Solicitors Regulation Authority

SRA Compensation Arrangements Review

A snapshot of the current arrangements

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1 The SRA's Compensation Arrangements Review - an overview

1.1 The SRA and other legal services regulators[1] are required to have in place appropriate professional indemnity insurance and compensation arrangements. These arrangements are there to provide consumers of legal services with protection from financial loss because of dishonesty, failure to account, fraud and dishonesty.

1.2 The SRA operates a compensation fund to help people who have lost money as a result of a law firm's dishonesty or failure to account for money received.

1.3 In recent years there have been significant changes in the way the legal services sector operates and is regulated. These changes include the separation of the representative and regulatory functions of professional bodies (such as the Law Society and Bar Council) which are approved regulators under the Legal Services Act 2007 (LSA) and the liberalisation of legal services business structures permitting non-lawyer involvement in various forms.

With the variety of services provided by law firms, the users of legal services have also changed significantly with different needs.

1.4 The SRA, created by the Law Society, is an independent regulator applying an explicitly risk-based and outcomes-focused regulatory strategy to the regulation of legal services in the liberalised market. Over time, the SRA is reviewing how it carries out all of its work, to ensure that it is based on risk and focused on outcomes. This review will apply those principles for the first time to our compensation arrangements.

1.5 Our regulatory work reduces the overall level of financial risk posed to consumers. However, regulation does not seek to eliminate all risks to consumers and it is therefore, important to consider what arrangements there should be to provide redress as a response to certain risks.

1.6 The SRA, in its strategic plan for 2013-15[2], has committed "...*to develop the SRA's regulatory arrangements to deliver more proportionate and better targeted outcomes-focused regulation in the public interest*." This includes a fundamental review of the current compensation arrangements.

1.7 The SRA will consider the current arrangements and what risk-based, outcomes-focused arrangements might look like, not only as a means of protecting the consumers of legal services, but also from the perspective of the broader public interest. Our compensation arrangements need to be consistent, not only with the SRA's regulatory objectives[3] but also with other obligations placed upon SRA by the LSA, for example adherence to better regulation principles.

1.8 The scope of the review needs to be broad enough and the methodology rigorous enough to establish a compensation regime which:

[1] http://www.legislation.gov.uk/ukpga/2007/29/schedule/4/part/1

[2] http://www.sra.org.uk/sra/strategy.page

[3] http://www.legislation.gov.uk/ukpga/2007/29/section/1

- provides appropriate protection for consumers of legal services;
- is in accordance with regulatory principles;
- meets the SRA's regulatory objectives; and
- stands the test of time.

1.9 The issues which the review will need to encompass include:

- the purpose of compensation arrangements within a wider client protection regime and the form that they should take;
- whether the eligibility criteria for claimants is appropriate;
- how the regime should be funded;
- how administrative costs related to the compensation fund should be accounted for; and
- the effectiveness and efficiency of the current compensation arrangements as part of the current client protection regime.

The purpose of this paper

1.10 The purpose of this paper is to provide background information to inform those who wish to contribute to that review and to encourage the widest participation. The SRA will consult on any proposals in due course, but this paper seeks to contribute to a common understanding of the current situation.

1.11 This paper incorporates details of the SRA's current compensation arrangements and how the arrangements currently work. Further research into these elements will continue during the course of the review to help define final policy proposals. A high-level comparison of other jurisdictions and other professionals has been carried out and forms part of this information pack.

Looking ahead

1.12 The SRA currently expects to issue a consultation paper later in 2014 with any proposals for change to be implemented from 2015 onwards depending on the scale and complexity of the changes.

1.13 The SRA would be interested to hear the views of our stakeholders on these issues, and any other to help us to identify what works well and what does not work well, in respect of the current arrangements.

1.14 We hope that consumers and consumer bodies will participate in the review, given the significance of the arrangements to the interests of consumers of legal services. The

existing compensation arrangements are paid for by law firms. These are challenging times for many firms and it is essential that they also have the opportunity to contribute to the review.

1.15 The SRA would encourage stakeholders to engage with the review. Those who wish to share their views can contact us at: policy@sra.org.uk

2 The legal services market

2.1 This section provides an overview of the legal services market and the SRA's role in regulating legal services.

The legal services market

2.2 According to research published in January 2013[4], the UK legal services market was valued at £26.1 billion in 2012, with business to business purchases accounting for 89% of the total market value. The industry consists of nearly 30,000 companies, with around 83% of entities reported to be micro businesses employing fewer than 10 people. In revenue terms, the largest 3% of law firms generated 55% of revenue in 2012. Government statistics[5] indicate that the sector contributed £20.9 billion to the UK economy in 2011, £4bn of which derived from exports.

2.3 There are three distinct legal systems in the UK; England and Wales, Scotland and Northern Ireland, each with their own framework for the regulation of legal services.

2.4 In England & Wales, there are approximately 15,000 barristers, 160,000 solicitors on the Roll and 12,000 individuals in other professional categories. Members of the different professions are regulated by different bodies. Individual lawyers comply with the rules and standards set by the regulator of their particular profession.

2.5 The SRA regulates part of the legal services market in England and Wales.

2.6 Research conducted by the Law Society[6] indicates that the legal services market in England and Wales comprises between 267,000 and 320,000 regulated and unregulated individuals supplying legal services in around 30,000 entities, generating turnover of £25.6bn, or 1.48% of gross value added (gross value added is a measure of the value of goods and services produced in an area, industry or sector of an economy) (2010 figures). Solicitors represent the largest group within the market accounting for 38-46% of individuals, 44% of entities and 58% of total UK turnover (UK figures) but the role of non-solicitor and non-barristers is significant.

2.7 The legal market is however, in a period of significant change. Much of this is driven by individuals and firms, as they seek to improve quality and service standards, develop new markets and new ways of working and greater competitiveness. Similarly, new entrants are impacting on how services are delivered.

2.8 Much also is driven by changes in the environment within which firms operate. For example, as a result of the opportunities presented by the LSA or new technologies, or by the challenges presented to them, as a result of changes in the economy or by recent government policy on referral fees, personal injury claims, civil litigation funding or legal aid.

[4] http://www.companiesandmarkets.com/Market/Business-Services/Market-Research/Legal-Services-in-United-Kingdom-ISIC-7411/RPT1134244

[5] http://www.justice.gov.uk/downloads/publications/corporate-reports/MoJ/legal-services-action-plan-0313.pdf

[6] Law Society Market Assessment Report 2012

What legal services are regulated?

2.9 Not all legal services are regulated. The LSA distinguishes between reserved legal activities, which can only be undertaken by an authorised person, and other legal activities which can be offered by anyone.

