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CLLS - PROFESSIONAL RULES AND REGULATION COMMITTEE

RESPONSE TO SRA CONSULTATION

A. INTRODUCTION

1. This is the response of the City of London Law Society ("CLLS") to the SRA's Consultation "*Client money in legal services - safeguarding consumers and providing redress*" issued in November 2024. The consultation is divided into three parts: (1) The model of solicitors holding client money; (2) Protecting the Client Money that solicitors hold; (3) Delivering and paying for a sustainable compensation fund. We intend to deal with all three parts in this response.

2. The CLLS represents City lawyers through individual and corporate membership, including some of the largest international law firms in the world. The CLLS represents over 21,000 solicitors who are members of the profession in the City of London. They represent 12% of all practising solicitors. The CLLS responds to a variety of consultations on issues of importance to its members through its specialist committees. This response has been prepared by the CLLS Professional Rules and Regulation Committee.

Context to the Consultation

3. The Consultation is focused upon the rules for holding client money, the supervision of those that do so, and how the Compensation Fund is funded. It is useful to make some introductory remarks as to the evolution of the overall scheme and the broader context to the Consultation.

4. Until the early part of the last century it was considered to be entirely proper for solicitors to hold clients' money in their own bank account. Indeed, substantial losses to clients were caused by solicitors using clients' money to invest for their own benefit. What is now the modern framework for the regulation of client money can be traced back to the recommendations of a Law Society Committee in 1906 and the essential scheme we have today was established by the Solicitors Act 1941.

5. The intervening 80 years has seen a radical development of the legal profession to the point where it is unrecognisable from the period when the current regime was put in place. For example, there were 13,000 solicitors in England and Wales in 1945, there are now over 167,000. In 1945 law firms were limited to 20 partners by statute and solicitors could only practise in general unlimited partnerships. Many firms now have

hundreds of partners are normally incorporated as LLPs but it is also possible to practise through a limited liability company. The growth and complexity of legal businesses has mushroomed. Technology and statutory reform have enabled high volume litigation and conditional fee arrangements and the market has evolved into different segments serving different societal needs. Some of these present a high risk to client money, some present essentially no risk. Yet they are all regulated in the same way under the same scheme. The arrangements to protect client money have remained stuck in the 1940s. It is disappointing that the SRA has not sought to be more radical in its thinking as to whether they remain fit for purpose.

6. The present position can be generally described as follows:

   a. The protection of client money has three layers. First, the Solicitors Accounts Rules ("SARs") themselves which provide a granular framework for dealing with client money. It has long been the case that misconduct arising out of breaches of the SARs are dealt with severely by both the SRA and the Solicitors Disciplinary Tribunal. Second, money held in client account is protected by the double lock of insurance under the SRA's Minimum Terms and the Compensation Fund. The latter deals with factual scenarios where insurance is not available such as dishonesty[1] or failure to account. Third, the intervention power which enables the SRA to act swiftly to control a firm's client account in order to stem losses to the Compensation Fund.

   b. Partly as a result of the protections set out above but also because of the strength of the solicitor "brand" and the power of a solicitor's undertaking, solicitors sit at the heart of many commercial and residential transactions. That is because they are collectively trusted to give effect to transactions where money is exchanged for assets. As a result, solicitors handle more money in a fiduciary capacity than any other profession. There were one million property transactions in 2022 almost all would have involved money passing through a solicitor's client account. As Lady Justice Smith observed in Briggs v The Law Society [2005] EWHC 1830 (Admin) at para 35:

      > "If property purchasers and mortgage lenders cannot have complete confidence in the safety of the money they put into the hands of a solicitor in the course of a property transaction, our system of conveyancing would soon break down."

