Bodies Regulations 2007 on or before the date of the relevant act or default provided that the ~~Council~~ SRA is reasonably satisfied that the applicant was unaware of such revocation.

~~(c)~~(4) A grant may be made in respect of a defaulting registered foreign lawyer even if, at the date of the relevant act or default, the registration of that lawyer in the register of foreign lawyers was suspended ~~or~~, or was cancelled under Schedule 14 paragraph 3(4)(a) of the Courts and Legal Services Act 1990 due to non-renewal ~~provided~~, provided that the ~~Council~~ SRA is reasonably satisfied that the applicant was unaware of the suspension or cancellation.

~~3.~~ 5. Grants to practitioners

(1) A grant may be made to a defaulting practitioner who or which has suffered or is likely to suffer loss or by reason of his, her or its liability to any client in consequence of some act or default of:

(a) in the case of a defaulting solicitor, registered European lawyer or registered foreign lawyer, any of his or her employees or any fellow manager;

(b) in the case of a defaulting recognised body, any of its managers or employees or any fellow manager,

in circumstances where but for the liability of that defaulting practitioner a grant might have been made from the Fund to some other person.

(2) No grant shall be made

~~(i) under section 36(2)(c) of the Act to any solicitor, or~~

~~(ii) under section 36(2)(c) of the Act to any registered European lawyer, or~~

~~(iii) under Schedule 14 paragraph 6(1)(c) of the Courts & Legal Services Act 1990 to any registered foreign lawyer, or~~

~~(iv) under Schedule 2 paragraph 6(2)(c) of the Administration of Justice Act 1985 to any solicitor, registered European lawyer, recognised body or registered foreign lawyer, or to any other individual or body corporate permitted under rule 14 of the Solicitors' Code of Conduct 2007 to be a member of a recognised body,~~

under paragraph (1) unless the ~~Council~~ SRA is satisfied that no other means of making good the loss is available and that ~~he or she~~ the defaulting practitioner is ~~fitted by reason of conduct, age and experience (or, in the case of a company it is~~ fit and proper ~~fitted by reason of the conduct, age and experience of its officers and employees, or in the case of a limited liability partnership it is fitted by reason of the conduct, age and experience of its members and employees~~) to receive ~~such~~ a grant.

(3) A grant under paragraph (1) may be made by way of a loan and shall be repayable by the recipient at the time and upon such terms as shall be specified by the SRA.

~~Guideline 1(e)~~

~~A grant may be made out of the Fund to a solicitor applicant, usually by way of a loan, in circumstances where a loss within the ambit of the Fund has been suffered by reason of misappropriation of clients' money by his or her partner or employee or where he or she is the purchaser of a practice from a defaulting solicitor, provided that the application is not tainted with the default. Exceptionally, such a grant may be made even though the applicant may be entitled to indemnity under the Solicitors' Indemnity Fund and without prejudice to that indemnity.~~

~~4.~~ 6. Foreign lawyers

~~(a)~~(1) If a registered European lawyer is exempted from contributing to the Compensation Fund ~~under the Solicitors' Compensation Fund (Foreign Lawyers' Contributions) Rules 1991~~ on the basis ~~of~~ that he or she has completely equivalent cover under home state rules, no grant shall be made:

~~(i)~~(a) ~~under section 36(2)(a) of the Act~~ in respect of any act or default of the registered European lawyer or his or her employee unless, in the case of an employee, the employee is:

~~(A)~~(i) a solicitor, or

~~(B)~~(ii) the employee of a partnership which includes at least one person who ~~is not exempted on the basis of that provision;~~ or which contributes to the Fund; or

~~(ii) under section 36(2)(b) of the Act in respect of any act or default of the registered European lawyer; or~~

~~(iii)~~(b) under ~~section 36(2)(c) of the Act~~ rule 5 to the registered European lawyer.

~~(b)~~(2) No grant shall be made ~~under section 36 of the Act~~ in respect of any act or default of a registered European lawyer or an exempt European lawyer, or the employee of a registered European lawyer, where such act or default took place outside the United Kingdom, unless the ~~Council~~ SRA is satisfied that the act or default was, or was closely connected with, the act or default of a solicitor or the employee of a solicitor, or that the act or default was closely connected with the registered European lawyer's practice in the United Kingdom.

~~(c)~~(3) No grant shall be made ~~under Schedule 14 paragraph 6(1) of the Courts & Legal Services Act 1990~~ in respect of the act or default of a registered foreign lawyer, or of the employee ~~or partner~~ of a registered foreign lawyer, where such act or default took place outside England and Wales, unless the ~~Council~~ SRA is satisfied that the act or default was, or was closely connected with, the act or default of a solicitor or the employee of a solicitor, or that the act or default was closely connected with practice in England and Wales.

~~*Guideline 2.*~~ 7. Losses ~~which cannot be the subject of a grant outside~~ the remit of the Fund

~~Certain losses are outside the ambit of the Fund because the Council has no power to make a grant. Examples are:-~~: A grant will not be made in respect of the following;

~~(a) losses arising as a result of misappropriation of money by a solicitor outside his or her practice as such or by a solicitor's employee acting outside the scope of his or her employment;~~

~~(b)~~ (a) losses arising solely by reason of professional negligence by a ~~solicitor~~ defaulting practitioner, or the employee or manager of a defaulting practitioner;

~~(c)~~ (b) losses ~~arising by reason of the failure of a solicitor to satisfy a money judgment against him or her~~ which are the personal debts of a defaulting practitioner and where the facts ~~of the judgment~~ would not otherwise give rise to a claim on the ~~Compensation~~ Fund;

~~(d) losses where the Council is satisfied that either no evidence of dishonesty is available or, where in the case of failure to account, an applicant is not suffering material hardship~~

~~*Guideline 3.* Losses in respect of which a grant may not be made~~

~~Notwithstanding the statutory provisions of section 36, there are certain losses in respect of which it is not normally the practice of the Council to make a grant. Examples are~~

~~(a)~~ (c) ~~losses which result~~ losses resulting from, but ~~do~~ does not form part of any misappropriation of, or failure to account for, money or money's worth. ~~This is subject to certain exceptions, e.g. legal costs incurred in applying for a grant and interest on the amount of the grant.~~

(d) losses resulting from the trading debts or liabilities of the defaulting practitioner.

Guideline 9. Personal liabilities of a solicitor

The Council will not normally make a grant in respect of the personal or trading debts or liabilities of a solicitor or a solicitor's firm or where the monies form part of a commercial transaction or business venture between the applicant and the solicitor outside the normal solicitor/client relationship.

(b) the application is tainted with the applicant's own dishonesty.

(c) (e) the where the applicant has contributed to his, her or its the loss as a result of his/her or its his activities, omissions or behaviour either before, during or after the transaction giving rise to the application or thereafter.

Guideline 10. Applicant's own behaviour

When considering any application, the Council takes into account the conduct of the applicant and/or the applicant's servants or agents both before and after the loss was sustained. If the Council, in the exercise of its discretion, considers an applicant and/or an applicant's servants or agents to have inter alia contributed to the circumstances of the loss, or to have failed to submit an application for a grant within a reasonable time (see also Rule 6 of the Solicitors' Compensation Fund Rules), or to have failed to pursue an application diligently, then the application may be rejected in its entirety or the amount of any grant substantially reduced.

(d) (f) in where in the case of an applicant who is a member of a profession, or is engaged in trade or business or performs a function, where the loss arises in connection with that profession or in the course of that profession, trade, business or function, and there is evidence that the applicant and/or the applicant's servants or agents contributed to the loss by failing to exercise a reasonable standard of care.

(e) (g) the loss amounts losses amounting to a claim for contractually agreed interest between the applicant and the solicitor defaulting practitioner. Where, following the authorisation of a principal grant, the Council makes a supplementary grant for a sum in lieu of lost interest, the sum is calculated at rates which may from time to time be prescribed by the Council.

(f) (h) the Society was not notified of the applicant's loss within six months of the date upon which the loss first came or ought to have come to the applicant's knowledge, and there are no exceptional circumstances which, in the opinion of the Council, justify the delay (see Rule 6 of the Solicitors' Compensation Fund Rules);

(h) (h) the losses occurring loss occurred in relation to an overseas partnership of which all solicitor partners are exempt from other provisions of Rules 12 and 13 of the Solicitors Overseas Practice Rules 1990 by virtue of Rules 12(6) and 13(6), and which does not fall within rule 15.27(1)(c) or (2)(b) of the Solicitors' Code of Conduct 2007, unless:

(i) the loss did not occur occurred as a result of a solicitor's dishonesty, or

(ii) the loss occurred as a result of failure to account by a solicitor acting as a named trustee.

~~(i)~~ (j) ~~the application is~~ applications by the Legal Services Commission for loss occasioned through making regular payments under the Commission's contracting schemes for civil and/or criminal work.

~~Guideline 3(g)~~ 8. Undertakings

~~the application is based on the failure by a solicitor to comply with an undertaking. The Fund does not generally underwrite a solicitor's undertaking. Failure on the part of a solicitor to comply with an undertaking is a matter of misconduct which may be the subject of a complaint to the Law Society's Consumer Complaints Service or the Compliance Directorate, but does not of itself entitle the recipient to make a successful application for a grant out of the Fund.~~ A grant in respect of a failure by a defaulting practitioner to comply with an undertaking ~~An application may, however,~~ will be considered ~~favourably~~ if it can be shown that ~~an~~ the undertaking was given in the course of the ~~solicitor's~~ defaulting practitioner's usual business ~~as a solicitor~~ acting on behalf of a client, that the recipient acted reasonably in accepting the undertaking and placing reliance on the ~~solicitor in his or her capacity as such~~ undertaking, and that:

(i) the undertaking was given with dishonest intent for the purpose of procuring money or money's worth, or

(ii) the undertaking, although not given with dishonest intent, is subsequently dishonestly not performed ~~by the solicitor~~ for the purpose of procuring money or money's worth.

The ~~Council~~ SRA does not consider the giving of an undertaking in circumstances which amount to the ~~solicitor~~ giving of a bare guarantee ~~either~~ of ~~his or her~~ the defaulting practitioner's personal liabilities ~~or~~, or the financial obligations and liabilities of a client or third party ~~to~~, to form part of the usual business of a solicitor~~, and such an undertaking would therefore not normally be regarded as having been given within the course of a solicitor/client transaction.~~ or other legal practitioner.

~~***Guideline 14.***~~ 9. Multi-profession frauds

~~In an application where~~ Where the loss has been sustained as a result of the combined activities of more than one profession, (e.g. a ~~solicitor~~ defaulting practitioner conspires with an accountant or surveyor, or ~~a dishonest solicitor~~ is assisted by a negligent accountant or valuer) the ~~Council~~ SRA will ~~normally~~ consider ~~how~~ the role of each contributing factor ~~affected~~ in causing the applicant's loss. The ~~Council~~ SRA will ~~normally endeavour to~~ base any grant on its assessment of that portion of the loss primarily attributable to the acts of the ~~solicitor~~ defaulting practitioner as opposed to that portion which is primarily attributable to the acts or omissions of the other professional parties, or to other factors. The ~~Council~~ SRA may decide to make a grant on a pro-rata basis in accordance with its assessment of the importance of each contributing factor in the loss, or may reject an application in its

entirety if it is of the opinion that the loss was primarily due to other factors rather than the ~~solicitor's~~ defaulting practitioner's dishonesty.

~~5. Application form~~

~~Every applicant shall complete and deliver to the Society an application in such form as may from time to time be prescribed by the Society.~~

~~6. Time limits~~ 10. Applications: form and time limit

Every application ~~shall~~ must be delivered to the ~~Society~~ SRA, in such form as may from time to time be prescribed by the SRA, within ~~six~~ twelve months after the loss, or likelihood of loss, or failure to account, as the case may be, first came, or reasonably should have come, to the knowledge of the applicant. The ~~Council~~ SRA may extend this period if satisfied that there are ~~exceptional~~ circumstances which justify the extension of the time limit.

~~7.~~ 11. Documentation in support

~~The Council may require an application to be supported by a statutory declaration and accompanied by any relevant documents and shall cause such enquiries to be made in relation to the application as it sees fit. Failure to provide documentation or information requested or to co-operate fully in the Council's enquiries may be taken into account when the application is considered.~~

~~Guideline 1(d)~~

~~The burden of satisfying the Council that a loss has been suffered within the ambit of the Fund rests with each applicant, but the Society will give guidance and, so far as possible, for the purpose of the application, allow the applicant reasonable access to records under the Society's control or to which the Society has access.~~

The burden of proving a claim rests with the applicant who must provide such documentation as may be required by the SRA including when requested, a statement of truth. Failure to provide such documentation or to co-operate with the SRA will be taken into account when determining the merits of the application.

~~Guideline 4. Requirements to be satisfied~~

~~Every applicant for a grant out of the Compensation Fund must satisfy the Council:-~~

~~(a) that he, she or it has suffered or is likely to suffer actual loss of money or money's worth;~~

~~(b) that such loss has been occasioned by (i) the dishonesty of a solicitor (or his or her employee) acting in the course of his or her practice as such or in connection with a Trust of which the solicitor was at the material time, a professional Trustee or (ii) the failure of a solicitor (or his or her employee) to account for money received in the course of his or her practice or in connection with a Trust of which the solicitor was, at the material time, a professional Trustee;~~

~~(c) that any alleged dishonesty is evidenced either by the conviction of the solicitor (or his or her employee), or by a finding of fraud in a civil action, or by evidence leading to an inevitable presumption of theft. Where an application is based on failing to account, the application must be~~

supported by sufficient documentation to substantiate that a failure to account has occurred and that the applicant is suffering or is likely to suffer hardship; and

(d) that the loss is not reasonably recoverable from any other source.

8. 12. Exhausting other remedies

Guideline 1(c) 4. Fund of last resort

(1) The Fund is administered as a fund of last resort. This means that a A grant may be limited or refused to an applicant refused or limited where the loss or part of the loss is an insured risk or where the loss is capable of being made good by recourse to another person some other means.

(2) The Council SRA may, before deciding whether or not to make a grant, require the applicant:

(a) to pursuit pursue of any civil remedy which may be available to the applicant in respect of the loss,

(b) to commence insolvency proceedings,

(c) the making of to make a formal complaint to the Police in respect of any dishonesty on the part of the defaulting practitioner or may require

(d) the assistance of an applicant to assist in the taking of any disciplinary action against the defaulting practitioner.

(3) In the absolute discretion of the SRA, a grant may be made from the Fund before requiring the applicant to resort to other means of recovery.

Guideline 7. Institution of civil proceedings

In some cases the Council may require an applicant to institute civil proceedings including, where appropriate, insolvency proceedings against the solicitor in respect of the loss suffered. The purpose of the proceedings may be to recover all or part of the alleged loss or to quantify precisely the amount of such loss.

No applicant should institute proceedings unless and until the written consent of the Society has been obtained and the question of who is to be responsible for the costs has been decided, otherwise any application for a grant in respect of such costs may be rejected by the Council.

Guideline 8. Prosecution of dishonest solicitors

In all appropriate cases, the applicant will be expected to assist the Police in connection with enquiries into the commission of any criminal offence by the solicitor in respect of the alleged acts giving rise to the application. However, the Council may consider an application for a grant notwithstanding that a defaulting solicitor has not been convicted of any such offence nor has been the subject of a finding of dishonesty by the Solicitors' Disciplinary Tribunal.

~~14.~~ 13. Notice to defaulting practitioner

~~(a)~~(1) The ~~Council~~ SRA shall not make a grant unless ~~a letter~~:

(a) a communication has been sent ~~(i)~~ to the defaulting ~~solicitor~~ practitioner at his or her last known correspondence address or to ~~any solicitors or other lawyers instructed by him or her~~ his or her appointed representative ~~(ia) to the defaulting registered European lawyer at his or her last known correspondence address or to any solicitors or other lawyers instructed by him or her, as well as to the appropriate regulatory body for the defaulting registered European lawyer within his or her home jurisdiction or jurisdictions, whether in Europe or elsewhere;~~

~~(ii) to the defaulting recognised body at its registered office as last communicated to the Council or the Society under rule 14 of The Law Society's Code of Conduct [2005]; or~~

~~(iii) to the defaulting registered foreign lawyer at his or her last known correspondence address or to any solicitors or other lawyers instructed by him or her as well as to the appropriate regulatory body for the defaulting registered foreign lawyer within his or her home jurisdiction or jurisdictions.~~

informing ~~him/her or it~~ the defaulting practitioner of the nature and value of the application ~~and~~; and

(b) not less than eight days have elapsed since the date of receipt of such ~~letter~~ communication, which shall be regarded as the day following the date of the communication.

~~(b) If by reason of death, insolvency or other disability, proper notification under sub-paragraphs (a)(i), (ia) or (iii) of this rule cannot be given to a defaulting practitioner then such notice may be given to a Personal Representative, Trustee in Bankruptcy or any other person who the Society is satisfied acts for or on behalf of the defaulter and/or his or her Estate.~~

~~(c) Where the defaulting practitioner is a recognised body and it appears to the Society that any letter sent under (a)(ii) above will not come to the attention of the recognised body (or any officer or employee thereof if it is a company, or any member or employee thereof if it is a limited liability partnership) then the letter may be sent to the liquidator and/or receiver of the recognised body or to any other person for the time being accountable for the affairs of the recognised body.~~

~~(d)~~(2) If it appears to the ~~Society~~ SRA that any ~~letters~~ communication sent under ~~sub-paragraphs (a)(i) to (iii) of this rule~~ paragraph (1) will not come to the attention of the defaulting practitioner or ~~any other person on~~ his or her ~~behalf~~ appointed representative, then the ~~Council~~ SRA may make a grant notwithstanding failure to comply with the provisions of this ~~Rule~~ rule.

~~9.~~ 14. Costs ~~for submitting applications~~

(1) **Litigation**

Where an applicant intends to or has already instituted proceedings for recovery of his loss and wishes to apply for a grant in respect of the costs of the proceedings, the SRA will only consider such costs where;

(a) they can be shown to be proportionate to the loss, and

(b) there is a reasonable chance of making a recovery in respect of the loss, or

(c) the proceedings were necessary to the making of an application to the Fund

(2) **Application costs**

Where a grant is made, the ~~Council~~ SRA may consider an application for a further grant in respect of the reasonable costs properly incurred by the applicant with either his solicitor or other professional adviser, provided that such costs were incurred wholly, necessarily and exclusively in connection with the preparation, submission and proof of the application. ~~If, in the view of the Council, such costs were not reasonably or properly incurred then the Council may decline to pay some or all of those costs.~~

~~Guideline 13. Payment of costs of application~~

~~The Council has the power to make a further grant in respect of the reasonable costs of an applicant's solicitor or other professional adviser relating to a claim where a grant is authorised (see Rule 9 of the Solicitors' Compensation Fund Rules). The Council may not, however, be prepared to make such a further grant or may grant less than the full costs if it is of the opinion that all or part of the costs should not have been incurred, or might have been saved by an earlier approach to the Society, or is of the view that the costs incurred are unreasonable or excessive.~~

(3) Costs where the defaulting practitioner has failed to complete work

If the defaulting practitioner did not complete the work for which he was paid, a failure to account shall be deemed to have arisen within the meaning of rule 3(2)(b) of these rules. In such circumstances, the SRA may consider making a grant in respect of the additional reasonable legal costs incurred by the applicant in completing the outstanding work or a grant by way of contribution towards those costs.

~~10.~~ 15. Interest

(1) The ~~Council~~ SRA may consider an application for a supplementary grant by way of a sum in lieu of lost interest on a principal grant. Such interest will ~~normally~~ be calculated in accordance with the rates prescribed from time to time by the ~~Council for Compensation Fund applications and~~ SRA. This will normally be calculated from the day upon which the loss which was the subject

of the principal grant was incurred, up to the next working day after ~~the despatch of the grant cheque~~ payment of the principal grant. Such payment will take into account that a grant is a gift and is therefore not subject to tax.

~~***Guideline 12. Payment of interest on claims***~~

~~In appropriate cases, the Council will consider an application for a supplementary grant in lieu of lost interest on the amount of the grant from the date of the loss (see Rule 10 of the Solicitors' Compensation Fund Rules). If paid, interest will normally be calculated at those rates prescribed from time to time by the Council which take into account that a grant is a gift and is therefore not subject to tax.~~

(2) Where the application for the principal grant is in respect of a failure to redeem a mortgage, the SRA may also make a grant in respect of the additional interest accrued to the mortgage account as a result of the defaulting practitioner's failure to redeem.

~~11.~~ 16. ~~Discretion to limit~~ Maximum grant

~~In relation to any loss sustained, or any sum of money which came under the control of a defaulting practitioner, after 10th June 1993, the Council will refuse to authorise a grant of an amount which would result in sums exceeding £1,000,000.00 (inclusive of all costs and interest) being paid to or on behalf of an applicant from either the Compensation Fund or the Solicitors Indemnity Fund or both together in respect of any individual transaction or matter.~~

~~***Guideline 15. Normal maximum payout***~~

~~For any loss sustained, or any sum of money that came into the possession of a defaulting solicitor, subsequent to 10 June 1993, it is the Council's policy not to authorise a grant with regard to any individual transaction which would result in an aggregate sum exceeding £1,000,000, inclusive of all interest and costs, being paid from a combination of the Compensation Fund and the Solicitors Indemnity Fund or the Compensation Fund solely.~~

Subject to rule 22, the maximum grant that may be made is £2 million.

~~12.~~ 17. ~~Assisting in recovering money~~ Recovery and Subrogation

Where a grant is made otherwise than by way of loan or if by way of a loan repayment of the loan is waived or otherwise the borrower has failed to repay part or

all of the loan, the Society shall be subrogated to the rights and remedies of the person to whom or on whose behalf the grant is made (the recipient) to the extent of the amount of the grant. In such event the recipient shall if required by the SRA whether before or after the making of a grant, and upon the SRA giving to the recipient a sufficient indemnity against costs, sue for recovery of the loss in the name of the recipient but on behalf of the Society for the purpose of giving effect to the Society's rights and to permit the SRA to have conduct of such proceedings.

~~Rule 12 An applicant to whom a grant has been made may be required to prove, on behalf of the Society in any insolvency and/or winding-up of the defaulting~~

practitioner and also to comply with all proper or reasonable requirements of the Council in the exercise of subrogated rights under section 36(4) of the Act.

Guideline 11. 18. Deduction from grants

(a)(1) The Council SRA may deduct from any grant the costs that would have been legally due to the solicitor defaulting practitioner provided that the work had been properly completed so that the applicant will not be in a better position by reason of a grant than he or she would otherwise have been in. A deduction in respect of notional costs may be made by the Council notwithstanding the fact that the defaulting solicitor may not have held a practising certificate at all material times. If defaulting solicitor did the work so badly, or did not complete it, with the result that the applicant has had to instruct another solicitor to carry out or finish the work, then a grant may be made for the additional reasonable costs incurred by the applicant.

(b)(2) The Council will normally seek to SRA may within its discretion deduct from any grant all monies already recovered by an applicant and monies which either will be or should have been recovered. For example, if an application is for a sum of £10,000 but an applicant has already recovered, from whatever source, a sum of £2,000, the Council will normally seek to base any grant on the balance of £8,000. This principle will usually apply even when an applicant believes that he is receiving re-payments at a contractually agreed rate, but where the solicitor has, in fact, actually misappropriated the money advanced and is, for example, making re-payments in lieu of interest in an effort to allay suspicion.

13. 19. Refusal of an application

(1) If the Council SRA refuses to make a grant of either the whole or part of the amount applied for then the Council shall cause for, the applicant to will be informed in writing of the reasons for the decision.

Guideline 16. Rejection of claim

(2) The most common ground for rejection of an application is that it does not come within the Compensation Fund's statutory framework. When the Council refuse or are unable to make a grant, the applicant will be informed in writing of the reason for this decision. The fact that an application has been rejected does not prevent a further application being submitted, or the rejected application being re-considered, provided that substantial new relevant evidence, information or submissions are produced in support of the new application or the request for re-consideration.

20. Appeals

Should the applicant wish to appeal against refusal of an application, written notice of intention to appeal must be delivered to the SRA within thirty days of the date of receipt of the decision, which shall be regarded as the day following the date of the written communication of the decision. Such notice must be accompanied by details of the grounds of appeal together with any additional evidence in support.

~~15.~~ 21. Notice of requirements

Any requirement of the ~~Council or the Society~~ SRA under these ~~Rules may~~ rules will be communicated ~~by a notice~~ in writing.

~~16. Guidelines~~

~~When exercising the discretion conferred upon it by Section 36(2) of the Act, Schedule 2 paragraph 6(2) of the Administration of Justice Act 1985 and Schedule 14 paragraph 6(1) of the Courts and Legal Services Act 1990, the Council may take into consideration the Guidelines contained in the Schedule to these Rules and decisions of the Council, and any other guidelines that the Council may approve, although these guidelines and decisions shall not fetter the Council's discretion.~~

~~Schedule - Guidelines~~

~~These guidelines form part of the Solicitors Compensation Fund Rules 1995 made by the Council on 26 January 1995, although were subject to amendment by the Council on 18th July 1996, 22nd May 2000, 25th February 2004, 17th March 2004 and 9th February 2005.~~

~~In these guidelines, reference to a solicitor shall include registered European lawyers; registered foreign lawyers practising in partnership with a solicitor or a registered European lawyer; and recognised bodies.~~

~~17.~~ 22. Waivers

The ~~Council~~ SRA may waive any of the provisions of these ~~Rules~~ rules excepting ~~Rule 14~~ rules 13, 19. 20 and 21.

~~18.~~ 23. Repeal and commencement

(1) These ~~Rules~~ rules shall come into operation on 1 March ~~1995~~ 2009, whereupon the Solicitors' Compensation Fund Rules ~~1975 (as amended)~~ 1995 shall cease to have effect save in respect of applications submitted before that date, which shall continue to be subject to the 1995 rules.