2.10 There are six areas of reserved activity that can only be provided by an authorised person (a regulated lawyer, such as a solicitor):

1. the exercise of rights of audience (i.e. appearing as an advocate before a court);
2. the conduct of litigation (i.e. managing a case through its court processes);
3. reserved instrument activities (i.e. dealing with the transfer of land or property under specific legal provisions);
4. probate activities;
5. notarial activities (i.e. work governed by the Public Notaries Act 1801); and
6. the administration of oaths (i.e. taking oaths, swearing affidavits etc).

(Note: different classes of authorised persons are authorised to provide different combinations of the reserved activities.)

2.11 Legal activities that are not reserved include the provision of advice, assistance or representation in connection with the application of the law or the resolution of disputes determining the nature of a person's legal rights or liabilities. However, if an individual or entity is authorised to provide reserved legal activities by one of the legal services regulators, all of their legal activities may fall within the scope of regulation.

The SRA's role in regulating legal service providers

2.12 Since 1 January 2010, the Legal Services Board (LSB) has been responsible for overseeing the regulation of legal services in England and Wales.

2.13 The SRA is the independent regulatory body established by the Law Society for the regulation of legal services provided by law firms and solicitors in England & Wales. So solicitors are regulated by the SRA and have to comply with the provisions contained within the SRA Handbook.

2.14 The SRA's powers arise from various statutes and regulations including the Solicitors Act 1974, the Administration of Justice Act 1985, the Courts and Legal Services Act 1990, the Legal Services Act 2007 and the SRA Handbook.

2.15 The SRA regulates in the public interest and is determined to ensure that the public is able to access safe, ethical, good quality legal services that meet their needs. The SRA shares these core principles with the great majority of those we regulate. However, given the rapidly evolving nature of the legal services market, how the SRA regulates and what the SRA focuses its resources on at any point in time will evolve.

2.16 Since October 2011, the SRA has adopted a risk-based, outcomes-focused approach to regulation. Rather than trying to regulate the details of how firms run their business this is a regulatory regime that focuses on the high level principles and outcomes which drives the provision of high quality services to clients and which promotes the effective management of

a solicitor's business. This approach allows for the SRA to focus on issues which really matter and fosters an environment where law firms are required to take responsibility for managing risks in particular contexts whilst allowing flexibility in how they deliver services to their clients. In short, the SRA seeks compliance with outcomes rather than checking for compliance with detailed rules.

Who/what does the SRA regulate?

2.17 The SRA's purpose is to protect the public by ensuring that solicitors meet high standards and to taking action when risks to the public are identified. The SRA regulates solicitors' firms and bodies licensed under the LSA as well as the individuals employed within those entities, in the public interest.

2.18 The SRA authorises individuals and firms to provide the reserved legal activities defined by the LSA, excluding notarial activities. The SRA is the largest of the approved regulators in England and Wales. The SRA regulates 128,169 practising solicitors, 4,653 other lawyers and 10,827 entities and their employees and managers[7]. The total number of solicitors on the roll (the record of individuals who are qualified, but not necessarily practising) at the end of February 2013 was 164,998. The SRA regulates Solicitors, Registered European Lawyers (RELs) and Registered Foreign Lawyers (RFLs).

2.19 The SRA also regulate solicitors' firms. Firms may will take the form of a:

- sole practitioner;
- recognised body; or
- licensed body (Alternative Business Structures (ABSs)).

Recognised and licensed bodies are commonly referred to as authorised bodies and may take the form of partnerships, limited liability partnerships or limited companies.

2.20 The SRA regulates the managers, owners and employees of the firms regulated, even if those individuals are not themselves lawyers.

2.21 The Law Society's sector analysis of firms regulated by the SRA identifies the 200 firms with the largest turnover as 'large firms'. These firms make up just under 2 per cent of all SRA regulated entities and generate fee income of more than £11.5million per annum. Large firms employ over two-fifths of all solicitors in private practice and generate two-thirds of total fee income. Nearly half of the income generated in England & Wales by large firms comes from business and commercial work for listed and non-listed companies. However, there is a great variety in the specialism of this group, which includes some of the leading personal injury firms and some that provide private client services to 'retail' consumers and High Net Worth Private Individuals (HNWPI), including wills and probate, tax and trusts.

2.22 For the remaining 98 percent of firms (known as 'small and medium' sized firms) work from private individuals accounted for approximately 50 per cent of total turnover and 56 per cent of their client base in 2011. Small and medium sized firms dominate in the provision of the most common 'retail' services: conveyancing, family, probate, wills, personal injury,

[7] SRA *Regulated population statistics*, accessed 22 March 2013. http://www.sra.org.uk/sra/how-we-work/reports/statistics/regulated-community-statistics.page

immigration, employment and crime. These firms are more likely to have experienced decreases in fee income over the past three years than the top 200 firms.

3 What are the risks to consumers' financial interests?

3.1 There are two main types of financial risk to consumers of legal services:

- risks associated with the delivery of legal services; and
- risks which result from a firm's ability to hold money and assets on behalf of clients.

Risks associated with the delivery of legal services

3.2 The delivery of legal services is often of significant value for the consumer. If clients receive a poor service or are charged excessive fees, this can lead to financial loss and a potential claim against the law firm.

3.3 Clients may also suffer loss if a firm is unable to complete work that has been paid for. This situation may arise if a firm becomes insolvent, or if the SRA's regulatory action means a firm cannot continue practising. When the continuity of providing legal services is disrupted in this way, clients may incur further costs due to procedural delays and/or the need to engage another firm to take on the work.

3.4 Losses arising from this risk are largely a matter for the Legal Ombudsman service and may also result in a claim being made on against the law firm's professional indemnity insurance. The role of the Legal Ombudsman and professional indemnity insurance as a means of client protection are discussed later in this paper.

Risks relating to the holding of client money

3.5 Firms regulated by the SRA handle large sums of money belonging to their clients, for example, in property transactions, damages received in personal injury matters, or when administering the estate of someone who has died.

3.6 The SRA Accounts Rules 2011 require all firms to keep client money separate from their own money.

3.7 The risk arising from firms holding client money include that it may be misused or stolen by someone in the firm or paid to the wrong client (usually to cover a previous misuse). Misuse of client money occurs when a firm or individual within it uses money from one client's account for the benefit of another, whether dishonestly or incompetently. Misappropriation involves the dishonest appropriation of client money by a firm or individual within it.

3.8 Where the risk does arise, the impact can be considerable. To take an example, the client accounts of intervened conveyancing firm Wolstenholmes LLP to 31 October 2009 revealed a shortfall of £19,878,466.84 after the SRA had intervened to close the firm.

3.9 Research shows that on average 1.1% of regulated firms had findings against them for matters relating to the misuse and misappropriation of client money, between 2007 and 2012. However, when this happens, consumers can suffer considerable impact. In the case

of Wolstenholmes LLP, clients were left in great uncertainty about the money the firm held for their house purchases. To date (June 2013), the net liability to the Compensation Fund, in respect of claims dealt with by the SRA following the closure of Wolstenholmes LLP is £7.66m.