We cannot find any available source as to how much money flows through solicitors' clients' accounts annually. However, it is certainly in the billions. It may be that in due course the market finds a different or better way of dealing with such transactions which require a central trust element particularly as technology advances. However, there is currently no realistic alternative. It would also follow that a regulator seeking to deconstruct such an enormous element of commercial life and therefore push against market forces is heading down the wrong path and risks disrupting the market, undermining economic growth and weakening the economic significance of those whom it regulates. We are also not convinced that a move to Third Party Managed Funds would lead to the regulatory nirvana that the SRA has suggested. Essentially, solicitors would be sub-contracting out the running of their client account. However, the existing fiduciary obligations would remain and as such the risk profile and costs associated with that risk including insurance will continue.

[1] An insurer will answer to a claim where there are other partners who are not dishonest so insurance is more likely to cover firms with multiple partners rather than a claim being made on the Compensation Fund.

7. We consider that the SRA should return to first principles and ask itself what a scheme to protect client money should look like in the 21st century. We would make the following observations on considerations that should be part of that process. A scheme should:

a. Protect client money. The paradigm scenario is that of an individual client (as opposed to a corporate entity) who has entrusted funds to a solicitor in order to complete a transaction. That client should expect and receive complete protection. However, there are other scenarios that fall within the current scheme that protects client money that need to be considered. These include: (1) money paid to solicitors on account of fees. It is not clear why in contrast to any other profession or businesses a client of a solicitor has protections beyond those provided for in general law relating to debts and insolvency; (2) overpayments by insurers and other third parties which again are in species a debt; (3) money provided by large commercial organisations who are able to negotiate their own insurance and protections. It is clearly a matter of debate as to whether these scenarios should have protection through the SARs and/or the Compensation Fund. However, at present the SRA is not even asking the question.

b. Be proportionate. The current arrangements effectively lead to the entirety of the solicitors' profession indemnifying the client account of every SRA authorised body in England and Wales. Whilst that might be right for the paradigm scenario the further one moves away from that the more proportionate the protections should become;

c. Minimise the regulatory burdens on authorised persons. This is arguable another aspect of proportionality but unnecessary burdens on firms will only increase their cost to clients and reduce their competitiveness. As the present government recognises, legal services are a driver of growth in the economy both through domestic and international transactions. Yet the SRA seems oblivious to the regulatory objective of "encouraging an independent, strong, diverse and effective legal profession"[2]. It is notable that almost all of the proposals put forward by the SRA in its Consultation have the effect of increasing the burdens on firms even where there are existing regulatory protections. However, what is noticeably absent is any passages addressing whether those steps are "proportionate" and "targeted".[3]

8. Before turning to the substance of the SRA's consultation we would make four general observations. First, it is notable that many of the justifications for action by the SRA are based on passages that start with phrases such as "we have heard" or "anecdotally". What is of course lacking is any sense of how widespread are the practices that the SRA has heard about. It would clearly be disproportionate to place additional regulatory burdens on the profession as a whole based on putative occurrences that might be very small in number and which can be dealt with under the existing framework. We met with the SRA during the course of its Consultation process and it made clear that at this stage it was seeking to raise issues for discussion and to get a wider understanding from the Consultation process itself. Whilst we consider that many of the points in this category reported by the SRA in its consultation are not a wider issue necessitating regulatory action, we now understand the SRA's approach.

[2] See Section 1(1)(f) of the Legal Services Act 2007

[3] See the statutory obligation on the SRA under the Legal Services Act 2007 Section 28(3)(a).

9. Second, the Consultation is silent in relation to the interventions. As we have observed above, the intervention power is an important element of client protection in that enables the SRA to "nip in the bud"[4] circumstances where there are risks to the Compensation Fund and indeed to insurers. The intervention powers similarly date back to the Second World War. We would suggest that the current intervention regime is no longer fit for purpose in that it has two fundamental flaws. First, it conflicts with the insolvency regime which means that it acts as an impediment to firms being dealt with through the insolvency process.[5] Second it is not apt for dealing with larger firms. Indeed, the Legal Services Board's report into Axiom Ince makes clear that the cumbersome nature of the current power inhibited the SRA from acting earlier. We entirely accept that any changes to the intervention arrangements would require at least an Order under Section 69 of the LSA. However, there is a clear need for reform which would benefit clients and the profession.

