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Chairman's Interim Report

Professional Indemnity Insurance for Bar Standards Board-Regulated Entities

In my predecessor's report of January 2011 it was noted that, in reply to the Bar Standards Board ("BSB")'s Third Consultation on the Regulation of Entities issued in August 2010, Bar Mutual had confirmed its intention to continue to provide high quality and fairly priced insurance cover to all entities and self-employed barristers regulated by the BSB. In response to the BSB's 2012 Consultation, given the uncertainty that had emerged as to the scope of the activities of multi-person entities that would be regulated by the BSB, Bar Mutual stated as follows:

> *"Bar Mutual is open to the possibility of providing professional indemnity insurance to entities regulated by the BSB. However it is concerned that some entities may not present risks compatible with those presented by the self-employed barristers Bar Mutual is required to insure and so is likely only to wish to consider applications for insurance from such entities on a case by case basis."*

Bar Mutual has indicated to the BSB its willingness to find a solution that would enable it to insure all such entities (eg by seeking reinsurance for any aspects of the activities of multi-person entities that presented risks which were not compatible with those presented by self-employed barristers). As at the date of this report, Bar Mutual has yet to receive from the BSB a definitive set of criteria as to the scope of activities by a multi-person entity that would allow it to fall within the purview of the BSB. Bar Mutual has throughout expressed its willingness to insure single-person entities (ie self-employed barristers who choose to practise through their own entity).

Bar Mutual has made it clear to the BSB on a number of occasions, however, that all entities regulated by the BSB which provide barrister-like services and which Bar Mutual would therefore regard as presenting risks which were compatible with those presented by self-employed barristers would not only have insurance made available to them by Bar Mutual but should also be obliged to insure with Bar Mutual, as is presently the case for the self-employed Bar. As Bar Mutual has explained to the BSB, firstly this would create a "level playing field" for the provision of professional indemnity insurance to those offering the same type of legal services to the public, regardless of the business model through which the services were provided, and secondly the absence of any compulsion to insure with Bar Mutual could jeopardise the long-term future of Bar Mutual. There have been material developments on this front over the past year and it is therefore appropriate - given their importance - that I deal first with this issue and at a little length.

Self-employed barristers were first compelled to have professional indemnity insurance as a pre-condition for practice in 1980, on the basis that a responsible profession had to have regard to the interest of consumers by ensuring that consumers with valid negligence claims should not be prejudiced by the potential inability of barristers to meet judgments entered against them. In introducing this requirement, the Bar rejected a proposal for a Master Policy, opting instead for an open market solution with the insurance being provided by various insurers. By 1985, however, the number of insurers offering insurance to the Bar had shrunk to only two, only one of which was willing to provide a quotation to all Chambers. And although insurers had agreed to adopt a common policy wording, premiums for each barrister were entirely at the discretion of the insurers and any claim (or even the threat of a claim) resulted in very substantial (sometimes in excess of 1000%) increases in premium. Not only were premiums increasing but also there was no transparency as to how they were calculated. Furthermore, insurers could accept or reject barristers without reason. Finally, barristers were not receiving quotations from insurers until the day before the expiry of their existing cover, which was causing immense uncertainty and rendering it impossible to obtain alternative quotations. In short, the supposed benefits of open market competition for the provision of insurance had proved to be illusory.

Responding to an urgent need for change, the Bar Council resolved at its Annual General Meeting in October 1987 to form Bar Mutual as the compulsory provider of primary layer professional indemnity insurance to the self-employed Bar in England and Wales. Bar Mutual has insured the self-employed Bar since April 1988. Its mission, then and now, is as follows:

- To protect the interests of consumers by ensuring that there will always be a solvent insurer available to pay valid claims against members of the self-employed Bar. It is noteworthy that, soon after Bar Mutual was established, a commercial insurer participating in one of the two prior schemes became insolvent leaving those in that scheme partially uninsured;

- To protect the interests of consumers by ensuring that access to the maximum number of barristers judged fit to practise by the BSB is not restricted by the vicissitudes of the insurance market cycle;

- To protect the interests of both the self-employed Bar and consumers by ensuring stability in the insurance arrangements for the self-employed Bar. Collective self-insurance allows rates to be set across the insurance cycle so that premiums collected in years of low claims activity can ameliorate the increase that would otherwise be required in years of high claims activity.

