



## Marsh Specialty

# Coping with the cost and effort of professional indemnity:

- Focus on what you can change
- Accept what you can't

John Kunzler,  
Risk and Error Management



## 1. Things that are hard to change - errors and root causes in law firm claims:

- Claims and premium trends in Solicitors PI England & Wales and Ireland
- Pandemic impact?
- Ransomware challenge
- More questions?
- Errors and Root causes

## 2. Focus on what you can Change 1 – tools to tackle root causes

- Retainer letters
- Collaborative review
- Conflict Management and independence
- Being realistic about Human Factors

## 3. Focus on what you can Change 2 - How to appeal to underwriters as a stand out firm

- Strategic choices and consequences – work undertaken and risk profiles
- Enterprise Risk Management – what is it and how difficult is it to do?
- Importance of Management Information and data
- Evidence trails on key risk management areas – retainers and audit actions

Appendix – Cyber risk scenarios

# Contents

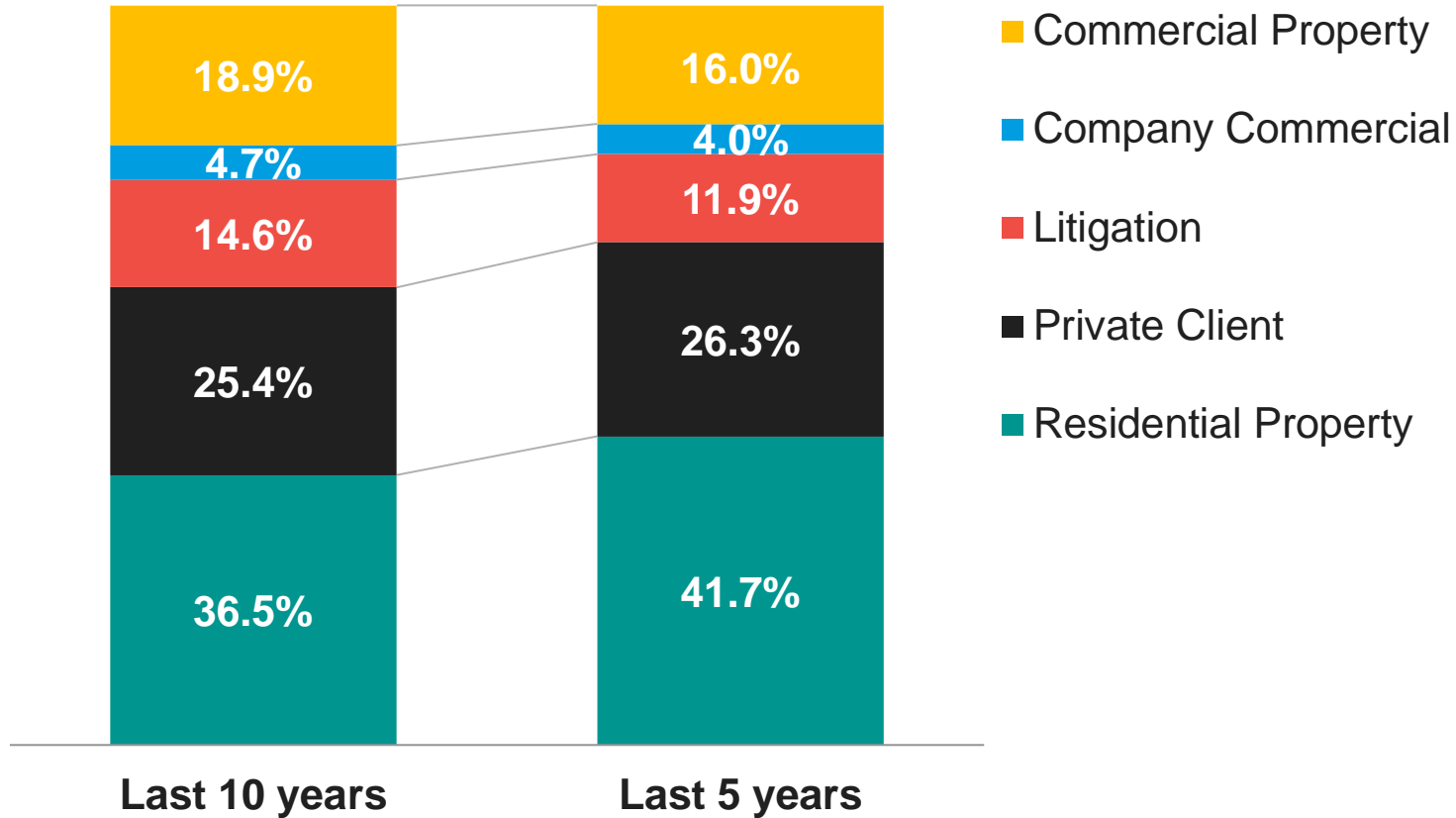
**Things that are hard to  
change -**

**Errors and root causes  
in law firm claims**



# Frequency by work type England & Wales

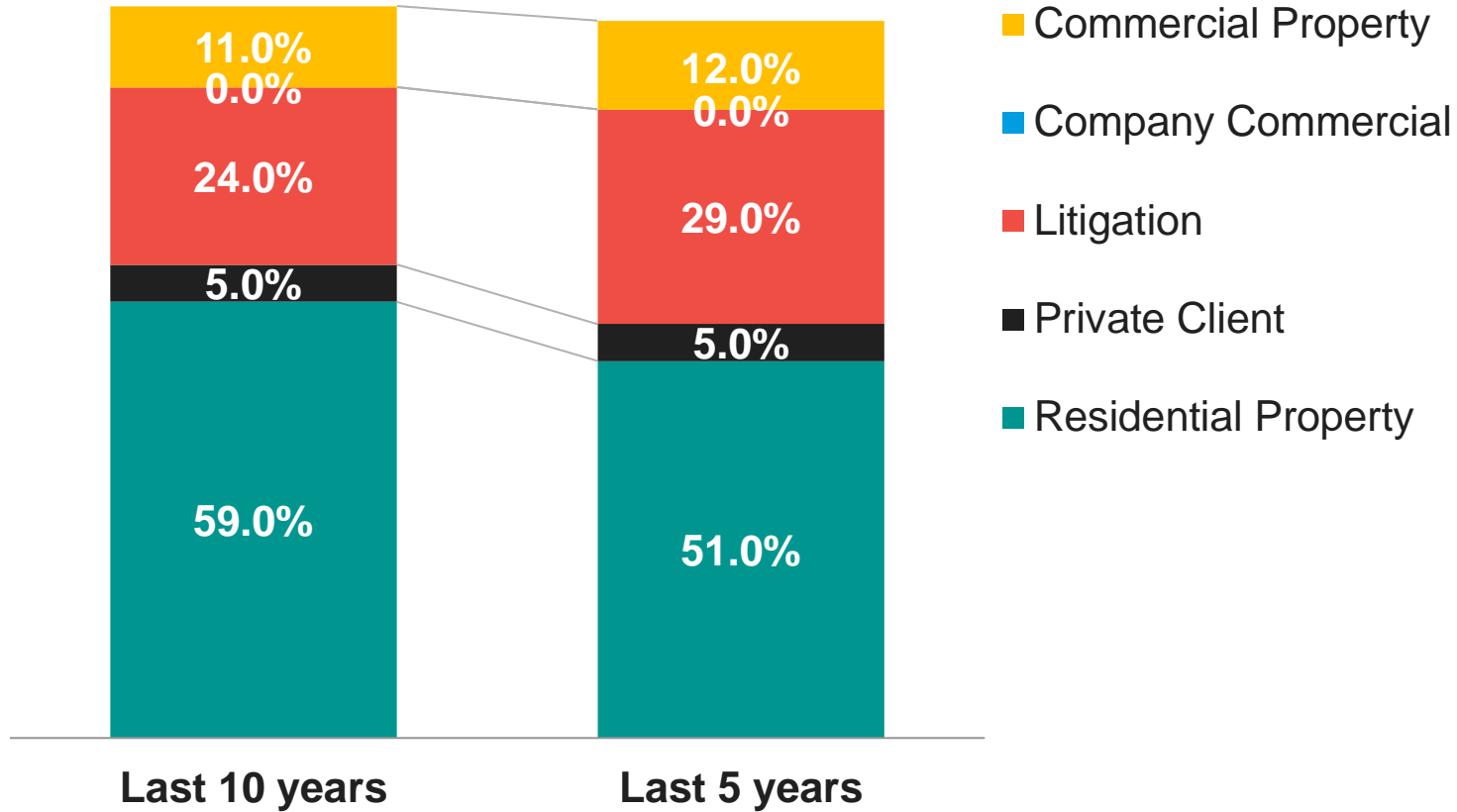
Period to 2020 comparison (excluding <4% disciplines)



**Minimal changes in frequency between work type.**

# Frequency by work type Ireland

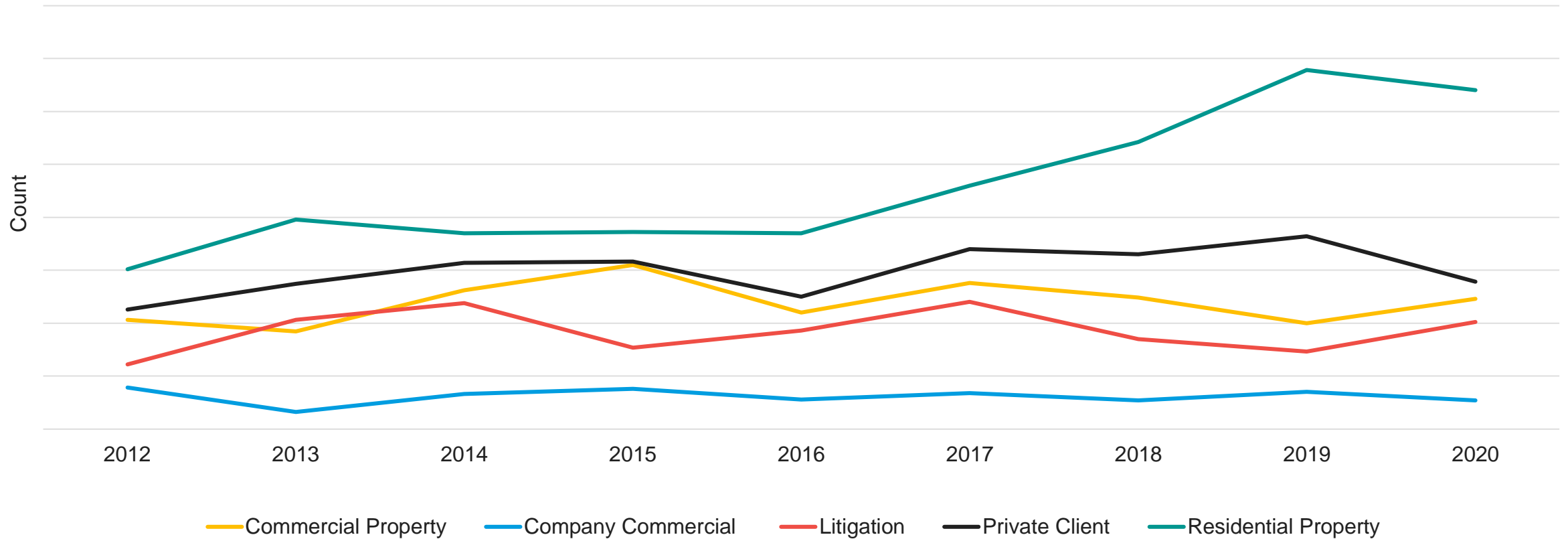
Period to 2020 comparison (excluding <4% disciplines)