10. Third, it is important to emphasise the that the operation of a client account is a service provided by law firms to clients as a necessary but subsidiary element to the provision of legal services. It is not a banking facility, as the SARs make clear. As such the legal services and the flow of money have to be closely integrated. Elements of the SRA's Consultation seem to overlook this fact. Particularly in relation to interest provisions but also with respect to the proposal of interposing third party managed funds into the service and how this will degrade the service to clients. We will deal with the practical impact of this below.

11. Finally, there is a consistent theme in the SRA's consultation of proposing additional regulatory burdens on firms where there are already provisions in the SRA regulatory arrangements to deal with the situation that is of concern. As we have already observed the SRA has a statutory obligation only to take action where it is needed. The SRA's approach is also inconsistent with the Government's view that over-regulation inhibits economic growth. Given the contribution that the legal professional has already made to economic growth this is a concerning approach.

B. <u>THE MODEL OF SOLICITORS HOLDING CLIENT MONEY</u>

<u>Residual Balances</u>

12. Client account residual balances are a perennial issue[6]. The starting point is that they are not deliberately created by law firms and can arise for a number of reasons. For example, interest may be credited to a ledger after a transaction has completed or there was a miscalculation as part of that transaction. They can also arise as a result of overpayments by third parties. We understand why the SRA might have mentioned that firms it intervenes into often have substantial numbers of residual client balances. However, that is just a symptom of the fact that such firms are by definition likely to have poor systems and processes for dealing with client money.

13. A well-run law firm will have an ongoing program for dealing with residual client balances and they will continue to arise as part of the normal operation of a client account. The SRA itself has had different approaches to client balances over the years. Approximately 10 years ago it had a big push on residual balances and brought cases before the SDT in relation to them. However, after concerns that this was

[4] See Sir Robert Megarry V-C in Buckley v The Law Society (No. 2) [1984] 3 All ER 313 at 317.
[5] As part of an intervention practice money (which includes office money) vests in the SRA to hold on trust for the purposes of the intervention. On an insolvency such money vests in the insolvency practitioner. Neither scheme recognises the other. The conflict between the schemes can inhibit an insolvency practitioner taking an appointment for fear that any assets would be taken by the SRA.
[6] The report of the Law Society in 1906 referred to at paragraph 4 above included a recommendation that: "clients' money be retained for the shortest possible time."

disproportionate it has adopted a more nuanced approach. The current Enforcement Strategy says: "*if a compliance officer for finance and administration (COFA) identifies a failure to pay to clients their residual balances and puts in place an action plan to remedy the breach, we may agree specific measures and targets in a compliance plan to which all the managers sign up. The plan would include regular updates to us so that we can monitor progress and escalate the matter if we have concerns about continuing risk.*"

14. In short there are existing rules in place to require firms to deal with residual balances promptly[7] and where appropriate the SRA monitors and deals with cases where this had not been complied with. Nothing has changed in this area for some time so it is not clear why the SRA now considers that this should be: "a key priority" for law firms or that additional rules are necessary. The SRA's proposals would inevitably mean more resources were allocated to dealing with the additional regulatory burdens which would either reduce resource in other areas or reduce the overall competitiveness of firms.

15. A better way forward would be to address the current administrative burden in dealing with residual balances. The SRA places onerous obligations on firms to trace clients before donating money to charity or seeking permission from the SRA to do so. A simpler regime such as one where say 2 letters are written to clients and after that money is paid into a central fund with an indemnity to return the funds if claimed by the beneficiary would be a better route as it would provide a simple clear route for firms to deal with residual balances.

16. Finally we do not understand the SRA's reference to reconciliations as being an opportunity to review residual balances. The exercise under SAR rule 8.3 is directed at reconciling the bank balance to the firm's ledger balances. In a firm of any size the reason for such underlying ledger balances are not part of that exercise.

