

Client funds in solicitors' accounts in the banking crisis and indemnity requests - a brief guide

Several charities have received letters from solicitors asking for an indemnity in the event, which may now be less likely, of a bank failing to honour deposits.

The Salvation Army has received what appears a more welcome request to advance money early in return for an indemnity.

Responses

Clearly it is not the fault of solicitors that there are concerns about bank solvency. The question arises as to how best to respond in a way that shows willing without compromising your interests.

- Request for indemnity where funds retained

At the end of this note is draft text (which should only be used if appropriate) which we think might be sensible to use instead of signing off on an indemnity where solicitors are still retaining the funds.

- Request for indemnity where offer to accelerate distribution

Where solicitors offer to pay out funds even before the six-month deadline for the issuing of a 1975 Act claim in return for an indemnity it is almost certainly appropriate to review the terms of the individual indemnity.

The risk of course is that if you take the funds but the bank in which those funds are then held 'goes under' the charity is potentially still liable to the executors if they face a claim from any 1975 Act claimant. The suggested text deals with that risk.

Law Society guidance

The position with regard to client funds held in solicitors' accounts is set out in the Law Society Practice Note. The note can be viewed via the website: <http://www.lawsociety.org.uk/productsandservices/practicenotes/bankingcrisis/1310.article>

The advice below is based on the current guidance. Please note that the guidance is being updated constantly, so please do not rely on this advice without checking for further updates.

In summary, solicitors are allowed to limit their liability for funds lost through banking failure, provided that they do so in a way that is consistent with the Law Society's guidelines and code of conduct.

Before accepting any limitations on liability it may be prudent to establish:

- Are the funds held in an authorised financial institution in accordance with the Solicitors' Accounts Rules - i.e. are the funds held in a bank or building society in England and Wales which has FSA authorisation to accept deposits?
- Is the firm aware of any issues which affect the credit worthiness of this institution? Solicitors do not have to have 'inside information', but it is reasonable to expect them to be aware of information which is in the public domain.
- Whether any proposed limitation of liability is in accordance with the Solicitors' Code of Conduct?

This means that, as well as bringing the proposed limitation clearly to your attention in writing, the solicitors should confirm that the limitation of liability does not breach the minimum standards of cover set out in the Solicitors' Professional Indemnity Insurance Rules.

To avoid complicated correspondence we suggest text for a standard response below.

Background – FSCS guarantees

The Financial Services Compensation Scheme ('FSCS') guarantees that in the event of a failure of a UK regulated bank, individual depositors will have their deposits guaranteed up to a maximum value of £50,000. This applies to funds held by solicitors on behalf of clients, provided that they are held with a UK regulated institution (which will almost certainly be the case).

If a solicitor is holding funds for a client on a number of matters, the total amount of funds held may be more than £50,000. It is likely that all of those funds will be held in the same bank. If this is the case, then even though the funds are related to separate matters and may be in separate accounts, they will be aggregated towards the £50,000 limit. If this situation applies, you may wish to discuss moving some funds to other regulated institutions so that the limit is not breached.

Single deposits in excess of £50,000 are not guaranteed. Neither are smaller deposits with an aggregate value of more than £50,000 held within the same institution or group. Currently the only way which they may be recovered in the event of the collapse of a bank is via the usual insolvency procedures. You are unlikely to receive all of the missing funds if this proves to be the case.

In certain circumstances funds may be held in a foreign bank. If this is the case, you should confirm that the solicitor has made appropriate investigations as to the status of the foreign bank and any applicable compensation schemes. Please note that the FSCS does not apply in the Channel Islands or the Isle of Man.

We understand from the FSCS that individual trusts each benefit from the £50,000 guarantee.

If there is a bare trust (which is the case if funds have been appropriated and are held by the executors as bare trustees for the charity) the funds will be deemed to belong to the charity and aggregated with any other funds held by the charity within the same institution or group.

We understand from the FSCS that individual estates each benefit from the £50,000 guarantee.

Suggested text responding to request for indemnity where solicitors are retaining funds

Dear Sirs

Thank you for your [insert date] letter [requesting an indemnity in the event that funds are lost as a result of bank failure].

We understand that the Law Society has issued detailed guidance. In view of that guidance we agree that your firm and the executors should not be liable in the event of a bank failure provided:

1. The funds are held in an authorised financial institution in accordance with the Solicitors

Accounts Rules; and

2. Your firm complies with the Law Society's guidance generally.

We hope this is helpful and trust that the concerns giving rise to the correspondence do not in fact materialise!

Yours faithfully

Suggested text responding to request for indemnity where solicitors propose early distribution

Dear Sirs

Thank you for your [insert date] letter [offering to distribute estate funds ahead of the six-month deadline for a 1975 Act claim in view of concerns about bank solvency].

We agree that we will indemnify the executors against the risk they run of personal liability to any 1975 Act claimants by distributing ahead of the six-month deadline for the issuing of a 1975 Act claim. The indemnity is limited to the amount we receive [and our proportion of the distribution].

The charity cannot be bound by the indemnity in the event of a 1975 Act claim if the institution in which we invest the distribution is unable to pay out. Obviously, we would expect you to notify us promptly if you are notified of any intended claim.

We hope this is helpful and trust that the concerns giving rise to the correspondence do not in fact materialise!

Yours faithfully

Please contact Paul Hewitt (Tel: 020 7597 6197 or email: paul.hewitt@withersworldwide.com) or Sue Medder (Tel: 020 7597 6196 or sue.medder@withersworldwide.com) if you have questions on individual indemnities as the above is guidance only.