3.10 Where misuse or misappropriation does occur, the most common driver is financial difficulty, either for a firm or for an individual at a firm. This will lead to misconduct or worse and often inadequate controls of client money leading to chaos or failure to prevent misappropriation.

3.11 In the current economic environment, there is a increased risk of misuse of client money by firms in financial difficulty. Therefore, there remains the risk of significant default of a common nature such as theft of conveyancing and probate funds and other situations where large sums of client money are held.

3.12 Where there are inadequate controls in a firm, which can range from automated accounting systems to poor cultural attitudes and inadequate training, the risk of client money being stolen or not accounted for becomes more likely to crystallise. In financial institutions, poor controls have been blamed for large scale misappropriation or misuse of funds. For example, at Barings Bank, the fact that Nick Leeson both led the trading desk and had control over the back office, meant he had "*ample opportunity to falsify the reporting aspect of the business and bypass critical regulatory and compliance requirements*"[8]. An absence of vetting procedures for staff or security clearance checks can also enable dishonest individuals to join a business. Other examples of poor controls include allowing unsuitable employees to have authorisation to transfer client monies, or failure to have accounts regularly reconciled.

3.13 A combination of financial difficulty (or other motive for theft) for a dishonest firm or individual, combined with inadequate systems and controls, creates the environment where misuse or misappropriation of client money can arise.

3.14 The temptation to misuse or misappropriate exists in any firm holding client money. Where large sums are held, the potential impact is higher. As such, conveyancing and probate firms are at a heightened risk for dishonest misuse and misappropriation of client funds, due simply to the scale of the money held. In law firms, funds are held for many different clients, and thus money missing from one client's account may be concealed by moving money from another client. With careful juggling of funds between accounts, it is possible for losses to be hidden for a considerable time.

3.15 Incompetent misuse represents a lesser risk than direct misappropriation, but it is still a risk. Fraud is easier if accounting systems in a firm are confusing and if financial managers do not have the skills to run their firm properly. Such inadequacies in management skills may well not be confined to accounting.

3.16 All such activity is entirely contrary to Rule 1 of the SRA Accounts Rules 2011 and represents serious dishonesty.

3.17 The primary impact of misuse and misappropriation of client money is upon those clients whose money has been misused. This can crystallise as an actual loss of money, requiring remedy from the Compensation Fund. It can also result in a delay in completion of a property or probate transaction as the solicitor seeks to cover a shortfall on one account by

[8] http://compliance.knowledgeplatform.com/Files/Attachments/651c5f93-c961-447a-9107-017e7d343b372004_TRRF_Barings%20case%20study.pdf

borrowing from others in an ongoing chain. Inevitably, these issues give cause for the SRA to intervene into a firm.

4 How does the SRA manage these risks?

4.1 The SRA manages financial risks to consumers by setting regulatory standards, supervising firms' in a proactive and risk-based way and by deterring misconduct. Supervision encourages firms to deal with their own risks, thus ensuring they provide the right outcomes for clients in line with the mandatory outcomes in the Handbook. The SRA achieves this by means of risk-based supervision, including constructive engagement with those firms willing and able to engage constructively with the SRA.

4.2 The SRA will take enforcement action if there is serious misconduct if there is a risk to the public which cannot be mitigated by working with the firm, or
the firm in question does not engage with the SRA so that the matter can be addressed by way of the Supervision approach and formal investigation is required.

4.3 Further details about how the SRA regulates can be found on the SRA's website[9].

Outcomes-focused regulation

4.4 The outcomes-focused approach to regulation means that our goal is to ensure that legal services providers deliver positive outcomes for consumers of legal services and the public, in line with the intent of the LSA regulatory objectives. This is in contrast to our historical rules-based approach: the SRA no longer focuses on prescribing how those regulated by the SRA provide services, but instead focuses on the outcomes for the public and consumers that result from the activities of those legal services providers.

4.5 The SRA defines desired regulatory outcomes by identifying what it expects to observe when legal services providers engage in providing services to clients in line with the intent of the regulatory objectives. This process provides us with a practical articulation of the characteristics or results that the SRA should be seeking to achieve through our regulation.

4.6 By adopting an outcomes-focused approach, we are able to encourage innovation within the market, regulating a broader range of business structures which bring new approaches to the provision of legal services, as well as providing greater freedom to those we already regulate.

4.7 As an outcomes-focused regulator we evaluate the impact of our regulatory activity on firms, consumers of legal services and the public and adapt our approach to continuously improve our delivery.

Risk-based regulation

4.8 Day-to-day regulatory activities are guided by a risk-based approach to regulation, focusing attention and activity on issues, firms and potential risks that pose the greatest threat to the objectives. In order to achieve this, the SRA needs:

[9] http://www.sra.org.uk/consumers/sra-regulate/sra-regulate.page

- a clear view on what the risks are to the objectives and our exposure to them;
- to be able to demonstrate where our most significant risks lie, what mitigation activities we are taking to address them, and that these actions are both proportionate and effective; and
- clear governance arrangements in place ensuring that risks are escalated as appropriate and that there is accountability for the effective management of risk.

4.9 These requirements shape the SRA's approach to every area of regulatory activity, for example authorising individuals joining the profession, supervising firms, enforcement activities and the setting of policies and standards.

4.10 Risk-based regulation enables us to consistently and proportionately target resources at those areas which pose an unacceptable threat to the outcomes we have identified in relation to the regulatory objectives.

4.11 The SRA's regulatory risk appetite describes the attitude towards risk, including those which will be tolerated or acceptable and the level at which risks become unacceptable. Some areas that may historically have attracted attention under the SRA's prescriptive rules-based approach may now be within the SRA's appetite for regulatory risk, allowing the SRA to divert resources to focus on more serious matters, and move from being reactive to being proactive in approach.

4.12 The SRA does not seek to eliminate risk completely, but to make the best use of its limited resources to proactively reduce the risks posed to an acceptable level. The SRA will also take an explicitly non-zero failure approach to regulation, meaning that it does not seek to prevent every harm from occurring, choosing instead to allow greater flexibility for the market to operate freely as far as risks remain within tolerable levels. In the course of letting the market operate freely, risks will crystallise that fall both within and outside our tolerance and we will respond accordingly.

4.13 Regulatory activity consists of both proactive and reactive controls that can be applied according to the nature, severity and immediacy of the risk or issue posed.

4.14 The SRA's powers and regulatory tools include, but are not limited to:

- controls on how a firm or individual practises;
- issuing a warning about future conduct;
- closing a firm with immediate effect or imposing a disciplinary sanction, such as a fine;
- informing the market about undesirable trends and risks;
- adapting regulatory policy to minimise recurrence of an issue;
- setting qualification standards and ongoing competency requirements.

4.15 The SRA is conscious that regulatory activities cost money - directly in the costs of the SRA, by imposing costs directly on firms, through the cost of compliance with SRA requirements and the costs which follow through restricting commercial or competitive activities and choices.