(2) On 1 July 2009, rule 4 shall be amended as follows:

(a) In paragraph (2):

(i) delete "cancelled under regulation 8 of the European Lawyers Registration Regulations 2000" and substitute "revoked under regulation 9.2(a)(ii) of the SRA Practising Regulations [2009]"; and

(ii) delete "suspension or cancellation" and substitute "suspension or revocation";

(b) In paragraph (3):

(i) delete "had expired for non-renewal under regulation 8.3" and substitute "was suspended or was revoked under regulation 9(c)"; and

(ii) delete "expiry" and substitute "suspension or revocation"; and

(c) In paragraph (4):

(i) delete "cancelled under Schedule 14 paragraph 3(4)(a) of the Courts and Legal Services Act 1990" and substitute "revoked under regulation 9.2(a)(ii) of the SRA Practising Regulations [2009]"; and

(ii) delete "suspension or cancellation" and substitute "suspension or revocation".

Annex 2
Solicitors' Compensation Fund Rules [2009]

Rules dated [1 March 2009] commencing [1 March 2009] made by the Solicitors Regulation Authority Board under sections 36, 36A and 79 of the Solicitors Act 1974 and section 9 of the Administration of Justice Act 1985, with the concurrence of the Master of the Rolls under section 9 of the Administration of Justice Act 1985 and the concurrence of the Lord Chancellor under paragraph 16 of Schedule 22 to the Legal Services Act 2007.

1. Interpretation

(1) In these rules:

"the Act" means the Solicitors Act 1974;

"applicant" means a person or persons applying for a grant out of the Compensation Fund under rule 3 of these rules;

"appointed representative" means the personal representative of a deceased defaulting practitioner; the trustee of a bankrupt defaulting practitioner; the administrator of an insolvent defaulting practitioner, or other duly appointed representative of a defaulting practitioner;

"compensation claim" means a claim in respect of a loss for which a grant may be made under these rules;

"defaulting practitioner" means:

(a) a solicitor in respect of whose act or default, or in respect of whose employee's act or default, an application for a grant is made;

(b) a registered European lawyer in respect of whose act or default, or in respect of whose employee's act or default, an application for a grant is made;

(c) a recognised body in respect of whose act or default, or in respect of whose manager's or employee's act or default, an application for a grant is made; or

(d) a registered foreign lawyer who is a manager of a partnership, limited liability partnership or company together with a solicitor, a registered European lawyer or a recognised body, and in respect of whose act or default or in respect of whose employee's act or default, an application for a grant is made;

and the expressions "defaulting solicitor", "defaulting registered European lawyer", "defaulting recognised body" and "defaulting registered foreign lawyer" shall be construed accordingly;

"exempt European lawyer" has the meaning assigned in rule 24 of the Solicitor's Code of Conduct 2007;

“manager” means a partner in a partnership, a member of a limited liability partnership or a director of a company, as defined in rule 24 of the Solicitor's Code of Conduct 2007;

“recognised body” has the meaning assigned by section 9 of the Administration of Justice Act 1985;

“registered European lawyer” means an individual registered with the SRA under regulation 17 of the European Communities (Lawyer’s Practice) Regulations 2000;

“registered foreign lawyer” has the meaning assigned by section 89 of the Courts and Legal Services Act 1990~~;~~

“SRA” means the Solicitors Regulation Authority.; and

when referring to a practitioner, applicant or other person which is a body rather than an individual, words denoting the masculine or feminine gender (such as "he or she" or "who") also include the neuter ("it" or "which").

(2) Other expressions in these rules have the meaning assigned to them by the Act.

(3) The Interpretation Act 1978 applies to these rules as it applies to an Act of Parliament.

2. Maintenance of and contributions to the Fund

(1) The Law Society (“the Society”) shall establish and maintain the fund called the Solicitors' Compensation Fund ("the Fund") for making grants in respect of compensation claims.

(2) Every solicitor, registered European lawyer, registered foreign lawyer and recognised body shall make contributions to the Fund in such amounts, at such times and in such circumstances, as may be prescribed from time to time by the SRA. Any unpaid contributions may be recovered as a debt due to the Society.

(3) Paragraph (2) shall not apply to a solicitor, registered European lawyer or registered foreign lawyer who is a Crown Prosecutor.

(4) The Society may invest any money which forms part of the Fund in any investments in which trustees may invest under the general power of investment in section 3 of the Trustee Act 2000 (as restricted by sections 4 and 5 of that Act).

(5) The Society may insure with authorised insurers, in relation to the Fund, for such purposes and on such terms as it considers appropriate.

(6) The Society may

(a) borrow for the purposes of the Fund;

(b) charge investments which form part of the Fund as security for borrowing by the Society for the purposes of the Fund.

(7) The Fund may be applied by the SRA for the following purposes (in addition to the making of grants in respect of compensation claims):

(a) payment of premiums on insurance policies effected under paragraph (5);

(b) repayment of money borrowed by the Society for the purposes of the Fund and payment of interest on any money so borrowed under paragraph (6);

(c) payment of any other costs, charges or expenses incurred by the Society in establishing, maintaining, protecting, administering or applying the Fund;

(d) payment of any costs, charges or expenses incurred by the SRA in exercising its powers under s36(A) of the Legal Services Act 2007 (intervention powers);

(e) payment of any costs or damages incurred by the SRA, its employees or agents as a result of proceedings against it or them for any act or omission of its or theirs in good faith and in the exercise or purported exercise of such powers.

3. Grants which may be made from the Fund

The object of the Fund is to replace client money which a defaulting practitioner or a defaulting practitioner's employee or manager has misappropriated or otherwise failed to account for. The applicant need not necessarily be or have been the defaulting practitioner's client.

(1) A grant out of the Fund is made wholly at the discretion of the SRA. No person has a right to a grant enforceable at law.

(2) For any grant to be made out of the Fund, an applicant must satisfy the SRA that:

(a) he has suffered or is likely to suffer loss in consequence of the dishonesty of a defaulting practitioner or the employee or manager of a defaulting practitioner or

(b) he has suffered or is likely to suffer loss and hardship in consequence of a failure to account for money which has come into the hands of a defaulting practitioner or the employee or manager of a defaulting practitioner, which may include the failure by a defaulting practitioner to complete work for which he was paid,

in the course of a transaction of a kind which is part of the usual business of the persons listed in rule 1 (1) (a),(b),(c) and (d).

(3) For the purposes of paragraph (2)(b):

(a) an individual whose dealings with the defaulting practitioner have been in a personal capacity and who has suffered or is likely to suffer loss due to a failure to account shall be deemed to have suffered hardship; and

(b) a body corporate, or an individual whose dealings with the defaulting practitioner have been in a business capacity, and who has suffered or is likely to suffer loss due to a failure to account must provide evidence to satisfy the SRA that the body or individual has suffered or is likely to suffer hardship.

(4) A grant may, at the sole discretion of the SRA, be made as an interim measure.

4. Grants in respect of persons not authorised to practise

(1) A grant may be made in respect of a defaulting solicitor even if the defaulting solicitor had no practising certificate in force at the date of the relevant act or default provided that the SRA is reasonably satisfied that the applicant was unaware of the absence of a valid practising certificate.

(2) A grant may be made in respect of a defaulting registered European lawyer even if, at the date of the relevant act or default, the registration of that lawyer in the SRA's register of European lawyers was suspended or was cancelled under regulation 8 of the European Lawyers Registration Regulations 2000 due to non-renewal provided that the SRA is reasonably satisfied that the applicant was unaware of the suspension or cancellation.

(3) A grant may be made in respect of a defaulting recognised body even if the recognition of that body had expired for non-renewal under regulation 8.3 of the Solicitors' Recognised Bodies Regulations 2007 on or before the date of the relevant act or default provided that the SRA is reasonably satisfied that the applicant was unaware of such revocation.

(4) A grant may be made in respect of a defaulting registered foreign lawyer even if, at the date of the relevant act or default, the registration of that lawyer in the register of foreign lawyers was suspended, or was cancelled under Schedule 14 paragraph 3(4)(a) of the Courts and Legal Services Act 1990 due to non-renewal, provided that the SRA is reasonably satisfied that the applicant was unaware of the suspension or cancellation.

5. Grants to practitioners

(1) A grant may be made to a defaulting practitioner who or which has suffered or is likely to suffer loss by reason of his, her or its liability to any client in consequence of some act or default of:

(a) in the case of a defaulting solicitor, registered European lawyer or registered foreign lawyer, any of his or her employees or any fellow manager;

(b) in the case of a defaulting recognised body, any of its managers or employees or any fellow manager,

in circumstances where but for the liability of that defaulting practitioner a grant might have been made from the Fund to some other person.

(2) No grant shall be made under paragraph (1) unless the SRA is satisfied that no other means of making good the loss is available and that the defaulting practitioner is fit and proper to receive a grant.

(3) A grant under paragraph (1) may be made by way of a loan and shall be repayable by the recipient at the time and upon such terms as shall be specified by the SRA.

6. Foreign lawyers

(1) If a registered European lawyer is exempted from contributing to the Fund on the basis that he or she has completely equivalent cover under home state rules, no grant shall be made:

(a) in respect of any act or default of the registered European lawyer or his or her employee unless, in the case of an employee, the employee is:

(i) a solicitor, or

(ii) the employee of a partnership which includes at least one person who or which contributes to the Fund; or

(b) under rule 5 to the registered European lawyer.

(2) No grant shall be made in respect of any act or default of a registered European lawyer or an exempt European lawyer, or the employee of a registered European lawyer, where such act or default took place outside the United Kingdom, unless the SRA is satisfied that the act or default was, or was closely connected with, the act or default of a solicitor or the employee of a solicitor, or that the act or default was closely connected with the registered European lawyer's practice in the United Kingdom.

(3) No grant shall be made in respect of the act or default of a registered foreign lawyer, or of the employee of a registered foreign lawyer, where such act or default took place outside England and Wales, unless the SRA is satisfied that the act or default was, or was closely connected with, the act or default of a solicitor or the employee of a solicitor, or that the act or default was closely connected with practice in England and Wales.

7. Losses outside the remit of the Fund

A grant will not be made in respect of the following;

(a) losses arising solely by reason of professional negligence by a defaulting practitioner, or the employee or manager of a defaulting practitioner;

(b) losses which are the personal debts of a defaulting practitioner and where the facts would not otherwise give rise to a claim on the Fund;

(c) losses resulting from, but not forming part of any misappropriation of, or failure to account for, money or money's worth.

(d) losses resulting from the trading debts or liabilities of the defaulting practitioner.

(e) where the applicant has contributed to the loss as a result of his activities, omissions or behaviour either before, during or after the transaction giving rise to the application.

(f) where, in the case of an applicant who is a member of a profession, or is engaged in trade or business or performs a function, the loss arises in connection with that profession, trade, business or function and there is evidence that the applicant and/or the applicant's servants or agents contributed to the loss by failing to exercise a reasonable standard of care.

(g) losses amounting to a claim for contractually agreed interest between the applicant and the defaulting practitioner.

(h) The loss occurred in relation to an overseas partnership which does not fall within rule 15, 27(1)(c) or (2)(b) of the Solicitors' Code of Conduct 2007, unless:

(i) the loss occurred as a result of a solicitor's dishonesty, or

(ii) the loss occurred as a result of failure to account by a solicitor acting as a named trustee.

(i) applications by the Legal Services Commission for loss occasioned through making regular payments under the Commission's contracting schemes for civil and/or criminal work.

8. Undertakings

A grant in respect of a failure by a defaulting practitioner to comply with an undertaking will be considered if it can be shown that the undertaking was given in the course of the defaulting practitioner's usual business acting on behalf of a client, that the recipient acted reasonably in accepting the undertaking and placing reliance on the undertaking, and that:

(i) the undertaking was given with dishonest intent for the purpose of procuring money or money's worth, or

(ii) the undertaking, although not given with dishonest intent, is subsequently dishonestly not performed for the purpose of procuring money or money's worth.

The SRA does not consider the giving of an undertaking in circumstances which amount to the giving of a bare guarantee of the defaulting

practitioner's personal liabilities, or the financial obligations and liabilities of a client or third party, to form part of the usual business of a solicitor or other legal practitioner.

9. Multi-profession frauds

Where the loss has been sustained as a result of the combined activities of more than one profession, (e.g. a defaulting practitioner conspires with an accountant or surveyor, or is assisted by a negligent accountant or valuer) the SRA will consider the role of each contributing factor in causing the applicant's loss. The SRA will base any grant on its assessment of that portion of the loss primarily attributable to the acts of the defaulting practitioner as opposed to that portion which is primarily attributable to the acts or omissions of the other professional parties, or to other factors. The SRA may decide to make a grant on a pro-rata basis in accordance with its assessment of the importance of each contributing factor in the loss, or may reject an application in its entirety if it is of the opinion that the loss was primarily due to other factors rather than the defaulting practitioner's dishonesty.

10. Applications: form and time limit

Every application must be delivered to the SRA, in such form as may from time to time be prescribed by the SRA, within twelve months after the loss, or likelihood of loss, or failure to account, as the case may be, first came, or reasonably should have come, to the knowledge of the applicant. The SRA may extend this period if satisfied that there are circumstances which justify the extension of the time limit.

11. Documentation in support

The burden of proving a claim rests with the applicant who must provide such documentation as may be required by the SRA including when requested, a statement of truth. Failure to provide such documentation or to co-operate with the SRA will be taken into account when determining the merits of the application.

12. Exhausting other remedies

(1) A grant may be refused or limited where the loss or part of the loss is an insured risk or where the loss is capable of being made good by some other means.

(2) The SRA may, before deciding whether to make a grant, require the applicant:

(a) to pursue any civil remedy which may be available to the applicant in respect of the loss,

(b) to commence insolvency proceedings,

(c) to make a formal complaint to the Police in respect of any dishonesty on the part of the defaulting practitioner or

(d) to assist in the taking of any action against the defaulting practitioner.

(3) In the absolute discretion of the SRA, a grant may be made from the Fund before requiring the applicant to resort to other means of recovery.

13. Notice to defaulting practitioner

(1) The SRA shall not make a grant unless:

(a) a communication has been sent to the defaulting practitioner at his or her last known correspondence address or to his or her appointed representative informing the defaulting practitioner of the nature and value of the application; and

(b) not less than eight days have elapsed since the date of receipt of such communication, which shall be regarded as the day following the date of the communication.

(2) If it appears to the SRA that any communication sent under paragraph (1) will not come to the attention of the defaulting practitioner or his or her appointed representative, then the SRA may make a grant notwithstanding failure to comply with the provisions of this rule

14. Costs

(1) **Litigation**

Where an applicant intends to or has already instituted proceedings for recovery of his loss and wishes to apply for a grant in respect of the costs of the proceedings, the SRA will only consider such costs where:

(a) they can be shown to be proportionate to the loss, and

(b) there is a reasonable chance of making a recovery in respect of the loss, or,

(c) the proceedings were necessary for the making of an application to the Fund

(2) **Application costs**

Where a grant is made, the SRA may consider an application for a further grant in respect of the reasonable costs properly incurred by the applicant with either his solicitor or other professional adviser, provided that such costs were incurred wholly, necessarily and exclusively in connection with the preparation, submission and proof of the application

(3) **Costs where the defaulting practitioner has failed to complete work**

If the defaulting practitioner did not complete the work for which he was paid, a failure to account shall be deemed to have arisen within the meaning of rule 3(2)(b) of these rules. In such circumstances, the SRA may consider making a grant in respect of the additional reasonable legal costs incurred by the applicant in completing the outstanding work or a grant by way of contribution towards those costs.

15. Interest

(1) The SRA may consider an application for a supplementary grant by way of a sum in lieu of lost interest on a principal grant. Such interest will be calculated in accordance with the rates prescribed from time to time by the SRA. This will normally be calculated from the day upon which the loss which was the subject of the principal grant was incurred, up to the next working day after payment of the principal grant. Such payment will take into account that a grant is a gift and is therefore not subject to tax.

(2) Where the application for the principal grant is in respect of a failure to redeem a mortgage, the SRA may also make a grant in respect of the additional interest accrued to the mortgage account as a result of the defaulting practitioner's failure to redeem.

16. Maximum grant

Subject to rule 22, the maximum grant that may be made is £2million.

17. Recovery and Subrogation

Where a grant is made otherwise than by way of loan or if by way of a loan repayment of the loan is waived or otherwise the borrower has failed to repay part or all of the loan, the Society shall be subrogated to the rights and remedies of the person to whom or on whose behalf the grant is made (the recipient) to the extent of the amount of the grant. In such event the recipient shall if required by the SRA whether before or after the making of a grant and upon the SRA giving to the recipient a sufficient indemnity against costs, prove in any insolvency and/or winding-up of the defaulting practitioner and sue for recovery of the loss in the name of the recipient but on behalf of the Society. The recipient shall also comply with all proper and reasonable requirements of the SRA for the purpose of giving effect to the Society's rights and shall permit the SRA to have conduct of such proceedings.

18. Deduction from grants

(1) The SRA may deduct from any grant the costs that would have been legally due to the defaulting practitioner so that the applicant will not be in a better position by reason of a grant than he or she would otherwise have been in.

(2) The SRA may within its discretion deduct from any grant all monies already recovered by an applicant and monies which either will be or should have been recovered.

19. Refusal of an application

(1) If the SRA refuses to make a grant of either the whole or part of the amount applied for, the applicant will be informed in writing of the reasons for the decision.

(2) The fact that an application has been rejected does not prevent a further application being submitted provided that substantial new relevant evidence, information or submissions are produced in support of the new application.

20. Appeals

Should the applicant wish to appeal against refusal of an application, written notice of intention to appeal must be delivered to the SRA within thirty days of the date of receipt of the decision, which shall be regarded as the day following the date of the written communication of the decision. Such notice must be accompanied by details of the grounds of appeal together with any additional evidence in support.

21. Notice of requirements

Any requirement of the SRA under these rules will be communicated in writing.

22. Waivers

The SRA may waive any of the provisions of these rules except rules 13, 19, 20 and 21.

23. Repeal and commencement

(1) These rules shall come into operation on 1 March 2009, whereupon the Solicitors' Compensation Fund Rules 1995 shall cease to have effect save in respect of applications submitted before that date, which shall continue to be subject to the 1995 rules.

(2) On 1 July 2009, rule 4 shall be amended as follows:

(a) In paragraph (2):

(i) delete "cancelled under regulation 8 of the European Lawyers Registration Regulations 2000" and substitute "revoked under regulation 9.2(a)(ii) of the SRA Practising Regulations [2009]"; and

(ii) delete "suspension or cancellation" and substitute "suspension or revocation";

(b) In paragraph (3):

(i) delete "had expired for non-renewal under regulation 8.3" and substitute "was suspended or was revoked under regulation 9(c)"; and

(ii) delete "expiry" and substitute "suspension or revocation"; and

(c) In paragraph (4):

(i) delete "cancelled under Schedule 14 paragraph 3(4)(a) of the Courts and Legal Services Act 1990" and substitute "revoked under regulation 9.2(a)(ii) of the SRA Practising Regulations [2009]"; and

(ii) delete "suspension or cancellation" and substitute "suspension or revocation".

Stop loss insurance guidance

The Compensation Fund Working Party instructed Marsh to advise on the suitability and cost of purchasing catastrophe cover for the Compensation Fund. With very little information to work on, other than estimations by the Fund itself for subscription setting purposes, Marsh sought to at least ascertain some feel for likely costs.

As a guide, based on Marsh's experience, the following might be achievable:

RISK TRANSFER

Period of Insurance:	3 years
Retention by the Fund:	£60m in the aggregate for all claims during the 3 year Period of Insurance
Limit:	£20m (excess of the £60m retention by the Fund)
Co-Insurance:	10% - in respect of the limit of £20m, once the aggregate retention has been exhausted, the Fund would be required to pay 10% of each insured claim.
Maximum Loss any one firm:	£2m
Term Premium:	£1.5m to £2m

These are Marsh's best estimates given the absence of detailed loss data and actuarial modelling. As an enhancement it should be possible to secure cash flow protection by means of a funding facility at Libor plus 300 basis points.

The advice from Marsh is that, even if it was possible to achieve a structure along the lines outlined, at face value the terms do not appear to be attractive if the Fund's out turn is close to its projection of losses. By its very nature the structure Marsh was contemplating is designed to deal with catastrophic and unexpected outcomes. The programme's ability to deal with this is somewhat constrained by the sub-limit of £2m in respect of any one firm. This sub-limit would apply in two ways, first for the purposes of eroding the Fund's £60m retention and second in respect of claims once the aggregate retention has been exhausted. The sub-limit could be increased, but combined with a significant impact on the amount of risk which the Fund would be required to retain and a somewhat lesser impact on the actual premium.

Marsh's assessment was that the prospect of a viable scheme was poor and currently difficult to justify economically.

Protecting Clients of a Globalised Profession: Implications of Members' Responses to the International Bar Association Survey of Client Compensation Arrangements: 2004-05

Adrian Evans and John Moorhouse[1]

Introduction

Proper professional conduct is at the centre of the standing and respect earned by lawyers throughout the world. Codified provisions and the decisions of the governing bodies of most bar associations strongly support the imperative of professional behaviour. Collectively, these rules and structures ensure that lawyers do not act abusively, negligently or in a manner inimical to the honour of the profession.

Nevertheless, the legal profession recognises that there is a minority of lawyers unworthy of the trust their clients place in them. When lawyers abuse trust or make mistakes, without providing compensation, clients and governments are entitled to assert that the profession is more interested in its members than the good of the community.

Some bar associations and law societies have established arrangements for *client protection* in order to demonstrate that their primary commitment is to clients and, by implication, the wider community. These arrangements compensate clients who have incurred economic loss occasioned by the dishonest conduct of a lawyer (in stealing trust funds) or in the negligent handling of legal work. Where client protection is provided by member bars, it usually takes the form of a specific Fund to compensate clients for lawyer theft (often through a Clients' Protection Fund Committee, established by the bar to receive, hold, manage and disburse from the Fund such monies as may be necessary to provide compensation), and an insurance scheme or pool of funds to compensate clients for negligent advice or representation.

Client protection arrangements have both benefits and some potential difficulties, as follows:

Potential Benefits of Client Protection

- Ensures aggrieved parties will be compensated for negligence or dishonesty of legal professionals
- Helps restore injured clients' confidence in the profession after receiving compensation from a Fund
- Ensures social accountability for lawyers, and can help to improve ethical standards
- Assists in demonstrating to all institutional stakeholders and governments that lawyers form a responsible profession that can continue to be trusted by society to

[1] Adrian Evans is Associate Professor of Law, Monash University, Australia and John Moorhouse is Executive Director, Attorneys Fidelity Fund, South Africa. The authors thank Valentina Zoghbi and Leslie Alekel of the International Bar Association , London, for their considerable efforts in compiling the information for this report.

hold clients' funds, and to deliver competent and ethical legal services to the global community.

Potential Difficulties

- Worldwide 'coverage' of compensation arrangements must be reasonable if the ethic of client compensation is to be credible
- If a particular Fund is not adequately financed, or if the conditions of compensation are too restrictive, this may provide a false sense of security to those who are likely to suffer financial loss, and impair the credibility of the profession more than if no Fund had existed at all
- In some jurisdictions, claimants are required to have been a client of the legal professional in order to make a claim, which excludes some third parties from recovery
- Compensation arrangements may embolden some unethical lawyers to act dishonestly or carelessly
- Average times for resolving contested claims on a Fund can be long, leading to further client dissatisfaction.

In order to clarify the extent of client compensation arrangements provided by member bars, and to better understand the level of the global profession's commitment to client compensation, the International Bar Association invited all its Member Organisations in 2004-05 to participate in a survey of their present compensation arrangements. This concise report summarises responses to that invitation, and makes key recommendations on the form, structure and extent of client compensation schemes worldwide. We note that the North American National Client Protection Organisation (NCPO) has published a comprehensive list of standards[2] for evaluating client compensation arrangements. The recommendations of this report overlap to some extent with these standards. Where overlap occurs, we refer to the relevant NCPO Standard.

A limitation of the analyses in this report arises from the wide divergence in cultural understandings and legal system traditions encountered by the surveyors. There is some evidence of linguistic misunderstanding and confusion among those who completed the survey, which for cost reasons could only be administered in English. These limitations dictate that the conclusions of this report should be interpreted cautiously. Nevertheless, the authors consider that the recommendations based on these conclusions are reasonable, not merely by reason of this survey, but also because of their understanding of global client compensation mechanisms.

[2] Adopted by the NCPO as official policy at the organization's Annual Meeting of June 2, 2006. See www.ncpo.org

Scope of the Survey Questionnaire and Range of Responses

In order to categorise the many different approaches to client compensation, member bars were asked to decide whether their arrangements consisted of either 'one Fund only' (theft or negligence compensation), 'two Funds' (compensation for both), a 'different Fund' structure or 'no client protection Fund'. The full text of the questionnaire can be viewed at www.ibanet.org.

In each sub-survey, the intent was to determine a number of parameters such as the control of compensation Funds (lawyer *v* non-lawyer); the extent and method of Fund advertising; fund size, coverage, income sources and asset balance; client awareness of ability to earn interest on trust balances; claims limits and pre-conditions (including prior disciplinary or civil proceedings); delay in claims processing; rights to re-hearing; the extent of claims reporting (including claims details and names of lawyers); methods of claims reporting; and finally, claims prevention strategies.

There was a great variety of responses to all of these questions. The primary category of loss for which a claim may be lodged is the dishonest conduct on the part of the lawyer within a lawyer/client or fiduciary relationship. This category involves theft or misappropriation of money or property by the client's lawyer - defalcation or embezzlement of money; the wrongful taking or conversion of money, property or other things of value; refusal to refund unearned fees received in advance where the lawyer performed no services, or the borrowing of money from a client without intention to repay.

On the issue of advertising the existence of a Fund - a key client protection strategy - the steps taken range from making information available on websites, to media releases (Oregon, New Zealand); co-operation with disciplinary counsel (Vermont); brochures and press releases (Hawaii); producing brochures and annual reports (Nova Scotia); mailing out newsletters (South Africa); general post mailing (Massachusetts); press releases and informational pamphlets to a wide variety of organizations and agencies (Ohio). One Fund relies on a website only (Ireland), and another on media releases only (New Jersey). A majority of the bars having client protection Funds do publish annual reports, but what is actually published and how it is published remain important issues where further improvement is warranted.

