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Professional Indemnity: solicitors' fees

IN BRIEF

The Court of Appeal confirmed that the professional indemnity policy issued by the claimants to the respondents, a firm of solicitors, included cover for the insured's fees.

Royal and Sun Alliance and others v Tughans (2023) EWCA Civ 999

This appeal raised an important issue as to the extent to which compulsory professional indemnity insurance ('PII') for solicitors provided cover for liabilities which included the firm's fees.

The appellants are insurers who subscribed to a PII policy ('the Policy') led by Royal and Sun Alliance Insurance Limited ('RSA') in favour of Tughans, a firm of solicitors practising in Belfast, at the relevant time as a general partnership under the law of Northern Ireland. The Policy, which was in standard terms required for all solicitors in Northern Ireland, was in favour of the partners, solicitors and employees of the firm.

Brown Rudnick LLP ('BR'), an English limited liability partnership affiliated to a US limited partnership with the same name, engaged Tughans to perform professional services, resulting in a claim against Tughans in the High Court of Northern Ireland. Tughans in turn commenced an arbitration against the Insurers under the Policy seeking declarations of an entitlement to indemnity in respect of such liabilities as might be found to be owed to BR, including their fees running to many millions of pounds. The arbitrator resolved the coverage issues in favour of Tughans and made a final award accordingly. The Insurers appealed pursuant to S69 Arbitration Act 1996, on the issue of the element of BR's damages claim which comprised the fee paid by BR to Tughans for the services.

A High Court Judge dismissed the appeal. The judge identified the Insurers' argument as being that if BR established liability against Tughans, it would follow that Tughans never became entitled to the Tughans Fee, and so could suffer no loss in having to return it; it was not the purpose of a professional indemnity insurance policy to pay solicitors a sum representing profit costs to which they were never entitled; and so granting Tughans cover in respect of the Tughans Fee would violate the principle of indemnity.

The insuring clause provided:

"The Insurers will indemnify the Insured in respect of claims or alleged claims made against the Insured…..in respect of any civil liability (including liability for claimant's costs and expenses) incurred in connection with the Practice…provided that no indemnity will be given

(a) to any individual committing or condoning any dishonest fraudulent criminal or malicious act….."

The Court of Appeal noted that three matters deserved emphasis.

First, the insuring clause was expressed in very wide terms. Secondly, the exception made clear that unless the claiming assured had themself committed or condoned fraud, the fact that it was the fraud of others which had given rise to liability was no bar to cover. Thirdly, one of the points which the Insurers might wish to argue in due course was that the partners "condoned" their managing partner's conduct so that exception (a) was engaged, contending that the Insurers were deprived of the opportunity to advance this argument as a result of a procedural irregularity. However, the Insurers' argument on the appeal was advanced on the assumption that exclusion (a) did not apply to the respondent partners, and that was the assumption on which this court addressed the argument.

Dismissing the Appeal, the Court of Appeal first considered the indemnity principle. The starting point was that the Policy wording in this case was in wide terms covering any civil liability; and that an ascertained liability was generally regarded as a loss (without the need for prior payment to discharge it), both in the general law and in liability insurance.

Against that background the indemnity principle did not assist the Insurers in this case for four reasons.

The first was that a solicitor who had earned a fee, so as to be contractually entitled to it, did indeed suffer a loss if deprived of it by reason of a liability claim.

The second reason was that it ran contrary to the public interest purpose of compulsory PII cover for solicitors identified in *Swain v The Law Society.* If the partnership and all the partners were insolvent, a client would not have this protection where it was seeking to recover damages which included the fee paid to the solicitor. In this case BR would be left without the derivative insurance rights which the scheme of compulsory PII insurance was intended to provide.

Thirdly, the ramifications of the Insurers' argument were inconsistent with the commercial and regulatory function of compulsory PII cover, which was to protect partners and employees from their own negligent mistakes and those of their fellow partners and employees, and from the fraud of those others, as well as its function of protecting clients.

The fourth flaw in the claimants' argument in reliance on the indemnity principle was that it ignored the composite nature of the Policy and the fact that the claims were made under it by individual assureds.

The claimants also argued that the indemnity principle precluded any cover for a liability for fees framed as a restitutionary claim; and that being so, liability for fees as part of a damages claim equally ought not to be covered, there being no reason for a distinction between the two.

The short answer was that even if the premise were correct, the conclusion would not follow because of the real differences between a restitutionary claim and a damages claim, to which the judge drew attention at the first appeal.

The claimants further argued that the effect of the declaration of cover in this case was to treat the Policy as granting first party cover for unpaid fees, which were not the proper subject matter of compulsory PII policies and were excluded from the Policy by the usual trading debts exception.

The Court of Appeal rejected this argument for two separate reasons. First it ignored the position of the individual partners under a composite policy. They would not be in the same position irrespective of whether or not the fee was received: they were worse off by reason of the fee having been paid because they each became liable for the whole of the fee element of the damages liability whilst each having a beneficial interest, at best, in only a proportion of the gross fee received by the firm.

Secondly, the argument appeared unsound even if examined from the point of view of Tughans as an entity. Where the fee was unpaid in the posited example the Policy did not respond; whereas, where there was a liability which included the fee element, the Policy did respond because there was a liability and a loss, which was exactly what professional indemnity insurance was designed to cover.

Jeremy Riley, Partner with **Kennedys** and a member of the FOIL Professional Negligence SFT comments:

Although not wholly surprising, this is not a decision that professional indemnity insurers will welcome. This judgment gives claimants the ability to tailor the way they plead a claim, so as to pursue the same as damages and, in turn, deny insurers a defence under the policy. These rather entrepreneurial fee arrangements (as adopted by Tughans in this case) are therefore a danger for insurers.

Unless and until the minimum terms for solicitors' professional indemnity cover can be adjusted to account for this kind of scenario, then this will remain an exposure for the insurance market. FOIL have advocated for some time that the minimum terms place too great an onus on insurers, which is illustrated by the express reference in this case to the wider public interest policy being a factor in the decision. The simple economics are that this drives up the premium payable by solicitors, due to the wider exposure being underwritten.

The full judgment may be found at: Royal and Sun Alliance Insurance Ltd & Ors v Tughans [2023] EWCA Civ 999 (31 August 2023) (bailii.org)

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