4.16 The risk-based approach enables the SRA to be flexible and adaptive to ongoing changes within the market. As new risks to objectives are identified, the SRA will learn more about them and adjust it's priorities to direct resources where they are most needed.

4.17 It should be noted that the SRA makes a distinction between operational and regulatory risk. Operational risks generated by the SRA's activities, including our activities to control regulatory risks, are identified and assessed separately to the regulatory risks caused by the market that we regulate and other external factors.

Standards to protect consumers' financial interests

4.18 The SRA Handbook contains ten principles ('the SRA Principles'[10]) that define the fundamental ethical and professional standards that all firms and individuals should meet when providing legal services. All of the Principles underpin the effective delivery of legal services. Those which are particularly relevant to the holding of client money are that the regulated community must protect client money and assets (Principle 10) and act with integrity (Principle 2).

4.19 The SRA Code of Conduct 2011 also requires the achievement of regulatory outcomes which are designed to ensure clients are provided with sufficient information and that firms have in place maintain systems and controls for monitoring the financial stability of the firm and risks to money and assets entrusted to the firm by clients.

4.20 The SRA Accounts Rules 2011 contain provisions to ensure that money held for clients or third parties is held safely and securely. Compliance with the SRA Accounts Rules should ensure are that:

- client money is safe;
- clients and the public have confidence that client money held by firms will be safe;
- firms are managed in such a way, and with appropriate systems and procedures in place, so as to safeguard client money;
- client accounts are used for appropriate purposes only; and
- the SRA is aware of issues in a firm relevant to the protection of client money.

4.21 The purpose of the SRA Accounts Rules is to keep client money safe by:

- keeping it separate from the firm's own money;
- protecting against dishonesty by firms and their employees;
- preventing the firm's accounts from becoming muddled and unclear.

4.22 The rules apply to all law firms regulated by the SRA when they handle client money, with very few exceptions:

- ABS can provide a range of services, not all of which are regulated by the SRA. The SRA Accounts Rules only apply in respect of activities that are regulated by the SRA. Money received in relation to the ABS' other activities is called 'out-of-scope' money.
- A solicitor practising as a manager or employee in a firm regulated by another approved regulator is subject to the rules of that regulator. However, if the solicitor receives any money in connection with work which is outside the scope of the authorisation granted by the other regulator, the funds would fall within the scope of the SRA Accounts Rules.

[10] http://www.sra.org.uk/solicitors/handbook/handbookprinciples/content.page

4.23 The SRA Accounts Rules are more prescriptive than other parts of the Handbook because the risk and impact of impropriety on consumers and others is high.

4.24 The client account must not be used simply as a banking facility; there must be an underlying transaction or service which is part of the firm's normal regulated activities.

Enforcement

4.25 Enforcement is only one of the SRA's regulatory tools. As a risk-based regulator, the SRA must target resources at areas which we think pose the main threats to the public. Whilst the SRA takes a proportionate approach, it is recognised that it is also important to avoid minimal compliance and assumptions that detailed obligations do not matter. They do matter - and where necessary they will be subject to enforcement action or will be noted for future action if necessary.

4.26 The SRA takes robust action against those who do not meet proper standards and who put members of the public at risk. Enforcement action deters the individual who is subject to action and provides a wider deterrent to misconduct by others.

4.27 Enforcement action can involve financial penalties, controls on how someone practises, strike off by the Solicitors Disciplinary Tribunal, or intervening into a law firm.

When can the SRA intervene?

4.28 The SRA can effectively close down a law firm by deciding to "intervene". The powers exist in order to protect the public, whether they are exercised on the grounds of suspected dishonesty, breaches of the SRA Accounts Rules or a breach of the Code of Conduct. The powers enable the SRA to step in, for example, to prevent escalation of default, including where some other regulatory breach is the basis of the exercise of the powers.

4.29 The SRA's primary objective when engaging with firms is at all times to ensure that clients are protected and to avoid intervention unless absolutely necessary. Intervention will usually be the last resort in such cases but will often be necessary more urgently in other situations such as to avoid risk to the public arising from the activities of a practitioner suspected to be dishonest or continuing risk to clients arising from a client account shortage.

4.30 The power to intervene is a regulatory tool available to the SRA. A decision to intervene will only be made where one of the grounds set out in legislation have been met and it is necessary to intervene in order to protect the public interest.

4.31 Intervention involves taking control of all documents and money the firm was holding.

4.32 Some of the circumstances giving rise to intervention are[11]:

- reason to suspect dishonesty by the solicitor
- breaches of our Rules
- bankruptcy or insolvency

[11] http://www.sra.org.uk/consumers/problems/solicitor-closed-down/intervention.page.

- the firm is abandoned; or
- under a general power to intervene to protect the interests of clients or former clients.

4.33 The effects of an intervention are very specific. It is not a takeover of a firm and neither is it a disciplinary outcome. It is a regulatory step taken to protect client interests and money.

4.34 Once a decision to intervene is made, the practice, in effect, ceases to exist and the solicitors whose practices have been intervened are personally liable for the costs of the intervention.

4.35 The practice monies will vest in the SRA, to be held on trust for those who are beneficially entitled and the practice documents will be taken into the SRA's possession to enable the SRA to distribute the files where necessary. If clients do not request their files then they will be stored by SRA.

4.36 Paragraph 13 of Schedule 1 to the Solicitors Act 1974 provides that the intervened solicitor is liable for the costs of the intervention. Such costs are recoverable as a debt.

4.37 The intervened solicitor remains able to raise bills and pursue outstanding costs due to the intervened firm (Kevin Dooley -v- The Law Society (2000)). Only the solicitor can do this because the SRA has no such power. Nevertheless, money recovered vests in the SRA and is used to offset the solicitor’s debt to us.

4.38 An intervention will have the effect of applications being made to the Compensation Fund by clients who have not had monies correctly accounted to them and possibly, where the solicitor has been dishonest.

5 How does the SRA protect consumers when firms fail to meet the necessary standards?

5.1 Regulatory action (supervision and enforcement) does not provide redress to individual consumers who have suffered loss.

5.2 Financial protection is afforded through a combination of three arrangements:

- the Compensation Fund;
- awards made by the Legal Ombudsman; and
- compulsory professional indemnity insurance.

The Compensation Fund

5.3 The Compensation Fund was set up following the Solicitors Act 1941. The Fund was continued, in modified terms, by the 1974 Act. As originally enacted, the 1974 Act authorised the Law Society to levy, in addition to the fee payable for a practising certificate, an annual contribution and, for those who held or received client monies, an additional "special levy": The provisions expressly authorised the Law Society to invest, borrow and insure.

5.4 The Legal Services Act 2007 made two important changes. It amended the 1974 Act, replacing s. 36 and Sch. 2 with new sections 36 and 36A. Section 36A contains express powers for the Law Society to require solicitors to make contributions, to invest fund monies, to insure, to borrow and to charge investments as security.

