



Consumer Panel Briefing – Financial Protection Arrangements

What is the issue?

Financial protection arrangements include professional indemnity insurance, compensation funds and other measures which are designed to compensate consumers who suffer losses due to events such as negligence, insolvency and fraud by lawyers.

While these events happen rarely, the consequences for consumers might be very severe. However, providing these protections has become increasingly expensive for lawyers who pass on these costs to their clients, so it is important to get the balance right.

In October 2012, the Legal Services Board asked us to examine whether these systems were working well and how much risk consumers should be expected to bear.

The Panel's view

The Panel developed a list of things that financial protection arrangements should seek to achieve and then assessed whether this was happening in practice. We also commissioned market research to find out what consumers think about these issues.

We found that on most occasions the arrangements cover the main risks facing consumers. However, we also identified some issues that regulators need to tackle, including:

- Scenarios where consumers could lose out due to gaps in coverage, e.g. insurers aggregating claims which then exceed caps on maximum payouts
- Compensation fund payouts are discretionary, but there is a lack of transparency about the criteria regulators use when deciding whether to award compensation
- A lack of information about the performance of compensation fund schemes
- A need for better sharing of information between regulators and organisations like insurers and banks, in order to help regulators prevent problems before they happen
- A lack of research on the consumer experience of accessing the schemes

Currently, all lawyers must take out indemnity insurance, but we were asked to consider whether, in certain situations, consumers should take out their own insurance instead. Consumers told us they did not want this option and said they would not choose firms who did not have insurance themselves. The Panel also thinks this would be a mistake: it is unfair as the lawyer is the source of the risk; it would be hard for consumers to make an informed choice; and poorer consumers may be tempted to take a chance in order to save on costs.

What is the Consumer Panel doing about it?

In June 2013, the Panel published a report on the regulators' financial protection systems with a series of recommendations about improvements that could be made. A separate paper on the division of risk between consumers and lawyers was also published.

One of our recommendations was to explore whether it would be a good idea to centralise the different arrangements used by the various types of lawyer within a single umbrella body. This could be simpler to understand for consumers, cheaper for lawyers and make it easier to base cover on the type of legal activity rather than the lawyer's professional title.

We also suggested regulators explore alternatives to client accounts for protecting client money. One option is to set up escrow accounts where an independent trusted third party is responsible for receiving and distributing the money. For consumers the main benefit is that the money put into the escrow by them is held for a particular purpose and may only be released with their consent. Some regulators have recently started to investigate this.

The Legal Services Board is currently considering our report and will decide their response soon. Our work will also inform a major review that the Solicitors Regulation Authority has started on the financial protection arrangements used by solicitors.

For more information:

[Report on Financial Protection Arrangements, June 2013](#)

[Consumer Challenge paper on Risk and Responsibility, June 2013](#)

[Consumer research on Risk and the role of regulation, February 2013](#)

About the Legal Services Consumer Panel

The Legal Services Consumer Panel is a central feature of a regulatory framework in England and Wales which is designed to transform the legal services market around the needs of its users. Created by the Legal Services Act 2007 we are an independent arm of the Legal Services Board. As a permanent, discrete champion for consumers we have an essential responsibility to ensure that regulators are able to consider and act on the user perspective.



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