Frequency of decision-making meetings provides some indication of concern for client compensation, and the practice is extremely variable. The most frequent interval is monthly (New Jersey, Ireland and Massachusetts), while the least frequent meetings only occur when claims are made (Vermont and New Zealand). Other jurisdictions range from 2-3 meetings annually (Finland, Nova Scotia and South Africa[3]), to quarterly (Kansas, Hawaii and Ohio), and every two months (Oregon). Another important indicator of client accountability relates to the availability of re-hearing or appeal processes, when a client is

[3] In South Africa, while the Fidelity Fund Board of Control meets four times a year, claims are sent to the members in different parts of the country on a round robin basis, so that in effect claims are examined on an ongoing process.

initially denied compensation, or receives a lower sum than claimed. The majority of the bars surveyed permit a rehearing (by the same committee), but do not allow any appeal or judicial review (the Danish Bar and the Danish Law Society, Finnish Bar Association, Kansas Lawyers, New Jersey Lawyers). There are nevertheless exceptions with some bars allowing for judicial review and/or appeal (e.g. Oregon State Bar, Law Society of Ireland).

Fund sizes differ enormously and there is a rough correlation between size and sophistication of procedures and compensation levels. The greatest number of lawyers covered by a Fund is 79,600 (New Jersey, which may be considered one of the most generous of United States' Funds) followed by Massachusetts with 47,700 lawyers. The least number is 1,200 (Nova Scotia).

Asset balances also often vary according to the number of legal practitioners in each particular jurisdiction, fees, the method of collection and the number of claims the Fund has experienced. The highest current asset balance was €152.7 million (South Africa) – whereas the lowest was US$220,000 (Vermont). Clients can earn interest on their trust balances (Danish Bar and Danish Law Society, Finnish Bar Association, South Africa, Kansas Lawyers, New Jersey Lawyers). Only one bar does not allow clients to earn interest on trust funds (State Bar of Montana). Unfortunately, quite a few respondents appear not to have understood the request for information about whether and how clients were made aware of the possibility of earning interest on trust balances, or simply did not answer this question.

Some Funds require any civil proceedings brought against the recalcitrant lawyer to be concluded before a claim is paid out (Danish Bar and Law Society, Massachusetts Clients' Security Board of the Supreme Judicial Court), while others do not have any requirement of this nature (Law Society of Ireland, Louisiana State Bar Association, State Bar of Montana, Supreme Court of Ohio).

Regarding current sources of income, the most common source of income is a lawyer levy/assessment premium, paid personally or via a law society/bar association. Lawyer levy constitutes the unique source of income for the Vermont Bar Association. In a fewer number of jurisdictions, interest earned on trust balances is also important (for example, in Australia and the Attorneys Fidelity Fund South Africa[4], Danish Bar and Danish Law Society), and finally, recoveries from defaulting lawyers which contribute a small percentage of income (New Jersey - 14%, Ireland - 5%, New Zealand - 4%, Massachusetts and Ohio).

Full details of members' responses can be found in **Appendix 1** to this report.

[4] The primary source of funding in these jurisdictions derives from interest on client funds which the lawyers to whom such funds are entrusted are not required to invest – essentially a multiplicity of deposits of day/overnight money received countrywide on day one, and paid out shortly thereafter. At present the Funds consider that the investment of these funds on behalf of the depositors would be costly or simply more trouble than it would be worth, though it is likely over time that desk top trust accounting will allow easy and low cost interest calculation, a process which has already commenced in Scotland.

Level of Responses

Only 44 of the bar organisations on the IBA members' list (**Appendix 2)**, together with another 19 organizations that were not on the list (see **Appendix 3**), responded to the survey. Of these 63 respondents:

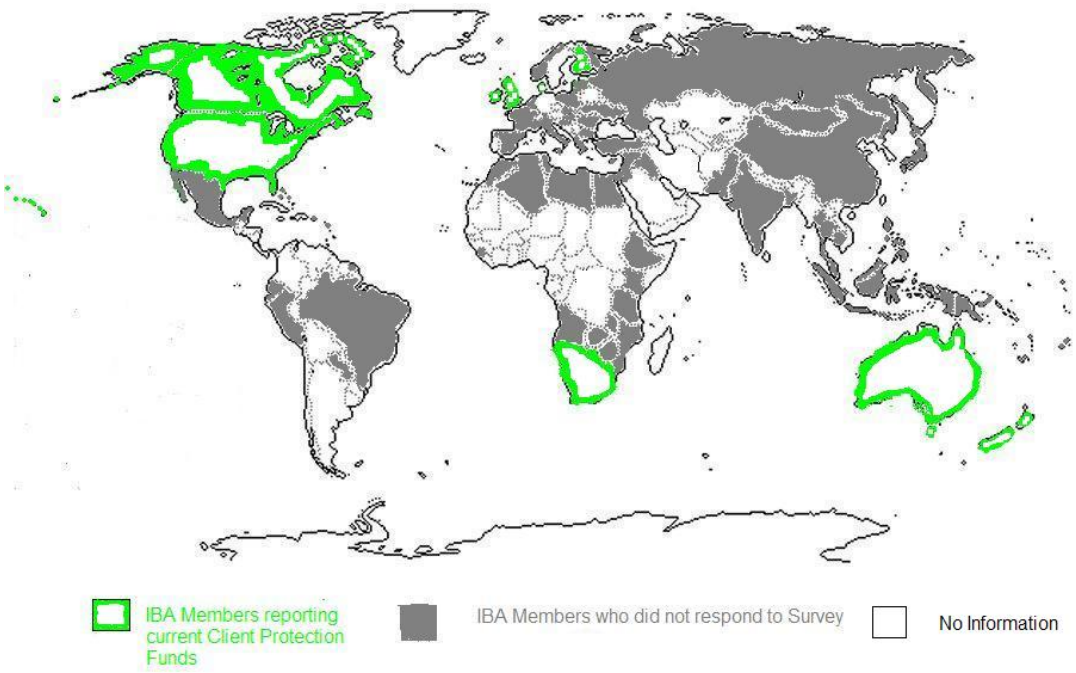
- 23 members currently have client protection Funds in place, with
  - 16 protecting from theft only
  - 2 protecting from mistakes/negligence only and
  - 5 protecting from both theft and negligence
- 31 members do not have client protection Funds in place, but a further 5 members do require lawyers to have mandatory professional indemnity liability insurance cover. Note however that
  - Quebec has only negligence compensation and has apparently had so little claims experience that it currently runs on accumulated investment income only, without the need for practitioner premiums
- 7 have a different type of Fund structure (not catagorised as a client protection fund). Note that
  - Denmark is proposing to combine its two funds into one, which would cover both theft and negligence compensation and that payment not be discretionary, (so that only 'applications', not 'claims', can be made) but based on ordinary liability principles
  - all eight Australian jurisdictions have extensive client compensation funds with income, structures and payments mechanisms similar to South Africa

Significant Non-Response by Member Bars

Non-respondents to the survey were unfortunately more numerous than those which did respond. Ninety-nine of the organisations on the IBA members' list did not respond – even to advise that they did not operate any client compensation scheme. This is a significant disappointment to the IBA.

The lack of response alone, in our opinion, justifies what might otherwise appear to be radical steps to remedy a lack of institutional concern for clients' rights, and upon which the IBA alone is in a position to give leadership. It is correct that many IBA Member Organisations are associations of advocates only, which groups typically do not hold clients' funds and do not require compensation schemes for lawyer theft. It is also possible that officials of these organizations may have concluded that the focus was only on fidelity compensation rather than also on compensation for lawyer negligence. Additionally, non-respondents may have failed to respond because of language or cultural difficulties; thus many civil law systems do not appear to have a tradition of client compensation. Nevertheless, a perusal of the list of non-respondents (see **Appendix 3**) indicates considerable diversity in this group and we are unable to conclude that communication or cultural difficulties provide an adequate reason for the poor response, particularly as the IBA staff went to considerable lengths to encourage all members to participate, even if that participation would only have been to record a lack of any compensation mechanisms in those jurisdictions.

The following map gives a broad indication of the low level of responses to the survey:



Common Themes in Responses

The following table provides quantitative information about specific questions asked in the survey: [Comments in square brackets reflect the opinions of the authors]

Questions	Yes	No
Formal hearing process for uncontested claims? [This response indicates that a desirable degree of informality prevails in respect of uncontested claims, and we believe this practice should be encouraged because it will aid speedy settlement of minor claims]	5	9
When claim is rejected, is there provision for -		
Re-Hearing? [This is an appropriate response]	10	4
Appeal? [An inappropriate response – appeal is important to demonstrate community accountability, especially where a Fund controlling body does not include any lay representatives]	3	13
Judicial Review? [Inappropriate response – see Appeal above]	2	14
Standard Claim Form? [An appropriate response]	13	4
Can clients earn interest on trust account balances? [An appropriate response – though respondents generally did not answer questions in relation to client awareness of interest availability on their trust account balances]	11	1

Questions	Yes	No
Re-insurance arrangements? [Inappropriate response for large Funds – large Funds are advised to consider reinsurance where actuarial calculation deems this to be appropriate]	3	12
Have Fund assets ever been inadequate to pay claims? [Occasional inadequacy does not appear to be major problem]	4	2
Maximum payment limits for any one claim? [Maximum payment levels are undesirable having regard to the primary compensatory purpose of Funds]	9	6
Maximum amount that the Fund will pay in respect of any one lawyer? [As above - maximum payment levels are undesirable]	5	9
Must Claimant be a Client? [Claims availability to third parties is preferable, providing their loss is directly referable to a lawyer's actions]	10	6
Compensation payable to foreign clients? [Appropriate response]	14	1
Are Fund administrators automatically advised of disciplinary action against a lawyer? [Appropriate and necessary response]	12	4
Must claimants conclude civil action against a lawyer accused of dishonest of negligent conduct, before a claim will be paid? [Views differ on this issue, but many claimants would find prior civil action a difficult, threshold financial barrier to accessing the client compensation system]	4	11
Disciplinary action required against a lawyer before paying a claim? [Claimants in jurisdictions with independent disciplinary systems may be in a better position to make a successful compensation claim if prior disciplinary action is required. We are inclined to agree with the Law Society of British Columbia, which considers that disciplinary proceedings must conclude before a compensation claim is considered, otherwise the lawyer is likely to perceive unfairness and pre-judgment]	5	8
Are Fund administrators personally protected from civil action against them by dissatisfied lawyers or claimants? [Appropriate response – administrators need to be able to deal fearlessly with claims – though this independence should be balanced by their governing bodies acceptance of consumer/client representatives]	12	3
Fund annual report published? [Appropriate response]	14	2
Support an IBA-sponsored training package or short course, to assist in meeting identified needs? [Appropriate response]	6	2
Are moneys available for indemnity enough for claims? [Appropriate response]	12	-
World Wide Web Address for Fund? [Appropriate response]	14	-

Significant Differences in Respondents' Views

While it is obvious from the above table that some members' views were dominant with little dissent, others expressed opinions that were more widely divergent. In particular, there was disagreement as to

- Whether informality in hearing processes should prevail with respect to uncontested claims
- Whether claims should be subject to maximum payout limits – highly contentious in United States jurisdictions
- Whether claimants must be clients – that is, should third parties who are adversely affected also be able to lodge claims?
- Whether disciplinary action must be concluded before a claim is considered
- When funds publish annual reports, most do not name the lawyers' in respect of whom payouts have been made, or if they do they are published in internal professional publications rather than on a website. While there are exceptions,[5] the decision not to publish names of recalcitrant lawyers on a freely accessible website does not aid the accountability of the profession.

We make recommendations in relation to each of these issues at the end of this report.

Compensation for Lawyers' Negligence

Negligence compensation provisions appear even less comprehensive than theft compensation (some United States jurisdictions have optional negligence cover) and this area of client protection deserves major attention. Where negligence compensation is available, it is based on compulsory insurance. However, the primary problem is that there is apparently little enthusiasm by member bars to take responsibility for their members' mistakes by making such insurance compulsory, although in a least one jurisdiction a basic level of cover is provided automatically by the profession for all practising members annually at no cost to them. But considering that the incidence of negligence is a far more frequent occurrence than theft, it is important, indeed overdue, for the IBA to consider providing suitable inducements to member organizations for the introduction of compulsory professional indemnity insurance regimes.

The Use of Interest on Trust Deposits

The use of interest earned on clients' trust funds by law societies and governments has a long history in a few jurisdictions. Almost without exception, these funds are used for worthy purposes, but clients commonly do not know that their funds – that is, the interest their own money earns while deposited in their lawyer's trust account – are being used for such purposes. It is common for member bars to leave the decision as to whether a client's funds are deposited in a controlled (interest-earning) or pooled (general) trust account, exclusively to the lawyer.

[5] for example, Oregon – www.osbar.org, Nova Scotia – www.nsbs.ns.ca and Massachusetts – www.mass.gov./clientssecurityboard

While our understanding has always been that the lawyer has a strict ethical duty to advise the client that where a "substantial" amount is involved, this should be invested in such a way that the interest should accrue to the owner of the money (rather than for the benefit of a Fidelity Fund), there is no contemporary definition of "substantial". United States IOLTA Guidelines (Jan '98) require large amounts, or small amounts which are to be held for a long term, to be invested in interest-bearing accounts for a client's benefit, with all other funds to be deposited in IOLTA schemes. The United Kingdom and Ireland have similar requirements.[6] Louisiana requires that clients must be 'reasonably informed', but no attempt has yet been made to clarify the costs of *calculating* such interest compared to the actual amount of interest, bearing in mind that digital computing now means that the ratio of the cost of calculation to the interest itself, is likely to be continually reducing.

We consider that there is a need for threshold disciplinary rules within law societies and bar associations requiring their members to consider and advise their clients when net interest is likely to be capable of being earned on a particular trust balance, in order to counter any client/consumer perception that lawyers' fiduciary obligations to their clients are being systematically ignored.

Risk Management: Significant 'Leadership' Initiatives: Audit Reform – Scotland, New Zealand and South Africa

SCOTLAND

During the 1990s the claims experience of the Law Society of Scotland's Guarantee Fund deteriorated dramatically in circumstances which indicated that fraud and irregularities by solicitors were not being detected by accountants. The profession demanded action, and the Fund responded by tightening its rules, the most significant of which provided for –

- the submission by practitioners of Accounts Certificates to the Law Society every 6 months
- a dedicated trust account partner, personally liable for overseeing the trust accounting work
- checking the accounting systems of all new firms within 6 to 9 months of commencement of practice
- routine inspections, which are much more testing than those of the accountants were, and special (cause-driven) inspections when necessary
- special seminars for trainee solicitors, new partners, trust account partners, cashiers and office managers.

[6] Ireland has a €100 interest threshold, beyond which that interest must be paid to the client.

Acceptance of the responsibility by solicitors for their own compliance with the accounts rules has been eminently successful and has even resulted in higher standards of disclosure than were provided by accountants previously.

The Society now constantly restates its view that it can regulate the profession better than an outside body can do.

NEW ZEALAND

The New Zealand Law Society's Fidelity Guarantee Fund also suffered extensive losses, in consequence whereof member solicitors were required to pay substantial contributions in order to replenish the capital base of the Fund. In New Zealand, too, it was found that the surveillance of the administration of solicitors' trust funds by means of audits of trust accounts carried out by firms of chartered accountants had proved to be of little use in detecting fraud.

During 1995 the Society took outside advice to review its customary audit scheme, and to suggest an alternative. The upshot of the review was that the Society resolved to abolish the traditional audit system, and to implement what is known as the Financial Assurance Scheme, the principal features of which are –

- no compulsory audits
- systematic compliance reviews – a simple check on a firm's trust accounting system every 2 to 7 years
- cause-driven compliance reviews
- cause-driven inspections of worrisome trust accounts
- random inspections – inspectors may call at any time without an appointment
- new practice compliance reviews – systems' checks by inspectors for newly-launched practices
- simplified recordkeeping – new rules to set a standard rather than to prescribe procedures
- trust account partner required to administer the account
- monthly and quarterly certificates to be submitted to the Society by practitioners
- relief for firms not handling client money
- better education in trust accounts
- improved intelligence system – for earlier detection

It will be seen from the above that there is a great deal of commonality in the features of the respective audit reform initiatives adopted in Scotland and New Zealand.

SOUTH AFRICA

The Attorneys Fidelity Fund in South Africa is presently funding a pilot project being administered by the KwaZulu-Natal Law Society (one of the four statutory law societies in the country), which is based on a combination of the best features of the systems described above, as well as the incorporation of such other features as may best suit

domestic arrangements in South Africa, and it is hoped that once the pilot project has been evaluated a system structured along the lines of the pilot project will be introduced throughout the country as a permanent risk management tool to minimise irregularities in the administration of trust funds by delinquent attorneys.

Recommendations

Taking into account the opinions of participants in the survey and our knowledge of the innovations in Scotland, New Zealand and South Africa, we make the following recommendations as to the future of client compensation and the most cost-effective approaches to claims prevention among IBA members:

- Among those Member Organisations offering legal services to the community, client compensation for negligence and fidelity breaches should become a qualifying pre-condition for IBA membership within five (5) years of the date of acceptance of such a recommendation by the IBA governing body

- The feasible and reasonable standards for such arrangements should include the following:

  Having regard to NCPO Standards (No 2.7), the following priorities in theft prevention strategies should be established
  - mandatory trust account education requirements for all law students *and* new practitioners
  - practitioners to file copies of monthly trust reconciliations for the first 6 months of a new practice
  - compulsory practice management courses, to reduce the risk of new practitioners mismanaging their operations and misappropriating trust funds
  - strict record-keeping
  - third party payee notification
  - new practice inspections by the regulator
  - monthly certificates by practitioners, certifying that their trust -accounts are in order
  - annual extemporaneous inspections of all trust accounts by the regulator, where feasible
  - automatic overdraft notification by banks where lawyers' trust accounts are held
  - regulatory penalties for failure to report a colleague suspected of having committed irregularities with respect to trust monies
  - free and anonymous 'whistleblower' phone lines
  - regular and well-circulated publication of payments from the Fund in respect of the thefts of named (former) lawyers
  - international claims information sharing to deal better with multinational law firms' operations

- automatic advice by disciplinary authorities to Fund administrators of all disciplinary investigations

assertive pursuit and discipline of offending lawyers, both as regards criminal prosecution and monetary recovery from such lawyers consequent upon claims paid by Funds

- Enshrining a requirement in legal professional conduct rules for the provision of threshold advice to clients and legal practitioners concerning the interest-earning capacity of trust deposits

- Claims should not be capped either for single claims or in the aggregate (see NCPO Standard No 4.1, 4.2)
- Adequacy of Fund reserves should be actuarially assessed (see NCPO Standard Nos. 2.1, 2.4.2.5)
- Controlling Boards should have some non-lawyer members to improve Funds' accountability to the community (NCPO Standard No 1.4)

- A standard claim form (example – see Solicitors Guarantee Fund Rules 1936 – statutory regulations at www.legislation.govt.nz) should be promulgated by the IBA Client Protection Constituent

- Informal administrative consideration should be introduced for the disposal of uncontested claims and progress on resolving contested claims should be reviewed at 3 monthly intervals by controlling boards (NCPO Standard No 4.4)

- A provision that rejected claims may be appealed and reviewed judicially on points of law

- Anonymised details of claims circumstances, and the names of lawyers against whom awards are made should be published as decided, on Fund websites

- An IBA-sponsored training package or short course should be established to assist Member Organisations in meeting the above standards

- The Client Protection Constituent of the IBA should be provided with designated resources to promote client compensation standards in those regions which appear in most difficulty of meeting the five-year deadline referred to above
- Federal jurisdictional systems which share similar legal histories should consider one national Fund (as in South Africa), rather than many provincial systems (as in USA, Russia, Australia and Canada), in order to minimise 'back office' expenses, and to reduce multi-jurisdiction compliance costs across each federal system.

Challenges Ahead and Conclusion

Significant emerging challenges will arise from rapidly emerging online property registration technology and electronic funds transfer technology, which are likely to open up new areas for thefts which can be committed more quickly and take longer to investigate and prosecute. Clients will expect, and are entitled to see, compensation mechanisms not just become the norm, but also to see these develop in sophistication, together with the ability to provide timely compensation mechanisms in the face of technologically-complex thefts.

The globalisation of business and the implications of the GATS agreement (allowing foreign lawyers to practise in host countries – with a possibility of increased risk of theft), will heighten the risk of *large-scale* theft, with money transcending borders. These developments add to the pressure for most jurisdictions to operate compensation schemes and for Funds to provide relatively uniform protocols and coverage, consistent with the resources of different jurisdictions.

We encourage members of the IBA to embrace the implications of this report positively as an opportunity to protect clients of the globalised profession, secure in the knowledge that if these steps are taken, external regulators will have little excuse to assert either that the profession is indifferent towards its clients or that we are not adopting best practice in claims prevention. Either charge, if sustained, will give governments the chance to interfere in client compensation regimes established by the profession, and to impose standards which could well prove unworkable.

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Appendices

1. Table of Responses
2. IBA Members who responded to the survey
3. Non-respondent Members.

Appendix 1
IBA Members Who Responded to Survey

- **23 members currently do have client protection funds in place**: Fonds d'assurance Responsabilite Professionnelle du Barreau du Quebec; General Council of the bar of England and Wales; Law Council of Australia; Finnish Bar Association; Law Society of England and Wales; Oregon State Bar; Vermont Bar Association; New Jersey Lawyers; Kansas Lawyers; Office of Disciplinary Counsel of Hawaii; New Zealand Law Society; Supreme Court of Ohio; Law Society of Namibia; State Bar of Montana; Louisiana State Bar Association; Danish Bar and Law Society; Law Society of Saskatchewan, Canada; Law Society of Ireland; Nova Scotia Barrister Society; Attorneys Fidelity Fund South Africa; Law Society of Botswana; Law Society of Prince Edward Island; Law Society of Newfoundland and Labrador.

  Of these 23 jurisdictions that do have client protection funds (in some form):

  - 16 protect from theft only: Finland, Oregon (U.S.), Vermont (U.S.), New Jersey (U.S.), Kansas (U.S.), Hawaii (U.S.), New Zealand, Massachusetts (U.S.), Ohio (U.S.), Louisiana (U.S), Montana (U.S), Namibia; Law Council of Australia (note that all eight Australian provincial jurisdictions offer client protection through separately funded arrangements for defalcation compensation and professional indemnity insurance); Law Society of Botswana, Law Society of Prince Edward Island, Law Society of Newfoundland and Labrador.

  - 2 protect from mistakes/negligence only: England and Wales and Fonds d'assurance Responsabilite Professionnelle du Barreau du Quebec

  - 5 protect from both theft and negligence: Ireland, Nova Scotia, South Africa, Danish Bar and Law Society and Law Society Saskatchewan, Canada (plus the 8 Australian jurisdictions)

- **31 currently do not have client protection funds in place**: Australian Bar Association; Austrian Bar Association; Bermuda Bar Association; Cape-Verdean Bar Association; Colegio De Abogados de Chile; Colegio de Abogados de Costa Rica, San Jose; Colegio de Abogados del Districto Federal, Caracas, Venezuela; Colegio de Abogados de la Ciudad de Buenos Aires, Argentina; Colegio de Abogados Santa Cruz De Tenerife; Colegio De Abogados De Madrid; Colegio De Abogados De Panama; The Faculty of Advocates, Scotland; General Counsel of the Bar of Northern Ireland; Ghana Bar Association; Hong Kong Bar Association; Indonesian Advocates Association (Peradi); Norfolk Island Bar Association; General Council of the Bar (South Africa); Nigerian Bar Association; German Bar Association (Deutscher Anwaltverein); The German Federal Bar; Hungarian Bar Association; Icelandic Bar Association; Mexican Bar Association; Swedish Bar Association; Swiss Bar Association; Ordem Dos Advogados De Portugal; Romanian National Union of Bar

Associations; Ordem Dos Advogados do Brasil; Colegio de Abogados De Uruguay, Montevideo; Japan Federation of Bar Associations.

- **No funds** – among these, the Swedish Bar Association; Romanian National Union of Bar Association, Hungarian Bar Association; Hong Kong Bar DO require lawyers to have mandatory liability insurance.
- **7 have a different type of fund structure, not categorised as a client protection fund**: Iran Central Bar Association; Law Society of South America; Law Society of Northern Ireland; Idaho State Bar Client Assistance Fund; Research Society of International Law, Pakistan; Law Society of British Columbia and Law Society of South Africa.

Closed-Question responses

Questions	Yes	No
Formal hearing process for uncontested claims?	5	9
When claim is rejected, is there provision for?		
Re-Hearing	10	4
Appeal	3	13
Judicial Review	2	14
Standard Claim Form?	13	4
Can clients to earn interest on trust account balances?	11	1
Re-insurance arrangements?	3	12
Have Fund assets ever been inadequate to pay claims?	4	2
Maximum payment limits for any one claim?	9	6
Maximum amount that the fund will pay in respect of any one lawyer?	5	9
Must Claimant be a Client?	10	6
Compensation payable to foreign clients?	14	1
Are Fund administrators automatically advised of disciplinary action against a lawyer?	12	4
Must claimants conclude civil action against a lawyer accused of dishonest of negligent conduct, before a claim will be paid?	4	11
Disciplinary action required against a lawyer before paying a claim?	5	8
Are fund administrators personally protected from civil action against them by dissatisfied lawyers or claimants?	12	3
Fund annual report published?	14	2
Support an IBA-sponsored training package or short course, to assist in meeting identified needs?	6	2
Are moneys available for indemnity enough for claims?	12	-
World Wide Web Address for fund?	14	-

More general comments:

- There are discrepancies between the above table and the larger qualitative report
- South Africa is a 2-fund model which has an offshoot PI insurer subsidiary which provides free or near free PI cover to South African practitioners – utilising surplus income from trust account interest.