5.5 Secondly, and separately, it established a new regulatory framework for ABSs, which are required to be licensed by a licensing authority. Licensing rules of a licensing authority are required by s. 85(3)(e) to contain "appropriate compensation arrangements". (The Law Society (which acts through its independent regulatory body, the SRA) is named as a licensing authority.)

5.6 The LSA defines compensation arrangements as "...*arrangements to provide for grants or other payments for the purposes of relieving or mitigating losses or hardship suffered by persons in consequence of —*

(a) negligence or fraud or other dishonesty on the part of any persons whom the body has authorised to carry on activities which constitute a reserved legal activity, or of employees of theirs, in connection with their activities as such authorised persons, and

(b) failure, on the part of regulated persons, to account for money received by them in connection with their activities as such regulated persons..."

5.7 The basis on which the Fund paid grants was embedded in the Solicitors Act 1974 but the LSA provided greater flexibility by removing detail and leaving it to be provided by rules made by the SRA. The current rules tend to reflect the position as it was in the Solicitors Act 1974 but it is important to bear in mind that it is not necessary for them to do so.

5.8 The SRA's Compensation Fund is a discretionary fund - a fund of last resort and therefore, the Fund's current stated aim is to replace money which has been misappropriated or not accounted for by a defaulting practitioner. Payment is unlikely to made from the Fund where an individual can be, or has been, indemnified against loss through other means.

5.9 A defaulting practitioner is defined (SRA Compensation Fund Rules 2011) as the person in respect of whose act or default a claim to the Fund is made. It includes:

- a solicitor or their employee;
- a registered European lawyer or their employee;
- a recognised body, or its managers or employees;
- a registered foreign lawyer who is a manager of a partnership, limited liability partnership or company together with a solicitor,
- a registered European lawyer; and
- a licensed body or its owners, managers or employees.

5.10 If the manager or employee of a recognised body is authorised by one of the other approved regulators, not by the SRA, the SRA has a discretion to consider a claim in respect of that individual's act or default[12]. However, if the other approved regulator has its own client protection fund, it is likely that the applicant would be directed to raise their claim with the other approved regulator's scheme in the first instance.

5.11 The Fund can also provide compensation for the civil liability of a defaulting practitioner who was uninsured.

Grants which may be paid from the Fund

5.12 For a grant to be made out of the Fund, an applicant must currently satisfy the SRA that:

- they have suffered loss because of the dishonesty of a defaulting practitioner, or
- they have suffered loss and hardship due to the failure of a defaulting practitioner to account for money they have received.

The applicant does not need to be a client or a former client of the firm.

5.13 In respect of uninsured firms, an applicant must satisfy the SRA that they have suffered loss as a result of the civil liability of the defaulting practitioner who should have had, but did not have, in place a policy of qualifying insurance against which a claim could be made.

5.14 Details of how an application can be made to the Compensation Fund are available on the SRA website[13].

Eligibility of claimant

[12] SRA Compensation Fund Rules 2011, rule 10.3

[13] http://www.sra.org.uk/consumers/problems/solicitor-owes-money.page

5.15 There is no restriction on who can apply for and be paid a grant out of the Fund. Anyone can make an application free of charge. They do not have to be the clients of the closed firm. A claim can be made by an individual consumer, company, charity or other entity and irrespective of the wealth and means of the applicant.

5.16 The highest claims by value come from lenders: banks and building societies, who will have released mortgage monies to a solicitor in a conveyancing transaction.

5.17 An applicant who can show that he or she has suffered loss as a result of failure to account for money is deemed to have suffered hardship if he or she is an individual whose dealings with the defaulting practitioner have been in a personal capacity. If the applicant's dealings with the defaulting practitioner have been in a business capacity they must provide evidence to show that the body or individual has suffered or is likely to suffer hardship.

5.18 If the applicant has suffered loss because of the firm or individual's dishonesty there is no 'hardship test ' to satisfy.

Losses arising in the course of activities that are regulated by the SRA

5.19 The Compensation Fund can only make payments in respect of losses that happened during the normal work of a law firm regulated by the SRA.

5.20 The Compensation Fund can only consider an application if the loss in question happened *"in the course of an activity of a kind which is part of the usual business of a defaulting practitioner."* Not all activities that a regulated person undertakes will satisfy this criteria. For example, it is not part of a solicitor's usual business to offer loans. Those who enter into commercial agreements with regulated individuals do so at their own risk and are not entitled to protection from the Compensation Fund.

5.21 ABS are authorised to undertake reserved legal activities, alongside other types of legal work, such as giving general legal advice, resolving legal disputes or representing clients in connection with the application of the law. The Compensation Fund protects consumers against losses that happen in the course of these activities, known as 'regulated activities.' Not everything an ABS does is regulated by the SRA or protected by the Compensation Fund. For example, if an ABS gives clients advice about how to invest their money, it is not carrying out a legal activity and any losses will not be covered by the Compensation Fund.

Burden of proof

5.22 It is for the applicant to prove his or her claim and if he or she is able to satisfy the SRA that his or her claim meets the criteria set out above, the SRA will have a discretion to make a grant out of the Compensation Fund. No individual is entitled to a grant as of right. If a payment is made a further grant may be made for interest and costs.

Interest

5.23 The SRA can make a supplementary grant by way of a sum in lieu of lost interest on a principal grant at rates prescribed by the SRA. As the grant is a gift it is not subject to tax in the hands of the recipient. Where the application 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.

Costs

5.24 The SRA may pay a further grant in respect of the reasonable costs properly incurred by the applicant with either his or her solicitor or other professional adviser, provided that such costs were incurred wholly, necessarily and exclusively in connection with the application.

5.25 Furthermore, if the defaulting practitioner did not complete the work for which he or she was paid, he or she will be deemed to have failed to account and the SRA may pay or contribute towards the payment of the additional reasonable legal costs in completing the outstanding work.

What is not covered

5.26 Except for applications made on the basis of an uninsured defaulting practitioner, the SRA will not make a grant in respect of the following[14]:

- losses arising solely by reason of professional negligence;
- personal debts of a defaulting practitioner which would not otherwise give rise to a claim on the Fund.
- losses that result from, but do not form part of, any misappropriation of, or failure to account for, money or money's worth.
- trading debts or liabilities of the defaulting practitioner;
- claims for contractually agreed interest between the applicant and the ; defaulting practitioner;
- 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.
- the application was received out of time, or not submitted in the correct form.

Time limits

5.27 Claims on the Compensation Fund must be made 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 can extend this period if we are satisfied that there are circumstances which justify the extension of the time limit.

Exhausting other remedies[15]

5.28 The SRA may refuse or limit a grant where the loss, or part of the loss, is an insured risk or one which could be made good by some other means. However, the Rules also state that at the absolute discretion of the SRA a grant may be made before requiring the applicant to

[14] Compensation Fund Rules 2011, rule 8.