Interest on client accounts

17. This is another area where nothing has changed save for the fact that the historically low level of interest rates came to an end during 2022. The SRA's Consultation does not make any compelling case for a change to a long-standing arrangement in relation to accounting fairly to clients. The starting point for considering this issue is that law firms are providing a service to their clients through the operation of a client account, they are not providing a banking facility. There would clearly be some disruption to firms if a different regime were implemented and again this would lead to a greater administrative burden on firms where there is no compelling case to do so. The SRA's principal concerns appear to centre around a small number of firms where interest on client money is an important part of their revenue. By definition this can only be an issue that has arisen in the last two years as interest rates have increased. In so far as those firms are not acting in accordance with the SARs then regulatory action can be taken.

Moving money from client account to office account

18. This section of the consultation provided an example of how the SRA has not asked more fundamental questions. In other areas of professional services a payment on account is dealt with as a debt. The issue that arises is whether costs should attract the same level of protection as life savings paid to a solicitor to buy a home. In short, are the current protections necessary and proportionate? Is disappointing that the SRA

[7] See Rule 2.5 of the SARs

has not addressed these questions but instead seeks to add more burdens through technical and complex provisions.

19. There needs to be some flexibility as to the commercial arrangements between firms and their clients. There are reasons why clients wish to pay in advance, such as for budget reasons or as part of a commercial arrangement. In principle there is nothing wrong with such approaches which should form part of the freedom of clients to contract in their best interests. We are deeply concerned that the purported justification given by the SRA for further action is: "We are now concerned that maintaining rule 2.3(c) in its current form provides firms with too much flexibility to put their own interest ahead of that of their client." All dealing between clients and solicitors provide an opportunity for the solicitor to put their own interest ahead of the client. That is why there are extensive provisions in the Codes of Conduct and elsewhere to address situations where a solicitor does not act in the client's best interests or takes unfair advantage. The logic of the SRA's position is that every such risk should be addressed by a specific rule so as to eliminate the "opportunity" for a breach. This again demonstrates an instinct by the SRA to overregulate the profession and is inconsistent with its statutory obligations.

Advanced Fees

20. Our experience is that the concern raised by the SRA, that firms are deliberately asking for more money on account than needed, does not represent a widespread practice. We note this information was received "anecdotally" by the SRA and we do not believe it is an issue that is significant enough to justify regulatory action.

21. Self-evidently the taking of money on account is a method by which solicitors seek security from clients and is a component of sensible financial management by law firms. There are particularly categories of clients who present a higher credit risk including those with limited assets or who are abroad. This is an entirely sensible and prudent commercial step.

22. Many clients are either resistant to paying money on account at all or will wish to limit the amount paid to solicitors to ensure that it only covers the likely costs for a prescribed period. In turn a solicitor would not want to ask for too much money on account as that is likely to deter the instructions or cause a client to instruct a firm whose request for money on account is lower. This aspect of the market has functioned without any issue for a considerable time and we do not consider that further regulatory burdens on firms is either necessary or proportionate to what appears to a fanciful risk. This is a further example where the SRA seems to instinctively consider that further regulation is an answer where there are adequate provisions to deal with egregious behaviours.[8]

Alternatives to holding client money

23. For the reasons we have already set out at paragraphs 6 above we do not consider it is realistic for the SRA to seek to change a practice that is central to commercial life in England and Wales. In any event there are significant practical issues with the operation of such accounts by law firms.

24. Client transactions form part of the service provided by law firms. There is risk involved whenever there is a movement of funds from one party to another, whether this transaction is carried out by a law firm, client or TPMA. Law firms have stringent

[8] Principe 7, "act in the best interest of each client" and 1.2 "you do not abuse your position by taking unfair advantage of clients and others".

processes and controls in place in relation to all client money transactions, which would probably be at least equal to the controls of a TPMA (oral verification of bank account details, test payments, written client approval, and certain other steps). By having a TPMA carry out the payment process would in effect duplicate the work associated with transactions as it would be necessary for the firm to give instructions and monitor the progress of the transaction. This would lead to an increased cost to clients and likely cause significant delays and lower the service to clients. Part of the operation of a client account in relation to a transaction involves tracking the flow of funds and understanding how a transaction is progressing. That includes understanding where the money is in the process such as whether it is held by the paying, intermediary or beneficiary bank (which happens often). A firm would be reliant on a third party to provide updates where the law firm currently has direct contact with the bank. We estimate that some of our members have 40-50 client account movements a week but expect that firms working in other sectors may have substantially more.