Appendix 2

IBA Members Who Responded to Survey

NAME LAW ORG	TYPE OF FUND	FEATURES OF THE FUND
Australian Bar Association	No Client Protection Fund	The Australian Bar Association does not intend to setup a fund, because of the nature of a barrister's practice, to establish a protection fund (Fidelity Fund). Barristers do not deal with client monies and therefore the problem does not present itself. There are no reported instances of theft of client funds by barristers. -If negligence is proven against a barrister causing loss to a client then the client is protected by a Barrister's Professional Indemnity Insurance. All Australian Barristers are required to hold a policy of insurance. -The minimum policy of insurance in most jurisdictions ranges between AUD $1M and AUD $ 1.5M. -It is a statutory requirement in most jurisdictions to hold professional indemnity insurance in order to obtain a practising certificate.
Law Council of Australia	One Fund that protects from theft	There are separate funds in each state and territory. Some are run by the governments and some are run by the law societies. The fund does not protect against malpractice because this is done by other funds/insurers.
Austrian Bar Association	No Client Protection Fund	It is compulsory for members of the branch of the profession to insure themselves against clients' claims for financial loss due to negligence. Each lawyer who works in Austria has to have his own professional indemnity insurance for a minimum amount of Euro 400.000. Some Bars offer the possibility to join voluntarily a group insurance on top of the basic minimum indemnity insurance.
Bermuda Bar Association	No Client Protection Fund	
Cape-Verdean Bar Association	No Client Protection Fund	The Members of the Cape-Verdean Bar Association do not handle clients money.

Colegio de Abogados de Chile	No Client Protection Fund	
Colegio de Abogados de Costa Rica, San Jose	No Client Protection Fund	
Colegio de Abogados del Distrito Federal, Caracas, Venezuela	No Client Protection Fund	
Colegio de Abogados de la cuidad de Buenos Aires, Argentina	No Client Protection Fund	
Colegio de Abogados de Uruguay, Montevideo	No Client Protection Fund	
Colegio de Abogados Santa Cruz de Tenerife	No Client Protection Fund	
Colegio de Abogados de Madrid	No Client Protection Fund	
Colegio de Abogados de Panama	No Client Protection Fund	
Danish Bar and Law Society	Two Funds – One protects from Theft and One Protects from Mistakes/ Negligence	**General Information:** - Name of the Fund is Det danske Advokatsamfunds erstatningsfond - Established: Theft Fund – 1953 Negligence Fund – 1975 - Number of Board/Committee members of Fund: 5 lawyers - Steps taken: The Fund is mentioned through a listing of the rules

regulating the Danish Bar and Law Society.

- Frequency of decision-making meetings: Monthly
- Successful judicial challenge to the existence or jurisdiction of the Fund: U 2003.380 H (Supreme Court) Hans Henrik Lund vs The Danish Bar and Law Society.
  The claimant contested the Danish Bar and Law Society to force its members to pay premium to an insurance and the funds. The Supreme Court voted against the claimant.
- Accounting period: 1/1/20xx to 31/12/20xx
- Currency: DKK (Danish kroner)
- Estimated number of legal practitioners covered by the fund: 4600.
- Current Asset Balance: 34.000.000,00 as of 1/1/2003

- **Current Sources of Income reflected as follows:**

Sources of Income:	Amount:	Per cent contribution to total amount
Lawyer levy/assessment premium or via Law Society/Bar Association:	8.352.464/-	81.4%
- Interest on - Fund Investments:	1.750.957/-	17%
- Recovery: Amount:	137.923/-	1%
- Other Sources: Delayed payments from previous fiscal years:	16.115/-	0.6%
Total	10.257.459/-	100%

- Amount paid by each lawyer annually: 1900/-

- It is possible for clients to earn interest on trust account balances

- Actual/Projected amount and percentage distribution of Fund balance for stated accounting period:

- Administration costs: 1.000.000
  Percent contribution to total: 15%
  Actual/Projected proved claims for compensation: 5.700.00
  Percent contribution to total: 85%
  Total Fund Expenditure: 6.700.000/-

- Distribution of any excess fund balances between the beneficiaries: Any available funds are transferred to the following fiscal year.
- The fund has enough assets to pay likely claims over the next 5

		years. - Method to protect fund's assets against unexpected claims: All payments from the fund are based on the fund committee's judgment.(1) No one has a legal claim to receive money from the fund, so the committee can reject claims. (2) Extraordinary premium from all members. (3) The fund can pay individual member's public liability insurance. - The fund does not have any re-insurance arrangements in place. - There has never been a situation where assets of the Fund were inadequate to pay claims. **Claims Against Fund**: - Categories of loss for which claims may be lodged: Fund A: Theft (72% of all claims). Fund B: Negligence (28% of all claims). In 94% of the A-claims and in 5% of the B-claims the lawyer is bankrupt or under similar proceedings. - There are maximum payment limits for one claim - There is also a maximum amount that the fund will pay in respect of any one lawyer. Fund A: No maximum limit. Fund B: 1.435.000/- - There is a requirement that the claimant was a client of the lawyer. Fund A: Client requirement. Fund B: Anyone, as long as the claimant has suffered a loss, the lawyer is liable and can not cover the damages himself and the claim is based on substantial evidence. - Foreign Clients: Compensation payable. There are no restrictions, as long as the above mentioned requirements are present. - Claims made: During 1.1.1991 and 31.12.2000 number of claims received: 841 and number of claims approved: 623. - Percentage of the claims approved over the stated period: 74% - Most common reasons for denying a claim: 1. Claims not covered by the Articles of the Danish Bar and Law Society's Regulations – 63% 2. Lack of evidence/documentation – 25% 3. Statute of limitations – 12% - There is a formal hearing process for uncontested claims. - If a claim is rejected, there is a provision for rehearing. But no provision for an appeal. - A rehearing is possible if the claimant is in possession of new substantiated evidence. Same body conducts the rehearing. - There is no provision for judicial review. - There is a Standard claim form in use and a copy is available to the IBA. - It is available in Danish. - Literature made available to the claimants: Standard claim form.

		- The funds administrators are not automatically advised of disciplinary actions against a lawyer. - The fund requires claimants to conclude civil action against a lawyer accused of dishonest of negligent conduct, before a claim is paid. - The fund does not require disciplinary action against a lawyer before paying a claim. - The fund administrators are personally protected from civil action against them by dissatisfied lawyers or claimants. - The fund does not publish an annual report. - The fund does publish its accounts from the two pervious years. This publication also brings a short account of some of its payments. **Strategies to reduce claims:** - Approach taken by the fund to the reduction of member's negligence and/or the audit of any trust or other member's accounts holding client's money: The membership of the Danish Bar and Law Society (DBLS) is mandatory. By law it is vested on the Society/Council to supervise that lawyers adhere to the legal and ethical rules. The Board of the Society has in that capacity adopted provisions regarding the handling of the member's accounts holding clients money (hereafter clients accounts). - Connections, assumptions, evidence established between these programmes and reduction in negligence: Forming independent audit reports. - Proposals or plans to reduce the level or range of protection to clients from the fund: It has been proposed that the member's mandatory insurance should be expanded to also cover gross negligence, which is now covered by Fund B. It has also been proposed that payment from Fund A should not be based on the funds discretion, but should follow the rules covering ordinary liability claims. - The organisation would support an IBA-sponsored training package or short course to assist the organisation in meeting needs identified here. **General Comments:** **Negligence:** - 1. All members are regulated by a professional code of conduct with guidelines stating the rights and duties of lawyers. A member can, if not working according to the abovementioned standards, as a final consequence be debarred. - 2. A lawyer is furthermore governed by a professional liability,

		when determining the fault liability. - It is compulsory for members to insure themselves against client's claims for financial loss due to negligence. - Negligence protection financing: The negligence insurance is mandatory. Each member must document that a negligence insurance for a minimum of 1.4 mio. kr. has been drawn. - If a member omits a payment on the premium, the Council has the possibility of drawing the money needed from the client's protection fund. - Annual premium cover: Each member takes out an individual policy for payment of any bonds or annual premium. - Details of the amount of negligence cover per lawyer, amount of any premium, main exclusions from indemnity, any limits on claims: Minimum covering 1.4 mio. kr. but most members have a greater covering. The insurance does not cover gross negligence or deliberate acts. - In their opinion, moneys available for indemnity are sufficient to meet claims. - There has never been a shortfall.
The Faculty of Advocates (Scotland)	No Client Protection Fund	The Faculty represents barristers and advocates that do not hold clients' funds in the course of their practices. In most cases, the members do not receive instructions directly from any client, or do so only for restrictive purposes, so there is therefore no need to establish any fund to insure against misappropriation of clients' funds.
Finnish Bar Association	One Fund Protects from thefts only	**General information** - The Committee of the Fund subscribes to Lawyers' Criminal Action. - Steps taken to make the Fund known: part of general information of the Bar. - Frequency of decision-making meetings: 2 or 3 annually (sometimes less often). - Accounting period: 1/1/2003 to 31/12/2003. - Name of currency used in this response: euro. - Estimated number of legal practitioners: 2,000. - Current asset balance: €500,000 as of 31/12/2003. - Current sources of Income: the main source is the lawyer levy/assessment premium which represents 94% of the total contribution (€497.000) followed by interest on Fund investments representing 6% of the total (€3.000). - No amount of money is paid by each lawyer annually at the moment. - Lawyers' failure to pay results in disbarment. - It is possible for clients to earn interest on trust account balances. - As for actual distribution of fund balance: projected proved claims for compensation represent 100% of the total. - The Fund allegedly has enough assets to pay likely claims over the next 5 years. - Method used to determine likely claims expenditure over the next 5 years: historical analyses. - The Fund does not have any re-insurance arrangement. **Claims against the Fund** - Claims against the Fund can be based on any lawyer's criminal action,

		such as stealing clients' funds. - There is not a maximum payment limit for any one claim or in respect to any one lawyer. - Applicants can be anybody who has suffered because of the lawyer's action. (Not necessarily his or her client). - Compensation is payable to foreign clients and no limits or restrictions apply. - Percentage of claims approved over the stated period: 67% (2 claims received and approved). - Regarding uncontested claims: - Average time in weeks between lodgement of claim and despatch of agreement: 5. - There is not a formal hearing process for uncontested claims. - Average time for contestation of a claim: 9 weeks. - Regarding rejected claims: there is a provision for rehearing. There is neither for appeal nor for judicial review. - There is not a standard claim form in use. - Fund administrators are not automatically advised of disciplinary actions against a lawyer. - It is not a requirement to conclude civil action or disciplinary action against a lawyer accused of dishonest of negligent conduct before paying a claim. - The Fund administrators are not protected from civil action against them. - The Fund publishes an annual report (also published on the website). This report does not name the lawyers against whom claims are made or give details of the payments made in each claim. **Strategies to reduce claims** - Approach taken by the Fund to the reduction of member's negligence and/or the audit of any trust or other members' accounts holding clients' money: random checks in about every tenth law office annually. - There is no special strategy contemplated to reduce negligence or prevent theft/defalcation. - There are no proposals or plans to reduce the level of protection to clients. - The organization would not support an IBA-sponsored training package or short course to assist the organization or Fund in meeting needs identified here. **General comments** Comments on client protection issues: their compensations are given by discretion. No claims can be made, applications only.
Fonds d'assurance responsabilité professionnelle du Barreau du Québec	Fund Protects from Mistakes / Negligence (or Breach of Mandate) only	**Negligence:** - Legal liability of lawyers to clients for mistakes (negligence) in their jurisdiction and any restrictions on liability: Exceptionally obligation of results, generally obligation of means to act as a reasonably competent lawyer - It is compulsory for members of the branch of the profession to insure themselves against clients' claims for financial loss due to negligence

		- Negligence protection: In the first ten years, our program was financed by levies (premiums) from insured members and in the last seven years, our program has been financed exclusively by investment revenues on equity - Underwriter/scheme manager of the Fund: The Barreau du Québec (the order)is the certified underwriter and it's professional liability insurance fund is a distinct patrimony dedicated exclusively to professional liability insurance operations - Annual premium: The premium, when any, are paid by members - Coverage:10 million dollars per loss no aggregate limitation, no deductible and no premium - Exclusions: D&O, fraud except innocent partners, fines, fees of insured, investment opinions, corporations owned by insured, inter-jurisdictional limitation of 1 million $, fidelity insurance limitation of 1 million $ - In their opinion, moneys are available for indemnity sufficient to meet claims
General Council of the Bar of England and Wales	One Fund Protects from mistakes / negligence only No client Protection Fund	- Under UK Law, barristers have full liability for negligence/mistakes. There is no restriction for lawyers. - It is compulsory to insure themselves against clients' claims for financial loss due to negligence. - Negligence Protection is financed by a compulsory mutual insurance fund. - Each barrister pays an annual premium. - Minimum cover for barristers is £250.000 (shortly to be increased to £ 500.000). No exclusions, no limits on claims. - Moneys available for indemnity are allegedly sufficient to meet claims. - There has never been a shortfall. --Barristers do not hold client funds, thus "compensation" funds, as opposed to insurance, are not relevant to the English Bar.
General Council of the Bar of Northern Ireland	No client Protection Fund	There is no plan to create a Fund.
Ghana Bar Association	No Client Protection Fund	There is no plan to create a Fund.
Hong Kong Bar Association	No Client Protection Fund	Barristers in Hong Kong are a referable profession and the members of the Bar do not hold funds for their clients. Hong Kong Bar has a

		compulsory professional indemnity scheme, however, operating to deal with negligence of Bar Members.
Indonesian Advocates Association (Peradi)	No Client Protection Fund	
Iran Central Bar Associations	Any Other or Different Fund Structure	No single Fund to protect clients for both mistakes in handling cases (negligence) and theft of their money. A very limited Public Fund to aid very poor clients.
Japan Federation of Bar Associations	No Client Protection Fund	There is no plan to create a Fund.
Law Society of England and Wales	One Fund Protects from theft only	The Compensation Fund may help persons who have suffered loss as a result of a solicitor's dishonesty or who are suffering hardship as a result of a solicitor's failure to account for money he or she has received. The loss must have arisen during a solicitor's normal work. If this is the case an application may be made to the Compensation Fund. The Fund is maintained pursuant to section 36 of the Solicitors Act 1974. The application will be investigated by a caseworker. It is the applicant's responsibility to prove the application but the caseworker will give help and guidance wherever possible. After the investigation the application will be referred to an adjudicator or adjudication panel who will decide upon the application.
Law Society of Prince Edward Island	One Fund Protects from theft only	
Law Society of Saskatchewan, Canada	One Protects from Theft and One Protects from Mistakes/Negligence	
Law Society of Newfoundland and Labrador	One Fund Protects from theft only	
Norfolk Island Bar Association	No Client Protection Fund	Norfolk Island, as such, does not yet have these statutory requirements, one reason being that the government lawyers are controlled by government legislation and private lawyers generally do not hold client funds as such, and the other being, that there is no demand for such from

		clients, the profession or government. Those who do all have registration and insurance protection in another jurisdiction as well as Norfolk Island.

Oregon State Bar	One Fund Protects from thefts only	**General information**
		
		- A standing Committee to the Boards of Governors which has final authority over all payments from the Fund. The BOG subscribes to the principles of good governance as it relates to public corporations.
		- Steps taken to make it known: media releases and information on the website (www.osbar.org).
		- Frequency of decision-making meetings: every two months, generally.
		- Accounting period: 1/1/2004 to 1/1/2005.
		- Name of currency used in this response: US dollars.
		- Estimated number of legal practitioners: 12,000.
		- Current asset balance: $896,392 as of 4/30/2004.
		- Current sources of Income: the main source comes from lawyer levy. ($63,000) followed by interest on Fund investments ($14,600).
		- $5.00 is the amount payable by each lawyer annually.
		- Suspension is the penalty for failure of payments by the lawyers.
		- Clients earn interest on deposits of significant amounts or smaller amounts. held for longer periods such that it is possible/convenient for the lawyer to account for the client's interest.
		- As for actual distribution of Fund balance: actual proved claims for compensation ($150,000), and administration costs ($46,960)) being the total expenditure of the accounting period of $196,960.
		- The Fund allegedly has enough assets to pay likely claims over the next 5 years.
		- Method used to determine likely claims expenditure over the next five years: prior history.
		- Method used to protect the Fund against unexpected claims: rules permit special assessments; also do not require payment of claims in full or at all if there is no money available.
		- The Fund has no re-insurance arrangement.
		- Situation where assets of the Fund were inadequate: the assessment was increased in subsequent year and balance of unpaid claims was paid. That led to development of reserve policy.
		
		Claims against the Fund
		
		- Claims against the Fund can be lodged alleging theft or misappropriation of money or property by client's lawyer.
		- Maximum payment limit for any one claim: $50,000.
		- There is not a maximum amount paid by the Fund in respect of any one lawyer.
		- It is a requirement that the claimant being a client of the lawyer.
		- Compensation is payable to foreign clients as long as the lawyer being a member of the OSB at the time of the loss.
		- Percentage of claims approved over the stated period: 80% (8 claims received of which 5 claims were approved).
		- Regarding uncontested claims:
		  - Average time in weeks: 8.
		  - There is not a formal hearing process for uncontested claims.
		- Time average for contestation of a claim: 24 weeks.

		- Regarding rejected claims: the most common reasons for denying a claim are 1) the lack of evidence of dishonesty (80%), 2) no lawyer-client relationship (15%) and 3) lack of proof of payment or loss (5%). There is no provision for either rehearing or judicial review. There is one for appeal conducted by the Board of Governors. - There is a standard claim form in use in English (available to IBA). - Brochure of rules and FAQs are available to claimants to help them prepare their claims. - The Fund administrators are automatically advised of disciplinary actions against a lawyer. - The Fund requires claimants to conclude civil action against lawyers before a claim will be paid. It does not require disciplinary action against the lawyer before paying a claim. - The Fund administrators are personally protected from civil action against them. - There is an annual report, also published on the website (www.osbar.org) in which the names of the lawyers and details of the payments of the claim made against them are reported (e.g. the nature of the lawyer-client relationship and how the loss came to occur). **Strategies to reduce claims** - Approach taken by the Fund to the reduction of member's negligence and/or the audit of any trust or other members' accounts holding clients' money: the Fund counts with trust accounts overdraft rules, programs to help lawyers with substance abuse problems. Oregon has mandatory malpractice insurance for lawyers and an active loss prevention program. - The organization would not support an IBA-sponsored training package or short course to assist the organization or Fund in meeting needs identified here.
Vermont Bar Association	One Fund Protects from thefts only	**General information** - Steps taken to make the Fund known: it cooperates with disciplinary counsel to advertise the existence of the Fund. - Frequency of decision-making meetings: organised when claims are made. - Accounting period as of 1/1/20xx to 12/31/20xx. - Estimated number of legal practitioners: 2,500. - Name of currency used in this response: US dollars. - Current asset balance: $220,000 as of 6/30/2004. - The unique source of Income for the Fund is that of the lawyer levy estimated in $20,000. - $10 is payable by each lawyer annually. - There is no penalty for non-payments. - It is not possible for clients to earn interest on trust account balances. - The Fund allegedly has enough assets to pay likely claims over the next 5 years. - Method used to determine likely claims expenditure: past history. - There are not any re-insurance arrangements in place. - Where assets of the Fund were inadequate, claims were prorated as they exceeded the maximum allowable under our rules. **Claims against the Fund** - Claims are lodged on the grounds of defalcations.

		- Maximum payment per claim: $15,000. - Maximum amount payable in respect of any one lawyer: $30,000. - It is a requirement that the claimant being a client of the lawyer. - Compensation is payable to foreign clients in the same way. - There is not a formal hearing process for uncontested claims. - Average time for contestation of a claim: 52 weeks. - Regarding rejected claims: not legal work is considered to reject a claim. There is a sole provision for rehearing conducted by the Boards of Managers of the VBA whereas there is not a provision for appeal or judicial review. - There is not a standard claim form available. - Fund administrators are automatically advised of disciplinary actions against a lawyer. - It is not required to conclude civil action before a claim will be paid whereas it is does require disciplinary action against the lawyer before paying a claim. - Fund administrators are personally protected from civil action against them. - No annual report is published by the Fund. **Strategies to reduce claims** - Existed or contemplated strategies for reduction of negligence or prevention of theft/defalcation: continuing legal education.
Law Society of South Africa	Any other or different Fund structure	Their single Fund (The Attorney Fidelity Fund) protects for both mistakes in handling cases (negligence) and theft of their money. The Attorney Indemnity Insurance Fund protects against member malpractice.
General Council of the Bar (South Africa)	No client protection fund	
Law Society of Northern Ireland	Any other or different Fund structure	It has two sets of arrangements made pursuant to statute-the solicitors (n.i.) order 1976. These are: 1) Compulsory compensation fund for dishonesty and failure to account. 2) Compulsory professional indemnity insurance to cover heads of civil liability.
New Jersey Lawyers	One Fund Protects from thefts only	**General information** - Steps taken to make the Fund known: quarterly press releases publish portion of annual report and notices of deadlines for filing claims. - Website: www.njcourtsonline.com/cpf/index.htm - Frequency of decision-making meetings: monthly. - Case name of any successful judicial challenge: GE Capital Mortgage v. NJ Title Ins. Et al, 333 N.J. Super. 1 (App. Div. 2000). - Description of any challenge: Superior Court lacks subject matter jurisdiction to review Fund claims. - Accounting period: 01/01/2003 to 12/31/2003. - Estimated number of legal practitioners: 79,600. - Name of currency used in this response: US dollars. - Current asset balance: $14,320,148 as of 12/31/2003.

		- Current sources of Income: lawyer levy represents the 76% ($2,961,210), recovery the 14% ($534,997) and interest on Fund investments the 11% ($413,229). - Amount paid by each lawyer annually: $50. ($25 for lawyers in 3rd or 4th year). - Penalty for failure to pay: lawyer is declared ineligible to practice law by order of the Supreme Court of New Jersey. - It is possible for clients to earn interest on trust account balances. - Regarding actual distribution of Fund balance: actual proved claims for compensation 2,638,349/837,800 (70.3%), administration costs $1, 114768 (29.7%), and being the total expenditure of $3,753,117. - In their opinion, the Fund counts with enough assets to pay likely claims over the next 5 years, in the absence of catastro. - None method is used to determine likely claims expenditure over the next 5 years. - There is no re-insurance arrangement. - Situations where assets were inadequate: 1) 1969/70 a big hit before there was a chance to collect enough. 2) Mid-70s, huge loss on one lawyer ($3.5 million) was paid in portions based on hardship of claimants. **Claims against the Fund** - Dishonest conduct such as theft within an attorney/client or fiduciary relationship is a matter to raise a claim. - $250,000 is the maximum payment limit per claim. - $1million is the maximum payment payable in respect of any one lawyer. - The claimant must be a client of the lawyer against whom claim is made. - Compensation is also payable to foreign clients. - Percentage of claims approved over the stated period: 55%. (171 claims received of which 106 were approved). - Regarding uncontested claims: - Average time in weeks: 10-12. - There is a formal hearing process for uncontested claims. - Regarding rejected claims: there is a provision for rehearing when the claim is actually rejected conducted by the Fund Boards of Trustees. There is not any provision for appeal or judicial review. - There is a standard claim form in use in English (available to IBA). - Brochure and extensive instructions are provided in order to help claimants to prepare their claims. - Fund administrators are automatically advised of disciplinary actions against a lawyer. - Claimants are not required to conclude civil action before a claim will be paid. The Fund does require disciplinary action against a lawyer before paying a claim. - Fund administrators are protected from civil action against them. - The Fund publishes a report annually (not published on the website) in which is named the lawyers against whom claims are made. Details of the payments of the claims are not provided. **Strategies to reduce claims** - Approach taken by the Fund to the reduction of member's negligence and/or the audit of any trust or other members' accounts holding clients'

		money: random audit program by Office of Attorney Ethics; overdraft notification; insurance payee notification; automatic permanent disbarment for lawyers who steal; Lawyers' Assistance Program. - Connections, assumptions, evidence established between these programmes and reduction in negligence: the three first mentioned above have caught and helped to stop lawyers misappropriating money. - Any need in relation to client protection matters: nothing in particular; information on what is occurring elsewhere is interesting. - The Fund most closely identifies with the National Client Protection Organization (NCPO) and American Bar Association (ABA). - The organization would support an IBA-sponsored training package or short course to assist the organization in meeting needs identified here. **General comments** - Question 45d regarding whether the Organization would support an IBA-sponsored training package or short course to assist the organization in meeting needs was not understood by the applicant.
German Bar Association (Deutscher Anwaltverein)	No Client Protection Fund	There is no plan to create a Fund.
The German Federal Bar	No Client Protection Fund	
Hungarian Bar Association	No Client Protection Fund	Mandatory liability insurance.
Icelandic Bar Association	No Client Protection Fund	Mandatory Professional Indemnity Insurance.
Idaho State Bar Client Assistance Fund	Any Other or Different Fund Structure	Their single fund protects clients for both mistakes in handling cases (negligence) and theft of their money. The Fund only pays for failure to return unearned fees to the client; and misappropriation or conversion of the client's funds. The Fund does not pay for negligence/malpractice claims against the lawyer.
Kansas Lawyers	One Fund Protects from thefts only	**General information** - The Fund and the Commission which administers the Fund are governed by Rules of the Kansas Supreme Court. - Steps taken to make the Fund known: information on Courts' website; printed brochures distribution and cooperation with the Kansas Disciplinary Administrator. - Website: www.kscourts.org - Frequency of decision-making meetings: quarterly. - Accounting period as of 7/1/2003 to 6/30/2004. - Estimated number of legal practitioners: 9,715.

		- Name of currency used in this response: US dollars. - Current asset balance: $1,576,013.59 as of 6/21/2004. - Current sources of Income: lawyer levy varies annually but it represents some 95% of total balance. Secondly, interest on Fund investments represents the 4% ($18,990) and finally, recovery represents less than 1 % of the total with $216. - Attorney Registration Fee: $135. - Penalty for non-payment: suspension of licence. - In Kansas, interest on lawyers' trust accounts is directed to the Kansas Bar Foundation. That interest is not used to support the Client Protection Fund. - It is possible for a client to earn interest on trust account balances. - No known rule governing opportunities to earn interest on those balances. - Regarding actual distribution of Fund balance: actual proved claims for compensation cover over 99% ($219,964.39) whereas administration costs cover 0.0025% of the total ($554.82) being the entire expenditure of the stated period of $220,519.21. Excess balance accumulates in the Fund. - In their opinion, the Fund has enough assets to pay likely claims over the next 5 years. - Method used to determine likely claims expenditure: review of past claims history. - The Fund does not have any re-insurance arrangement. **Claims against the Fund** - Claims can be lodged for: 1) Acts committed by a lawyer in the wrongful taking or conversion of money, property, or other things of value; 2) Refusal to refund unearned fees received in advance where the lawyer performed no services or such an insignificant portion of the service that the refusal to refund the unearned fees constitutes a wrongful taking or conversion of money; 3) The borrowing of money from a client without an intention to repay it or with disregard of his or her inability or reasonably anticipated inability to repay it; or 4) A lawyer's act of intentional dishonesty which proximately leads to the loss of money or property. - Maximum payment limit per claim: $75,000. - $250,000 is the maximum amount payable in respect of any one lawyer. - The claimant must be a client of the lawyer against whom claim is made. - Compensation is payable to foreign clients as long as the foreign client sustained a loss caused by the dishonest conduct of an active member of the Bar of Kansas and the loss arose in the course of a lawyer-client relationship. - Claims approved: 69 out of 82 claims. - Regarding uncontested claims: - Average time in weeks: 8. - There is not a formal hearing process for uncontested claims. - Average time for contestation: approx. 20 weeks. - Regarding rejected claims: the most common reasons for denying a claim are malpractice that constitutes 60% and secondly, legal work done but client is not satisfied with covers the 40%.

