

Investment business — opportunities and risks for solicitors

A recent decision of the Solicitors Disciplinary Tribunal (SDT) holds many lessons for solicitors seeking to embrace new business opportunities.

Imagine you are one of 12 partners in a successful, full-service firm in a regional town. You are a long-established firm, holding several valuable accreditations such as Lexcel, liP and a legal aid franchise in crime and family. Integrated at every level of the local community, your firm's partners have provided presidents of the local Law Society for years.

This success has been built on a highly professional approach, embracing new opportunities when they arise. One such new approach is to integrate a financial services offering within the firm in the form of an IFA making available advice on investment products for the victims of personal injury, beneficiaries and others. Your commitment is such that no less than six firms of IFAs are invited to a well-organised beauty parade. The successful IFA enters into a sophisticated written agreement to ensure the interests of the client are protected. The agreement also provides for your firm to share one-third of the commission otherwise wholly payable to the IFA.

This was in fact the innovative approach adopted by one such regional firm who, with little notice were recently the subject of a visit by the Investment Business Unit (IBU) of the Solicitors Regulation Authority (SRA). The investigation officers found that the firm had committed breaches of no less than 11 professional rules.

For the next two years the partners most closely involved spent substantial parts of their working lives in interviews with the IBU (described as being more like police interrogations), instructing solicitors to manage the investigation and the seemingly endless correspondence leading to referral to the SDT.

Of the original 11 allegations against all 12 partners, only seven were pursued, of which the most serious (unprofessional conduct) was withdrawn. All partners earned a reprimand, another a £500 fine and the remaining four allegations were dismissed with the Tribunal expressing surprise that the matter was brought before it. The Tribunal reduced the SRA's claimed costs of over £17,600 to £6,000 including VAT. The SRA only succeeded with two of the 11 allegations.

As the Tribunal said, the case is a salutary lesson in how careful solicitors must be when sharing commission.

Including the sums payable to the SRA, the cost of managing this investigation and the Tribunal proceedings was almost £100,000. However, the loss of otherwise chargeable time, damage to

partnership morale and the business opportunities not pursued while engaged defending this matter is incalculable.

These difficulties arose because of a technical breach of rule 10 of the Solicitors Practice Rules, 1990 (now rule 2.06 of the 2007 Code). The requirement to obtain the client's consent to sharing commission is not a duty which can be delegated to non-solicitors, i.e. the IFA in this case. A solicitor must ensure that a form is signed by the client. That form must:

- * state the client's agreement that the solicitor may share commission;
- * state the precise amount in cash terms of the commission;
- * be signed by the client having had its contents explained by the solicitor.

A central record must be kept and the forms have to be preserved. A written procedure will help to demonstrate compliance but there must be evidence of actual compliance too. Compliance comes at a cost, but a fraction of the cost of managing a regulatory investigation (see above).

What about the allegations that were not pursued before the Tribunal? These were dealt with as follows:

- * Breach of confidentiality
 - ◇ The agreement with the IFA provided for the physical presence of the IFA in the solicitors' office for parts of the working week to raise the profile of this aspect of the firm's offering among fee-earners. The agreement included a confidentiality agreement.
 - ◇ Notwithstanding the confidentiality agreement, the SRA took the view there was a breach of confidentiality. It is not surprising this was not pursued, but costs were nevertheless incurred in making the points and seeking (successfully) to deter the SRA from pursuing this before the Tribunal.
- * Professional misconduct
 - ◇ The decision to pursue this major allegation (until just before the SDT hearing) reflects a failure on the part of the SRA to distinguish between a firm which made a mistake but was otherwise compliant (in fact passionate about compliance and excellence in client service), and firms which pay little or no regard to such matters.

In fact the commission in this case would never have belonged to the client and was not paid out of client funds. As such the commission was probably not commission of a kind caught by rule 10. This point did not occur to the IBU and is typical of the approach adopted by the SRA. Case workers tend to focus on the letter of the rules paying less attention to the law underlying the rules.

How to cope with such an investigation

The lessons of this case are many but unfortunately not unique to this particular matter. Tips to bear in mind when first approached by the SRA:

- Seek advice from solicitors experienced in this arena
- Be represented in any interview – it's the equivalent of a police interview
- Notify your professional indemnity insurers and seek payment of your legal costs under your policy – it may cover this kind of investigation.

This technical paper has been written as a general guide only. It should not be relied upon as a substitute for specific legal advice. No responsibility can be accepted by the author or the firm for any loss occasioned as a consequence of acting or refraining from action on the basis of this paper.

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