[15] Compensation Fund Rules 2011, rule 13.

resort to other means of recovery. This gives the SRA scope to make a grant where that would be in the public interest. A particular example of this is the provision of Emergency Funding (discussed below).

5.29 The Fund is a discretionary fund and in the past it was referred to as a fund of "last resort". This implied that before making any grant the SRA would require applicants to exhaust other civil remedies. However, the Compensation Fund Rules were reviewed and updated in March 2009 to reflect the fact that in many ways, the Fund often acted as fund of "first resort" in order to best protect the public interest.

5.30 The SRA may also require the applicant to take certain steps before deciding whether to make a grant, such as:

- pursuing any civil remedy which may be available to the applicant;
- commencing insolvency proceedings;
- making a formal complaint to the police in respect of any dishonesty on the part of the regulated individual/firm; and
- assisting the SRA in taking action against the regulated individual/firm.

Contribution to the loss

5.31 No person has an automatic right to a grant. A grant is made wholly at the discretion of the SRA who may in exercising its discretion take into account factors such any contribution to the loss being claimed from the Fund.

5.31 The SRA may reduce or reject grants, if an applicant has contributed to the loss as a result of his, her or its activities, omissions or behaviour.

5.32 If the loss results from the combined activities of more than one party (e.g. a solicitor conspires with a surveyor to conduct mortgage fraud), the SRA will consider the role each played in causing the loss and assess the portion of the loss primarily attributable to the acts of the defaulting practitioner and other factors[16]. If the loss was primarily due to other factors, the SRA may reject an application or make a grant on a pro-rata basis depending on each contributing factor to the loss.

5.33 In respect of ABS firms, it may not always be simple to identify whether a loss occurred due to an act or default in the course of performance of an activity that is regulated by the SRA, or due to other factors. In these circumstances the SRA assesses the extent (if any) to which the loss is attributable to behaviour that took place in the performance of a regulated activity.

Maximum grant

5.34 The maximum grant that may be made is £2million[17], although the SRA may waive this provision at its discretion[18].

[16] Compensation Fund Rules 2011, rule 10

[17] Compensation Fund Rules 2011, rule 17.

[18] Compensation Fund Rules 2011, rule 24.

Emergency funding

5.35 The provision of emergency funding by the Compensation Fund in the course of interventions provides urgent public protection for consumers who may have suffered loss.

5.36 The SRA provides emergency funding to enable urgent cases to be fast tracked, perhaps because clients have to complete buying of a house and would be in breach of contract if they were unable to do so. Applications are considered on a priority basis and, depending upon value, usually adjudicated by authorised officers on the day of the intervention or on day of receipt of the claim if received afterwards.

Statutory Trust Accounts

5.37 When the SRA intervenes, it becomes the legal owner of practice money and holds papers for safe-keeping.

5.38 The SRA proactively seeks out and invites claims from potential beneficiaries. Client money is held on a statutory trust account, for the benefit of those entitled to it. As a consequence payments out cannot be made until all beneficial entitlements to the money are established.

5.39 The SRA reconciles and verifies the accounts, considers whether any funds are missing and investigates how to properly distribute the remaining sums to the correct beneficiaries. The Intervention Powers (Statutory Trust) Rules 2011 sets out how this is done.

5.40 Tracking a client is no easy task and it can take, in some cases, a number of years before any payments are made. It inevitably takes time from the intervention to check and decide to whom money should properly be paid. Former clients may be able to claim on the Compensation Fund in the meantime. Also, if the money held is not enough to pay all the claims in full, funds can be shared out on a pro rata basis with those affected being referred to the Compensation Fund to claim the shortfall.

5.41 The rules provide for the payment of residual funds (where it has not been possible or where it would be disproportionate to trace the owner) into the Compensation Fund, where they are available to fund grants to clients generally.

Other payments from the Compensation Fund

5.42 The Solicitors Act 1974 enables payment from the Compensation Fund for certain activities related to its operation (in addition to the making of grants in respect of compensation claims). These activities are:

- payment of premiums to insure the Fund;
- repayment of money borrowed for the purposes of the Fund and payment of interest on any money so borrowed;
- payment of any other costs, charges or expenses incurred in establishing, maintaining, protecting, administering or applying the Fund;

- payment of any costs, charges or expenses incurred by the SRA in exercising its intervention powers[19]
- payment of any costs or damages incurred by the Law Society, the SRA, their employees or agents as a result of proceedings against any or either of them for any act or omission in good faith, and in the exercise or purported exercise of their intervention powers.

5.43 The Compensation Fund is applied to cover the costs of interventions. Due to the increased financial pressures being experienced by firms there was a concern surrounding the viability of those firms going forward. This concern is being managed by applying increased resource to assess the scope of the difficulties and to supervise the highest risk/impact firms more closely. To date the SRA has seen firms Cobbetts, Blakemores and Atteys fail, together with an increasing number of smaller, lower impact, firms. The SRA's financial stability programme has identified a significant number of other firms in serious financial difficulty.

5.44 The increase in intervention costs has resulted in a difference between budgeted costs (in 2012) and the unpredicted costs of interventions in 2013 of approximately £7 million greater. These increased costs could not be accommodated within the SRA budget.

5.45 The Solicitors Act 1974 (as amended) provides express statutory power for intervention costs to be paid from the Compensation Fund. The SRA Compensation Fund Rules 2011 support the overall principle that the Compensation Fund is the source for the funding of urgent or unpredictable costs (arising, by definition, from default). In the circumstances, the SRA considered it appropriate for these statutory provisions to be applied and for the costs resulting from interventions to be met from the Compensation Fund. The Compensation Fund is sufficiently maintained and has provision outside an annual budgeting process to deal with significant events and to ensure that monies are available to protect the public by intervention and the payment of grants.

5.46 The SRA continues to develop ways to manage firms in financial difficulties and policy measures to manage costs associated with a decision to intervene.

The Legal Ombudsman

5.47 Clients should try to resolve their concerns with the firm directly, using its internal complaints handling procedure. If a client is unhappy with a firm's response, it may be possible to ask the Legal Ombudsman to consider the complaint.

5.48 The Legal Ombudsman only investigates complaints made by the client, i.e. the person to whom legal services were provided or on whose behalf they were procured. There is no charge to clients for this service, but the Legal Ombudsman does not consider complaints made by large businesses or organisations. The Legal Ombudsman only accepts complaints raised by the following types of client:

- an individual;
- a micro-enterprise;
- a charity with annual income below £1 million after tax;

[19] Under Part 2 of Schedule 1 to the Solicitors Act or Schedule 14 to the LSA

- a members' club, association or organisation with annual income below £1 million after tax;
- a trustee of a trust with an asset value of les than £1 million; or
- the personal representative or beneficiary of the estate of a person who had not referred a complaint to the Legal Ombudsman before they died[20].