		There is a provision for rehearing conducted by the same 7 member Commission whereas there is neither a provision for appeal nor for judicial review. - There is a standard claim form in use in English (available to IBA). - Printed brochure and copy of rules are available to claimants to them prepare their claims. - Fund administrators are automatically advised of disciplinary actions against a lawyer. - It is not a requirement for claimants to conclude civil action before a claim will be paid. No disciplinary action against a lawyer is required before a claim will be paid. - Fund administrators are personally protected from civil action against them. - The Fund publishes an annual report in which it is not named the lawyers against whom claims are made or given details of payments made in each claim. It is not published in the website. **Strategies to reduce claims** - Approach taken by the Fund to the reduction of member's negligence and/or the audit of any trust or other members' accounts holding clients' money: Kansas Insurance Commissioner requires client notification of insurance checks issued to an attorney in excess of $5,000. The Disciplinary Administrator conducts random audits of lawyer trust accounts. - Connections, assumptions, evidence established between these programmes and reduction in negligence: no empirical evidence exits. Safeguards have been implemented which might have alerted parties to dishonest conduct in prior claims. - There is no plan to reduce the level of protection to clients. - The Fund most closely identifies with the National Client Protection Organization. - The organization would not support an IBA-sponsored training package or short course to assist the organization or Fund in meeting needs identified here.
Office of Disciplinary Counsel of Hawaii	One Fund protects from theft only	**General information** - The Supreme Court of Hawaii which created the Fund (RSCH 10) imposes the duty upon the Trustees to be audited at least annually, hold organizational meetings annually, adopt rules, maintain Fund assets in a separate account, and disburse monies only upon the action of the Trustees pursuant to the rules. The Trustees must obtain a bond unless a trust company has the assets. Other duties include developing an annual budget and financial policies, and to propose an annual fee to the Court. Monies must be deposited into interest-bearing accounts at federally insured financial institutions. - Steps taken to make the Fund known: brochures are available from the Fund; judiciary, bar association, disciplinary authorities and other information centers; notices of claims paid are published monthly in the bar journal; a brochure mail out to all bar members is impending; press releases; claim forms are automatically sent to theft victims identified in disciplinary cases. - Website: coming soon. - Frequency of decision-making meetings: quarterly. - Accounting period: as of 1 January to 31 December, 2003.

		- 4,308 estimated legal practitioners covered by the Fund. - Name of currency used in this response: US dollars. - Current asset balance: $942,580. - Current sources of Income: $163,875 comes from lawyer levy (98% contribution to total), $3,368 from interest on Fund investments (2%) and $400 from recovery being the total Fund Income of $167,643. - Amount paid by each lawyer annually: $25 if less than 5 years in practice and $50 if more than five years in practice. - Failure to pay results in financial penalty assessed and kept by the Bar association and administrative suspension. - It is possible for clients to earn interest on trust accounts balances. The determination of whether a client's funds should be deposited into a pooled or separate account rests exclusively with the attorney. - Actual distribution of Fund balance: actual proved claims for compensation $200,000 (67%), administration costs $91,008 (31%) and legal education $7,250 (2%) being the total Fund expenses for the stated period of $298,258. Excess funds are rolled over to the next year. - In their opinion, the Fund counts with enough assets to pay likely claims over the next 5 years. - Method used to determine likely claims expenditure: projected payments based upon past experiences plus allowance for one large payoff. - Method used to protect the Fund's asset base against unexpected claims: payouts are solely at the trustees' discretion. They determine the amount and timing of payouts. - There is no re-insurance arrangement. **Claims against the Fund** - Claims may be lodged on the grounds of purpose, dishonest conduct. The words "dishonest conduct" as used herein mean wrongful acts committed by an attorney in the manner of defalcation or embezzlement of money; or the wrongful taking or conversion of money, property or other things of value; or refusal to refund unearned fees received in advance where the attorney performed no services or such an insignificant portion of the services that the refusal constitutes a wrongful taking or conversion of money; or borrowing money from a client without intention or reasonable ability or reasonable anticipated ability to repay it. - $50,000 is the maximum payment limit for any one claim. - $150,000 is the maximum amount payable in respect of any one lawyer. - It is not a requirement that a claimant being a client of the lawyer. Applicants could be also fiduciary relationship customary to the practice of law i.e., administrator, executor, trustee of an express trust, guardian or conservator. - Compensation is also payable to foreign clients as long as these three conditions apply: 1) Conduct must have occurred in Hawaii, 2) Claimant must have retained attorney in Hawaii and 3) Attorney must have been Hawaii-licensed and have office in Hawaii. - In the stated period, 27 claims were received and 9 of them approved. - Regarding uncontested claims: - Average time in weeks: 2 years. - There is not a formal hearing process for uncontested claims.

		- As for rejected claims: the most common reasons for denying a claim are listed as follows: 1) No dishonest conduct (90%), 2) Insufficient evidence (9%) and 3) Third party recovery (1%). There is a provision for rehearing conducted by the trustees and whom decision is final. Nevertheless, there is not such provision for appeal or judicial review. - There is a standard claim form in use in English (available to the IBA). 2 page letter is provided to claimants to them prepare their claims. - Funds administrators are automatically advised of disciplinary actions against a lawyer. - The Fund does not require the claimant to conclude civil action before a claim will be paid but it does require disciplinary action against a lawyer before paying a claim. - Fund administrators are personally protected from civil action against them. - The Fund provides with an annual report published on the website (www.hsba.org). This report provides neither the names of the lawyers nor the details of the payments made in each claim. Monthly bar journal notices identify the attorney and claimant, amount, and the reason for the payment. **Strategies to reduce claims** - Approach taken by the Fund to the reduction of member's negligence and/or the audit of any trust or other members' accounts holding clients' money: disciplinary system handles the strategies to reduce claims. - Other existed or contemplated strategies for reduction of negligence or prevention of theft/defalcation: random audit rule; trust account overdraft notification rule; strict recordkeeping rule. Proposing strategies such as payee notification rule. - Connections, assumptions, evidence established between these programmes and reduction in negligence: past experience. - The Fund most closely identifies with the National Client Protection Organization.
Mexican Bar Association	No client Protection Fund	There is no plan to create a Fund.
New Zealand Law Society	One fund protects from thefts only	**General information** - A management committee administers the Fund, reporting to the NZLS Board and Council. The Fund moneys are kept in a separate bank account and audited annually. Annual accounts are published. - Steps taken to make the Fund known: information is published on the website (www.lawyers.org.nz) and in media releases from time to time. Lawyers must advise clients when instructed to invest moneys, that investment moneys are not protected by the Fund. - Frequency of decision-making meetings: held as required. - Case name/citation of any successful judicial challenge: 1) Florence v New Zealand Law Society (1989) 1NZLR 132 (CA) 2) Amptmeyer v New Zealand Law Society (1994, not reported) 3) McDonald v FAI (NZ) General Insurance Co Ltd & New Zealand

		Law Society (1997 not reported). - Brief description of any challenge: 1) Meaning of "pecuniary loss" (term used in statute) 2) Whether there is an obligation to restore Fund to solvency when inadequate 3) Whether pecuniary loss includes obligation to pay interest. - Accounting period: 1 December to 30 November. - Name of currency used in this response: $NZ. - 6,000 estimated legal practitioners covered by the Fund. - Current asset balance: $9.829 million as of 30/11/03. - Current sources of Income: lawyer levy represents the 66% of the total contribution ($1,237) followed by interest on Fund investments representing the 30% ($564) and thirdly, recovery constitutes the 4% ($82). The total Fund Income for the stated period is $1,883. - Amount paid by each lawyer annually: $390 in 2004 is payable by lawyers practising on own account i.e. in sole practice or in partnership in private firms. - Payment is required in conjunction with the annual practising fee- until paid the practitioner is not entitled to practise. - It is possible for clients to earn interest on trust accounts balances. - Actual distribution of the Fund for the stated period: actual proved claims for compensation represent the 81% contribution to total ($69), investigation and legal costs represent the 13% ($160), administration costs constitute the 6% (69) and contingency provisions for claims (2.93 M*) being the total Fund expenditure of $1,209. (* no provision in accounts other than a note of contingency allowance). - Balance on Fund at year's end remains in the Fund. - Not able to assess likely claims over the next 5 years. - Method used to determine likely claims expenditure over the next 5 years: five year period not applicable. An annual fee is set, having regard to the funds in hand and likely claims to be paid. - Method used to protect the Fund's asset base against unexpected claims: statutory provision for annual fees and special levies. - The Fund does not have any re-insurance arrangement. - Situation where assets of the Fund were inadequate to pay claims: in 1992 a special levy of $10,000 per practitioner was fixed to meet claims. On other occasions smaller special levies have been made to resolve funding issues. **Claims against the Fund** - Claims may be lodged for pecuniary loss by reason of theft by a solicitor in the course of his practice of a solicitor (excluding investment-related money). Covers practitioners and their employees or agents. - There is a maximum payment limit neither for any one claim nor in respect of any one lawyer. - Compensation is payable to foreign clients. - Data in respect of claims made in the stated period are not available. - As for uncontested claims: there is not a formal hearing process. - Regarding rejected claims: there is not a prescribed appeal process but the management committee may review claims were further submissions are made and further information provided. There is a provision for judicial review. - There is a standard claim form in use in English (attachment 1). Claim form is prescribed by the Solicitors Guarantee Fund Rules 1936. (Refer Statutory Regulations at http://www.legislation.govt.nz)

		- Fund administrators are not automatically advised of disciplinary actions against a lawyer. - It is not a requirement for the claimant to conclude civil action against a lawyer before a claim will be paid. Disciplinary action is not required against a lawyer before paying a claim. - Fund administrators are personally protected from civil action against them. - The Fund publishes an annual report, also published on the website (www.lawyers.org.nz). It is not set any policy on the names of the lawyers or details of payments of claim made against them. **Strategies to reduce claims** - Approach taken by the Fund to the reduction of member's negligence and/or the audit of any trust or other members' accounts holding clients' money: the organisation has a financial assurance scheme aimed at detecting fraud and theft. Rules and regulations govern lawyers' management of client funds. - Other existed or contemplated strategies for reduction of negligence or prevention of theft/defalcation: 1) solicitors need proper written authorities for application of client money, 2) law firms must submit monthly certificates, certifying that trust accounts are in order, 3) inspection visits to new law practices, 4) minimum training requirements for Trust Account Partners, 5) an ethical requirement for practitioners to report suspicions of possible defalcation or improper acts by another practitioner, 6) free-phone lines for reporting suspicions of dishonesty, anonymously if preferred. - Connections, assumptions, evidence are established between these programmes and reduction in negligence: period between detection and offending starting has reduced markedly in recent years.
Research Society of International Law, Pakistan	Any Other or Different Fund Structure	Their single fund does not protect clients for mistakes in handling cases (negligence) and theft of their money. The Punjab Bar Council does not have any client protection fund as such.
Swedish Bar Association	No Client Protection Fund	Mandatory indemnity insurance.
Swiss Bar Association	No client protection Fund	Swiss lawyers have a professional duty to keep clients' money separate form the attorney's personal money, and have anti-bankruptcy agreements with banks. There is no further client protection.
Law Society of Botswana	One Fund that protects from theft only	Botswana has a fund, established by the Legal Practitioners Act, that protects against losses arising from the theft of monies. The fund is entitled "the Fidelity Fund" and does not protect against member malpractice.

Law Society of Ireland	Two Funds- One Protects from Theft and One Protects from Mistakes/Negligence	**General information** - The Committee of the Fund subscribes to the principles of good governance through: 1) Annual audited accounts 2) Disclosure and publication of all claims paid 3) Publication of all disciplinary findings. - Steps taken to make the Fund known: details of the Fund are published on website. If a practise collapses all clients of the firm are contacted by the Society and made aware of the existence of the Fund. - Website: www.lawsociety.ie - Frequency of decision-making meetings: monthly. - Accounting period: 1 January to 31 December. - Name of currency used in this response: euro. - Estimated number of legal practitioners: 6,500. - Current asset balance: 31.5 million as of 31/08/2004. - Current sources of Income: firstly, lawyer levy represents the 65% of the total (€2,635,000). Secondly, interest on Fund investments represents the 30% and thirdly, recovery constitutes the 5% of the total contribution. - Amount paid by each lawyer annually: €400. - Payment is included as part of practising certificate fee. If practising certificate fee is not paid, practising certificate will not be issued and the lawyer will be practising illegally. - It is possible for clients to earn interest on trust account balances. - Information given to clients regarding interest on those balances: a statutory instrument, S.I. No.372 of 2004 Solicitors (Interest on Clients Moneys) Regulation, 2004 is in existence outlining treatment of clients moneys and the requirement to pay interest earned in excess of €100 to the client. - Regarding actual distribution of Fund balance: administration costs (€2,519,000) followed by actual proved claims for compensation (€500,000). - If there is extra money available, this is maintained within the Fund to build up reserves to meet future potential claims and costs. - In their opinion, the Fund has enough asset balance to meet likely claims over the next 5 years. - Method used to determine expenditure on likely claims over the next 5 year: historical claims, economic environment and review of practices in difficulties. - Method used to protect the Fund against unexpected claims: the Fund has built up reserves of €31.5 million and hold insurance cover of €20 million in excess of €5 million. - The Fund has got a re-insurance arrangement. - Level of protection, underwriter and financial market in which it was negotiated: €20 million in excess of €5 million. AIG Internation. London. **Claims against the Fund** - Categories of loss for which claims can be lodged: where it is proved to the satisfaction of the Society that any client of a solicitor has sustained loss in consequence of dishonesty on the part of that solicitor or any clerk or servant of that solicitor arising from that solicitor's practice as a solicitor within the jurisdiction of the State then subject to certain provisions the Society may make a grant to that client out of the Fund. Losses include proceeds of sale misappropriated, stamp duty received

		from client and misappropriated and defalcations from estates. - Maximum payment limit for any one claim: €700,000 as provided by Section 16 of the Solicitors (Amendment) Act, 2002. - There is not a maximum limit payment in respect of any lawyer. - It is a requirement that the claimant being a client of the lawyer. - Compensation is payable to foreign clients. There is no restriction except for the €700,000 limit on any one claim as outlined above. - Percentage of claims approved over the stated period: 5% (35 claims received of which 29 were approved). - Regarding uncontested claims: 6 weeks time average elapse between lodgement of claim and despatch of agreement. There is a formal hearing for uncontested claims. - Average time for contestation of a claim: 12 weeks. - As for rejected claims: the main reason for denying a claim is the no evidence of payment of funds by client (70%). Secondly, negligence not dishonesty on the part of the solicitor (15%) and finally, no dishonesty on the part of the solicitor (15%). There is a provision both for rehearing and for judicial review. There is not for an appeal. - There is a standard claim form in use in English (available to the IBA). - Copy of the relevant Solicitors Acts Claim forms are provided to claimants in order to them easier prepare their claims. - Fund administrators are automatically advised of disciplinary actions against a lawyer. - The Fund does not require claimants to conclude civil action against a lawyer before a claim will be paid. In the same way, it is not required disciplinary action against a lawyer before paying the claim. - Fund administrators are personally protected from civil action against them. - The Fund publishes an annual report (not published on the website). This report does not provide with the names of the lawyers or the details of payments made in each claim. The claims paid on a monthly basis are published in the Law Society Gazzette indicating name of solicitor and amounts paid. **Strategies to reduce claims** - Approach taken by the Fund to the reduction of member's negligence and/or the audit of any trust or other members' accounts holding clients' money: 1) Investigation of solicitors practices on a rotational five years cycle. 2) Random investigations. 3) Annual report received from independent reporting accountants on a yearly basis. 4) Necessity to have a practising certificate in place each year. 5) Publication of payments from the Fund. 6) Publication of the findings of the Disciplinary Tribunal. - Other existed or contemplated strategies for reduction of negligence or prevention of theft/defalcation: 1) Inspection of solicitors practices who are in arrears with the accountants report requirements. 2) Referral to Disciplinary Tribunal where no practising certificate is in place. 3) Compulsory practice management course. - Connections, assumptions, evidence established between these programmes and reduction in negligence :

		1) Regular inspections lead to better compliance with the Solicitors Accounts Regulations. 2) Claims arising have dropped since the increase in the compliment of inspection staff. - Any need in relation to client protection matters: need for co-operation between Law Societies to inform other Societies through references of previous/current problems/disciplinary procedures in place against solicitors seeking to establish in other jurisdictions. - The Fund most closely identifies with the Law Society of England and Wales. - The Organization would support an IBA-sponsored training package or short course to assist the organization or Fund in meeting needs identified here. **Negligence** - Legal liability of lawyers to clients for mistakes (negligence) and any restrictions on liability: all solicitors in private practice are required to have professional indemnity insurance cover in place for €1.3 million each and every claim (including claimants legal costs), together with the insured's own legal costs up to a maximum of €130,000. - It is compulsory for members to insure themselves against clients' claims for financial loss due to negligence. - Negligence protection financing: each solicitor is required to obtain their own professional indemnity insurance cover from a qualified insurer and pay their respective premium. - Underwriter/scheme manager of the Fund (if any): each qualified insurer is responsible for underwriting the risks assumed by the insurance policies they issue. Insurers may apply to become a qualified insurer by signing an Assigned Risks Pool Participation Agreement, thereby agreeing to provide cover for a limited period to members of the profession who are unable to obtain cover on the open market. - Annual premium cover: each solicitor's practice is responsible for the premium applicable to their own cover. - Details of the amount of negligence cover per lawyer, amount of any premium: the various insurers providing cover set the level of premium in each case. The amount of the premium may vary between the different insurers as they base the premium on the type of legal services provided, the fee income of the practice as a whole and the practice's claims history. - Main exclusions from indemnity: the various exclusions are set out in the Appendix to the Society's professional indemnity insurance Regulations (S.I. No 312 of 1995) and additional exclusions are included in S.I. No. 114 of 2004. Copies of which are available on request. - Any limits on claims: as the cover provided is for each and every claim there is no limit on the aggregate of claims. The limit per claim depends on the individual insurance policy but must be not less than the above stated. - In their opinion, money available for indemnity is sufficient to meet claims. - There has never been a shortfall.

Law Society of Namibia	One Fund protects from Theft and Malpractice	The Namibian Legal Practitioner Fidelity Fund protects against losses arising from the theft of trust monies and also protects against member malpractice.
Nova Scotia Barristers' Society	Two Funds- One Protects from Theft and One Protects from mistakes/negligence	**General information** - The Reimbursement Fund Committee meets ad hoc, depending on claims, via notices of meeting, in person. Minutes are taken and approved. The Committee policies and procedures are set out in a Handbook, together with case precedents. The Committee frequently reviews its regulations, policies and procedures. Hearings with claimants or lawyers are recorded and transcribed claims recommendations are made to Bar Council to approve or reject. Letters of reason are provided to claimants. Claims are processed expeditiously. Claim payments are published. Information about the claim process is easily accessible on our website. The Committee's authority is clearly set out in one Act plus Regulation. - Steps taken to make the Fund known: website, brochures and annual reports. - Website: www.nsbs.ns.ca - Frequency of making-decision meetings: ad hoc. Usually 2 or 3 times a year. - Accounting period: 1May 2003 to 30 April 2004. - Name of currency used in this response: Canadian dollars. - Estimated number of legal practitioners covered by the Fund: 1,200. - Current asset balance: $ 2.2 million as of 31/03/2004. - Current sources of Income: $100 comes from lawyer levy and $86,319 comes from interest on Fund investments. - Amount paid by each lawyer annually: $100. - Penalties for non-payment: included in annual levy. Failure to pay results in automatic suspension. - In their opinion, the Fund has enough assets to pay likely claims over the next 5 years. - Method used to determine likely claims expenditure over the next 5 years: the Fund has two capitals which prevent exhaustion. These are the following: 1) Per lawyer capital of $300,000 and 2) Per annum capital of the lesser of $750,000 or half the capital in the Fund. - The Fund does not have any re-insurance arrangement. **Claims against the Fund** - Claims may arise from misappropriation or conversion of money or other valuable property entrusted to or received by a lawyer in his/her professional capacity. - There is no maximum payment for any one claim. - Maximum amount payable in respect of any one lawyer: $300,000. - It is a requirement that the claimant being a client of the lawyer. - Compensation is payable to foreign clients as long as claims criteria meet. - Number of claims over the stated period: 2 claims received and approved. - Regarding uncontested claims:

		- Average time in weeks: 3-4 months. - There is not a formal hearing for uncontested claims. - Average time for contestation of a claim: 6 months. - As for rejected claims: the most common reasons for denying a claim are the following: 1) No solicitor-client relationship (loans, investments) 2) Failure to prove misappropriation 3) Filed outside 12 months time period The Committee makes recommendations to Bar Council, who has final authority. Grants are discretionary in our Act, so there is no right to appeal. Neither for judicial review. - There is a standard claim form in use in English (available to IBA). - Brochure and detailed application form are available to claimants to them prepare their claims. - Funds administrators (same Director) are automatically advised of disciplinary actions against a lawyer. - Claimants are not required to conclude civil action against a lawyer before a claim will be paid. - Disciplinary action against a lawyer is not required before paying a claim. - Fund administrators are personally protected from civil action against them. - The Fund publishes an annual report, also published on the website (www.nsbs.ns.ca) in which appear the names of the lawyers, amount paid, when approved. Not names of claimants appear. **Strategies to reduce claims:** - Approach taken by the Fund to the reduction of member's negligence and/or the audit of any trust or other members' accounts holding clients' money: 1) Annual written reports filed by lawyer and accountant confirming compliance with regulations for trust account maintenance. 2) Society written follow-up on all reported breaches of trust regulations to confirm correction can require lawyers to file copies of monthly trust reconciliations. 3) Internal Audit Program: NSBS retains a certified Accountant to conduct risk-based audit of firms. Firms are selected based on risk profile data and breaches of trust regulations (approximately 20 per year. Firms are called by Accountant within a week of audit). 4) New requirement that lawyers with sole control over states or trusts must hold such funds in firm trust account unless beneficiaries waive requirement. 5) Spot audits can be ordered by Discipline Committee in response to complaint information. 6) Requirement to report bankruptcies and judgements against lawyers. Society monitors until satisfied or discharged. - Other existed or contemplated strategies for reduction of negligence or prevention of theft/defalcation: 1) Trust accounts training programme for law students (mandatory). 2) Trust accounts manual. 3) Cooperative training programs with Institute of Chartered Accountants. 4) New requirement that new sole practitioners or new firms must file copies of monthly trust reconciliations for first 6 months. If any problems, then internal audit.

		- Connections, assumptions, evidence established between these programmes and reduction in negligence: 1) 2000 Risk Analysis: done to identify trends and profiles re-lawyers and areas of law where thefts occurred over 10 year period. This analysis continues annually. 2) 2003/04 Trust Accounts Program Analysis: survey of audited firms, accountants, etc. assessment of success with audit program reducing trust account problems, risk assessment, to assess success of program in reducing risks, trust account breaches and theft. - Any need in relation to client protection matters: 1) Learning about Fund policies, procedures and best practices in other jurisdictions. 2) Trend identification and analysis. 3) Networking. - The Fund most closely identifies with the National Client Protection Organization (NCPO). - The organization would support an IBA-sponsored training package or short course to assist the organization in meeting needs identified here. **General comments** Client protection and risk management issues are the new area for "best practices" for compensation funds. Better to devote resources to preventing claims rather than just processing claims well. Mortgage fraud is one of the loss leaders in Canada now. $40 million in BC, $1 million in Newfoundland. Rapidly emerging on-line property registration technology and electronic funds transfers open up new areas for fraud and are changing how lawyers do business. This survey is an excellent first step in hopefully developing a global client protection community for networking, trend identification, articulation of best practices and development for new and emerging Funds. **Negligence** - Legal liability of lawyers to clients for mistakes (negligence) and any restrictions on liability: NSBS members are required to hold current professional liability insurance coverage to cover for errors or omissions and negligence. - It is compulsory for members to insure themselves against clients' claims for financial loss due to negligence. - Negligence protection financing: lawyers pay an annual premium, deductibles, and excess insurance can be purchased from the Canadian Lawyers Insurance Association up to $1 million. - Underwriter/scheme manager of the Fund (if any): CLIA with local management by the Nova Scotia Barristers' Liability Claims Fund. - Annual premium cover: paid by individual members. - Details of the amount of negligence cover per lawyer, amount of any premium, main exclusions from indemnity, any limits on claims: 1) Annual premium 04/05: Regular Practising Insured ($800 net of accumulated surplus credits of $1,000). $350 for government lawyers. 2) No claims limit. 3) Regular insurance covers first $100,000; excess insurance covers up to $1 million. - In their opinion, moneys available for indemnity are sufficient to meet claims.