**Residential Property claims down, Litigation somewhat higher**

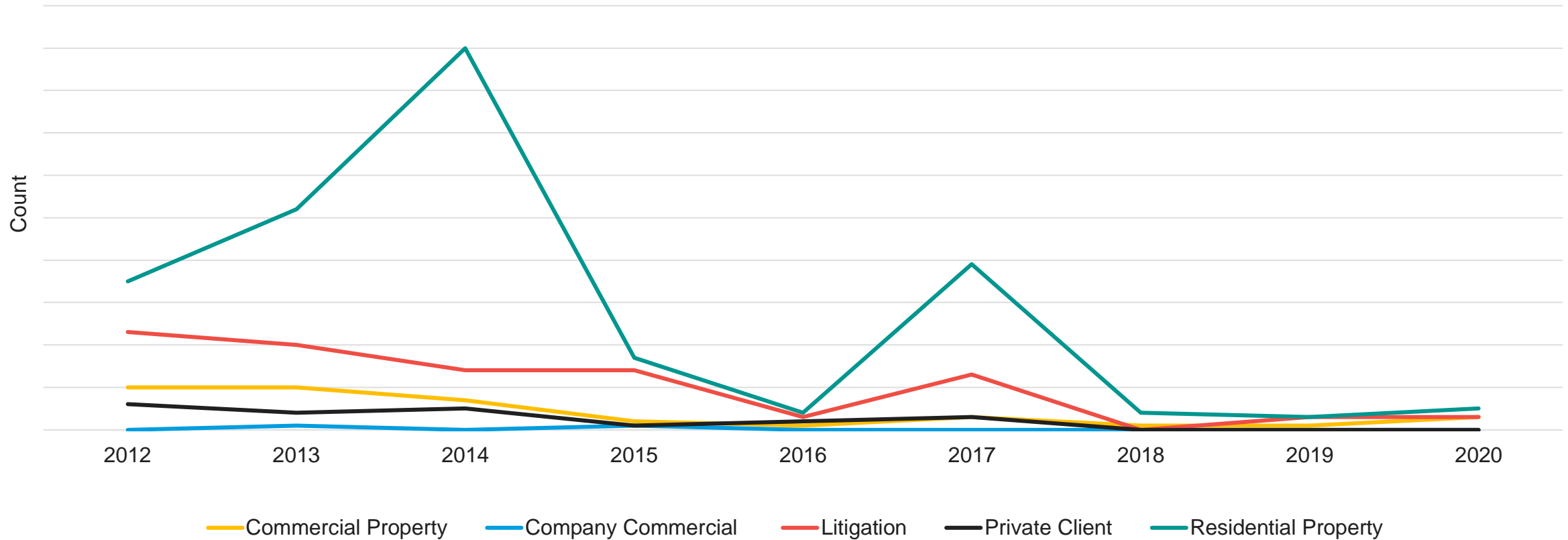
# Frequency by work type – England & Wales

Trend 2012 to 2020



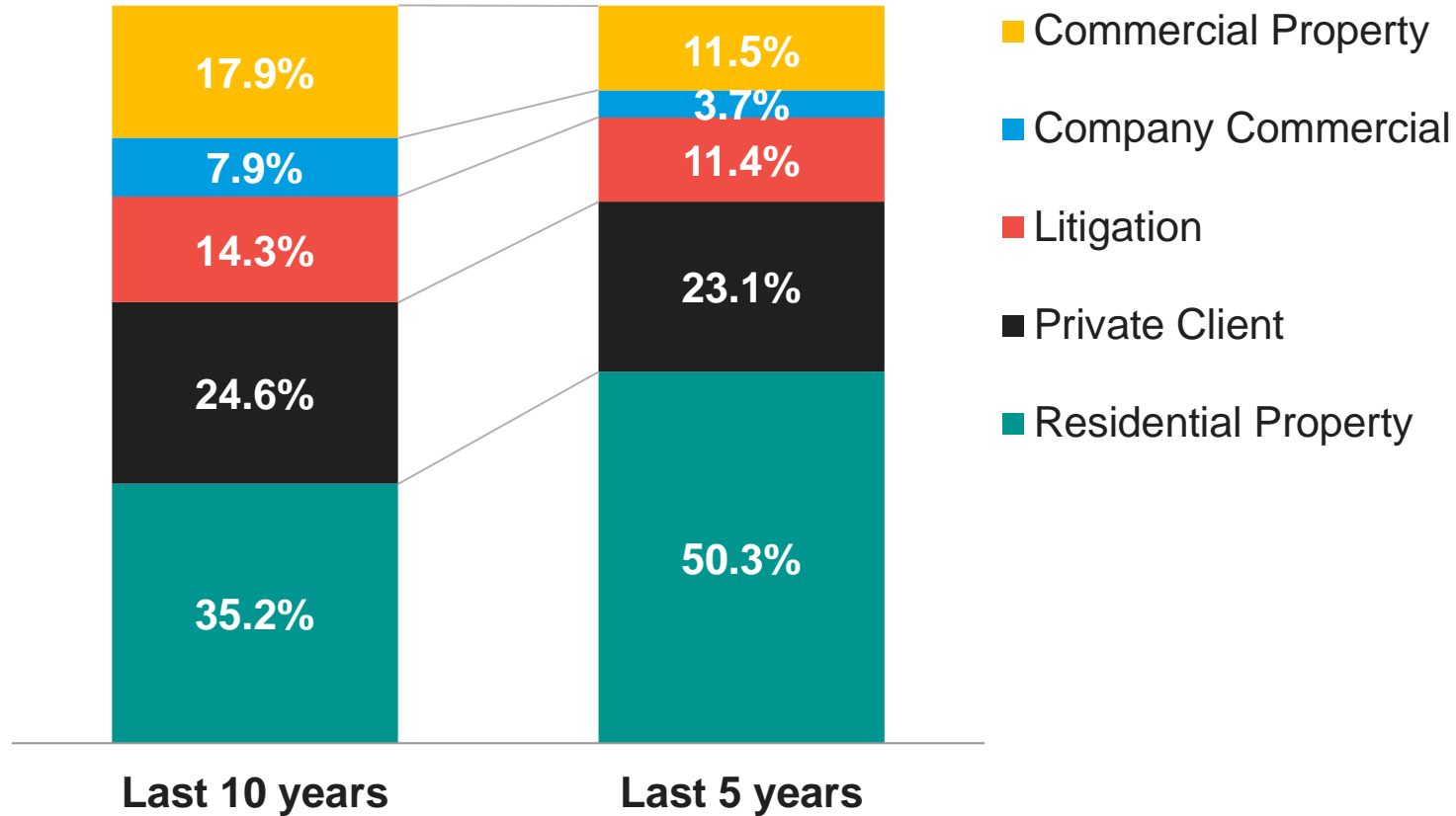
# Frequency by work type – Ireland

Trend 2012 to 2020



# Severity by work type – England & Wales

Period to 2020 comparison (excluding <4% disciplines)



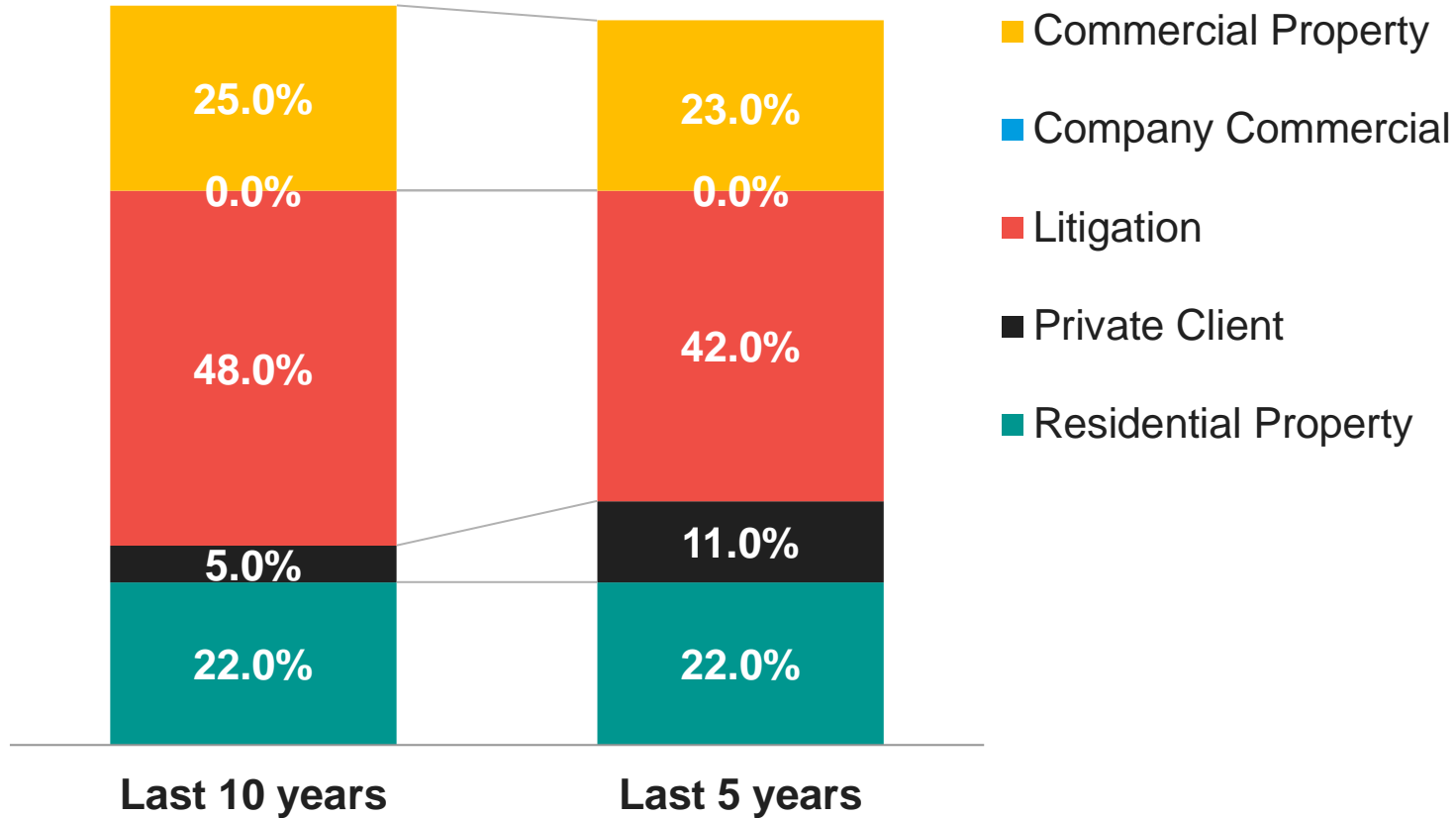
# 15%

increase in severity  
of residential  
property losses.