All these goals have to date been achieved, in marked contrast to the turmoil that has in recent years beset the market for professional indemnity insurance for solicitors (the solicitors' mutual indemnity insurance arrangements having ceased in 2000).

On 28 November 2014 the BSB secured approval from the Legal Services Board to authorise and regulate entities. It will start accepting applications to approve entities this month and authorising them from April 2015.

As single person entities will be offering the same services as the self-employed Bar, Bar Mutual's position on the insurance of single person entities is that the BSB should require all of them to insure with Bar Mutual. With regard to multi-person entities, Bar Mutual's position is that where these entities provide barrister-like services (services that would broadly fall within the definition of "Insured Practice" in Bar Mutual's current Terms of Cover), then these entities should also be required to insure with Bar Mutual.

Unfortunately, the BSB Handbook does not currently include a requirement for entities (whether single person or multi-person) to insure with Bar Mutual. Nonetheless, as regards Bar Mutual's 2015 policy year which will commence on 1 April 2015, Bar Mutual's position is as follows:

- Bar Mutual will provide primary layer professional indemnity insurance at the 2015 renewal to all single person entities on the same basis as if the individual behind the single person entity were seeking cover as a self-employed barrister;

- Bar Mutual will provide primary layer professional indemnity insurance at the 2015 renewal to BSB-regulated multi-person entities on a case by case basis, with the intention of providing insurance to barrister-like entities;

- Bar Mutual will not provide run-off cover to those of its self-employed barrister Members who elect to establish any entity that will be regulated by the BSB where that entity does not purchase its primary layer of professional indemnity insurance with Bar Mutual.

It is the opinion of the Board of Directors that if the BSB is unable to secure a change to the provisions of the Handbook to extend the requirement to insure with Bar Mutual so that it applies to these entities (such a change requiring the approval of the Legal Services Board), Bar Mutual's future may be at risk. This is because Bar Mutual's survival cannot be guaranteed in an environment where a (potentially) significant number of single and multi-person entities are enticed to insure with commercial insurers with offers of rates artificially below Bar Mutual's in an attempt to build market share, corner the market and then increase rates once Bar Mutual - as a not for profit company - is forced to cease operating. It is far from being fanciful that, faced with the prospect of commercial insurers cherry-picking all the best risks (ie those generating the highest premiums and with the best claims records) with "loss-leader" premiums, leaving Bar Mutual as, in effect, insurer of last resort, the

Board may conclude that the protection of the Members' interests would be best served by winding up Bar Mutual. It is therefore critically important that the BSB amends its Handbook during 2015 so as to require all single and multi-person entities offering barrister-like services to place their primary level of professional indemnity insurance with Bar Mutual.

Should that not prove possible, Bar Mutual will have to review whether, and if so on what basis, it will continue to be in the interest of its Members to insure entities at the 2016 renewal, which must include reserving the right to adopt a selective approach to the insurance of entities and taking into account the individual claims records of each applicant, which of course is not currently the case.

When the original version of this report (dated 6 January 2015) was sent for printing, the BSB had yet to issue its promised minimum terms of cover for entities (hitherto, the BSB has been content to leave the Terms of Cover for the self-employed Bar to Bar Mutual). The original version of this report therefore contained a caveat that Bar Mutual would need to review its position if there was any material difference between Bar Mutual's current terms and the terms proposed by the BSB. A first draft of the terms to be proposed by the BSB was finally received on 9 January 2015. Although they do generally follow Bar Mutual's current terms, there are some issues on the draft terms which will need to be resolved before Bar Mutual could be able to offer insurance to entities. I apologise for the delay in issuing this report that its necessary revision has caused.

Rates for the 2015 Renewal

Bar Mutual rates each area of practice according to the risk each presents. As a result, the rate applied, and the resulting premium Members pay in respect of their practice areas, is directly related to the claims experience for those areas of practice. In setting the rates, the Board has to balance, on one hand, collecting sufficient premium to ensure that Bar Mutual has the financial resources to meet its projected liabilities and any unexpected adverse developments in its claims experience with, on the other, the need to avoid setting rates at a level that results in an overcollection of premium.