		- There has never been a shortfall.
Ordem Dos Advogados De Portugal	No Client Protection Fund	
Romanian National Union of Bar Associations	There is no client protection fund	There is no plan to create any Fund. Clients are protected through lawyer's mandatory insurance in accordance with Law 51/1995, Chapter III, Sect.2, Art. 40 and Art. 215 (1) from the Statutul Profesiei de Avocat (SPA).
Attorneys Fidelity Fund South Africa	Two Funds- One Protects from Theft and One Protects from Mistakes/Negligence	**General information** - The Board of control is committed to the highest standards of corporate governance, based on the principles of discipline, transparency, independence, accountability, responsibility, fairness and social responsibility. The Board recently adopted a charter to ensure that the business of the Fund is conducted in accordance with the principles particularised above. So Board members acting on behalf of the Fund are accordingly made aware of their duties and responsibilities as board members, the various legislative and regulatory measures having a bearing on their conduct and on the business of the Fund, and so that the principles of good corporate governance are applied in all their dealings with respect to the Fund. - Steps taken to make the Fund known: the 4 statutory Law Societies in South Africa act as agents for the Fund in carrying out curatorship-type functions relative to the trust accounts of delinquent attorneys whose names have been struck off the roll. In this way, trust creditors are directed to the Fund for the purpose of submitting their claims for reimbursement of loss as a result of theft of money or property entrusted to, and stolen by such attorneys. In addition, the Fund publishes a bi-annual newsletter for circulation within the profession while full particulars of the Fund and the services it provides are published on its website. - Website: www.fidfund.co.za - Frequency of decision-making meetings: 3 times per annum. - Accounting period: 01/01/2003 to 31/12/2003. - Name of currency used in this response: south African rands ZAR. - Estimated number of legal practitioners: 16,000. - Current asset balance: ZAR 860m as of 31/08/2004. - Year established : 1942 - Number of members of the Board of Control: 16 lawyers. No non-lawyer members. 2 additional (lawyer) observer members without voting rights, have unofficially been permitted to attend Board meetings with a view to the promotion of gender transformation. - There has been no successful judicial challenge to the existence or jurisdiction of the Fund - Current sources of Income should be reflected as follows -

		Lawyer levy/assessment premium ZAR Nil %contribution to total Interest on client deposits ZAR 320M 86% Interest on Fund investments ZAR 36M 10% Other sources (dividend and other income) ZAR 15M 4% ZAR 371M 100% Actual distributions Administrations costs ZAR 16M 6% Actual proved claims for compensation ZAR 40M 16% Legal Education ZAR 35M 14% Other expenses: Reinsurance (stop loss) ZAR 3M 1% Contributions towards trust a/c bank costs and audit fees of practitioners ZAR 78M 31% Professional indemnity insurance cover for all practitioners ZAR 33M 13% Trust interest agency fees to law societies (collection fees) ZAR 46M 19% Total Fund expenditure for period ZAR250M 100% - Penalties for non-payment: subject to disciplinary authority of the statutory law societies. The Law Societies ensure that interest is paid over by practitioner firms. - Interest earned on deposits in lawyers' trust accounts are collected via the statutory Law Societies, which retain an agency fee from the interest they collect. The amounts collected, net of agency fees are remitted to the Fund. - It is possible for clients to earn interest on trust account balances. - Information given to clients regarding the opportunities to earn interest on those balances: practitioners will, in the best interests of their clients/ other depositors of trust Funds, operate separate trust savings or other interest-bearing bank accounts in the name of each client/depositor (if the amount warrant this). On occasion a client/depositor will stipulate the bank to be used. Legislation does not permit of the use of any other investment vehicles. - Actual distribution of the Fund balance: proved claims cover the 16% (ZAR 40m), legal education covers the 14% (34m) and administration costs cover the 6% (ZAR 16m). Other expenses such as reinsurance (stop loss) premium sum ZAR 3m. The total Fund expenditure is of ZAR 250m. - If extra money is available it is capitalised to reserves. No distribution. Excess funds will, however, have a positive impact on the funds made available for projects in the succeeding year. The available funding is

		actuarially determined each year, as part of a budgetary process. - In their opinion, the Fund has enough assets to pay likely claims over the next 5 years. - Method used to determine likely claims expenditure over the next 5 years: past trends, taking into consideration the number and value of claims on record. - Method used to protect the Fund's asset base against unexpected claims: an actuarial determination, annually, of the asset base required to meet claims into perpetuity, taking into consideration expected future income and expenditure. The above exercise builds in the possibility of disaster-type claims arising. - The Fund has a re-insurance arrangement. - Level of protection, underwriter and financial market in which it was negotiated: ZAR 300m XS ZAR 100m in the aggregate. Lead underwriters Ace Global Markets Ltd. Cover placed in the London market. **Claims against the Fund** - The Fund entertains all claims based on loss suffered consequent upon the theft of money or property entrusted to an attorney in the course of hi/her practice as such. The main areas of practice giving rise to claims are the following: 1) Personal injury claims: motor vehicle collisions (theft of award by attorney) 2) Conveyancing 3) Deceased/insolvent estates 4) Administrations (statutory debt administrations) 5) Litigation 6) Commercial matters. - No maximum payment limit applies (regarding any one claim or in respect of any one lawyer). - There is not a requirement that the claimant being a client of the lawyer. - Compensation is payable to foreign clients. - Percentage of claims approved in the stated period: 74% (1017 claims received of which 751 were approved). - Regarding uncontested claims: - Average time in weeks: 10. - There is not a formal hearing process. - Average time in weeks for contestation of a claim: 130 weeks. - As for rejected claims: the most common reasons for denying a claim are no entrustment, statutory exclusions and insufficient proof. The Fund does not keep particulars of the relative percentage breakdown of the reasons particularised above. There is not a provision for rehearing or for appeal. There is a provision for judicial review. - There is not a standard claim form in use. - Pamphlet setting out the procedure to be followed in the preparation and submission of claims to the Fund are available to claimants to help them prepare their claims. - Fund administrators are not automatically advised of disciplinary actions against a lawyer. - Claimants are required to conclude civil action against a lawyer before a claim will be paid. - Disciplinary action is not required before paying a claim.

		- Fund administrators are personally protected from civil action against them. - An annual report is published, also published on the website (www.fidfund.co.za). The report does not name the lawyers or the details of the payment of any one claim against them. **Strategies to reduce claims** - Approach taken by the Fund to the reduction of member's negligence and/or the audit of any trust or other members' accounts holding clients' money: the Fund only covers for loss consequent upon theft of trust money or property, but not for loss resulting from negligent conduct. "Every firm of attorneys in South Africa is required to keep proper accounting records with respect to both its business (practice) and trust accounts. A firm is required each year to appoint an accountant approved by the Council of the statutory law society having jurisdiction over the firm, to act on behalf of and as the representative of the Fund, to discharge the following duties - • within six months of the annual closing of the firm's accounting records, to furnish an annual audit report relating to the trust account • without delay report any trust shortage, and provide particulars of any material queries raised with the firm but not dealt with to the auditor's satisfaction • report any reasonable request for access to the member firm's records not satisfactorily dealt with. "Accountant" means a person who is registered as an accountant and auditor in terms of the relevant legislation applicable to accountants in South Africa, and who actively practise as such. The annual audit is done at the cost of the firm, but a portion of such costs may be recovered from the Fidelity Fund. The furnishing of an unqualified annual audit certificate with respect to a member firm is a prerequisite for the issue of Fidelity Fund certificates annually to the principals within the firm, without which they may not practise. In that sense, therefore, a valid Fidelity Fund certificate can be considered as being a licence to practise as an attorney." - Other existed or contemplated strategies for reduction or prevention of theft/defalcation: the KwaZulu-Natal Law Society, one of the 4 statutory Law Societies in South Africa, is presently conducting a so-called. 1. Audit Reform pilot project on behalf of the Fund. The system is similar to those employed by the Law Society of Scotland and the New Zealand Law Society, and dispenses with traditional trust account audits by accountants. In terms of the model being tested, practitioners are required to report on the correctness of their trust accounting records at specified intervals. The system is underpinned by a system of routine and cause-driven inspections of firms by an Inspectorate employed by the Society. 2. Monitoring Units administered by each of two other statutory law societies on behalf of the Fund, each of which also carry out routine and cause-driven inspections by an Inspectorate. However, the programme is run *pari passi* with the traditional system of annual audits of practitioners' trust accounts by firms of external auditors. These Units

		are substantially funded by the Fund. 3. The four statutory law societies also conduct a programme of so-called practice support on behalf of the Fund, which entails visiting (generally newly-established) practices to provide assistance in regard to teething and other problems being experienced by such practitioners with respect to accounting records and systems, the theory being that minor problems rectified at an early stage are likely to obviate larger problems developing in time. 4. The Fund contributes the greater preponderance of funding required for Practical Legal Training in South Africa, i.e. pre-admission training to LLB. graduates who aspire to enter the profession and practise as attorneys. 5. In the near future, Mandatory Practice Management Training will be introduced in South Africa for admitted practitioners. 6. The KwaZulu-Natal Law Society runs a "whistle-blower" programme (known as *Tip-Offs Anonymous*) by way of a pilot project on behalf of the Fund. The system enables any member of the public or an employee of an attorney, who might have a reasonable apprehension of dishonest conduct on the part of any practitioner, to report the matter on a confidential telephone line to a service provider, which in turn screens and relays the report to the relevant statutory law society for investigation. 7. The Fund is developing a Risk Profiling model to identify troublesome practitioners who might present a risk to the Fund. The project is still in the early stages of development. - Any need in relation to client protection matters: the Fund points out the importance to maintain contact through the IBA's Client Protection Committee with other Law Societies, Bar Associations and fidelity/client protection Funds, in order to keep abreast of developments in regard to client protection in general, and more particularly the approach to risk management/loss prevention in other jurisdictions. The Fund has found this association to be of great value, and as a direct thereof has resolved in principle to examine, and possibly adopt the following: 1) Audit models as they pertain in Scotland and New Zealand. 2) Concept of risk profiling 3) Third party payee notification systems as applied in other jurisdictions. - The Fund most closely identifies with the IBA. - The organization would support an IBA-sponsored training package or short course to assist the organization in meeting needs identified here. **General comments** Not herein. **Negligence** - Legal liability of lawyers to clients for mistakes (negligence) and any restrictions on liability: in South Africa, partners in legal practice are jointly and severally liable for the debts which any one of them incurs in the course of partnership business. Those debts would include liability as a result of any act or omission by that partner in the course of his practice. Although attorneys may incorporate their practice under the relevant company legislation, they remain jointly and severally liable,

		together with the Company, for all debts and liabilities contrasted during their periods of office. - It is not compulsory for members to insure themselves against clients' claims for financial loss due to negligence. - Negligence protection financing: the Attorney Fidelity Fund (aff) provides a basic level of cover to all practitioners at no cost to them, ranging from ZAR1 million to ZAR2 million, depending on the number of principals in every firm. Cover is provided on a per annum aggregate basis, rather than a per claim basis. Practitioners may elect to reduce their limits of indemnity and deductibles to 50% or 75% of the standard limits of indemnity and deductibles provided by the scheme. This is permitted in order to accommodate practitioners who feel that the standard limits of indemnity are in excess of their needs, and that deductibles at those levels are concomitantly high. The above arrangements therefore in effect amount to the provision of automatic, rather than compulsory, cover to practitioners. As regards the FINANCING of such cover, the arrangements detailed above are provided trough a registered short-term insurer, the Attorneys Insurance Indemnity Fund (aiif), an association not for gain, which is wholly controlled by the aff. The aff provides the aiif with an annual premium (currently ZAR45 million), which generates a substantial investment income for the aiif, and enables it to pay claims of some ZAR1, 40 from every ZAR1,00 received by way of premium income during the run-down period of approximately 7-8 years during which claims w.r.t..a particular year of insurance are ultimately settled. - Underwriter/scheme manager of the Fund: the scheme is conducted through the aiif, which in effect is a "captive" insurer of the aff. There is accordingly no commercial underwriter to the scheme as such, although the scheme is reinsured by way of aggregate stop loss and excess of loss cover. The management of the scheme (essentially claims, financial and reinsurance placement functions) are outsourced to a South African concern known as Glenrand M.I.B. Professional Services, in Johannesburg. - Annual premium cover: the scheme is fully funded by the aff. For particulars of funding, see the highlighted part that says "Current Sources of Income". - The main exclusion from indemnity relates to claims based on the theft of attorney's trust funds (to which the aff responds). - In their opinion, moneys available for indemnity are sufficient to meet claims. - There has never been a shortfall.
Law Society of British Columbia	Any other or different Fund structure (Two Funds from theft only)	**General information** - The committee operates within the formal governance structure of the Law Society. The committee has a specific, published mandate, which it adheres to with a high degree of fidelity. The committee is significantly autonomous, as required by statute, but its process is well defined, transparent (as far as requirements of confidentiality permit) and its decisions are subject to review. The committee's work is supported by highly skilled and specialized staff, and the committee has access to

		additional special expertise when required. The committee provides regular performance reports to the Board. Committee membership is reviewed annually. - Steps taken to make the Fund known: details found on main Law Society website (lawsociety.bc.ca) - Frequency of making-decision meetings: monthly. - Accounting period: January 1 through December 31, 2003. - Name of currency used in this response: Canadian dollar - Estimated number of legal practitioners covered by the Fund: in 2003, there were 9101 practising legal practitioners. - Current asset balance: $4,086,834 as at December 31, 2003. - Current sources of Income: lawyer levy $5,496,650 (99.80%), recovery $97,792 (1.78%), interest of Fund investments -$86,716 (-1.57%). Total fund income $5,507,726. - Amount paid by each lawyer annually: The 2003 Special Compensation Fund Assessment was $600 per lawyer. - Penalties for non-payment: if a lawyer fails to pay the annual billing fee, of which the Special Fund Assessment is included, by the deadline set, the lawyer ceases to be a member and will not be issued a practice certificate. - It is possible for clients to earn interest on trust account balances if money is held in a segregated account. - Actual distribution of Fund balance: administrative costs $2,076,778 (37.11%), professional services $2,050,221 (36.63%), proved claims for compensation $389,817 (6.97%), staffing costs 1, 00,632 (17.88%), external program costs 50,954 (.91%), meeting expenses 28,105 (.50%). Total distribution $5,596,507. Any excess Fund balance remains as part of the Fund. - In their opinion, the Fund has enough assets to pay likely claims over the next 5 years, although some borrowing may be necessary. - Method used to determine likely claims expenditure over the next 5 years: past experience. The TPC will use an actuarial estimate. - Method used to protect the Fund's asset base against unexpected claims: for 2003, the insurance bond provided that total claims attributable to the period in excess of $2,500,000 were 90% reimbursed by a commercial insurer up to a maximum of $15,000,000 for claims against one lawyer and in total. - Any re-insurance arrangement in place: for 2003 the Fund had excess insurance of $15M in place as described above. Since May 2004 there has been a Part B amendment to the B.C. Lawyers' Compulsory Professional Liability Insurance Policy (as provided through the Lawyers Insurance Fund) that provides defined insurance coverage for dishonest appropriation of money or other property entrusted to and received by insured lawyers in their capacity of barrister and solicitor and in relation to the provision of professional services. This coverage is $17.5M per annum. - Level of protection; underwriter; financial market: for 2003, American Home Insurance. - In 2002, the Benchers agreed to allow the Special Compensation Fund Committee to exceed the $17,500,000 cap the Benchers had imposed on the Committee by way of the Society rules. Since May 2002, the Special Compensation Fund Committee has received 523 claims concerning Mr. Wirick. To date claims concerning Mr. Wirick have been approved in the amount of approximately $25Million, further claims are anticipated to be approved.

		Claims against the Fund - Categories of loss for which claims may be lodged: the Fund is available to reimburse persons who sustain a pecuniary loss as a result of a misappropriation or wrongful conversion by a lawyer of money or other property entrusted to or received by the lawyer in his or her capacity as a barrister or solicitor. Any person who has sustained a financial loss as a result of a lawyer's dishonest handling of funds entrusted to that lawyer is eligible to receive payment from the Fund. - No maximum payment limit for any one claim or in respect of any one lawyer. - There is not a requirement that a claimant was a client of a lawyer. Any claimant who suffers a loss as a result of a misappropriation or wrongful conversion by a lawyer of money or other property entrusted to or received by the lawyer in his or her capacity as a barrister or solicitor. - Compensation is payable to foreign clients. - Regarding claims made in the stated period: 118 claims received an 37 claims approved. - Uncontested claims: - Average time in weeks: 38 weeks for claims considered in 2003 only. Fund Administrators act as counsel to the Committee, they do not contest claims. - There is a formal hearing process is in writing for all claims. - Most common reasons for denying a claim: 1. No evidence of dishonest or fraudulent conduct or the dishonest or fraudulent conduct is unrelated to the lawyer's dealings with the claimant's property or money. 2. Lawyer was not acting in his or her capacity as a lawyer at the time when the fraud or dishonesty took place. 3. Claim for payment is made more than 2 years after the facts that gave rise to the claim were known to the person making it. - There is no provision for rehearing or appeal. There is one for judicial review. - There is a standard claim form in use in English (a copy available to the IBA). - Literature (if any) is made available to claimants to help them prepare their claims: introduction to the Special Compensation Fund, Guidelines for Early Consideration, Information Sheet and Instructions, Statutory Declaration and Application Form to the Fund, and case law. - Funds administrators are automatically advised of disciplinary actions against a lawyer. - The Committee has the discretion to require the claimant to obtain a judgment, or tax an account, depending on all the circumstances of the claim. That discretion is to be exercised with special regard to whether there is likelihood of recovery, clear evidence of theft and hardship to the claimant. - The usual procedure is that applications to the Fund are considered only after discipline proceedings are concluded, as there may be a strong perception of unfairness on the part of the lawyer for the Special

		Compensation Fund Committee to make a decision on an allegation of misappropriation or wrongful conversion before the Discipline Hearing Panel has made their decision on that very issue. The Committee has been able to exercise its discretion to consider a claim before the completion of the professional conduct investigation or the conclusion of discipline proceedings in those cases there have been what the Committee considers there is hardship. - Fund administrators protection: Section 86 of the *Legal Profession Act* sets out that: (1) No action for damages lies against a person, for anything done or not done in good faith while acting or purporting to act on behalf of the society or the foundation under this Act. (2) The society or the foundation, as the case may be, must indemnify a person referred to in subsection (1) for any costs or expenses incurred by the person in any legal proceedings taken for anything done or not done in good faith while acting or purporting to act on behalf of the society or the foundation under this Act. - The Fund publishes an annual report, published on the website (http://www.lawsociety.bc.ca/library/report/docs/2003AnnualReport.pdf). Generally no names are provided. The 2003 Annual report does make mention of one lawyer, Martin Wirick. The report does not provide details of payments. **Strategies to reduce claims** - Whatever type of fund please describe the approach taken by your Fund/your organization to the reduction of member's negligence and/or the audits of any trust or other members' accounts holding client's money – including details of the rules (if any) about the independence of auditors, frequency of audits, notifications of intending audits, qualification of auditors and checks to be made by auditors: Law Society Rules Trust report (1) Subject to Rule 3-73, a lawyer must deliver to the Executive Director completed trust reports for reporting periods of 12 months covering all the time that the lawyer is a practicing lawyer. (2) The date on which a firm ceases to practice law is the end of a reporting period. (3) A lawyer must deliver a completed trust report to the Executive Director within 3 months of the end of each reporting period. (4) As an exception to sub rule (1), on a written request made before the due date of a trust report, the Executive Director may allow a lawyer to submit a trust report covering a time period other than 12 months. (5) A trust report delivered to the Executive Director under this Rule must

		(a) be in a form approved by the Discipline Committee, (b) be complete to the satisfaction of the Executive Director, and (c) include all signatures required in the form. A lawyer who does not deliver a trust report under Rule 3-72 … is suspended: Rule 3-74.1(2). A trust report must be completed and signed by a person in public accounting practice who is permitted to perform audit engagements by the Institute of Chartered Accountants of British Columbia, or the Certified General Accountants Association of British Columbia: Rule 3-75 (1). - Other strategies/programmes exist or are contemplated for reduction of negligence or prevention of theft/defalcation, for encouragement of preventative peer review, or for peer reporting of likely theft: as a preventative strategy, the Law Society has three lawyers on staff whose responsibility is to provide confidential practice advice to lawyers. Chapter 13 Ruling 1 of the Professional Conduct Handbook sets out where one lawyer must report another to the Law Society: Reporting another lawyer to the Law Society Subject to Rule 2, a lawyer must report to the Law Society another lawyer's: breach of undertaking that has not been consented to or waived by the recipient of the undertaking, shortage of trust funds[7], and other conduct that raises a substantial question as to the other lawyer's honesty or trustworthiness as a lawyer. An insolvent lawyer, as defined by the Act and the Rules, must only operate a trust account with the permission of the Executive Director, and a second signatory who is a practicing lawyer, not an insolvent lawyer and approved by the Executive Director: (Rule 3-45 (4)). - Connections, assumptions, evidence are relied on to establish links between such programs and (whichever is appropriate), reduction in negligence claims and/or theft prevention or reduction: the Executive Director may at any time order an examination of the books, records and accounts of a lawyer for the purpose of determining whether the lawyer is maintaining and has been maintaining books, records and accounts in accordance with (the Rules) and designate a chartered accountant or a certified general accountant to conduct the audit: (Rule 3-79 (1)). - Any proposals or plans to reduce the level or range of protection to clients from your Fund: the development and implementation of the TPC

[7] Law Society Rule 3-66 imposes additional duties on lawyers respecting their own trust shortages or their inability to deliver up trust funds when due.

		Program (Trust Protection Program) through the Lawyer's Insurance Fund which took effect May 1, 2004. The TPC is an insurance based fund while the Special Compensation Fund has been a discretion based Fund. The implementing of the TPC moves the Special Fund to a fund of "last resort" to claimants claiming misappropriation. - The Fund most closely identifies with the American Bar Association Client Protection Funds.
Massachusetts Clients' Security Board of the Supreme judicial Court	One Fund Protects from Theft Only	**General Information** - While many of the customary good corporate governance principles are not applicable to our Fund, the following safeguards are in place: 1) An independent auditor who completes an annual audit 2) The State's highest court, the Supreme Judicial Court appoints each member of the Board to non-renewable 5 year terms. - Steps taken to make the Fund known: 1) Maintains web site 2) Distributes annual report, approximately 2,000 mailings to the Media (more than 300 major, local, and community newspapers, 39 major, community and public TV and radio stations), local bar associations, pro bono lawyers who represented claimants before the Clients' Security Board from its inception in 1974 to present, 205 banks holding IOLTA accounts, over 400 law schools', academic, public and community libraries, Massachusetts court departments at all levels, District attorneys, organizations, e.g. National Client Protection Organization, Alternate Dispute Resolution agencies, pro bono legal services and other private and governmental agencies that assist poor and indigent clients. - Website: www.mass.gov/clientssecurityboard - Frequency of decision-making meetings: monthly - Accounting period: 1 September to 31 August. - Name of currency used in this response: US dollars. - Estimated number of legal practitioners: 47,700. - Current asset balance: $5,450,506.28 as of September 1, 2004. - Current sources of Income: lawyer levy covers approximately $2.5m and recovery represents approximately $0.25m being the total Fund Income for period of approximately $2.75m. - Amount paid by each lawyer annually: approximately $48.40 which represents 22% of the annual registration fee. - Penalties for non-payment: administrative suspension from practice. - It is possible for clients to earn interest on trust account balances. - Threshold information regarding the opportunities to earn interest on those balances: The Supreme Judicial Court of Massachusetts requires lawyers and law firms to establish interest-bearing accounts for client deposits, which are nominal in amount or expected to be short-term. All interest generated from such client accounts is remitted to the IOLTA (Interest On Lawyer Trust Accounts) Committee, which distributes it to three charitable entities: The Boston Bar Foundation, the Massachusetts Bar Foundation and the Massachusetts Legal Assistance Corporation. The Funds must be used to improve the administration of justice and to support the delivery of civil legal services to the poor. "Large short-term deposits or modest amounts to be held for a significant period of time will continue to be invested in interest-bearing

		accounts for the client's benefit. The decision as to which account to use rests, as always, in the sound discretion of the lawyer" (Source: IOLTA Guidelines, Revised January 1998) - Actual distribution of Fund balance: all the costs associated with the following categories (administration costs, proved claims for compensation, legal education, legal research, legal aid, contingency provisions for claims) are paid by a sister agency. The total Fund Income for period is $2.4m. - All excess monies remain in the Fund. They are rolled over into the Fund balance of future years. - In their opinion, the Fund has enough assets to pay likely claims over the next 5 years. - Method used to determine likely claims expenditure over the next 5 years: a review of the docket, interviews with the disciplinary counsel office regarding likely claims, and an examination of claims expenditures for the most recent 5 years and 10 year periods are activities undertaken to predict likely future expenditures. - Method used to protect the Fund's asset base against unexpected claims: none other than to report to the Supreme Judicial Court the rise in claims. - No re-insurance arrangement. **Claims against the Fund** - Claims may be lodged for defalcation (theft) by the claimant's former lawyer and failure of deceased lawyer to account for client Funds. - No maximum payment limit for any one claim. - No maximum amount payable in respect of any one lawyer. - Claimant is required to be a client of the lawyer. - Compensation is payable to foreign clients. There are no special restrictions for foreign claimants. - Percentage of claims over the stated period: 25%. At the start of the fiscal year the Board had 176 pending claims on its docket. During the fiscal year the Board received 90 new claims. The Board decided 159 claims during the course of the year, making awards in 101 and dismissing 58. At the end of the fiscal year the Board had 107 claims on its docket. - Regarding uncontested claims: - Average time in weeks: 9-12 months. - There is not a formal hearing process. - As for rejected claims: the most common reasons for denying a claim are as follow: 1) Recovery from third party (60%) 2) Fee dispute/no defalcation (14%) 3) Restitution by attorney (12%) 4) Balance of reasons for denying claims: voluntary withdrawals, no lawyer-client relationship and insufficient data. There is a provision for rehearing. There is not for appeal or judicial review. - There is a standard claim form in use available in English, Spanish and Vietnamese (available to the IBA). - Descriptive brochure, board rules, court rules related to board procedure and case summaries of all matters adjudicated by the board are available on the website to help claimants prepare their claims. - Fund administrators are automatically advised of disciplinary actions against a lawyer.