# Severity by work type Ireland

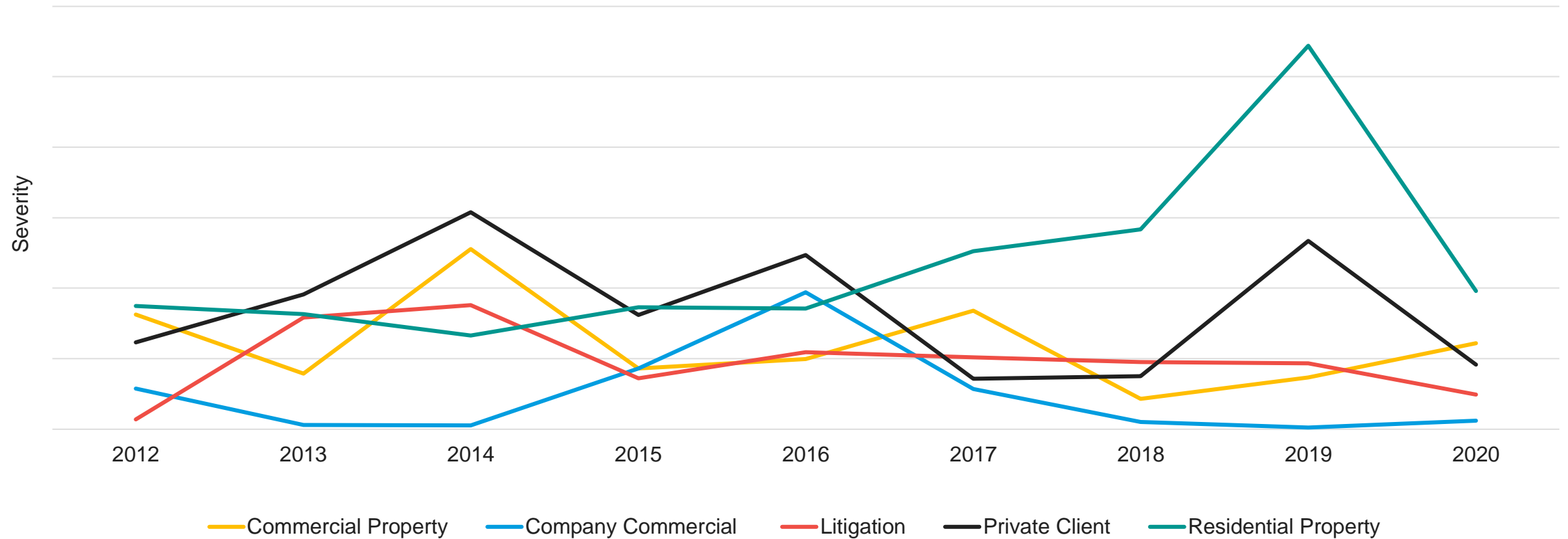
Period to 2020 comparison (excluding <4% disciplines)



**Smaller changes in frequency between work type. Trust & Probate up**

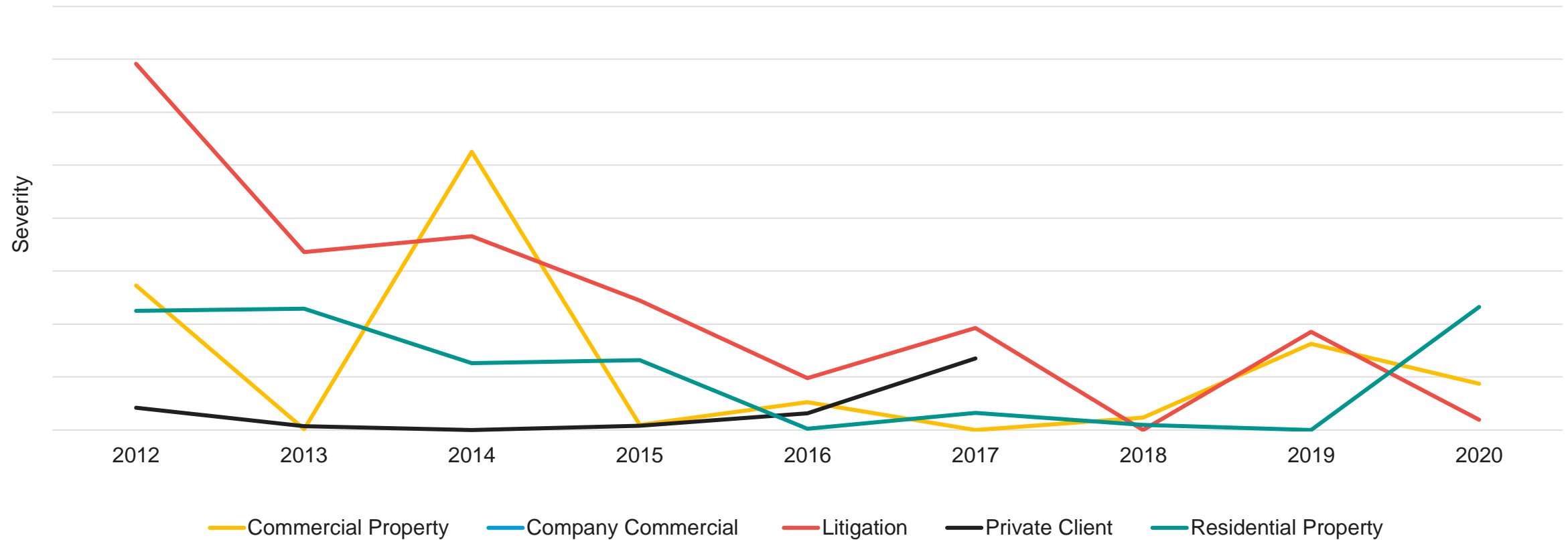
# Severity trend by work type – England & Wales

Trend 2012 to 2020



# Severity trend by work type – Ireland

Trend 2012 to 2020





# Residential property years E+W 2019-2021\*

## Closer analysis



Stamp Duty Land Tax (SDLT) 'holiday' notifications not forthcoming as feared. Only a couple of standalone cases where it was thought maybe other mistakes had occurred due to associated pressures.



2019/2020 saw a number of ground rent notifications. 2020/2021 saw a slight increase in 'Title' errors e.g. failing to ensure full title transferred/transferring the wrong part of land.

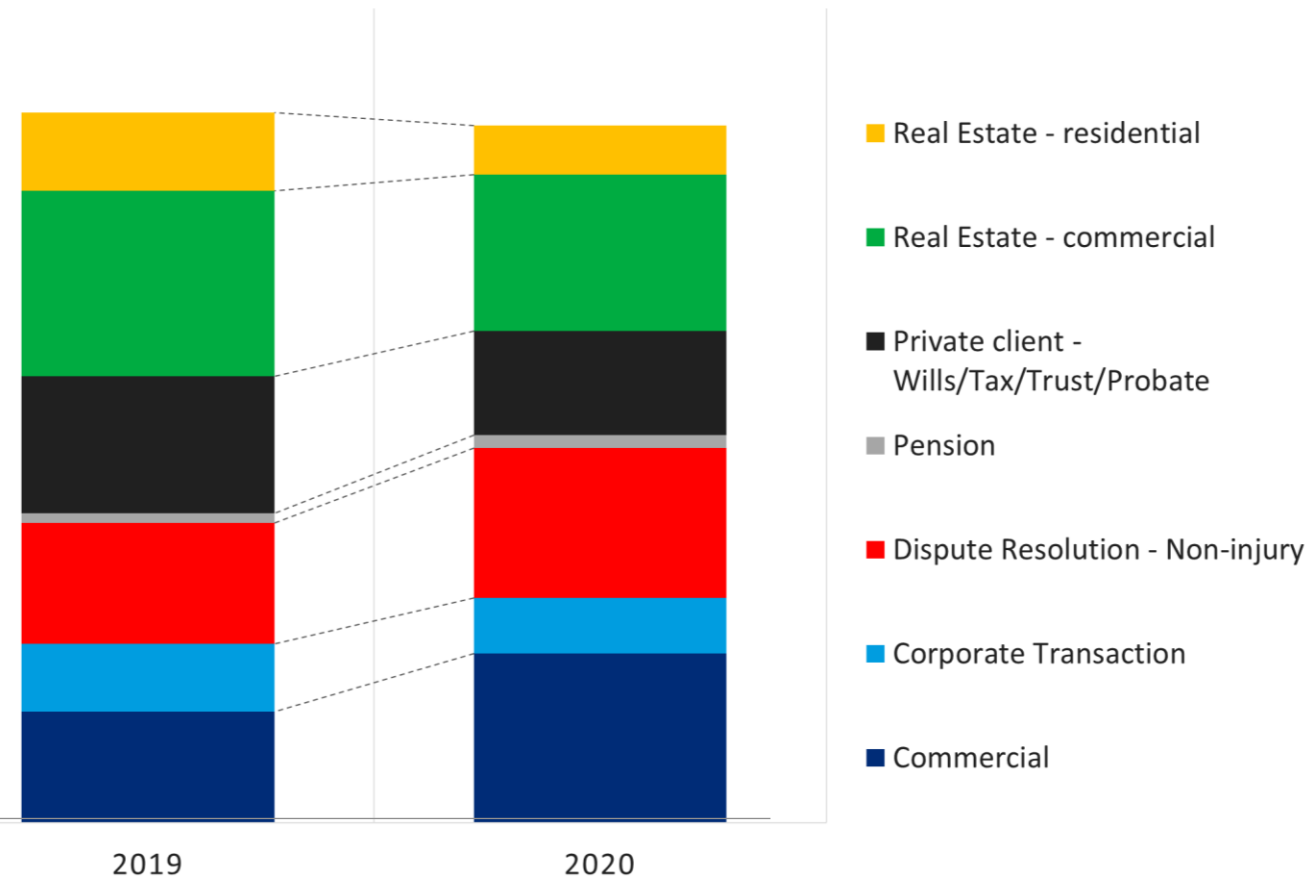


Significant number of notifications linked to 'Incorrect advice', followed by 'defective drafting' and 'inadequate communication'. When analysing 'inadequate communication' errors appear to be more mistakes as to law as opposed to slips or lapses.

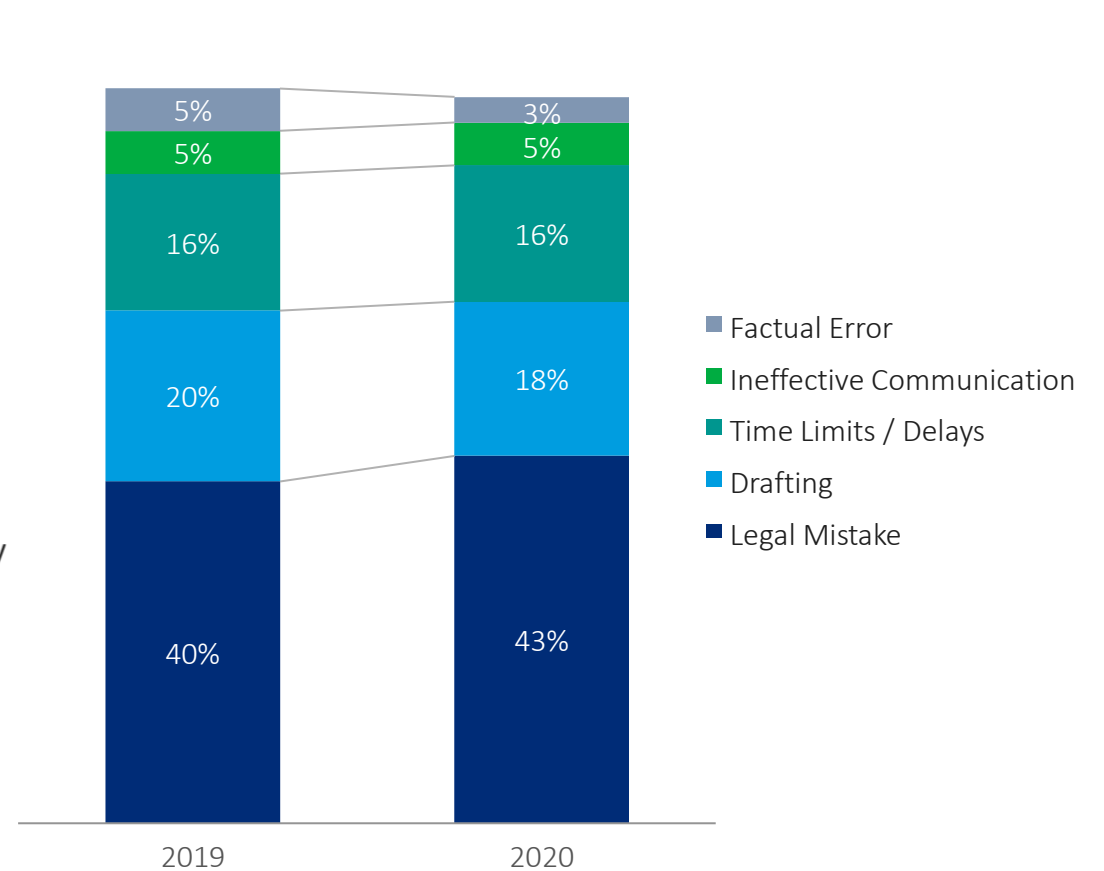
# Pandemic impact?