5.49 If the complaint raises questions of professional negligence, the Legal Ombudsman will consider on a case-by-case basis whether the issue is one that it can deal with, or whether the issue would be better dealt with in court[21].

5.50 The Legal Ombudsman has the power to make an award of up to £50,000 in total if its upholds a complaint. This can be in respect of:

- compensation for loss suffered;
- compensation for inconvenience / distress caused;
- costs of rectifying any error, omission or other deficiency; and
- costs of taking any specified action in the interests of the complainant.

5.51 The Legal Ombudsman can award interest on any award of compensation for loss, inconvenience or distress. This is permitted on top of the £50,000 limit. It can also order a firm to limit its fees to a specified amount and to pay interest on any sum to be refunded.

5.52 Awards are all enforceable before the High Court against the regulated individual or regulated firm (if the firm has its own legal personality).

5.53 In the financial years between 2011-2013, the Legal Ombudsman resolved 110 cases which included a financial remedy of over £10,000. In the last financial year, 17 cases resulted in the Ombudsman making an award of over £20,000.

Professional indemnity insurance

5.54 If the consumer falls outside the Legal Ombudsman's remit, or if the value of the claim exceeds £50,000, consumers should seek independent legal advice in respect of their loss, with a view to a civil action before the Courts if appropriate.

5.55 A firm's civil liability arising from private legal practice (and any defence costs in relation to such a claim) is usually covered by compulsory professional indemnity insurance. The SRA defines the minimum coverage firms must have in respect of their regulated business. Insurers are free to issue their own policy terms, so long as they provide at least the coverage set out in the Minimum Terms and Conditions 2013[22]. As a safety net for the public and for firms, the insurers that provide professional indemnity insurance to solicitors have committed to the SRA that the coverage set out in the minimum terms and conditions will apply as a minimum, regardless of the wording of the policy actually issued.

[20] Legal Ombudsman Scheme Rules: http://www.legalombudsman.org.uk/downloads/documents/publications/OLC_Scheme%20rules_v1_201104-1_FINAL.pdf

[21] Legal Ombudsman Scheme Rules, Rule 5.7(g)

[22] http://www.sra.org.uk/solicitors/handbook/indemnityins/appendix-1/content.page

5.56 Recognised bodies and licensed bodies must insure themselves for a minimum sum of £3 million in respect of any one claim. All other regulated entities must secure cover for a minimum of £2 million for any one claim[23]. The firm and the insurer are free to agree what excess should apply and on what terms[24], but if the firm fails to settle an amount within the excess within 30 days of it becoming due for payment, the claimant can notify the insurer, which is then liable to settle the claim on the firm's behalf[25].

5.57 If a regulated individual or entity should have had professional indemnity insurance in place, but did not have such a policy, the SRA has discretion to make a grant from the Compensation Fund to compensate the consumer[26]. The Compensation Fund can only make a grant if the claim would have been covered by the Minimum Terms and Conditions. A grant will not be made if there is a policy (or policies) of insurance against which a claim could be or has been made[27].

5.58 A risk associated with professional indemnity insurance, is poorly rated or unrated insurers and the potential insolvency of the insurer. An insurer who ceases to trade during a policy period may not be able to meet claims. Clients of law firms will in these circumstances, have to make a claim to the Financial Services Compensation Scheme.

[23] SRA Minimum Terms and Conditions of Professional Indemnity Insurance, rule 2.1

[24] SRA Minimum Terms and Conditions of Professional Indemnity Insurance, rule 3.1

[25] SRA Minimum Terms and Conditions of Professional Indemnity Insurance, rule 3.4

[26] Rule 5, Compensation Fund Rules 2011

[27] Rule 8.2, Compensation Fund Rules 2011

6 Funding the Compensation Fund

6.1 Contributions to the Compensation Fund are mandatory for all regulated by the SRA.

The overall contribution required is currently split evenly between firms holding client money and regulated individuals. Both firm-based and individual contributions are then calculated on a flat rate fee basis. 50 per cent of the funding requirement is met by a fixed contribution from regulated firms, and 50 per cent by a fixed contribution from all regulated individuals.

Contributions in 2013/14

The individual contribution

6.2 All individuals who applied for a Practising Certificate to commence on or after 1 November 2013[28], and all RELs or RFLs registered with the SRA, were required to pay a flat fee of £56 as an individual contribution to the Compensation Fund. This was due irrespective of whether the individual lawyer held client money during the relevant period.

The firm contribution

6.3 The firm based contribution only applied to those entities that held or received client money (as defined in the SRA Accounts Rules) in the previous practising year (between 1 November 2012 and 31 October 2013). Both recognised sole practitioners and recognised or licensed bodies were required to pay a contribution of £836 irrespective of the size of the practice.

6.4 The SRA had discretion to waive the contribution above if the initial application was made by a body which had changed its legal status or succeeded to the practice of another recognised body or recognised sole practitioner, in circumstances where the predecessor entity had already paid a contribution to the Compensation Fund.

Calculation of the contribution

6.5 The annual contribution is calculated by calculating the minimum reserve and forecasting future cash outflows and inflows for the year ahead. The overall contribution to be collected from regulated individuals/ entities is the balancing figure required to ensure that the minimum reserve is maintained at the end of the year.

[28] The only exemption from this is for the Crown Prosecution Service, whose staff benefit from a statutory exemption from paying the individual contribution.

Revised forecast of the closing balance for the Compensation Fund at year end

6.6 The first stage is to calculate the expected closing balance on the Compensation Fund at the end of the practising year (i.e. to forecast the balance at 31 October of the current year).

6.7 This is achieved by reviewing the Compensation Fund accounts for the first five months of the practising year and extrapolating the expected cash inflows and outflows for the remaining seven months of the year to 31 October.

6.8 For example:

- The Compensation Fund accounts for the first five months of the 2012/13 practising year show a balance of £67.1m.
- The grants to be paid in 2012/13, based on the original value of open claims at the end of March 2013 of £110.6m, is estimated to be in the region of £25.1m, broken down as follows:

£ 6.0m actual grants paid to date (Nov12 to Mar13)
£ 4.7m forecast grants on open business as usual claims*
£12.2m forecast for open mortgage fraud claims
£ 1.9m forecast for grants relating to future claims
£ 0.3m forecast for negligence claims re uninsured firms
£25.1m

* "Business as usual" claims in progress are evaluated by reference to the expected payout, applying historical payout rates for claims of a similar size and complexity.

Calculating the minimum reserve

6.9 The minimum level of reserves required in the Fund is calculated according to the following formula:

Minimum reserve =

(1.5 times average grants paid in previous 7 years)
+ (3 months' recharges & costs borne)

Forecasting future cash inflows and outflows

6.10 The main cash inflows to the Fund, excluding contributions, are transfers from Statutory Trust accounts (STAs) through rights of subrogation[29] and the transfer of residual balances[30]. Future cash inflows are calculated by extrapolating historical distributions, returns and recoveries.