25. When processing client transactions, law firm cashiers teams have access to confidential agreements and undertakings which are used as part of the payment authorisation process, which may cause issues with client confidentiality agreements if shared with a third party. There are many transactions where the amounts to be received or paid can change quickly and it is questionable whether a TPMA will allow for any movement in a transaction without adding additional delays or costs. These delays could result in the collapse of client transactions or additional costs.

Q1.	**We want to ensure we fully understand the issues firms encounter in returning excess funds to clients or third parties – please outline:**

- the circumstances in which residual balances may arise on a particular matter
- the steps that firms can take to make sure their client contact details remain up-to-date and any challenges with doing this
- mechanisms that firms use to trace clients/third parties and any challenges with this

Q2.	**Do you agree that we should replace the term 'promptly' in rule 2.5 of the Accounts Rules and introduce more prescriptive requirements around returning funds to clients and third parties?**

Q3.	**Would a 12-week timeframe, from the conclusion of a case, provide sufficient time in which to identify an excess balance on a client account and return the funds to the client or third party where the firm holds their up-to date contact details?**

If not, please give your reasons and include any specific examples of relevant issues.

Q4.	**Should it not be possible to return excess funds to the client or third party within 12 weeks of the conclusion of a matter, is a further 12 weeks a reasonable timeframe to make all reasonable attempts to trace the relevant client/third party and where this is unsuccessful,**

	donate the residual balance to charity or apply to us for approval to do so?

In relation to questions 1 to 4 see paragraphs 12 to 16 above.

Q5.	**We would like to understand current practices around interest on the client account. Please tell us about your experience of the arrangements for interest on clients' money, including:**

- The extent to which client accounts generate interest, and – if so – how interest is apportioned between the firm and the client?
- Any arrangements firms have to receive less or no interest on client accounts and what, if anything, the firm receives in return?
- Whether and how firms make their clients aware (either directly or via terms and conditions) that their money could earn interest?
- Whether clients are aware that firms may retain some of the interest earned on their money?

Q6.	**What are your views on the suggestion that we amend our rules to prevent firms retaining any of the interest earned on client money (subject to a de minimis)?**

Q7.	**Are there circumstances where firms retaining some of the interest earned would be of benefit to the client?**

Q8.	**What do you think would be the impacts of removing the ability for firms to earn interest on money held in client accounts? How could any short-term and/or long-term challenges be overcome?**

In relation to questions 5 to 8 see paragraph 17 above.

Q9.	**Are there any circumstances in which it is in the client's best interests to transfer client money from the client account to the office account before the work to which it relates has been completed? If so, please describe these circumstances.**

Q10.	**Do you agree with our proposal to progress the amendment to rule 2.1(d) of the SRA Accounts Rules? Please explain your answer.**

Q11.	**Do you agree with our proposal to progress the amendments to rules 4.3, 4.3(a) and 4.3(c) of the SRA Accounts Rules, and the addition of rule 4.4? Please explain your answer.**

Q12.	**What are your views on the option to remove the ability for firms to enter into alternative arrangements about where client money will be held and how it will be used under rule 2.3(c)? Please explain your answer.**

In relation to questions 9 to 12 see paragraphs 18 to 19 above.

Q13.	**What approaches do firms take when calculating the amount of money they request from clients in advance? In your response, please outline:**

- Any areas of practice where you consider that it is important to take advance fees
- How a reasonable amount to request in advance can be calculated
- Any alternatives to requesting advance fees

Q14.	**When and how do you think we should, or should not, be more prescriptive about how much client money firms can request in advance of work being completed? In the areas where you think we should be more prescriptive, please outline what you think the implications would be for both clients and firms.**

In relation to questions 13 and 14 see paragraphs 20 to 22 above.