# Claims notification trends E + W – pandemic impact? (Ireland figures too low to analyse)

**Core work types and errors claims bare frequency**  
Claims notification frequency 2019/2020 and 2020/2021



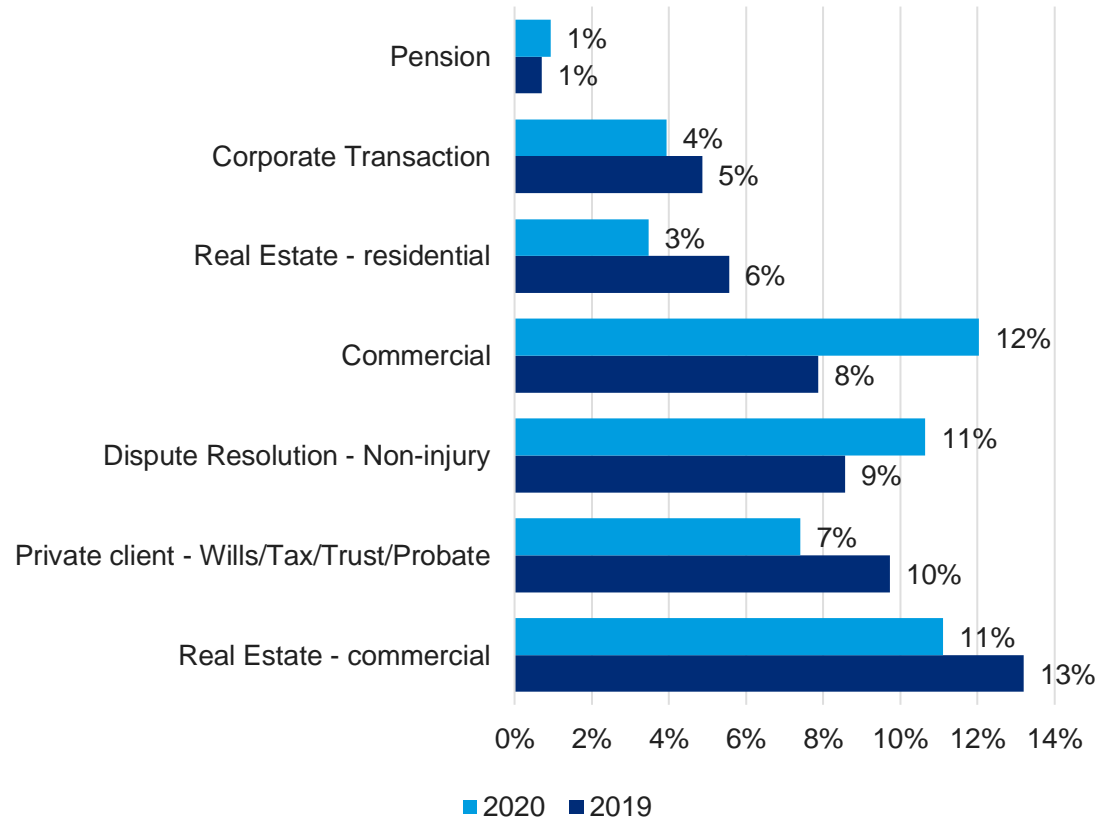
**Analysis of notifications**  
24 March to 1 October – 2019 and 2020



# Error type trends – pandemic impact? (Ireland figures too low to analyse)

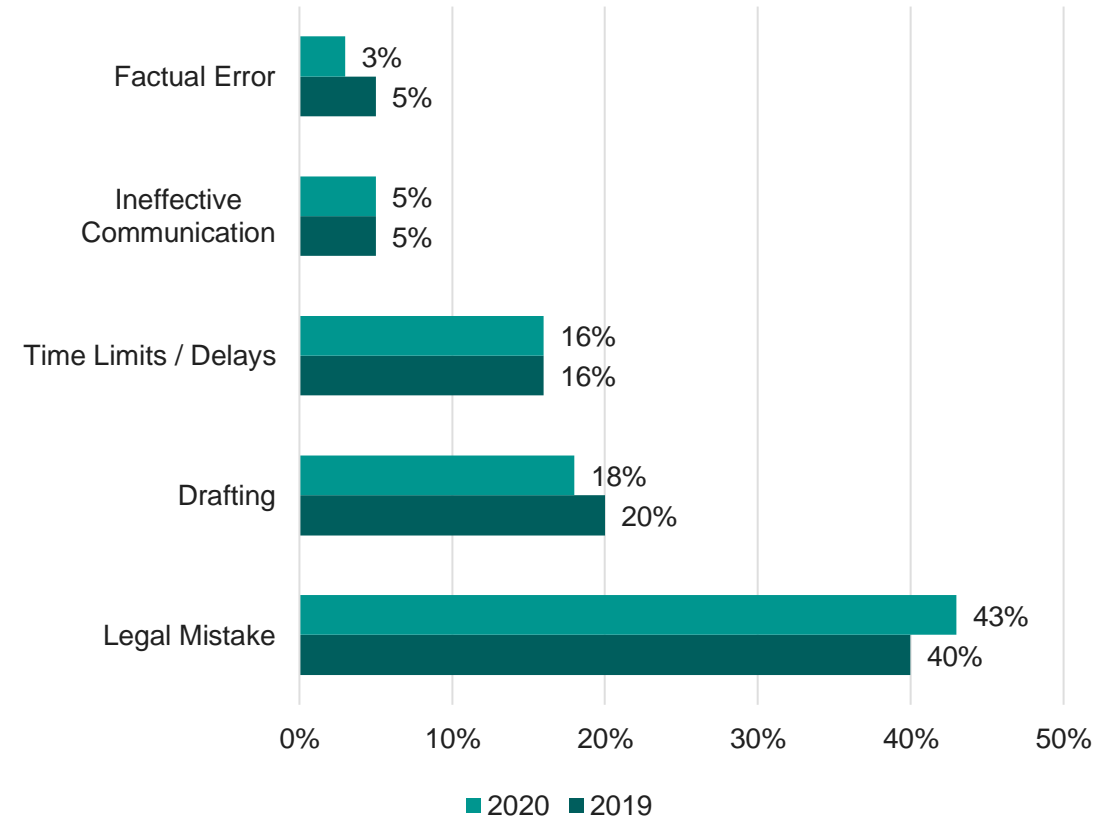
## Core work types and errors

Claims frequency 2019/2020 and 2020/2021



## Analysis of notifications

24 March to 1 October – 2019 and 2020



# Ransomware challenge



# Ransomware challenge - Ireland

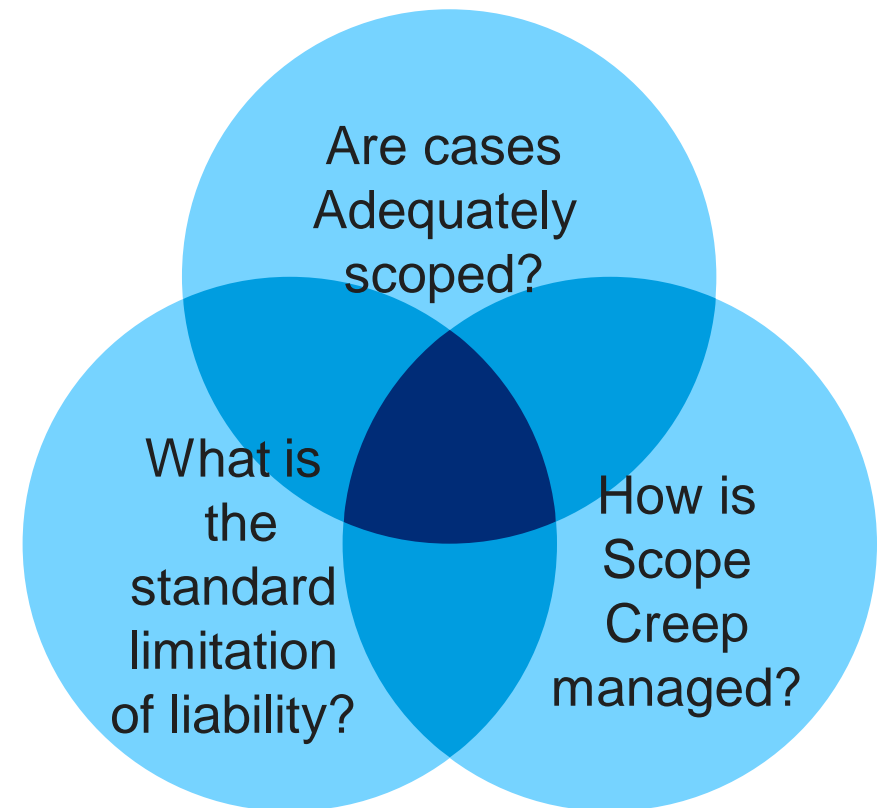
- Over the last 5 years anecdotally we understood there were fairly limited Cyber attacks on Irish firms compared with England & Wales – however 2017 reports suggest the 20 largest firms experienced increasing (60%) attacks in twelve months (<https://www.independent.ie/business/technology/cyber-attacks-on-countrys-top-20-magic-circle-law-firms-surge-60pc-36334838.html>).
- More recent reports suggest 30% of all Irish businesses have been hit by attacks.
- The Law Society has continued to receive reports of successful cyber-attacks:
  - Compromised email systems.
  - Interception of Funds.<https://www.lawsociety.ie/News/News/Stories/cyber-security---mitigating-the-risks>
- Guidance on Cyber security published including ransomware.
- Ransomware risk has changed.