[29] Recovery of grants paid where funds are found to be held by the Society in STAs

[30] Remaining funds in STAs once all reasonable efforts have been made to trace beneficiaries

6.11 The most significant cash outflows from the Fund are the payment of grants, the recharge of SRA and Law Society costs to the Compensation Fund and intervention costs. The Fund also bears the costs of legal challenge against decisions relating to the Fund, or legal action taken to protect and safeguard the Fund (such as the Willmett case in which the application of an aggregation clause by insurers could cause claims to fall on the Fund which it is considered should be paid by insurers).

6.12 The Client Protection directorate reviews the following when forecasting future cash inflows and outflows:

- expected number of future interventions
- estimated payouts for business as usual claims, by reference to historical pay out rates for claims of a similar size and complexity.
- mortgage fraud claims
- claims arising from the Assigned Risk Pool and uninsured firms
- SRA costs paid from or recharged to the Compensation Fund.

Consideration of Additional High Risk Potential Liabilities

6.13 If the Client Protection directorate is aware of other factors which suggests an additional level of risk to the Compensation Fund for the coming year, its impact on the contribution calculation is evaluated as part of the fourth and final stage of the calculation. For example, legal disputes which might result in an additional liability on the Fund in terms of claims or costs may present additional potential liabilities.

Costs of intervention

6.14 The costs of interventions will be used in the calculation of the following:

- cash outflows for the current year forecast;
- the minimum reserve; and
- cash outflows forecast for the coming year.

The amount forecast to be recharged in the current and subsequent practising years based on current figures is £4.0m.

7 How the SRA manages applications to the Compensation Fund

7.1 The primary function of the SRA's Compensation Fund is to make payments to those who have suffered loss as a result of fraud or dishonesty or by a failure to account for client money and provides client account funds for intervention agents to use immediately on an intervention where there are insufficient funds in a client account to protect clients' interests.

This section explains how claims on the Fund are handled by the SRA.

How do claimants know to make a claim?

7.2 The majority of claims on the Compensation Fund follow on from an intervention although this is not a pre requisite. If there has been an intervention the SRA's intervention agent will advise clients of the intervened firm on how to reclaim their money and papers.

7.3 Other applicants learn about the Compensation Fund through the SRA's website, on the advice of our Contact Centre or are directed to the Fund by other organisations such as the Legal Ombudsman or the Citizen's Advice Bureau.

Process for applications to the Compensation Fund

7.4 Applicants have to fill in an application form.

7.5 If the application falls outside the remit of the Fund or if further information is required applicants will be advised of this. Otherwise, the application will be allocated to a claims investigator to deal with it.

7.6 Some applications require detailed and sometimes lengthy investigations whilst others can be resolved swiftly, depending on complexity and the availability of evidence.

7.7 When Claims Investigators have completed their investigation they explain their view of the claim to the applicant. A report will then be prepared for adjudication including the Claims Investigator's recommendation. If the Claims Investigator is of the view that the claim should be refused whether in part or fully the applicant will be informed and given an opportunity to comment upon the report.

7.8 If the claim is refused in full or part the SRA will inform the applicant in writing of the reasons for the decision. The applicant has 30 days within which to appeal against the decision.

8 Value of claims on the Compensation Fund

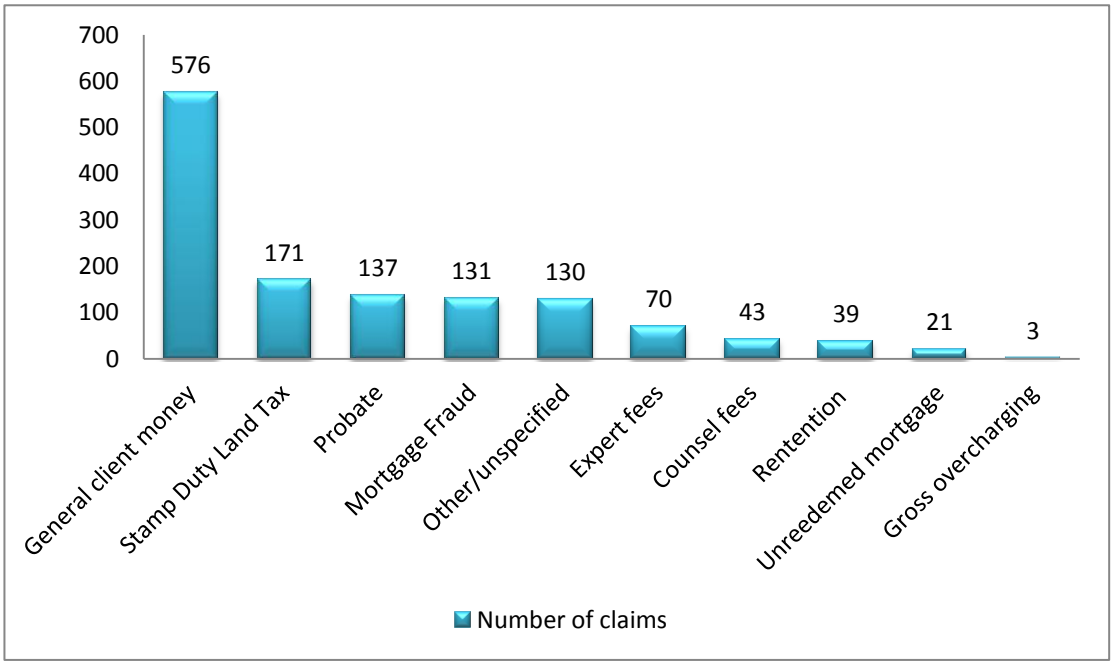
Claims made in 2012

8.1 In 2012, 1,321 claims were made to the Compensation Fund, for a total value of £31.56 million.

The majority of claims (576) related to general client money (misappropriation/failure to account), followed by claims relating to stamp duty land tax, probate and mortgage fraud.

Number of claims

Source: SRA



Matters closed in 2012

8.2 The SRA closed 2,292 applications to the Compensation Fund in 2012. Payments were made in respect of 684 of these files (29.8% of matters closed) with a total value of £18.54 million[31].

Claims refused in 2012

8.3 No payment was made in respect of 1,608 applications. These matters were closed without payment for the reasons listed below. The majority of claims were refused/not progressed because the customer had not responded or where there was another remedy which could be pursued.

Final Outcome	Number of Matters
Customer did not respond	474
Applicant to exhaust other remedies	366
Application withdrawn	324
Assessed claim: losses outside the remit of the Fund	136
Assessed claim: applicant contributed to own loss	84
Losses outside the remit of the fund	82
Assessed claim: loss due to other factors	60
Adjudicated claim rejected	39
Claim Rejected	26
Other	9
Assessed claim: other	5
Statutory Trust Claim	3
Total	1608

Source: SRA

[31] SRA Quarterly stakeholder report, December 2012