		- Claimants are required to conclude civil action against a lawyer accused of dishonesty of negligent conduct before a claim will be paid. Disciplinary action against a lawyer is required before paying a claim. - Fund administrators are personally protected from civil action against them. - The Fund publishes an annual report, published on the website (www.mass.gov/clientssecurityboard). The report gives the names of the lawyers. No details of payments of claims are provided. However, summaries of decided claims (by month) appear on website. **Strategies to reduce claims** - Approach taken by the Fund to the reduction of member's negligence and/or the audit of any trust or other members' accounts holding clients' money: there are three specific rules designed to reduce negligence. 1) Mass.R.Prof. C.1.15 –Safe keeping property is a rule with strict procedures that lawyers must follow in receiving, holding, and distributing client funds. 2) Mass. R. Prof.C.1.15 (h) dishonoured check notification is a rule whereby all banks where lawyers have their client funds on deposit must notify the lawyer disciplinary office when a lawyer's check or draft drawn on a client funds account is dishonoured for insufficient funds. 3) A proposed rule Mass. R. Prof. C.1.4 requiring lawyers to inform clients if they do not have professional liability insurance with coverage of at least $250,000/$500,000. There is no specific audit rule in Massachusetts. However, where the lawyer disciplinary officer determines that an audit is necessary, it may be as simple or comprehensive as is appropriate for the situation. - Other existed or contemplated strategies for reduction of negligence or prevention of theft/defalcation: changes are proposed to Mass. R. Prof. C1.4 requiring lawyers who do not have professional liability insurance to disclose that fact to their clients. In addition, changes are proposed to SJC Rule 4.02(3) requiring lawyers to certify on their annual registration statements whether they are covered by liability insurance described in Mass.R.Prof.C.1.4. - Connections, assumptions, evidence established between these programmes and reduction in negligence: before preventive rules or procedures are put in place, a review of such measures in other jurisdictions is conducted. If those measures demonstrate success in preventing theft or negligence, the measures are proposed for implementation with modifications some of the time. - Any need in relation to client protection matters: sharing of information regarding: - Methods of educating the public of the existence of the Fund. - Prevention tools, measures, or procedures that do appear to be effective in decreasing theft and negligence. - The Fund most closely identifies with the NCPO- National Client Protection Organization (www.ncpo.org). - Connections, assumptions, evidence established between these programmes and reduction in negligence. **General Comments** - The need for a Client Protection Fund appears to be nationwide- but only lawyers affiliated with client protection know about the existence of

		funds. - How can Funds better educate lawyers, judges, and non-lawyers about Funds? Through education more people will be served. Unless there is a need to "protect" funds from claims or "protect" the public from knowing about theft by lawyers, better efforts to educate must be taken.
Ordem dos Advogados do Brasil	No Client Protection Fund	

Supreme Court of Ohio	One Fund Protects from Theft only	**General information**
		
		- The CSF of Ohio is governed by Court Rule. The responsibilities of the Board are set forth in the Rule.
		- Steps taken to make the Fund known: the Fund sets out press releases and informational pamphlets to a wide variety of organizations and agencies. Through the website as well.
		- Frequency of making-decision meetings: quarterly.
		- Accounting period: 7/1/2004 to 6/30/2005.
		- Name of currency used in this response: US dollars.
		- Estimated number of legal practitioners: 39,000.
		- Current asset balance: $687,838.37 as of 6/30/2004.
		- Current sources of Income are reflected as follows:
		  - Lawyer levy: $1,250,000.00
		  - Recovery: $34,547.22
		  - Interest on Fund investments: $9,550.95
		- It is not possible for clients to earn interest on trust accounts balance.
		- Actual distribution of Fund balance: actual proved claims cover $1,019,555.54; administration costs ($355,093.00); other sources such as attorney fees ($1,450.00). The total Fund Income for the period is $1,376,098.54.
		- In their opinion, the Fund has enough assets to pay likely claims over the next 5 years.
		- No re-insurance arrangement.
		
		Claims against the Fund
		
		- Claims may be lodged for unearned fees, theft of settlement proceeds, theft of estate assets and theft by fiduciaries.
		- Maximum payment limit for any one claim: $75,000 per claim.
		- No maximum payment limit in respect of any one lawyer.

		- It is a requirement that the claimant being a client of the lawyer against whom the claim is made. - Compensation is payable to foreign clients. - Claims over the stated period: 133 approved and 112 dismissals. - There is not a formal hearing for uncontested claims. - As for rejected claims: the main reasons for denying a claim are these regarding fee dispute; inability to verify loss; no discipline against a lawyer. There is a provision for rehearing conducted by the Board of Commissioners. There is not for appeal or judicial review. - There is a standard claim form in use in English (available to IBA). - Letters and pamphlets are both used to help claimants prepare their claims. - Fund administrators are automatically advised of disciplinary actions against a lawyer. - Claimants are not required to conclude civil action against a lawyer before the claim will be paid. - Disciplinary action against a lawyer is required before paying a claim. - Fund administrators are personally protected from civil action against them. - The Fund publishes an annual report, not published on the website. The reports name the lawyers against whom claims are made. It gives no details of any payment. **Strategies to reduce claims** - Connections, assumptions, evidence established between these programmes and reduction in negligence
State Bar of Montana	One Fund Protects from Theft only	**General Information** - The Board operates under the By-Laws of the Montana State Bar; currently meets approximately every 6 months. - Steps taken to make the Fund known: advertising through the State Bar webpage and by referrals from the Office of Disciplinary Counsel. - Frequency of making-decision making: semi-annually or sooner if necessary based on claim issues. - Accounting period: as of the 7/1/2004 to 6/30/2005. - Name of currency used in this response: dollars. - Estimated number of legal practitioners currently covered by the fund: 2,800. - Current asset balance of the Fund: $690,696.07 FY 2004. - Current sources of Income for the Fund: Lawyer levy represents the 51% (62,220); Interest on client deposits covers the 34% (37,754.42); and, Interests on Fund Investments covers the 15% (16,984.50). - Amount paid by each lawyer annually: $20. - Penalties for non-payment: loss of license. - It is not possible for clients to earn interest on trust account balances. - Actual distribution of the Fund balance: actual proved claims for compensation represent the 81% (52,962.91); administration costs constitute the 14% (16,000); and, legal education constitutes the 5% of the total (3,390.19). Total Fund Income for period is of 72,353.10. - Method used to determine likely claims expenditure over the next 5 years: payment of claims will continue to be based on board decision

		within the rules of the Fund.
		- Method used to protect the Fund's asset base against unexpected claims: because the Montana LFCP is not required to pay 100% of a claim, the amount paid will always reflect the available balance to avoid overdrawing the fund.
		- No re-insurance arrangement in place.
		
		Claims against the Fund
		
		- Categories of loss for which claims may be lodged: theft of trust funds resulting from a lawyer dishonest conduct.
		- No maximum payment exists.
		- It is a requirement that the claimant be a client of the lawyer.
		- Compensation is not payable to foreign clients. This is currently being discussed and has not been challenged at this time.
		- Claims over the stated period: 33%. 4 claims received (plus 14 of the prior period) and 5 claims approved.
		- Regarding uncontested claims:
		  - Average time in weeks: 20.
		  - There is a formal hearing.
		- As for rejected claims: there is not a provision for rehearing or for appeal or for judicial review.
		- Average time in weeks elapsed for contestation of the claim: 40.
		- There is a standard claim form in use, one copy available to IBA, in English.
		- Rules of the LFCP and Frequently Asked Questions are provided in order to help claimants prepare their claims.
		- Fund administrators are automatically advised of disciplinary actions.
		- The Fund does not require claimants to conclude civil action against a lawyer before paying a claim.
		- The Fund does require disciplinary action against a lawyer before paying a claim.
		- Fund administrators are personally protected from civil action against them.
		- The Fund publishes an annual report (not published in the website).
		- The report does not name the lawyers nor give details of the payment of the claim.
		
		Strategies to reduce claims
		
		- Approach taken by the Fund to the reduction of member's negligence and/or the audit of any trust or other members' accounts holding clients' money: there are no requirements for random audits of trust accounts.
		- Other existed or contemplated strategies for reduction of negligence or prevention of theft/defalcation: there is an overdraft protection program where the Board is automatically notified when an attorney's trust account becomes overdrawn. Additionally, there is a program titled Lawyers Helping Lawyers that offers confidential peer reporting.
		- Connections, assumptions, evidence established between these programmes and reduction in negligence: with the overdraft protection program, Lawyers Helping Lawyers and the Office of Disciplinary Counsel, there is often prior notice when an attorney is struggling.
		- The organisation would support an IBA-sponsored training package or short course, to assist the organization in meeting needs.
		
		General Comments

		The Montana LFCP has the benefit of a review by the ABA Standing Committee on Client Protection in March of 2002. A number of good suggestions were made at that time and some have been implemented. Montana has a very strong program.
Louisiana State Bar Association	One Fund Protects From Theft Only	**General Information** - Name of the Fund is 'Client Assistance Fund'. - Established in 1962 - Committee members of the fund in total are 21 lawyers. - Rules of Procedure of the Bar Association attached. - Steps taken to make the Fund known: Information on LSBA website: www.lsba.org. All disciplinary complaints are informed of the fund. - Estimated number of legal practitioners currently covered by the fund are 20,000. - The Frequency of the decision-making meetings are generally quarterly or upon need. - Current asset balance: $ 755,101.00 as of 30/09/2004. - Exact information about the current sources of Income for the Fund for stated accounting period is not available. - It is possible for clients to earn interest on trust account balances. - There is no specific requirement for threshold information. Under rules client must be reasonably informed. - Specific amount of funds are collected for compensation each fiscal year. Various funds return to general funds for allocation in next year. - The Fund has enough assets to pay likely claims over the next 5 years. - The method used to determine likely claims expenditure over the next 5 years is the average of preceding years knowledge & knowledge of pending claims. - Basis or formula applied to decide on the distribution of any excess fund balances between the beneficiaries (if any): Specific amount is collected per fixed years. Any additional amount must have a special allocation, to protect the Fund's asset base against unexpected claims. - The Fund does not have any re-insurance arrangement in place. - There has never been a situation where assets of the Fund were inadequate to pay claims. But the Association did have funding problems several years ago, though they have been solved now. **Claims Against the Fund** - Claims may be lodged under the categories of fraudulent and dishonest conduct. - There are maximum payment limits for a claim, which is, £ 25,000/- - There is no specific requirement that the claimant should be a client of the lawyer. - Compensation is payable to foreign clients, but with certain restrictions and limits on such payments. These are:

		- Wrongful acts of Louisiana attorney must be committed in Louisiana State, or - With substantial connection to Louisiana State. - During 1 July, 2003 till 30 June, 2004, there were 90 claims received out of which 11 claims have been approved and 62 claims are pending. - Most common reasons for denying a claim, is 1. Dishonest conduct 2. Fee Dispute - There is a formal hearing process for uncontested claims. When a claim is rejected by the fund administrators, there is a provision for rehearing and not for appeal. - The Client Assistant Fund Committee conducts the rehearing. - There is no provision for a judicial review. - There is a standard claim form, which is in use. A copy is available to the IBA. - Fund administrators are automatically advised of the disciplinary actions against a lawyer. - LSBA sends all applications for relief to the Office of the Disciplinary Counsel - The Fund does not require claimants to conclude civil action against a lawyer accused of dishonest or negligent conduct, before a claim will be paid. - The Fund does not require disciplinary action against a lawyer before paying a claim. - The Fund administrators are not personally protected from civil action against themselves by dissatisfied lawyers or claimants. - The Fund does not publish an annual report. **Strategies to reduce claims**: - Approach taken by the Fund to the reduction of member's negligence and/or the audit of any trust or other members' accounts holding clients' money: The LSBA does not have random trust audits of overdraft notification. - There is a requirement of one hour of Client Education in Ethics and Professionalism. Eight Hours of Client Education credits are required for new attorneys in Ethics, Law Office Management & Professionalism. - Another preventive strategy used by the LSBA and the Office of the Disciplinary Counsel, is to aggressively pursue and discipline offending lawyers. Presumably suspended or dis-banned lawyers do not steal again. - The LSBA would support an IBA-sponsored training package or short course, to assist their Fund in meeting identified needs. **General Comments:** - The LSBA would continue to try and improve their Client Assistance Fund.

Nigeria Bar Association	No Client Protection Fund	

Appendix 3
IBA Members Who Did Not Respond to IBA Survey

1. Algeria – Organisation Nationale des Avocats Algeriens Palais de Justice
2. Angola – Angola Bar Association
3. Armenia – Bar Association of Armenia
4. Australia – (a) Law Society of New South Wales
   (b) The Law Society of the Australian Capital Territory
   (c) The South Australian Bar Association
   (d) Victorian Bar Council
5. Bahamas – Bahamas Bar Association
6. Bahrain – Bahrain Bar Society
7. Bangladesh – National Bar Association of Bangladesh
8. Barbados – Barbados Bar Association
9. Belgium – (a) Institut des Juristes d'Entreprise
   (b) Nederlandse Orde van Advocaten
   (c) Ordre Francais des Avocats du barreau de Bruxelles
   (d) Orde van Vlaamse Balies
10. Brazil – (a) Centro de Estudos das Sociedades de Advogados (CESA)
    (b) Instituto dos Advogados do Rio Grande do Sul
    (c) Sao Paulo Lawyer's Association
11. Bulgaria – (a) Bulgarian Bar Association
    (b) Sofia Bar Association
    (c) Interadvocat Bar Association
12. Cambodia – Bar Association of the Kingdom of Cambodia
13. Cameroon – Cameroon Bar Association
14. Canada – (a) Canada Bar Association
    (b) Chambre des notaires du québec
15. Cayman Islands – Cayman Islands Law Society
16. Channel Islands – The Law Society of Jersey
17. China – All China Lawyers Association
18. Croatia – Croatian Bar Association

19. Cyprus - Cyprus Bar Association
20. Czech Republic – Czech Bar Association
21. Dominica – Dominica Bar Association
22. Ecuador – (a) Federacion Nacional de Abogados del Ecuador
    (b) Colegio de Abogados de Pichincha
23. Egypt – Egyptian Bar Association
24. England – (a) Law Society of England and Wales
    (b) The Commercial Bar Association
    (c) The City of London law Society
    (d) European Young Bar Association
25. Equatorial Guinea – Colegio de Abogados de Guinea
26. Estonia – Estonian Bar Association
27. Ethiopia – Ethiopian Bar Association
28. Fiji – Fiji Law Society
29. France - (a) Arab Association for International Arbitration
    (b) Association Francaise des Avocats Conseils d'Entreprises
    (c) Association Francaise des Juristes d'Entreprise
    (d) Ordre des Avocats de Paris
    (e) Confederation Nationale des Avocats
30. Gambia – Gambia Bar Association
31. Gibraltar – The General Council of the Bar in Gibraltar
32. Greece – Thessaloniki Bar Association
33. Guyana – Guyana Bar Association
34. Hungary – (a) Budapest Bar Association
35. India - (a) Bar Association of India
    (b) Society of Indian Law Firms (SILF)
    (c) The Bar Council of India
36. Indonesia – Indonesian Bar Association
37. Iraq – Iraqi Bar Association
38. Ireland (Republic) – The Bar Council of Ireland
39. Isle of Man – Isle of Man Law Society

40. Israel - The Israel Bar
41. Italy - (a) Ordine degli Avvocati di Milano
    (b) Ordine degli Avvocati Di Perugia
    (c) Ordine degli Avvocati di Roma
    (d) Ordine degli Avvocati Genova
42. Jamaica – Jamaican Bar Association
43. Japan – (a) The Japan Bar Association
    (b) Tokya Bar Association
44. Jordan – Jordan Bar Association
45. Kenya – (a) International Federation of Women Lawyers (FIDA)
    (b) Law Society of Kenya
46. Kuwait – Kuwait Bar Association
47. Latvia – The Latvian Council of Sworn Advocates
48. Lesotho – Law Society of Lesotho
49. Liberia – Liberian National Bar Association
50. Libya – Libyan Bar Association
51. Liechtenstein – Liechtensteinische Rechtsanwaltskammer
52. Lithuania – Lithuanian Bar Association
53. Luxembourg – Le Barreau de Luxembourg
54. Macedonia – Macedonian Business Lawyers Association
55. Malawi – Malawi Law Society
56. Malaysia – (a) Bar Council Malaysia (Majlis Peguam)
    (b) Sabah Law Association
57. Malta – Chamber of Advocates – Malta
58. Mauritius – Mauritius Bar Association
59. Mexico – Asociacion Mexicana de Abogados AC
60. Mongolia – Association of Mongolian Advocates
61. Morocco – Ordre des Avocats au Barreau de Casablanca
62. Mozambique – Ordem dos Advogados de Mocambique
63. Namibia – Society of Advocates of Namibia
64. Nepal – (a) Nepal Bar Association

(b) Nepal Law Society

65. Netherlands – (a) Amsterdam Bar Association

(b) Netherlands Bar Association

(c) Netherlands Antilles

66. Norway – Norwegian Bar Association

67. Pakistan - Pakistan Bar Council

68. Papua New Guinea – Papua New Guinea Law Society

69. Paraguay – Colegio de Abogados de Paraguay

70. Peru – Colegio de Abogados de Lima

71. Philippines – (a) Integrated Bar of the Philippines

(b) Philippine Bar Association

(c) Philippine Lawyers Association

72. Poland – (a) The Polish Bar Council

(b) National Council of Legal Advisers of Poland

73. Puerto Rico – Puerto Rico Bar Association

74. Romania – Bucharest Bar Association

75. Russian Federation – (a) Federal Union of Russian Advocates

(b) International Union (Commonwealth) of Advocates

(c) Russian Lawyers Guild

76. Rwanda – Ordre des Avocats Rwanda

77. Scotland – (a) Glasgow Bar Association

(b) The Law Society of Scotland

78. Sierra Leone – Sierra Leone Bar Association

79. Singapore – The Law Society of Singapore

80. Slovak Republic – Slovak Bar Association

81. Solomon Islands – Solomon Islands Bar Association

82. South Africa – (a) Corporate Lawyers Association of South Africa

(b) Law Society of Northern Provinces

(c) KwaZulu-Natal Law Society

(d) Society of Advocates of Natal

(e) The Law Society of the Cape of Good Hope

83. Spain – (a) Consejo General de la Abogacia Espanola
(b) Illustre Collegio d'Advocats de Barcelona
84. Sri Lanka – Bar Association of Sri Lanka
85. St. Lucia – St. Lucia Bar Association
86. St. Vincent – St. Vincent and Grenadines Bar Association
87. Swaziland – The Law Society of Swaziland
88. Syria – Syrian Bar Association
89. Tanzania – (a) East Africa Law Society
(b) The Tanganyika Law Society
90. Thailand – (a) Thai Bar Association
(b) Lawyers Council of Thailand
91. Tonga – Tonga Law Society
92. Trinidad and Tobago – The Law Association of Trinidad and Tobago
93. Tunisia – Ordre National des Avocats de Tunisie
94. Turkey – (a) Ankara Bar Association
(b) Union of Turkish Bars
95. USA – (a) American Bar Association
(b) Customs and International Trade Bar Association
(c) The Florida Bar Association – International Law Section
(d) Los Angeles County Bar Association
(e) National Conference of Women's Bar Associations
(f) State Bar of Michigan – International Law Section
(g) National Association of Women Lawyers
(h) The Association of the Bar of the City of New York
96. Uganda – Uganda Law Society
97. Ukraine – Union of Advocates of Ukraine
98. Zambia – The Law Association of Zambia
99. Zimbabwe – The Law Society of Zimbabwe

List of Organisations not mentioned in the IBA Member Organisations List that have responded to the CP Fund Survey:

1. Colegio de Abogados Santa Cruz de Tenerife
2. Fonds d'assurance responsabilite professionnelle du Barreau du Quebec
3. Law Society of Prince Edward Island
4. Law Society of Saskatchewan of Canada
5. Law Society of Newfoundland and Labrador
6. Oregon State Bar
7. Vermont Bar Association
8. New Jersey Lawyers
9. Idaho State Bar Client Assistance Fund
10. Kansas Lawyers
11. Office of Disciplinary Counsel of Hawaii
12. Research Society of International Law, Pakistan
13. Nova Scotia Barristers' Society
14. Attorneys Fidelity Fund South Africa
15. Law Society of British Columbia
16. Massachusetts Clients' Security Board of the Supreme Judicial Court
17. Supreme Court of Ohio
18. State Bar of Montana
19. Louisiana State Bar Association.

Jurisdiction	USA (New York Lawyers' Fund)	USA (North Carolina State Bar)	Law Society of Upper Canada	Law Society of Ireland	Law Society of Scotland	Law Society of New South Wales
1. Value of fund and how funded	$125million. Funded by registration fee, restitution, interest, judicial sanctions and contributions.	$1.45million funded by annual contributions.	$21.6million plus unpaid liability of $9.8 million. Fully funded by profession.	€25million funded by contributions.	Value varies. Funded by subscription. In may 2008 reserves running at between £1m and £2m	$56million raised by contributions, interest on investments and recoveries.
2. Amount of contributions from profession and when collected.	Biennial registration fee $350 of which $60 goes to Fund. Collected once every two years on attorney's birthday. 237,000 registered lawyers	$25 per lawyer – can vary if needed. Highest has been $50. Collected annually 21,300 lawyers	$200 per member, collected as annual membership.	€400 per member – 8,000 members collected as part of Practising Certificate fee.	£600 per principal collected 1st November from Practising Certificate fee.	Private practitioners $50. Corporate practitioners $25. Part of Practising Certificate renewal. Adjust level of contributions due to claims position. Currently at lowest ever – highest $645.
3. Average value of total claims paid in last 3 years.	$7.5million	$100,000	$2.8million	€2million	£272,000	$2.6million
4. Maximum grant paid in respect of any one claim.	$300,000 per individual loss. No per attorney cap.	$100,000	$150,000 per claimant after 24.04.08 $100,000 per claimant after 25.05.90	€700,000	No cap	Legal Profession Act 2004 enables Council to fix cap per claim – but never have done.

Jurisdiction	USA (New York Lawyers' Fund)	USA (North Carolina State Bar)	Law Society of Upper Canada	Law Society of Ireland	Law Society of Scotland	Law Society of New South Wales
5. Whether cap applied to claims in respect of a series of related acts/omissions.	No cap	No cap	No cap	No cap	No cap	No cap although permitted by legislation
6. Whether have power to make payments in respect of losses by dishonesty or failure of account.	No	Failure to return a fee where no work was done	No.	No	No	No
7. Whether Fund underwritten by insurance and if so how does it work.	No insurance	No insurance is available	No insurance	Yes - Insurance in place - €30m excess of €5m.	Yes Insurance in place for 07/08 - £5m excess of £2m.	No

National Client Protection Organization

STANDARDS FOR EVALUATING LAWYERS FUNDS FOR CLIENT PROTECTION

Enacted - June 2, 2006

Lawyers Funds for Client Protection ['Funds'] can only benefit from articulating standards to measure performance. There are four fundamental building blocks for any Fund that strives for excellence:

(1) An organizational structure that secures the Fund's independence;
(2) Steady, secure and adequate funding;
(3) Accessibility; and
(4) Responsiveness to the need.

On this foundation are constructed the 31 specific policy standards that follow. Because all four building blocks are necessary, they are interdependent, and their corresponding standards are interrelated. Cross-references are provided.

Standards in a developing field cannot be permanent. As progress is made and aspirations evolve, however, Funds must consider, in detail, what they can and should accomplish in order to offer a high level of protection to clients. The fundamental question will always be: ' Is the need being met?' These standards provide an analytical framework for answering that question, and impetus thereafter to develop a plan of action for reaching the desired level of excellence. In short, these standards for evaluating Funds are presented to assist a Fund in determining whether it is truly protecting the law clients in its jurisdiction.

Over the last several decades, the American Bar Association has developed an evolving Model Rule for structuring and operating a Fund. The philosophical underpinnings of these standards are consistent with those of the Model Rule, the use of which is greatly encouraged. Even a cursory review of the ABA's Triennial Survey of Funds will show that there are many ways to structure Funds, however, and even more variability in the actual delivery of the services by Funds. These standards are intended to compliment the Model Rule by establishing aspirational criteria by which jurisdictions can evaluate the performance of their programs, whether they use the Model Rule or significantly depart from it.

1. Structure/Organization

1.1 The Fund should be an entity of the jurisdiction's highest court as an exercise of the Court's power and duty to regulate the practice of law.

1.2 The Fund should be created and maintained by court rule with enabling statute only where necessary under the jurisdiction's constitution.

Commentary

Regulation of the practice of law, including such things as admissions, rules of practice, rules of professional conduct, and discipline, are generally the responsibility of a jurisdiction's highest court ['Court']. In that capacity, the Court should create and maintain the Fund by court rule. Some jurisdictions may prefer to have an enabling statute; in other jurisdictions an attempt to create a Fund by way of statute may be considered a violation of separation of powers.

In any event, the Court should create and maintain a Fund as a critical aspect of its professional responsibility rule making power, recognizing the appropriateness of creating a remedy for those who have had their trust violated by lawyers licensed by the Court.

Where statute vests authority for regulation of lawyers with a body other than the Court, as is the case with Canadian law societies, care must be taken to give the Fund the autonomy and independence it needs to ensure it meets these standards. 'Court' as used in these standards shall be meant to include any governing body with the authority to create and maintain the Fund.

1.3 The Fund shall constitute a trust separate and independent from any other fund or entity of the Court, bar association, law society or government agency.

Commentary

It is essential to the success of a Fund that it constitute a trust, inviolate from other uses and unavailable to all other entities. Lawyers contribute to the Fund each year on the basis that the money will be used to pay victims of lawyer dishonesty, to administer the Fund, and to take steps to prevent such losses. To permit other agencies or organizations to utilize the money so collected for any other purpose, however meritorious, would be to countenance the sort of breach of trust for which lawyers are suspended or disbarred.

It is therefore appropriate to refer to those appointed by the Court to manage the Fund as 'Trustees', which term is not used lightly. Funds that are nothing more than line items in bar associations' budgets, subject to political whim and competition for scarce resources, cannot be relied upon to fill the need or fulfill the purpose of the Fund.

1.4 The Court should appoint to the Fund's Board of Trustees only those individuals who have demonstrated a combination of achievement, professionalism and concern for the public. Diversity of background should also be a factor in Trustee selection, including members who are not lawyers.

1.5 The Fund's Trustees should have sole discretion to decide claims, make awards and determine the Fund's procedures and policies within the court rule.