**More questions?**

# More questions - Renewal preparation

## Hints and Tips

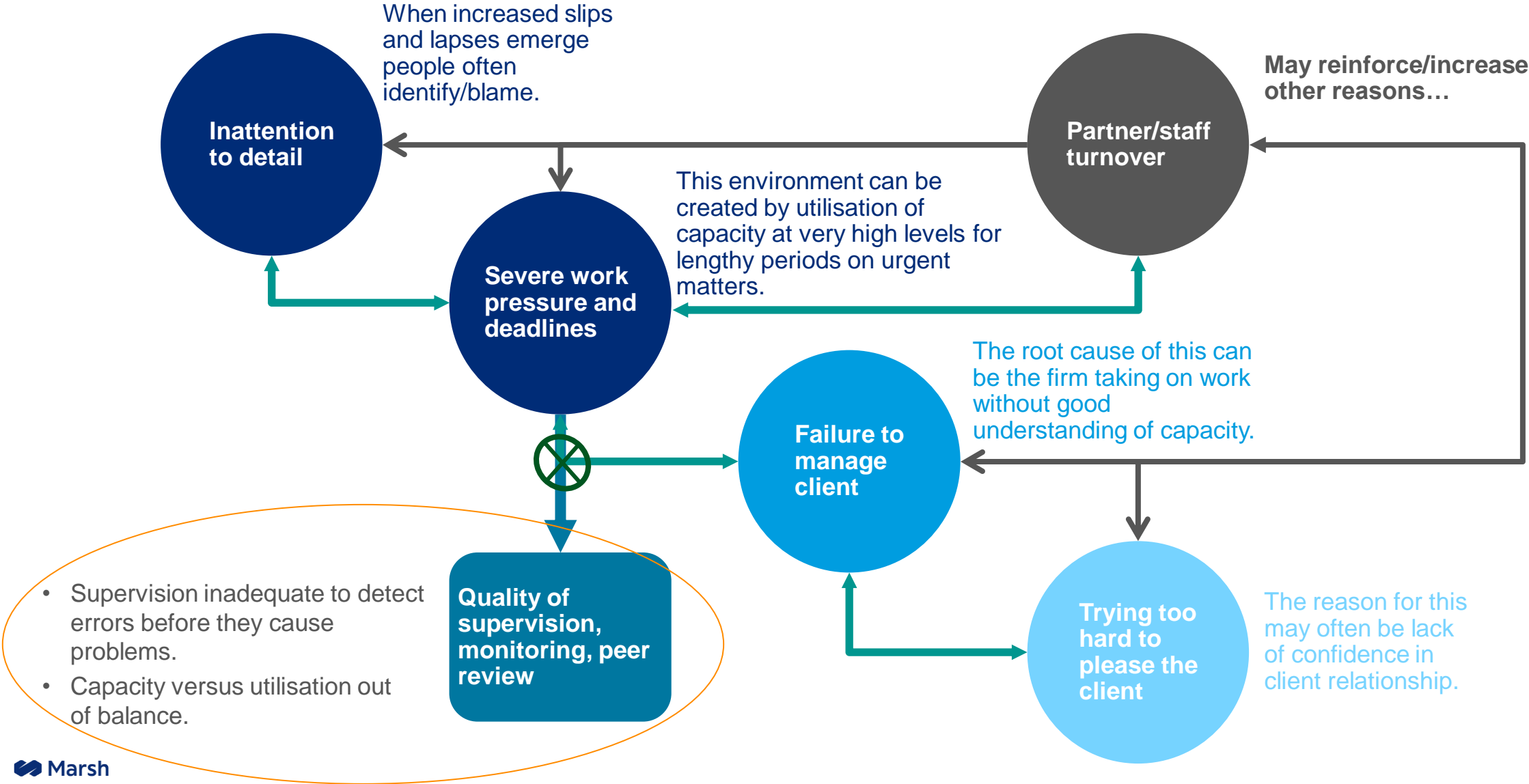
1. Find out the “new” excess layer underwriter questions (almost all of which are driven by paid losses or world events (e.g. sanctions) early, and work out any data collection requirement.
2. Fee growth in conveyancing, probate and commercial is likely to push up pricing from underwriters more than litigation and family due to claims size and/or frequency.
3. Law Society website explains which brokers are exclusive (Marsh deals with 5 of the 7 insurers). Take care that the same underwriter does not see your application from multiple brokers.
4. More questions on retainer letters over the last year or so:



# Root causes of error

# Root causes of error – insights

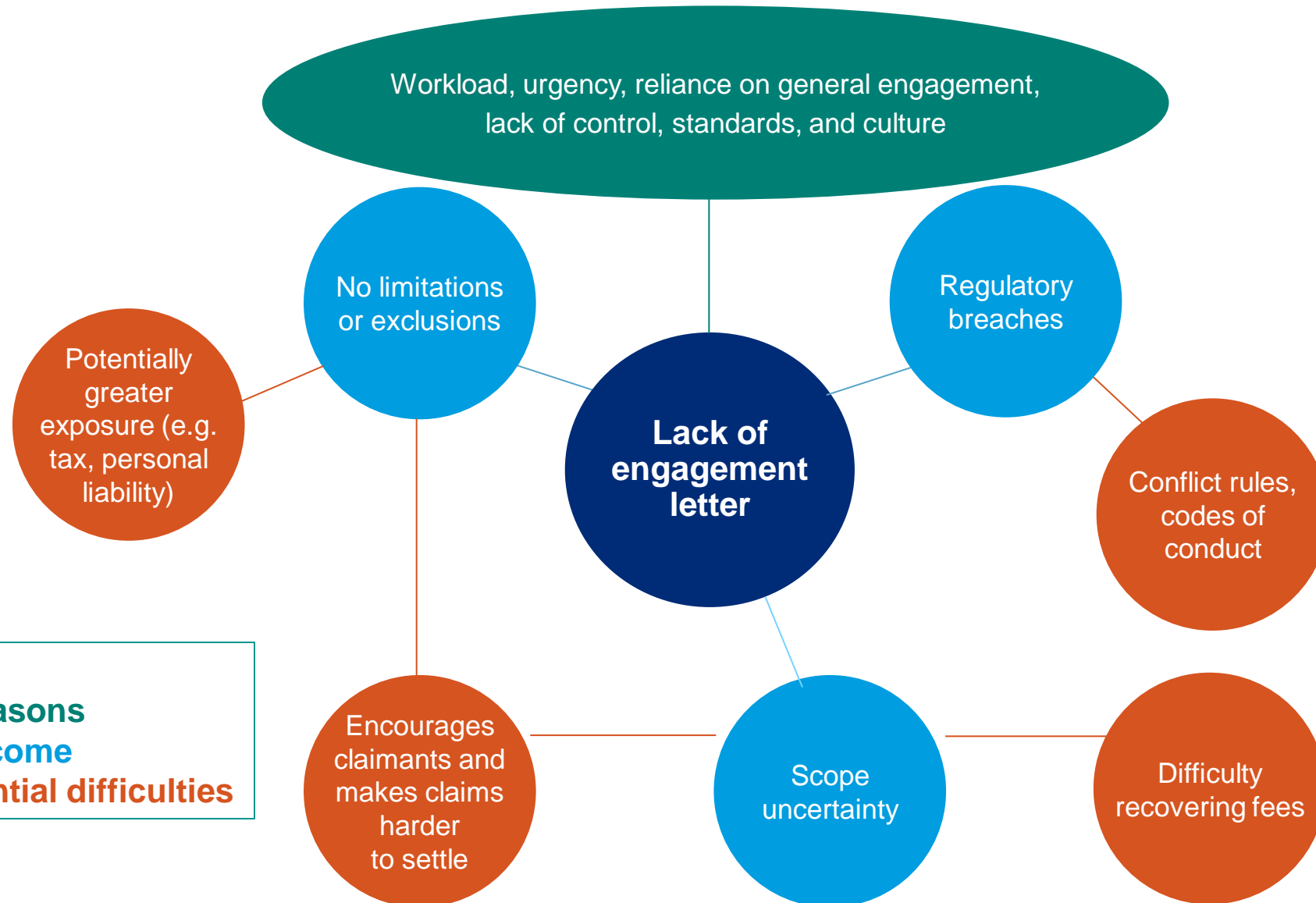
Are the reasons for errors interlinked?



**Focus on what you can  
change 1 – tools to  
tackle root causes**

# Retainer letters

# Lack of retainer letter and claims



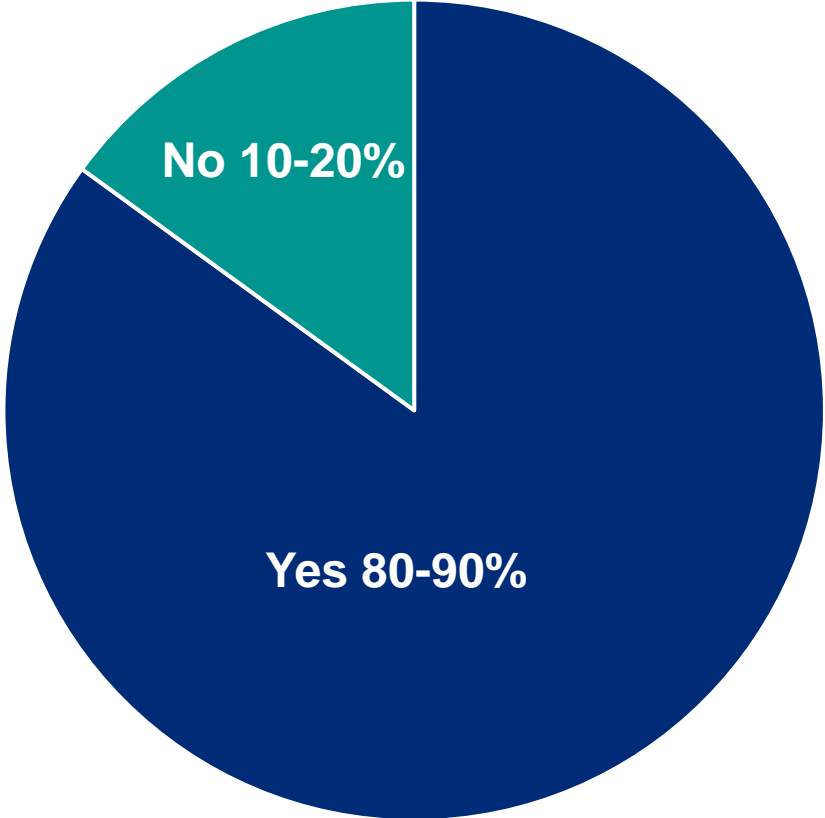


# What proportion of files have a fully scoped retainer letter?

Last 24 months

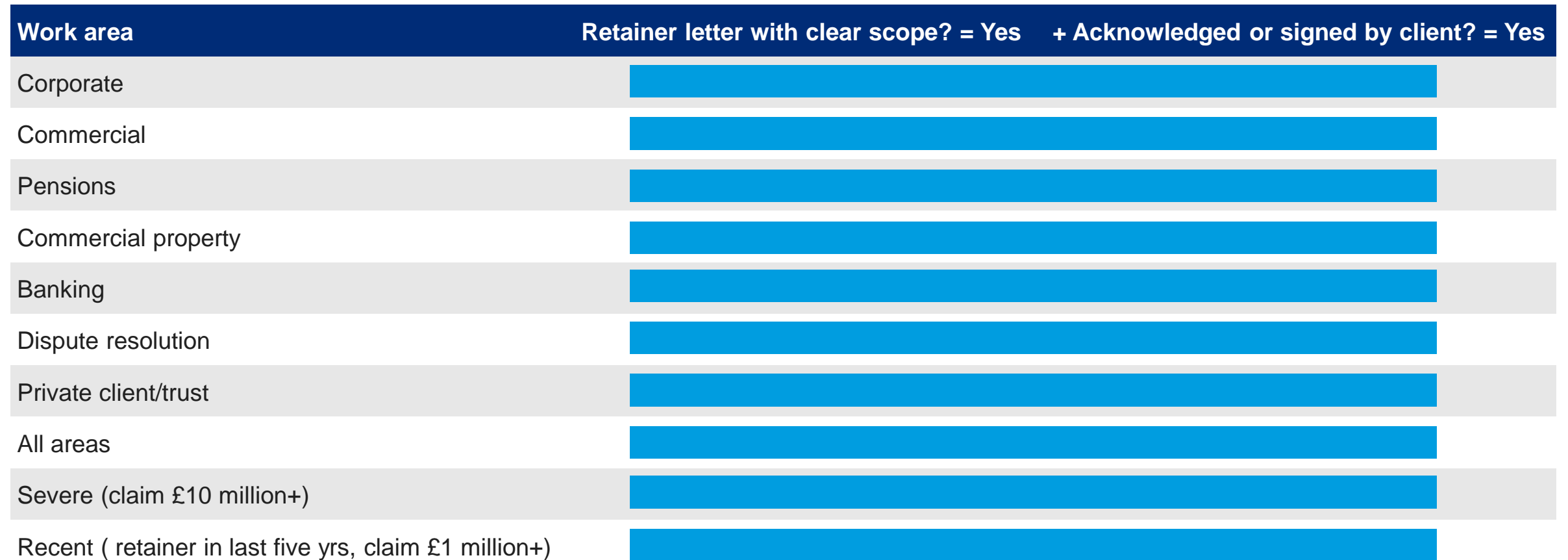


## What we hear from law firms:



# Survey of claims files with panel firms

## Work areas and retainer/scope documentation



# Retainer letters – case law

Extent of economic loss

Risk of retainer drift

# Extent of economic loss

## *Manchester Building Society (MBS) v Grant Thornton (GT) UK LLP<sup>1</sup>*

### Facts

- MBS sold fixed interest “lifetime” mortgages.
- To hedge the business risk from variable interest rates, MBS entered into long-term swap contracts.
- In 2006 GT incorrectly advised MBS that its accounts could be prepared using a method called ‘hedge accounting’, reflecting the value of the swaps. On this advice, MBS entered into a series of further swaps.
- In 2013 GT became aware its advice was wrong.
- MBS had to restate accounts, which showed reduced assets and insufficient regulatory capital. MBS was required to close the interest rate swap contracts early at a loss of £32 million.
- Supreme Court needed to decide if MBS could receive £32 million cost of closing contracts early.