Q15.	**What are your views of the long-term option of changing the model of firms holding client money? Please outline what you think the impact would be if firms were to hold no or substantially less client money?**

Q16.	**In your experience, are there areas of law or services in which it is essential for a firm to hold client money? What would happen if solicitors were not able to hold client money in these areas?**

Q17.	**Do you have experience of any alternative method(s) of holding client money (such as a TPMA or other methods)? If you have experience of any alternative method, what has that experience been? What was the impact on clients and the firm?**

Q18.	**If you have knowledge or experience of alternative approaches to holding client money, would you be open to further discussion with us as part of future development in this area? If yes, please confirm that you are happy for us to use the details you have provided to contact you, or please provide alternative contact details.**

For questions 15 to 18 see paragraphs 6 and 23 to 25 above

Q19.	In the context of this consultation, do you agree with our assessment of equality, diversity and inclusion considerations in our impact assessment? If not, what else do you think we should consider?

We have nothing additional to add.

C. PROTECTING THE CLIENT MONEY THAT SOLICITORS HOLD

26. We entirely understand that this section of the Consultation reflects some of the contents of the LSB's report into Axiom Ince and the criticisms of the SRA and that the SRA is being finessed into making changes by the approach of the LSB. The Axiom Ince case sits in a regrettably long line of once in a generation frauds committed by rogue solicitors some of which led to the setting up of the protections we describe in paragraph 6a above[9]. In that sense it is not new or different. However, it would be wrong to ignore the fact that the legal services market is evolving and more variegated. The challenge for the SRA is to evolve with it and to devise a framework that alerts it to firms that may present a greater risk than other firms in the market. In devising that framework, we consider that the following principles apply:

    a. There needs to be a clear understanding by the SRA as to what are real risks and what are merely features of an evolving market. For example, the LSB seemed concerned about consolidators and ABSs neither of which seem without more to be indicators of risk. Whilst we note that the SRA has commissioned desk-based research from Frontier Economics on future risks, we consider that the SRA should take this matter further and consider appropriate indices of risk that it can use to triage firms within its authorisation process;

    b. Any additional burdens placed on firms needs to be targeted and proportionate. Not all authorised firms will present the same risks and some will not present any realistic risk. It would be wrong to burden all of the regulated community when it is disproportionate to do so;

    c. The SRA should not stray outside those areas where it has the competence to assess facts. It would be dangerous for the SRA to seek to make judgments on business plans or whether firms are likely to be successful in the market;

    d. More generally the SRA must be mindful that additional processes inherently inhibit the operation of the market. Where firms are seeking to merge or attract external investment, the SRA's processes add uncertainty and delay.

<u>Improving Oversight of Firms</u>

27. Provided the SRA's approach reflects the principles set out above we do not see any issue with the SRA's proposals to increase their level of monitoring although there might be practical issues around implementation and it would be helpful if they consulted informally with relevant groups on the impact of any steps. In particular we can see the need for the SRA to be alerted to significant changes to a firm's structure and work type outside the normal reporting cycle.

[9] Whilst more recent cases include Blavo and Durnford Ford, such cases arose as early as 19th century. A mid century example is Eichholz where the Compensation Fund paid out £525,851 in respect of a fraud that came to light in 1957 where money was taken from Jewish refugee clients who had moved to England before the war.

Mitigating the Risk Associated with Dormant Law Firms

28. We can also see that there is a need for the SRA to monitor dormant law firms but would urge caution in being overly prescriptive in this regard. Dormant firms (in a similar way to residual balances) can arise for a variety of reasons particularly in a group structure, and a necessity for firms registered with overseas bars and regulators and the approach adopted by the SRA should be proportionate to the risk.

Accountants Reports

29. Our preference would be for the SRA to re-introduce the requirement for non-exempt firms to submit accountants reports to the SRA which was the previous practice. As this is an established methodology it is less likely that this would lead to unintended consequences.