After careful consideration, the Board is satisfied that it should change the rates for only three areas of practice for the 2015 policy year. The first is Criminal. Following incremental deterioration in the claims experience for Criminal in recent years, the position has now been reached where the rate has to be increased. Accordingly, the rate for Criminal will increase from 0.15% to 0.2%. As the rate increase is only 0.05%, this will cost many practitioners no more than about £1 per week. The rate for Professional Discipline will increase from 0.25% to 0.5%. Once again, the rate increase is due to the claims experience of the area of practice over a sustained period. The final area of practice for which the rate will increase in 2015 is Planning. The rate here will increase from 0.9% to 1.2%. As with the other areas facing a rate increase, the adjustment is the result of adverse claims experience, albeit combined with a decline in declared fee income which, although now improving, is insufficient to compensate for the claims experience.

As Bar Mutual exists to provide insurance to its Members at cost, it tries to avoid building up a surplus over and above that which is required to strengthen its financial position in order to ensure its long-term survival. One way in which Bar Mutual seeks to limit the cost of insurance to its Members and to minimise the risk of the collection of surplus funds is through the premium deferral, which is an arrangement by which Bar Mutual defers collection of a portion of the premium due from Members. Given the need to prepare for the introduction of Solvency II in 2016 and the Board's assessment of the reserve "buffer" Bar Mutual should hold above its regulatory capital requirements, the premium deferral for the 2015 policy year will be reduced from 20% to 17.5%. At the same time, however, Bar Mutual will waive its entitlement to the £2.237m of premium deferral for the 2008 policy year, which means Bar Mutual has now waived its entitlement to call for payment of the premium deferral for all policy years up to and including that policy year.

Turning to the level of the income cap, which is the limit on the fee income Bar Mutual takes into account for the purposes of calculating Members' premiums, the current cap of £1m has been in place since 2008. As the cap has not kept pace with fee income inflation, the Board has decided to increase it to £1.2m.

Directors

We are fortunate to have a balanced and dedicated Board made up of individuals with a cross-section of relevant experience and practice. Recruitment to the Board is overseen by the Nominations Committee, which applies a policy agreed by the Board and incorporates the highest standards of corporate governance. Since my last report in June 2014, Bar Mutual has lost the services of two directors, Catherine Gibaud QC and Colin Wynter QC. Catherine served on the Board for over five years and her contribution to the work of the Audit and Risk, Investment, Legal Services Act and Nominations Committees was greatly appreciated and will be missed. I thank her for her dedication and wish her well for the future. Colin Wynter QC joined the Board in February 2014 but unfortunately decided, for personal reasons, to stand down. I thank him for the contribution he made and wish him well for the future.

Bar Mutual is fortunate to be able to attract the highest calibre of Directors and I am pleased to inform you that two new directors have recently joined the Board. They are Joanna Smith QC and Rebecca Sabben-Clare QC. I welcome them both to the Board. As it has been some time since the full list of Directors was provided to you, I list the members of the Board below:

Colin Edelman QC (Chairman)
Christopher Symons QC (Deputy Chairman)
Michael Brindle QC (Deputy Chairman)
Charles Flint QC (Deputy Chairman)
Stephen Arthur
Gregory Denton-Cox
Jasbir Dhillon QC
Alexandra Healy QC
Michael Horne
Leigh-Ann Mulcahy QC
Christopher Pocock QC
David Railton QC
Rebecca Sabben-Clare QC
Sharif Shivji
Joanna Smith QC
David Wolfson QC

Adequacy of Insurance Cover

I close with my usual exhortation to all Members to ensure that they purchase adequate primary and, where necessary, excess layer insurance. In its twenty-seven year history Bar Mutual has unfortunately had to address the fall-out for Members with inadequate limits of cover on several occasions. In almost all cases the problem was avoidable. I remind you that the costs of purchasing additional limits of primary layer cover from Bar Mutual is only £100 for each additional £500,000 of cover; and the cost of purchasing cover in the excess layers remains relatively inexpensive. I should also mention that the new regulatory requirement in the BSB Handbook for all self-employed barristers to ensure that the limit of their insurance cover is adequate for the nature of their practices.

This year, two insurance brokers have confirmed to the Managers that they will be able to arrange excess layer insurance above Bar Mutual's £2.5m primary layer of cover. In the normal course their contact details will be on each Member's renewal form.

Colin Edelman QC
Chairman

12 January 2015