# Extent of economic loss

## *Manchester Building Society (MBS) v Grant Thornton (GT) UK LLP<sup>1</sup>*

**Outcome:** SC ruled in favour of MBS.

The key question of law in cases involving all professional advice was to focus on:

- The “purpose” of the advice or information.
  - The “risk” this advice was intended to protect against.
- The purpose of the advice here was to advise whether MBS could use hedge accounting to reduce volatility on its balance sheet and pursue its intended business model. If the advice was wrong, the swaps wouldn’t serve the intended purpose, and MBS would be exposed to the risk of having to close the swaps.
  - This happened and, thus, the losses suffered by MBS exiting the swaps was within the scope of duty and recoverable.

**A clear retainer letter creates a good record of the purpose and risk – having no record makes life easier for the claimant.**



# Retainer Drift: Whelan & Ors v Allied Irish Bank Plc & Ors<sup>1</sup>

## Facts:

Mr Lynch + family jointly purchase land plot with Mr Conlon.

Execution and acceptance of a facility letter for €25M by AIB and execution of a charge over land.

Different Firms Acting with different retainers:

- **LK Shields ‘LKS’**: Lynch family (Mr Lynch usual solicitors). Advice on co-ownership agreement terms.
- **Matheson Ormsby Prentice ‘MOP’**: Mr Conlon (usual solicitors). Deal with conveyancing and drafted co-ownership agreement.
- **Ernst & Young ‘E&Y’**: Lynch family. Advising on tax. Indicated to MOP that Lynch family should be owners and named on facility letter.

- MOP retainer initially with Mr Conlon (generally).
- Ultimately, Lynch family named as co-owners and paid 50% of MOP fees.

# Retainer Drift: Whelan & Ors v Allied Irish Bank Plc & Ors<sup>1</sup>

## Claim:

### Mr Lynch and Lynch Family claims:

- Believed loan was non-recourse beyond value of the land. Would not have proceeded otherwise.
- Entirely reliant on LKS (third defendant) for advice in relation to all aspects of the loan transaction.
  - MOP owed them a duty to advise on the terms of the loan and changes.

### LKS claim:

MOP negligently misled them as to the terms of the loan.

# Retainer Drift: Whelan & Ors v Allied Irish Bank Plc & Ors<sup>1</sup>

## Findings:

- Final terms of loan facility received by MOP from AIB made the loan clearly full recourse. MOP sent new wording to LKS.
- LKS misunderstood and did **NOT** advise Lynch family that the loan was full recourse.
- MOP had **NOT** flagged that loan wording changed or that it was full recourse, but:
  - No express instruction by Lynch family to MOP or LKS that had to be non-recourse.
  - Loan facility was at all times a recourse loan.
  - No direct contract between MOP and Lynch family prior to completion.

- LKS retainer changed and broadened. Extended without any specific retainer to pass information communicated by MOP in relation to facility letter.
- MOP retainer – even if not part of retainer MOP **would** be negligent **if**:
  - Informed by AIB that clause removal made loan full recourse and was aware this important to Lynch family, or
  - MOP thought new version changed loan from non-recourse to recourse.



# Retainer Drift: Whelan & Ors v Allied Irish Bank Plc & Ors<sup>1</sup>

## Held:

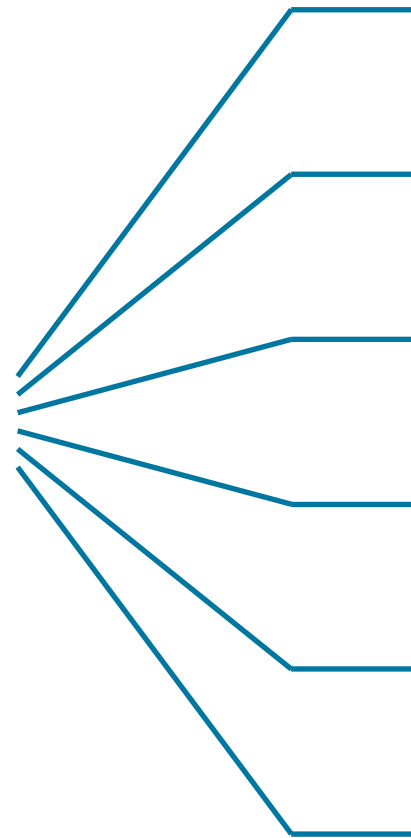
- Change to drafting did not alter what was always a recourse loan.
- No instructions to MOP that only a non-recourse loan was acceptable.
- None of the firms had overall responsibility to advise the Lynch family.
- MOP had no overall duty to tell LKS of the changes made and their impact.
- MOP's duty was discharged by passing the information to LKS .

- LKS were in breach of duty. Provided incorrect information to Lynch family.
- BUT no reliance on error in entering loan agreement.
- No loss - MOP not liable.

# Lessons Learned?

## Changes to retainer

- New parties
- Variations
- Extensions



Clearly identify changes

Beware Clients with different levels of sophistication

Revisit advice – what is purpose?

Review conflict

Consider exclusions

Who is relying on advice?

# Recommendations

ACTION



Provide scoping letters on all matters and periodically review.

At the end of a matter review the retainer letter.

If you want to improve:  
Consider league tables between departments.

# Collaborative Review

# What Do we Mean by Collaborative Review?

- Group review of work output – drafts, opinions, strategies.
- Increased value in current environment – risk, people management, and morale.
- Recording such meetings is a simple way to create evidence of supervision and of effective review.
- Often found in “pockets” – based on local leadership preference which may be difficult to change.
- Marsh survey indicates most Top 10 firms (88% of sample) are using Collaborative Review.\*



\*Source: Marsh JLT Specialty Top 10 Supervision and Collaboration Survey October 2020

# Driving Best Practice – Promoting Wider Adoption (1)

Why now?



**Dovetails with most firms' existing culture and supports remote working.**



**Already successful in risk improvement** in aviation and medicine.

“Team discussions which focus on threats and errors before and after team activities can be an important part of safety.”\*



**Demonstrates risk improvement and change** – aligning (best) practice across the firm consistently.



**Aligns with stakeholders**

- Large corporates (e.g. insurers) have implemented collaboration requirements to mitigate risk.
- SRA looking at supervision.
- Underwriters identify “silo” working/reduced communication as risk to quality/wellbeing.

\*Helmreich and Wilhelm (1991) in Nemeth C.(2008) Improving Healthcare Team Communication

## Supervision and Collaborative Review (CR) - Summary of Survey Results

(45 firms in the UK Top 100 responded)

- **62%** of the firms have given specific training to supervisors or altered systems/controls to collect evidence of supervision or were already doing so.
- **91%** of the firms consider CR may at least to some degree reduce the risk of errors compared with partner sign-off (however, **40%** of the yes group consider it impractical to use on every matter).
- **60%/88%** of the firms regularly use CR involving **25%** or more of the firm's practitioners.
- **58%** of the firms consider CR could play a significant role in achieving good remote supervision, with a further **35%** considering it might.
- **53%/87%** of the firms have procedures requiring (**29%/37%**) or encouraging (**24%/50%**) CR or a similar type review.

# Conflict Management and Independence



# Case studies - Client/conflict management – common themes

## Common Themes - scenarios

Tail end of long relationship. Focus is on serving key individual	Accountability/oversight of partner weak.	Failure to exercise independence.
Transaction/assets value: usually £2M-150M.	Dishonesty/misfeasance by individual client/director/trustee. Dishonesty and knowing assistance often alleged against the firm.	No previous ethics concerns about individuals.
Often commercial but can easily be private client, tax or litigation.	Clients often Trustees or individual director or ultra high net worth individuals with little oversight.	Client and own interest conflicts.

# Outcomes from getting conflict wrong - client/conflict management

## Common Outcomes for Firms and Individuals

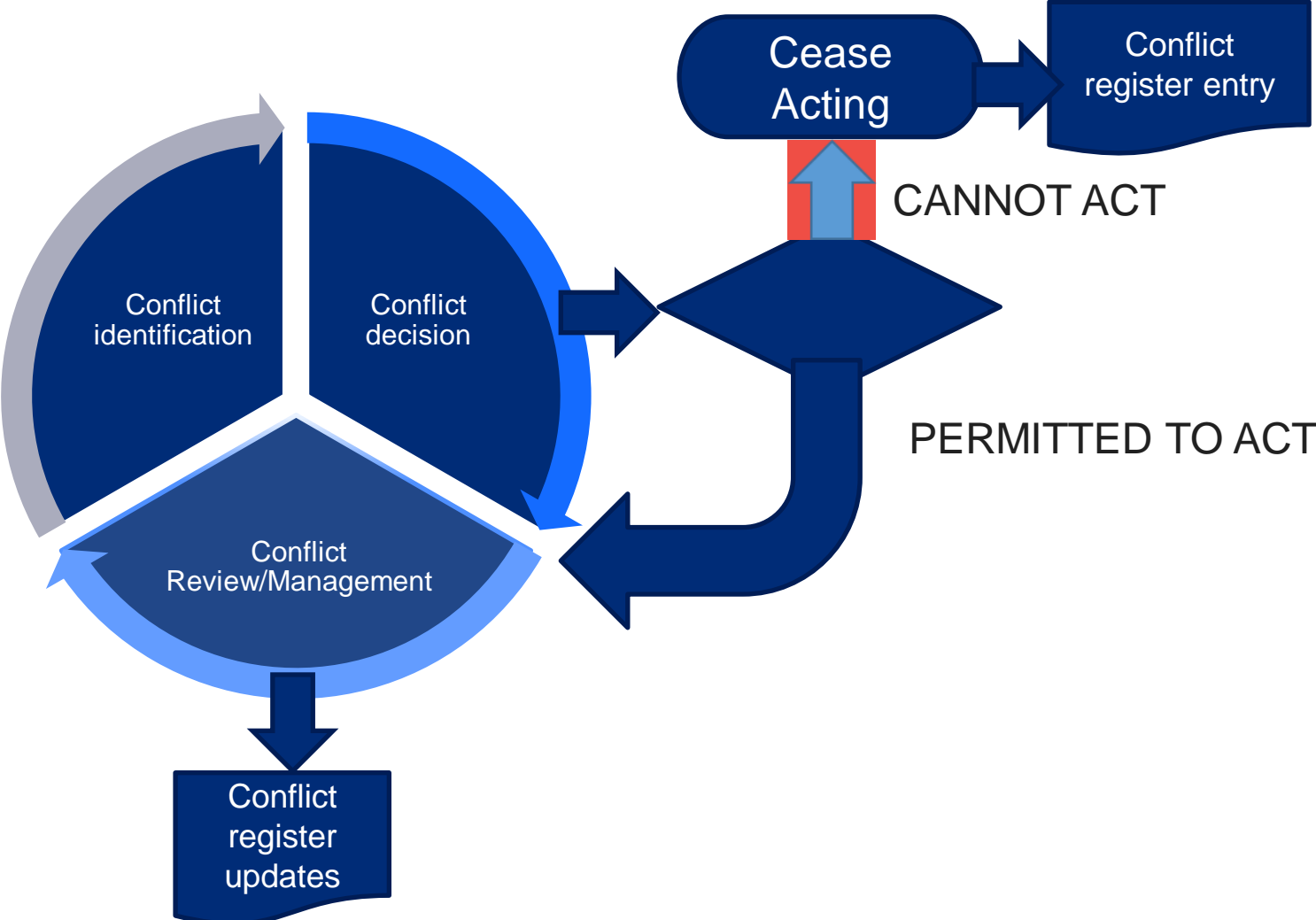
Claims which develop are large (usually £1M+), newsworthy and painful to manage.