30. We note that the SRA has not produced any evidence to support its suggestion that firms be required to change their reporting accountants periodically. In many firms the SAR Report sits alongside the same accountancy firm carrying out a statutory audit. This arrangement is beneficial because the auditors in their wider work are likely to be better informed as to a firm's systems and controls than if the work was limited to the SAR Report. An SRA requirement to change Reporting Accountants would add an unnecessary complication and burden. This is particularly so in respect of CLLS members where the accountancy firms that can undertake such work is limited and is further constrained by the auditor's own professional obligation to be free of any relationship with a firm that might undermine independence. In any event, there are already provisions in place by regulators of the accountancy profession to address this risk. The previous government also consulted on widening the definition of Public Interest Entities which, if implemented, could bring some CLLS members within that scheme of regulation in respect of their auditors.

31. We do not have a view in relation to the existing exemptions save to say that these should be evidence based. We note the SRA's observations in relation to exploring further options to strengthen guidance which we presume will be the subject of further consultation.

Strengthening Checks and Balances within Law Firms

32. It is implicit in the SRA's proposals that it considers that as a matter of governance there should be a separation of the management of a law firm from the compliance functions of COLP and COFA. We do not consider that this is the only governance model that is available and the SRA's approach should be more flexible. For example in some firms the COLP role is held by the Managing Partner because it is considered beneficial for that individual to hold the overall responsibility for SRA Compliance. This model has advantages not least that it places the SRA responsibilities at the heart of decision making which is essential given the SRA's regulatory reach extends well beyond rules of professional practice (such as confidentiality and conflicts of interests) into broader conduct and work place related issues.

33. If the COLP is less directly involved in day to day management there is a risk that they are inadvertently unaware of relevant matters. We consider that there are dangers in the SRA being too prescriptive as to how the COLP and COFA role operates in a firm. The important consideration is that firms have integrated the roles into their governance and are able to justify the steps they have taken if asked by the SRA. The overriding consideration should be outcome based and the SRA should not prescribe how firms should manage themselves.

34. In this area there is a risk that the exceptional circumstances of Axiom Ince experience where all roles were held by one person will lead to a level of unnecessary regulation of the entire profession. Such a concentration of roles would be known to the SRA and could operate as a “red flag” requiring investigation without the need to add further regulation.

35. Finally we look forward to learning the outcome of the SRA’s thematic review in relation to COLPs and more detail of the intended support package.

Q1.	**Do you think that we should be more prescriptive around the information that we must be notified of outside of our annual practicing certificate renewal exercise? If so, what information should we require and what risks should we target?**

Q2.	**Do you think certain changes should require pre-approval by us and/or after-the-event monitoring and supervision? If so, which changes should this apply to and what risks should we target?**

Q3.	**What impacts might arise from notifying us of changes in advance? Please provide specific examples of where firms provide information about changes to other third parties, eg insurers.**

For questions 1 to 3 see paragraph 27 above.

Q4.	**To what extent to you agree or disagree with our proposed approach to addressing dormant firms - taking action where a firm has not provided legal services and/or recorded zero turnover for 12 months, unless legitimate circumstances apply?**

For questions 4 and 5 see paragraph 28 above.

Q5.	**Are there other circumstances not presented here where you think a law firm can legitimately record zero turnover for an extended period?**

For questions 4 and 5 see paragraph 28 above.

Q6.	**Which of these three options for improving compliance with our requirements for accountants' reports and our ability to monitor this do you prefer and why?**

Q7.	**What are your views on whether we should consider requiring firms to periodically change their reporting accountant to safeguard independence, and if so, how often we should require this?**

Q8.	**Should we retain the existing exemption from obtaining an accountant's report, amend it, or remove it?**

For questions 6 to 8 see paragraph 29 to 31 above.

Q9.	**To what extent to do you agree or disagree that any manager that can unilaterally make decisions that impact client money handling should not also be able to hold a COLP or COFA role? Please explain your answer and include any suggestions for ensuring appropriate internal checks and balances.**

Q10.	**Do you think this proposal should apply equally to all law firms, or should certain law firms – such as sole practitioners – be exempt if certain conditions are met? If so, what should these conditions be? Please explain the reasons for your answer.**

Q11.	**To what extent do you consider our proposals to build and launch a package of support for compliance officers, and to strengthen our expectations for law firms to support their compliance officers, are sufficient? Are there issues we should target to enable compliance officers to meet their responsibilities effectively?**

For questions 9 to 11 see paragraphs 32 to 35 above.

