THE INSTITUTE OF CHARTERED ACCOUNTANTS IN ENGLAND AND WALES

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Our ref: ICAEW Rep 20/10

Mahtab Grant
Legal Services Board
7th Floor Victoria House
Southampton Row
London WC1B 4AD

Dear Ms Grant

Consultation paper - Alternative Business Structures - approaches to licensing

The Institute of Chartered Accountants in England and Wales (the ICAEW) welcomes the opportunity to comment on the consultation paper Alternative Business Structures – approaches to licensing - published by the Legal Services Board in November 2009

Preliminary comments from the ICAEW on:

Question 3 – *do you have views on how indemnity and compensation may work for ABS?*

We would welcome the opportunity to participate in the Task Force to be established.

We have two initial observations.

- Page 35 of the Consultation paper provides a summary of our PII arrangements. However, our primary conduct requirement is that firms take *reasonable* steps to meet claims arising from being in public practice. Accordingly many firms will have arrangements well in excess of the figures stated.

- It is vital that PII requirements are not set so that the insurance industry deems them undeliverable or are prohibitively expensive. Our insurance arrangements were developed by working with insurers and while tensions do arise these can be worked through. The imposition of unrealistic arrangements will be counterproductive.

Turning to the detailed points we would make the following comments.

ABS as new entities

We also agree with the comment attributed to the SRA. We so not believe that there is a greater PII risk in an entity merely because it is structured as an ABS. Many of our firms are effectively ABSs already (in that they include non-chartered accountants as principals) and they do not seem to face any greater hurdle to obtaining PII than firms comprising solely of chartered accountants.

Initial principles and individual involvement

Setting levels of PII can in reality only be done by individual firms. They will have a view of the 'risks' posed by their client base and procedures (other than PII) that mitigate those risks.

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Practical implications

Our view is that firms should be required to make appropriate arrangements, part of which includes a minimum amount of PII. It would be entirely wrong for a firm to view PII as an alternative to proper internal quality control procedures.

Larger entities

The larger firms with more diverse service lines would have more PII. However, such firms would also have greater resources and should be allowed to take a larger 'risk' internally by virtue of a differential excess value (the amount which must be paid by the firm before the insurer pays).

Individual position of LAs

For the above reasons, we do not believe that all LAs should set the same PII levels.

Indeed an entity may have different levels of PII for the different activities it undertakes. This can already be seen with the operation of the PII required for insurance mediation activities. This is set at €1.5m (even though we are not in the euro-zone). Some firms will have insurance greater than this. For others, this may be too much, so they have an extension to their policy which increases the PII cover to these limits but only for insurance mediation activities. Provided the activities are well defined this is another option, although it may depend on the willingness of the insurance market to provide the solutions.

A master policy solution?

We see no reason why a master policy should not work for ABSs. However, we would suggest that they are suitable only if the of those firms covered by the master policy are relatively homogenous.

Run off cover

We agree that there should be arrangements for 'run-off' cover when a practice ceases, but they should be flexible.

Our arrangements allow a firm to obtain its own run-off cover, or in the case of a take-over or merger, the continuing practice can include claims arising from the work of predecessor practice on its policy. This is frequently the better solution as the continuing firm will retain the clients (and the client files) and have a continuing interest in speedy resolution of the issues.

Compensation fund issues

The Consultation paper rightly points out that a requirement for a compensation fund will act as a barrier to new licensing authorities and hence to the regulatory objectives of improving access to justice and increased compensation between providers.

We believe, as set out in the Consultation paper, that there are viable alternatives, bearing in mind that the Act requires compensation 'arrangements', not a fund. These could range from prohibiting firms from holding client assets (the loss of which seems to cause the majority of claims on compensation schemes), to requiring an indemnity bond to be held to requiring fidelity insurance. As always, one size does not fit all and there should be flexibility in the permitted arrangements.

Input and experience from Third Category regulators may be useful here to help the debate.

The fact that an entity is an ABS does not automatically mean that it offers multiple service lines. However, this issue already exists in the financial services world. The FSA compensation scheme only covers certain services provided by a firm and then only for certain individuals (large corporate entities

are deemed not to need access to a compensation scheme). These differences would be referred to in the letter of engagement. Any compensation arrangements should take these factors into account.

We would also observe that activities such as preparing the papers to obtain probate do not require the preparer to have unfettered access to the assets of the 'client'. While there would be a need to examine documents of title such as share certificates, there is no need to take possession of physical assets, bank accounts or cash.

Please contact me should you wish to discuss any of the points raised in this response.

Yours sincerely

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