Internal and external reputation may suffer as processes/judgement/integrity examined.

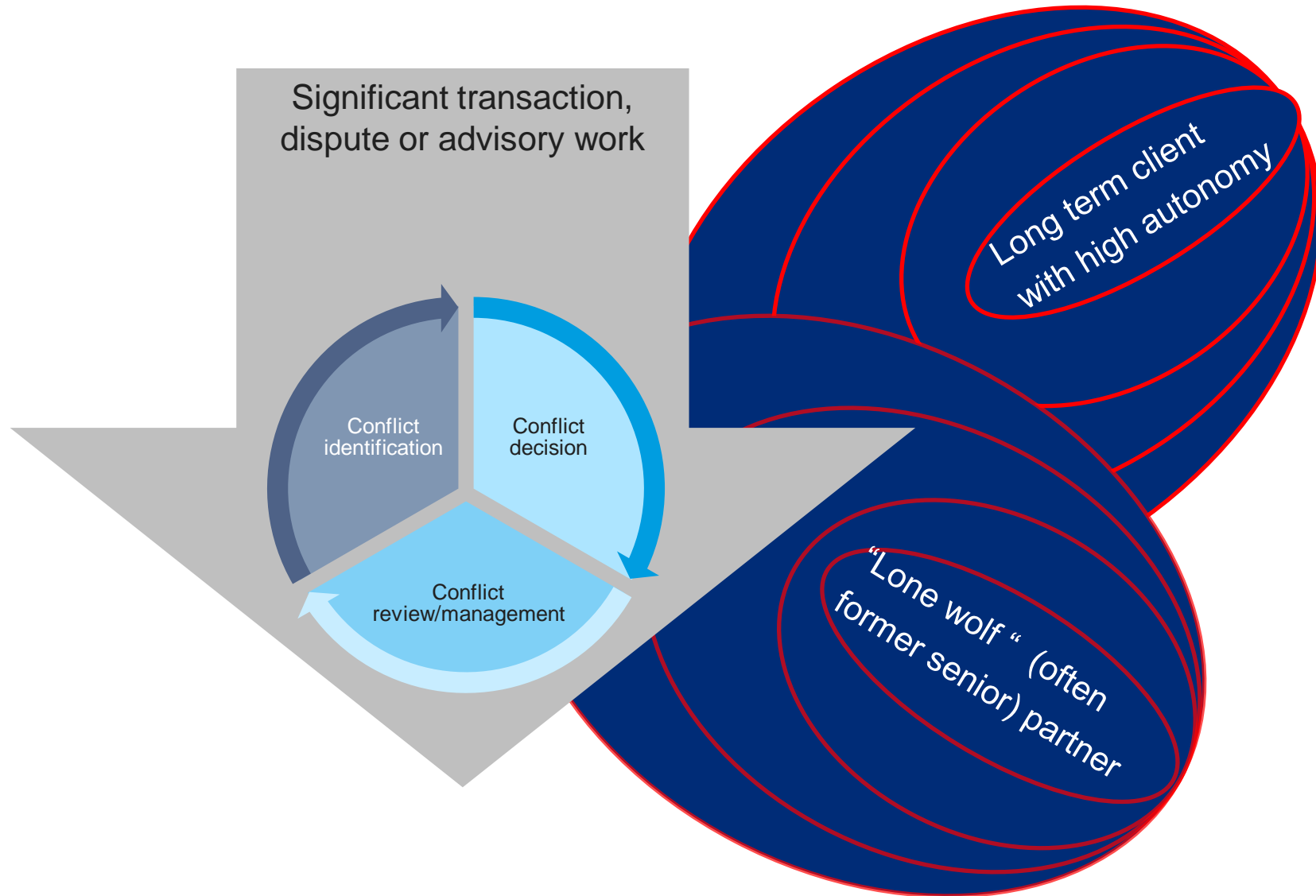
All stakeholders (clients, regulators, partners, staff) may question governance - Stakeholders increasingly want to know what processes exist to prevent known risks?

Confidence can be reduced - does the culture exposed match the aspirations and messaging of assurance/high ethical standards.

# Conflict of interest - process

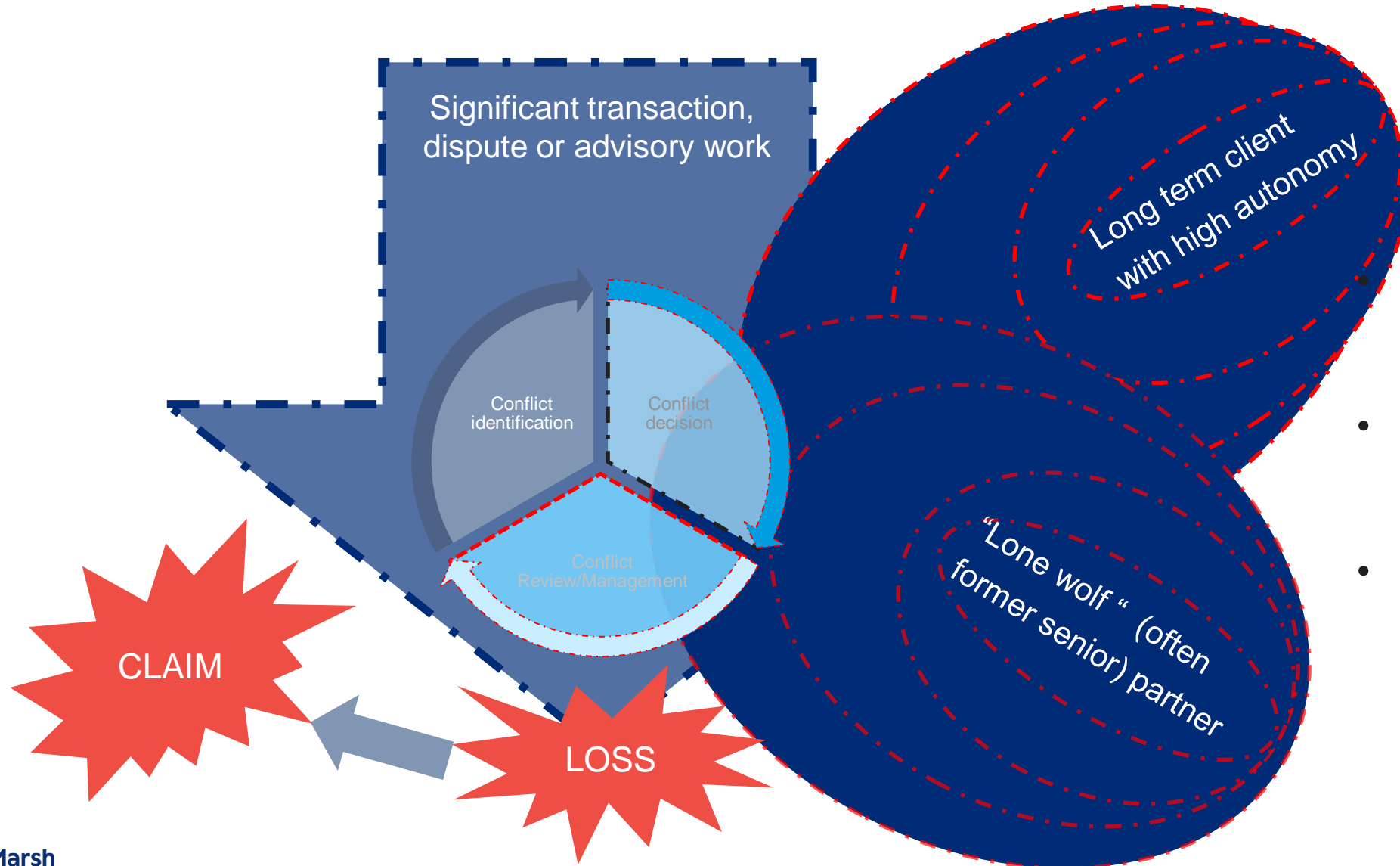


# Conflict of interest – process undermined



# Conflict of interest – process undermined

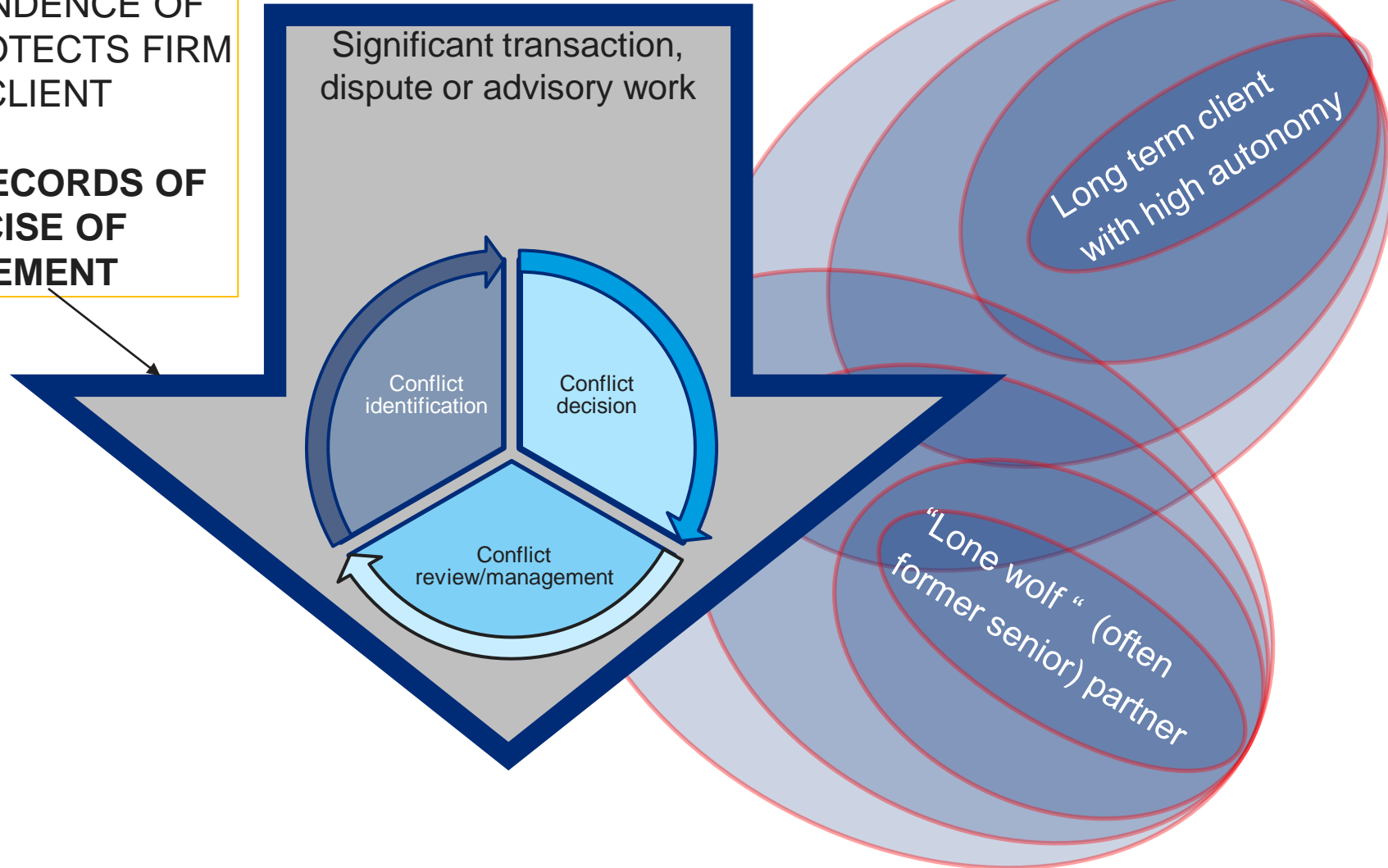
Often no sudden single event but situation creeps in over time.....