Commentary

Apart from creating a truly independent Fund (see Standards 1.1 - 1.3, above), and providing it with appropriate funding (see Standards 2.1 - 2.5), the next most important thing that the Court can do to ensure a successful Fund is to appoint only outstanding individuals to serve as Trustees. Only those who have already distinguished themselves professionally and in service to the public should be considered for these appointments, whether they are positions for lawyers or non-lawyers.

Once outstanding persons have been selected to immerse themselves in the purpose and policies of the Fund, they should be permitted and expected to make all significant decisions on claims and policy in their sole discretion. Expertise borne of handling the Fund=s matter combined with commitment to the Fund's purpose engender just and timely decisions.

Trustees should recuse themselves from consideration of matters in which they have a conflict of interest, or the potential for such conflict.

1.6 To manage the Fund's daily affairs, the Trustees should employ a staff sufficient to permit them to (a) render the most just and timely decisions attainable in all matters, and (b) efficiently implement their decisions. The staff should serve at the pleasure of the Board.

Commentary

However committed they may be to the Fund, the Trustees cannot be expected to manage every aspect of the Fund's business on a daily basis. The Trustees should not hesitate to employ such staff as is necessary to assist them in attaining just and timely results, and in protecting the Fund's rights. Full time staff devoted to the Fund's affairs is preferable. Where, as a practical reality, staff must be shared with other entities or functions within an organization, the independence of the staff in handling the Fund's affairs must be guaranteed.

1.7 Staff salaries and all other obligations of the Fund should be paid or reimbursed by the Fund out of its income and assets to maintain the Fund's independence.

Commentary

Once established on firm financial ground, the Fund should be financially beholden to no other entity. Rather, it should pay its own way, thus securing the Fund's independence.

2. Funding

2.1 The Fund must have a source of income that is steady, secure and adequate to meet its standards of accessibility and responsiveness.

Commentary

Client protection is a field in which good intentions are not enough. A Fund in hiding or unable to meet the need (see Standards 3.1 - 3.6, and 4.1 - 4.10, below) cannot be considered a Fund at all. In many ways, funding is the ultimate Fund issue. Not only must funding be adequate, but it must be steady - every year or every other year - and secure. Given the Fund's importance to maintaining trust and respect within the legal profession, it cannot be permitted to go begging each year with clients' financial viability hanging in the balance.

2.2 Primary funding should be by regular, periodic assessment of lawyers. The assessment should be conducted by authority of the Court, with appropriate sanctions for non-compliance.

2.3 All, or nearly all, licensed members of the profession should pay into the Fund.

Commentary

Voluntary contributions should be gladly and thankfully accepted, but cannot be relied upon to maintain a fully accessible and responsive Fund. Funds are based on the principle of professionalism and are not insurance companies. Lawyers are not asked to pay the assessment on the basis that they contribute to the risk covered by the Fund. To the contrary, it is a source of pride to note how few lawyers conduct themselves in a way that threatens Funds.

With the overwhelming majority of honest lawyers paying for the misdeeds of a few, the Fund is a testament to the bar's honesty and integrity. Just as instances of dishonesty by lawyers besmirch all lawyers, so too do payments by the Fund to rectify these situations result in benefits to all lawyers. Virtually all licensed members of the bar should participate in taking care of these debts of honor. Exemptions, if any, should be narrowly drawn.

2.4 The assessment should not be halted, suspended, or reduced because the Fund has a positive balance. To the contrary, a substantial reserve should be sought, as interest income will help the Fund meet the need in times of large or numerous claims.

2.5 There should be no cap on the Fund's reserve short of self-endowment with full reimbursement of victims.

Commentary

Because of the vagaries of lawyer misconduct, it is not possible to determine the exact amount a Fund will need to reimburse each year. Funds should neither be expected to spend everything it assessed for a given year, nor limited to reimbursing losses only up to the annual assessment. Comparisons with the operating budgets of state agencies are inappropriate. Sound financial health for Funds needs no apology; indeed, it is required for fiscal responsibility in the public interest**.** With the attainment of an adequate balance, the resulting interest income helps ensure the Fund's continued viability and the ability to meet unforeseen future needs.

Some Funds have a cap on the Fund's reserves whereby the periodic lawyer assessment is halted, suspended or reduced when a certain level is attained. This is to be avoided for a number of reasons. The first is that halting an assessment short of providing full reimbursement of all victims misses the point of the Fund. Second, it is extremely difficult to know how much is 'enough'. Over the years, some Funds have halted their assessment with a reserve less than the per claim maximum of other Funds. No jurisdiction's Fund is self-endowed (that is, fully able to meet all obligations without infusion of fresh capital), and Funds that employ this mechanism are likely to regret it.

2.6 The Fund should take an assignment of each successful claimant's rights and, within sound business judgment, pursue those rights in vigorous attempts to replenish the Fund with subrogation receipts.

Commentary

The Fund should take an assignment of claimants' rights. Subrogation is a legal doctrine operating under common law. Inherent in the Fund having claimants' rights is that claimants should not 'double-dip'. The Fund as assignee and subrogee of its successful claimants is entitled to seek recovery for money paid on claims. Pursuit may be of both the wrongdoer and collateral sources of recovery. Funds have found it a sound business practice to pursue such rights with vigor. As to the potentially competing subrogation rights of Funds and their successful claimants, see Standard 4.3. Funds and their claimants should share information with prosecutors and discipline authorities, as permitted by law.

2.7 The Fund should seek implementation of appropriate loss prevention mechanisms. Among those that should be sought are trust account overdraft notification, minimum financial recordkeeping, random audits of trust accounts, insurance payee notification, and education of the bar and the public. Lawyer assistance and practice assistance programs should be encouraged and assisted in making their services known.

Commentary

While seeking to raise sufficient revenues to meet the need, the Fund must also strive to limit or prevent losses. In addition to participating in efforts to educate the bar and the public about sound practice and risk avoidance, the Fund should encourage the implementation of loss prevention mechanisms such as those listed above. Each is successfully operating in a number of jurisdictions, and each has a Model Rule of the American Bar Association available to support it.

3. Accessibility

3.1 The Fund should make every reasonable effort to make its existence, nature and purpose known to the bar and the public. In particular, the Fund should ensure that those most likely to be approached by victims of dishonest lawyers - such as prosecutors, ethics committee counsel and members, ombudsmen, receivers/custodians, bar associations and judges - understand the Fund and the importance of appropriate

and timely referrals. Similarly, copies of claims should be provided to respondents whose whereabouts are known, with invitations to respond.

3.2 The Fund should issue and publish an annual report. Quarterly or semi-annual news releases should be done as well, even in the absence of high volume activity.

Commentary

The Fund should not be the profession's secret. To the contrary, the profession should be proud to make its existence known to the public in the interests of transparency and accountability. A Fund fearful of receiving valid, compensable claims has a funding problem. (See Standards 2.1 - 2.7, above.) All reasonable measures should be taken to ensure that clients with compensable losses find their way to the Fund. Regular reports on the Fund's activity should come to be expected. A lack of activity may well be noteworthy in itself.

3.3 Ineligibility for classes of persons to qualify as claimants, like any limitation on the Trustee's discretion, is not to be favored.

3.4 Strict scrutiny in light of the Fund's purpose and mission should be applied to any suggested barriers to the Trustees' consideration of claims on their merits.

3.5 Claim forms and accompanying instructions should be in plain language and, where appropriate, available in other languages.

3.6 Time limitations on the filing of claims should be reasonable. Trustees should have the authority, in their discretion, to relax the time limitations for good cause.

Commentary

There are a number of ways to make a Fund inaccessible to those who need it, and none serve the Fund's purpose. Defining away claimants, imposing unrealistic time limitations, using incomprehensible forms and instructions, and setting up other impenetrable barriers have the same effect on otherwise deserving claimants as hiding from them.

While a Fund must be able to bring closure to matters within a reasonable time frame, doing justice to the claimants in the Trustees' discretion should remain paramount. Strict or automatic prohibitions from consideration for an award should therefore be avoided. Trustees may consider the following factors presented by claimants: relationship to the respondent, legal status, extent of need, education and sophistication, negligence, or unclean hands. Such factors should not be used harshly to deny meritorious claims, however. (See Standard 4.10.) Trustees should also recognize the particular vulnerability of claimants with limited, or no, ability with the English language, or the inability to read or write, and should provide reasonable accommodation as the circumstances warrant.

3.7 The Fund's rules should be supplemented with regulations and written procedures

as needed.

Commentary
The Fund, its Trustees, staff, claimants and the public all benefit from having supplemental policies and procedures reduced to writing and made available on request. This also serves to enhance the Fund's transparency and accountability, as well as creating greater consistency in decision-making. Claimants and potential claimants should know what is expected of them and what limitations the Fund has established to address their needs.

4. Responsiveness To The Need

4.1 The ultimate goal of the Fund is to fully reimburse all clients victimized by the dishonest conduct of their lawyers in as timely a manner as possible.

Commentary
If a Fund is to be anything other than window dressing or a public relations ploy, no other ultimate goal makes sense. If full reimbursement is not possible at any given time, efforts should be redoubled to meet the Standards on Funding (2.1 -2.7, above).

4.2 Limitations on the payment of awards - whether per claim, per claimant, per year or in the aggregate against any one lawyer - are not to be favored. Every opportunity should be sought to eliminate such limitations on the Trustees' discretion to pay awards.

Commentary
Artificial limits on the payment of otherwise compensable claims are, at best, necessary evils. Their necessity should be questioned, and their impact lessened at every opportunity. Raising such limits is well worth doing when their elimination cannot be attained. High caps limit only the most catastrophic of claims and do the least damage to the Fund's mission, because they affect so few claimants. An acceptable dollar figure for an appropriate intermediate goal, short of doing away with all payment limitations, may vary considerably with jurisdictions' cost of living.

While it may not yet be attainable for many Funds to restore wealth to the wealthy, families of modest or average means should not face losing their homes for having trusted a lawyer. Therefore, an acceptable intermediate goal is to maintain the Fund's ability to save a middle-class family's home in the jurisdiction's economy.

Aggregate maximums are especially to be disfavored, there being little, if any, justification for disparate treatment of persons victimized by unusually prolific dishonest lawyers.

4.3 In the event awards must be made short of amounts otherwise compensable, the assignments taken by the Fund, under Standard 2.6 shall be limited to the amounts

paid by the Fund. Further, the Fund shall work with the claimants to pursue subrogation receipts, which shall be recovered for the benefit of claimants until all are made whole as to misappropriated principal, and then to the Fund to replenish awards made.

Commentary

Until the Fund reaches the goal of making all victims whole, the invoking of payment limitations raises an issue: Who collects first from subrogation receipts? Simply put, the claimants should, until made whole as to stolen principal, even if the Fund's efforts generate the recovery.

Where the source of the recovery is specific to one claimed transaction, that claimant should be made whole first out of the money recovered. Otherwise, claimants should share recoveries *pro rata* until all are made whole.

Then, the Fund should recover for the awards paid before claimants seek interest, consequential damages, lost opportunity, or other damages.

4.4 Claims should be decided, and compensable claims paid, as quickly as possible consistent with sound and just decision making, and in no event more than three months after claims are perfected. Claims are perfected when jurisdictional thresholds have been met and all reasonably obtainable proofs are received.

4.5 While a claimant has the burden of proving a claim's compensability, the Fund should not hesitate to use its subpoena power to expedite the perfection of a claim, without regard to whether the information obtained ultimately assists a claimant's position or that of the lawyer against whom the claim is filed.

4.6 The Board of Trustees should meet at least quarterly unless there is no claim or policy business requiring attention. If there is little or no claims activity, the Fund should examine whether it is adequately accessible. (See Standards 3.1 - 3.6, above.) While in-person meetings are to be favored, meetings may consist of teleconferences and mail ballots where appropriate.

4.7 Informal hearings should be held by the Fund where credibility is an issue, the claim presents novel issues, the facts remain unclear, or the claim is too close to decide on the papers.

4.8 Reimbursement checks should be issued as soon after approval of claims as is practicable, and in no event more than thirty days after receipt of papers assigning the successful claimants' rights to the Fund (Standard 2.6).

Commentary

A second aspect of a Fund's responsiveness to the need, beyond the amount paid, is the timeliness of payment. The ameliorative effects of a Fund award can be greatly and tragically diminished with the passage of time. Claimants typically have had a problem or a transaction of great significance before they ever approached the defalcating attorney; where an award is to be paid, the respondent has, by definition, greatly added to the claimant's problems.

While the most important goal is to make the best and most just decision possible for each claim, doing so as quickly as possible is a close second. As suggested in Standard 3.3, jurisdictional barriers should only be those that are necessary. Once those barriers have been hurdled, resolution of the claim should follow as quickly as facts will permit.

Clearly compensable claims should not languish for want of a meeting, even if 'meetings' must sometimes be by teleconference or mail ballot. Check-writing procedures should be streamlined to get relief into the hands of victimized clients. The Fund should have and use subpoena power where the claimants or respondents face difficulty in producing documentation. When needed, hearings should be conducted by the Board of Trustees after all reasonably available documentation has been produced. Hearings provide the Trustees an opportunity to consider the concerns of claimants and respondents in context and can help personalize the process to an appropriate extent.

4.9 A Fund is not a remedy of last resort, but claimants should be required to take reasonable steps to recover from wrongdoers or third parties to mitigate losses. The Fund should not hesitate to pay a claim and pursue a claimant's rights where such pursuit would place an undue burden or hardship on a claimant, or where it is in the Fund's own best interest to do so.

Commentary

Requirements such as the attaining of judgment against the respondent lawyer or full-fledged litigation against collateral sources in complex commercial matters are not to be favored. In some instances, such as where the respondent is known to be judgment proof, such a requirement is an empty formality for the claimant. Where claimants are incapable of such pursuit, requirements of this nature operate as the denial of remedy to the most vulnerable of such victims. Fund are best seen as remedies of last resort *vis-a-vis* collateral sources, not victimized clients. Furthermore, there are instances in which the Fund would be best served by controlling the litigation against a collateral source.

4.10 The Trustees should not utilize over-technical distinctions or harshly restrictive interpretations of the Fund's rules in an endeavor to deny or limit claims. The favored exercise of discretion is to seek opportunities to reimburse victims within the scope of the Fund's rules.

Commentary

It does not serve the public or the profession if Trustees utilize their discretion so as to deny

claims in order to conserve Fund assets. Trustees' fiduciary duties to maintain the fiscal integrity of the Fund are not properly carried out by avoiding the Fund's principal goal and reason for existence, that is, taking care of clients victimized by dishonest lawyers. If a Fund is running out of money, it needs to increase revenues (Standard 2.1) and limit losses (Standard 2.7) rather than reject claims for reasons incomprehensible to the average claimant and contrary to the philosophy of the Fund.

Assessment of Compensation Fund against ANCPO standards for evaluating lawyers Funds for client protection

1. Structure/Organisation

1.1 The Fund should be an entity of the jurisdiction's highest court as an exercise of the Court's power and duty to regulate the practice of law.

Whilst the Compensation Fund is not an entity of the court it is set up by statute. The actual circumstances in which payment may or may not be made are set out in 2009 Rules made by the SRA Board with the concurrence of the Master of the Rolls and the Lord Chancellor.

1.2 The Fund should be created and maintained by court rule with enabling statute only where necessary under the jurisdiction's constitution.

The Fund has been set up by Act of Parliament and is governed by statute and prescribed Rules. The regulation of lawyers is covered by the Legal Services Act 2007 under which the Legal Services Board oversees the work of the regulators of the legal profession, including the Solicitors Regulation Authority. The Solicitors Act, as amended, provides for the SRA to establish and maintain a Compensation Fund in order to pay compensation for loss caused by an act or omission of a solicitor (or employee) or by virtue of an intervention (practice monies being vested in the SRA).

1.3 The Fund shall constitute a trust separate and independent from any other fund or entity of the Court, bar association, law society or government agency.

Clearly this does not effect the separation that ANCPO propose.

1.4 The Court should appoint to the Fund's Board of Trustees only those individuals who have demonstrated a combination of achievement, professionalism and concern for the public. Diversity of background should also be a factor in Trustee selection, including members who are not lawyers.

The Society is the trustee so there is no selection or appointment process.

1.5 The Fund's Trustees should have sole discretion to decide claims, make awards and determine the Fund's procedures and policies within the court rule.

Decisions on claims are made by Delegated Adjudicators for smaller claims and for larger claims by an Adjudication Panel. Panel members are appointed on merit and having demonstrated high achievement in their field of expertise and come from diverse backgrounds. The Panels make up includes both solicitors and lay members and they have absolute discretion to decide on claims made upon the Fund. They have independence of decision making which cannot be interfered with by any other entity; the only means of challenge is by way of Judicial Review through the higher courts. The Fund

can reconsider applications on new evidence and there is also an appeals process (from March) against refusal of a claim.

1.6 To manage the Fund's daily affairs, the Trustees should employ a staff sufficient to permit them to (a) render the most just and timely decisions attainable in all matters, and (b) efficiently implement their decisions. The staff should serve at the pleasure of the Board.

Applications on the Fund are dealt with by suitably qualified staff, some with many years experience. All staff are trained upon appointment and thereafter trained and supported by experienced staff to enable them to deal with applications commensurate to their abilities. The more complex files are allocated to the most experienced members of staff. All staff have set performance targets for throughput of work depending upon the complexity of the claim and also as to quality, so that staff have optimum case holding and investigations are conducted in a fair and timely manner.

1.7 Staff salaries and all other obligations of the Fund should be paid or reimbursed by the Fund out of its income and assets to maintain the Fund's independence.

The staff costs are met by the Fund and the Act specifically provides for the application of the Fund, in addition to the payment of compensation, towards the costs and expenses of administration.

2. Funding

2.1 The Fund must have a source of income that is steady, secure and adequate to meet its standards of accessibility and responsiveness.

The Law Society is empowered to collect contributions to the Fund from the profession and decides the amount and times for payment. Contributions are collected on an annual basis.

2.2 Primary funding should be by regular, periodic assessment of lawyers. The assessment should be conducted by authority of the Court, with appropriate sanctions for non-compliance.

The SRA carries out an assessment of the contribution requirement for the forthcoming year based on the anticipated level of claims and the level of reserves held in the Fund. Recommendations are made to the Council. The Council sets contribution rates.

2.3 All, or nearly all, licensed members of the profession should pay into the Fund.

The Fund is currently maintained by annual contributions made by practising solicitors, register European lawyers, registered foreign lawyers and recognised bodies all of whom have to contribute with limited exceptions e.g. CPS and newly qualified.

2.4 The assessment should not be halted, suspended, or reduced because the Fund has a positive balance. To the contrary, a substantial reserve

should be sought, as interest income will help the Fund meet the need in times of large or numerous claims.

Whilst contributions have in the past varied markedly from year to year, an annual contribution of some sort has always been collected.

2.5 There should be no cap on the Fund's reserve short of self-endowment with full reimbursement of victims.

In this context "self endowed" means fully able to meet all obligations without the infusion of fresh capital. There is no cap on the Fund's reserve but there is to be a target level of reserve (see Chapter 2 of the report).

2.6 The Fund should take an assignment of each successful claimant's rights and, within sound business judgement, pursue those rights in vigorous attempts to replenish the Fund with subrogation receipts.

Claimants are specifically required to assign the right to recover the loss from the solicitor, to the Fund, up to the value of any grant paid and the SRA will pursue the solicitor for any shortfall where it is feasible to do so.

2.7 The Fund should seek implementation of appropriate loss prevention mechanisms. Among those that should be sought are trust account overdraft notification, minimum financial recordkeeping, random audits of trust accounts, insurance payee notification, and education of the bar and the public. Lawyer assistance and practice assistance programs should be encouraged and assisted in making their services known.

This work is carried out elsewhere in the SRA rather than by the Compensation Fund.

3. <u>Accessibility</u>

3.1 The Fund should make every reasonable effort to make its existence, nature and purpose known to the bar and the public. In particular, the Fund should ensure that those most likely to be approached by victims of dishonest lawyers – such as prosecutors, ethics committee counsel and members, ombudsmen, receivers/custodians, bar associations and judges – understand the Fund and the importance of appropriate and timely referrals. Similarly, copies of claims should be provided to respondents whose whereabouts are known, with invitations to respond.

The Fund has been established since 1942 and its existence is therefore well known to those in the legal profession. Almost all the claims on the Fund result from an intervention and the SRA's intervention agents are required to inform the clients of the intervened firm as to how and when to make a claim on the Fund. In a particular intervention, with a large and vulnerable client base, representatives from the Fund attended a public meeting held in the town where the solicitor had practised, to deal with any concerns that prospective claimants had, with respect to the intervention and compensation for loss suffered. The SRA's website which contains detailed information about the Fund, circumstances in which a payment may and may not be made, procedure, evidence required etc.

3.2 The Fund should issue and publish an annual report. Quarterly or semi-annual news releases should be done as well, even in the absence of high volume activity.

The Fund does not produce a stand alone report but it is included in the Law Society's annual report and accounts. Completion of the review of the provision of information to stakeholders is a future action point.

3.3 Ineligibility for classes of persons to qualify as claimants, like any limitation on the Trustees' discretions, is not to be favoured.

There is no restriction on the persons who may apply to the Fund i.e. whether it is lay client, corporate bodies, financial institutions or even the defaulter's partner.

3.4 Strict scrutiny in light of the Fund's purpose and mission should be applied to any suggested barriers to the Trustees' consideration of claims on their merits.

This would be done if the need ever arose.

3.5 Claim forms and accompanying instructions should be in plain language and, where appropriate, available in other languages.

The application form and Funds literature sent to claimants is written in easy to understand language, without any legal jargon, and has been awarded the crystal mark by the Plain English Campaign.

3.6 Time limitations on the filing of claims should be reasonable. Trustees should have the authority, in their discretion, to relax the time limitations for good cause.

Claimants had 6 months from the date of loss to apply for compensation but this will be extended to 12 months as from 1 March 2009. The Adjudicators may extend the time limit if it is justified in the particular circumstances of the case.

3.7 The fund's rules should be supplemented with regulations and written procedures as needed.

There are documented procedures as to the process of claims within the Fund so that claims are dealt with in a consistent and even handed manner.

4. <u>Responsiveness to the need</u>

4.1 The ultimate goal of the Fund is to fully reimburse all clients victimized by the dishonest conduct of their lawyers in as timely a manner as possible.

The Fund seeks to compensate claimants where a solicitor has misappropriated or failed to account for their money and if through no fault of their own, to replace the money in full.

4.2 Limitations on the payment of awards – whether per claim, per claimant, per year or in the aggregate against any one lawyer – are not to be favoured. Every opportunity should be sought to eliminate such limitations on the Trustees' discretion to pay awards.

There is no limit as to the amount that may be paid out as against any solicitor or claimant as the Fund deals with applications, on a claim by claim basis, with a limit of £2 million per claim but extendable in exceptional cases.

4.3 In the event awards must be made short of amounts otherwise compensable, the assignments taken by the Fund, under Standard 2.6 shall be limited to the amounts paid by the Fund. Further, the Fund shall work with the claimants to pursue subrogation receipts, which shall be recovered for the benefit of claimants until all are made whole as to misappropriated principal, and then to the Fund to replenish awards made.

This would be the case if the situation ever arose.

4.4 Claims should be decided, and compensable claims paid, as quickly as possible consistent with sound and just decision making, and in no event more than three months after claims are perfected. Claims are perfected when jurisdictional thresholds have been met and all reasonably obtainable proofs are received.

There are specified targets for staff within which to complete an investigation. The time varies depending on the complexity of the matter. Upon conclusion of the investigation the claim is referred for adjudication. A decision is made within a matter of weeks, and no more than, a month.

4.5 While a claimant has the burden of proving a claim's compensability, the Fund should not hesitate to use its subpoena power to expedite the perfection of a claim, without regard to whether the information obtained ultimately assists a claimant's position or that of the lawyer against whom the claim is filed.

The onus is on the claimant top prove his claim, in practice the Fund will try and assist in obtaining the necessary evidence to support the claim and routinely does so for example where an application is made by a person who was not a client of the solicitor concerned. The SRA has power to obtain documents from the solicitor in relation to an investigation.

4.6 The Board of Trustees should meet at least quarterly unless there is no claim or policy business requiring attention. If there is little or no claims activity, the Fund should examine whether it is adequately accessible. (See standards 3.1 – 3.6 above). While in-person meetings are to be favoured, meetings may consist of teleconferences and mail ballots where appropriate.

This is on the assumption that the Board of Trustees are deciding claims which is not the case. The Council does not meet as a Board of Trustees.

4.7 Informal hearings should be held by the Fund where credibility is an issue, the claim presents novel issues, the facts remain unclear, or the claim is too close to decide on the papers.

Claims are investigated and decisions made on documentary evidence but where it proves to be particularly difficult in determining the facts staff may meet with the claimant and his/her representatives. The Adjudication Panel may in an exceptional case allow an oral hearing.

4.8 Reimbursement checks should be issued as soon after approval of claims as is practicable, and in no event more than thirty days after receipt of papers assigning the successful claimants' rights to the Fund (Standard 2.6).

Payment is made immediately after approval of a claim.

4.9 A Fund is not a remedy of last resort, but claimants should be required to take reasonable steps to recover from wrongdoers or third parties to mitigate losses. The Fund should not hesitate to pay a claim and pursue a claimant's rights where such pursuit would place an undue burden or hardship on a claimant, or where it is in the Fund's own best interest to do so.

The Rules provide for the payment of a grant before a claimant has exhausted other remedies but the Fund expects claimants, where it is reasonable to do so, to pursue other remedies first. The Fund does however make available 'Emergency Funding' to be utilised by the SRA's agent on the day of the intervention for urgent cases which meet set criteria.

4.10 The Trustees should not utilize over-technical distinctions or harshly restrictive interpretations of the Fund's rules in an endeavour to deny or limit claims. The favoured exercise of discretion is to seek opportunities to reimburse victims within the scope of the Fund's rules.

The Fund's literature makes clear that one of the purposes of the Fund is to protect the public interest and applications are dealt with this principle in mind.

Claims are considered by reference to the Funds Rules but, subject to certain exceptions, these may be waived where necessary in the particular case. Claimants who are unsuccessful on the Fund may nevertheless be reimbursed in full or part out of any practice monies received by the SRA upon intervention.