Q12.	**In the context of this consultation, do you agree with our assessment of equality, diversity and inclusion considerations in our impact assessment? If not, what else do you think we should consider**

We do not have anything additional to add.

D. DELIVERING AND PAYING FOR A SUSTAINABLE COMPENSATION FUND

Contributions to the Fund

36. The SRA's approach to contributions does not expressly recognise that CLLS member firms will pay the contribution of individual solicitors who are either partners or employees. As such the contribution made by firms is the aggregate of the individual fees and the entity fee. As member firms employ 12% of the profession, they contribute significantly to the Fund in circumstances where the risk of them causing any grants to be made by the Fund are remote. The proportion of the contribution by CLLS members will increase if the split between individual and firm contributions shifts towards individuals. However, the CLLS recognises that there is a wider public interest in the profession as a whole maintaining trust and confidence through the Compensation Fund.

37. We can see no compelling reason to depart from the current simple system. A payment based on risk profile will be contentious and complex although, as the Consultation recognises, it is likely to benefit CLLS members. A turnover based calculation also seems to put a greater burden on those firms who are least likely to cause a claim. Whilst we note some large firms (defined by the SRA as the largest 1000 firms) have caused claims they are numerically small and the practical effect is that the burden of the scheme would fall even more on the very large firms such as CLLS members where insurance rather than the Compensation Fund will bear any losses to clients.

Payments from the Compensation Fund

38. As we have observed above we consider that a more fundamental review is needed as to what should be dealt with as client money and what therefore is protected by the Compensation Fund. In that context the SRA's proposals are an extension of a process that has been going on for a number of years tactically to reduce claims once they have arisen by imposing caps and other limitations[10]. Whilst we can understand the desire to reduce payments made out of the Fund we are concerned that this results in even more complexity for clients and an increase in the likelihood that they will feel aggrieved by a claims process where their claim is frustrated by matters beyond their control such as being a connected claim. This raises a greater risk to the central public interest in maintaining confidence in the delivery of legal services by those regulated by the SRA.

39. We therefore consider that the Fund needs to be simplified not made more complex.

Q1.	**Do you agree that changing the apportionment of Compensation Fund contributions to 70% individuals and 30% firms is an appropriate and proportionate approach to setting contribution levels for 2025/26? Please give reasons for your answer.**

Q2.	**Are there any other important apportionment issues you think we have not considered here? If so, please explain what they are.**

Q3.	**What are your views on the possibility of setting differential contribution levels for different firms?**

Q4.	**What are your views on the possible alternative methods of setting differential contributions to the Compensation Fund (based on enhanced requirements, risk categorisation, the amount of client money held, or annual turnover)?**

Q5.	**Are there other alternative approaches to differential contributions you think we should consider?**

For questions 1 to 5 see paragraphs 36 and 37 above.

Q6.	**To what extent do you agree we should move away from the current arrangements that allow us to impose a cap of £5m for connected claims?**

Q7.	**Would you support any of the other options discussed (a flexible cap for connected claims, removing the cap for connected claims,**

[10]See for example R v The Law Society ex parte Mortgage Express, [1997] EWCA Civ 1234

	guaranteeing compensation up to a specified amount)? Please explain why.

Q8.	**Are there other important considerations you think we have not considered here? If so, please explain what they are.**

Q9.	**What are your views on the idea of amending our Compensation Fund Rules to explicitly exclude specific types of claims? If you think specific types of claim should be excluded, which ones are these?**

Q10	**Are there any other considerations we should take into account in relation to payments from the Compensation Fund? If so please explain what they are.**

Q11.	**In the context of this consultation, do you agree with our assessment of equality, diversity and inclusion considerations in our impact assessment? If not, what else do you think we should consider?**

We have nothing additional to add.