- Situation changes over time.
- Problems clear with benefit of hindsight.
- Often hard to identify any single action amounting to an intentional ethical breach.

# Conflict of interest – process preserved

- REMEMBER:**
- INDEPENDENCE OF REVIEW PROTECTS FIRM AND CLIENT
  - KEEP RECORDS OF EXERCISE OF JUDGEMENT



## WARNING SIGNS

-  Client not shared.
-  Record-keeping Unavailable.
-  No other expert at firm and/or lack of respect for others.

# Being realistic about Human Factors

# Errors – Preventive measures – understanding true cause

	NEGLIGENT ACTS			
MENTAL FOCUS	UNINTENTIONAL		INTENTIONAL	
ERROR CLASSIFICATION	Slips	Lapses	Skill based mistakes	Misconduct & violations
MENTAL ELEMENTS	Attention – knew what to do but failed to execute.	Memory failure.	Faulty factual basis or application of knowledge, rules or experience.	Dishonesty regulatory breaches.
OBSERVED BEHAVIOUR	Distraction from simple task.	<ul style="list-style-type: none"> <li>• Key step omitted from standard routine.</li> <li>• Time limit missed.</li> </ul>	<ul style="list-style-type: none"> <li>• Time limit miscalculated.</li> <li>• Advice errors.</li> </ul>	<ul style="list-style-type: none"> <li>• Conflict of interest.</li> <li>• Theft.</li> </ul>
ACTION AREAS	HUMAN FACTORS		CONTINUING COMPETENCE	ETHICS
PREVENTIVE MEASURES	<ul style="list-style-type: none"> <li>• Process improvement.</li> <li>• Workplace design.</li> <li>• Redundant back ups.</li> </ul>	<ul style="list-style-type: none"> <li>• Checklists.</li> <li>• Workflow systems.</li> <li>• Risk training.</li> </ul>	<ul style="list-style-type: none"> <li>• Continuing competence.</li> <li>• Professional training.</li> <li>• Awareness of common errors.</li> <li>• Peer &amp; four eyes reviews.</li> </ul>	<ul style="list-style-type: none"> <li>• Ethics training and standards.</li> <li>• People selection.</li> <li>• Audits.</li> <li>• Financial controls.</li> </ul>



# Preventive measures? Simple slips

## Conformity check – e.g. final draft of lease/contract checked against Heads of Terms/instructions

- Significant risk control to mitigate against final drafts not corresponding with Heads of Terms or client instructions.

## Peer or supervisor reviews - on valuable or unusual cases

- Important risk control in reducing unique freehand drafting errors and typos.

## Client focussed controls based on risk

- Increased scrutiny when acting for seller/assignor as more claims occur.

## Checklists – Create lists based on actual known claims in the firm and across the profession

- Can learn from own experience and that of others.

# Missed time limits – what we see



# Preventive measures?

## Critical date calendars with escalation processes

- Consequences/wider distribution as time limits approach.

## Supervision and workload

- Ensuring adequate capacity to absorb existing and new demand.

## File transfer

- Importance of handover notes and time limit commentary.

## Buddy system

- Peer checks of time limit calculation.

**Focus on what you can  
change 2 - How to appeal  
to underwriters as a  
stand out firm**

# Strategic choices and consequences

## Work undertaken and risk profiles

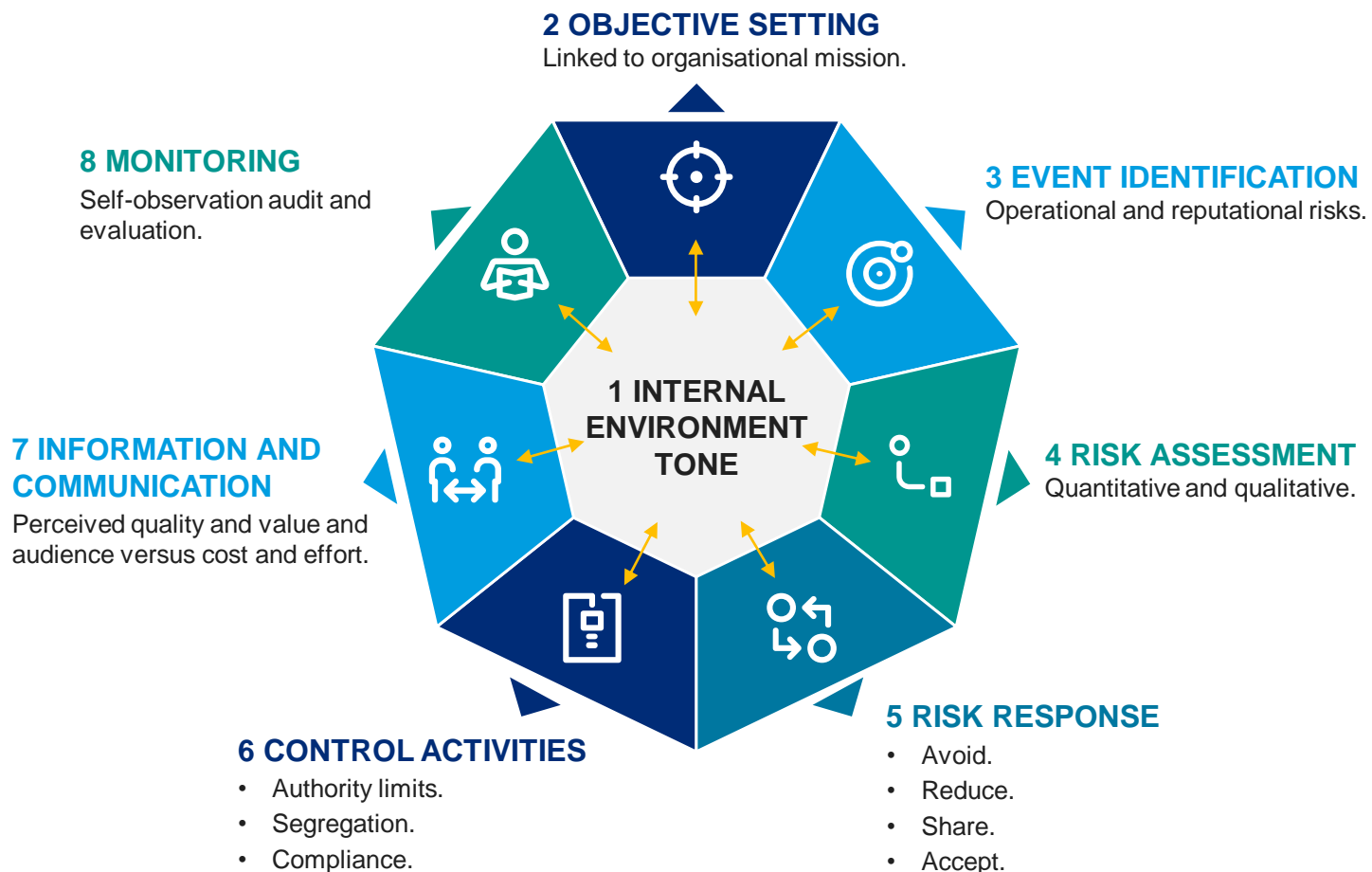
- Is there a business plan that identifies the “target business” to the firm?
- Demonstrate the key risks in the various work areas known/understood by everyone in the firm:
  - How is that achieved and what records exist?
  - Is the understanding driven by claims and mistakes inside and outside the firm?
- Demonstrate how these risks controlled
  - Who takes responsibility?
  - Provide records exist of systems in action:
    - Audit follow up,
    - Change in procedure

# Enterprise Risk Management

# 2

# Enterprise Risk Management – Committee of Sponsoring Organisations (COSO 2004)

“...a process.....applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risks to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives (COSO 2004:2).”



## Identify Assess Control Monitor

<b>2,3,4 Identify Assess Key risks</b>	<b>Ransomware data exfiltration, payment interception fraud, conflicts of interest, flood/fire disaster.</b>
<b>5,6,7 Control and communicate</b>	Insure or absorb risks, and set controls to prevent or mitigate risks.
<b>Monitor</b>	Create auditable monitoring – records of testing, results and actions from internal and external audit.

# What makes a firm stand out

## Hints and Tips

1. Significant growth, new offices and partners sound positive but are potentially increase risk and reduce management oversight. How have systems and supervision flexed to cope?
2. Identify **what is different and good about the firm** and might **positively differentiate it from the average, the best firms provide hard data to demonstrate, and don't simply "tell"**:

Questions	"Tell"	"Demonstrate....."
How do you manage risk?	We have a "great culture" and have an "open door" approach	Evidenced examples about risks identified and relevant changes made on what dates, and what is still in progress.
How do you ensure engagement letters are used?	"We have a policy that all files must have a retainer letter"	Here is the MI on % of files with retainers, it is up x% on prior year, we are working towards 100%



# Importance of MI and data + evidence trails on key risk management areas

## Retainer letters and audit actions

1. If you have a policy that all files should have a retainer letter, how is this measured, monitored and what actions are taken – is there a document trail?
2. If you have an internal quality audit system, can you demonstrate audit findings and actions and confirmation that action was taken?
3. If you have a Disaster Recovery Plan when was it last tested, what was the result and what were the recommendations arising from the test

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Chartered

A business of Marsh McLennan

# Appendix – cyber risk scenarios and mitigants

# Cyber Risk reduction – 3<sup>rd</sup> party payment

Use encryption.

Password protect PDF files (communicate password by different medium).

Contact the client.

Update retainer letters/email footers:

- Highlight that any requests for payment should always be verified by the client using the telephone details contained in the original retainer letter before any payment made.



**Sending invoices by email is always risky**



**Invoices are particularly targeted by cyber criminals**

# Cyber Risk reduction – client payments

Always follow procedures.

Consider in-person or video call to verify account changes.

Consider threshold amounts as to transfers – significant funds having increased measures in place.

Be aware on new tactics to elicit uncomfortable situations.



**Authorized push payment (APP) frauds on the increase.**



**Cyber criminals are targeting the property industry heavily.**

# Cyber Risk reduction – ransomware blackmailers threaten publication of client data not service interruption

Implement MFA if not already in use (on all systems).

Install patches immediately using firm systems. Upgrade defences.

Use encryption.

Don't keep data for longer than necessary.

Consider Cyber Essentials accreditation - designed to build minimum standards of cybersecurity in small and medium-sized businesses.

**In the first quarter of 2021, there were three times as many ransomware attacks as there were in all of 2019.**

*NCSC annual review 2021*

**Newer ransomware steals data as well as encrypting it. Increased pressure on firms - threats to release client data if they don't pay demands.**

# Cyber Risk reduction – 3<sup>rd</sup> party reliance

## Consider cyber due diligence on certain providers.

Check that:

- You are dealing with businesses that are well reviewed and trusted.
- You know your providers' service level guarantees in the event of service interruptions or data losses.
- You know how quickly your provider is likely to recover in practice.
- You know how your provider will prioritise service restoration among its clients.

**“As firms inevitably come to depend more on their IT providers and other third parties, it will be ever more important to establish that those providers can be trusted.”**

Source: [SRA | Risk Outlook report: information security and cybercrime in a new normal | Solicitors Regulation](#)