Accounts Rules Update

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This month Regulation Report focuses on three topical Accounts Rules issues.

DORMANT CLIENT ACCOUNT BALANCES

At the SRA Board meeting in July, the proposal to increase the maximum dormant client account balance that firms can donate to charity without SRA approval was approved. The change to Rule 20 of the SRA Accounts Rules 2011 ("2011 Accounts Rules") will take effect on 30 October 2014. It will apply to all client balances that a firm is holding on that date not just balances that accrue after 30 October 2014.

It is rumoured that some of the more crafty firms may be leaving a long overdue review of residual client account balances until after 30 October to take advantage of the increase. Partial donations to charity are not permitted. For example where a balance of £2000 is held donating this to charity in four instalments of £500 would not be compliant. The figure of £500 applies to the total sum held for each client per matter.

On a practical note, it is worthwhile ensuring that all of the firm's chosen charities are able to provide an indemnity to return the monies in the event that the client suddenly turns up unexpectedly from a sojourn in Tibet requiring repayment of £499. The firm is still liable to repay the client even if the monies have already been donated to charity.

Another sensible measure is to include in your terms and conditions of business at the outset of the solicitor/client relationship an obligation upon the client to keep you updated with his contact details. Finally, a standard paragraph in your final debrief letter at the end of a case could also remind the client of the importance of keeping you advised of current contact details and request instructions in the event that monies are received unexpectedly.

USING CLIENT ACCOUNT AS A BANKING FACILITY

Rule 14.5 of the 2011 Accounts Rules prohibits the use of client account to provide banking facilities to clients on the basis that it is not a proper part of a solicitor's everyday practice to do so. Payments into, and withdrawals from, a client account must relate *"to instructions relating to an underlying transaction (and the funds arising therefrom,) or to a service forming part of your normal regulated activities"*

There are two High Court decisions which have clarified the meaning of *"underlying transaction"* and *"normal regulated activities"*. In *Patel v Solicitors Regulation Authority [2012] EWHC 3373 (Admin)* it was held that the underlying transaction must be one that involves the solicitor's legal expertise. Holding funds in client account for a client's car import business did not find favour with the court.

In *Fuglers LLP v Solicitors Regulation Authority [2014] EWHC 179 (Admin)* the Tribunal's original decision that there must be a reasonable nexus between the nature and scope of activity and the original retainer was upheld. The problem here was holding funds on behalf of Portsmouth Football Club whilst it was suffering financial difficulties.

The question of whether a firm is in breach of Rule 14.5 very much depends upon the facts of each case. If a firm is just providing advice to a client as opposed to acting in litigation or conducting a transaction then it is more difficult to demonstrate a *"nexus"*. Also, what these two cases demonstrate is that no underlying mischief e.g. money laundering is necessary for a breach of Rule 14.5.

Solicitors hold money on behalf of their clients in a variety of ways. Escrow accounts; stakeholder accounts; as Power of Attorney and as trustee are just a few examples. It would be a loss to clients if these services had to be curtailed.

The SRA Professional Ethics Team is working on guidance and want as many examples from the profession as possible – email professional.ethics@sra.org.uk – if you have any contributions to make.

CLIENT ACCOUNT SHORTAGES

A client account must not be overdrawn (Rule 20.9). If this does occur, the shortage must be replaced *"promptly upon discovery"* from the principals' own resources even if there is a pending insurance claim and/or claim on the Compensation Fund (Rule 7).

A number of firms have recently been the victims of internet banking fraud. The size of the fraud has made it very difficult for the firms to replace the client account cash shortage so as to comply with their duties under Rule 7. In this type of case, firms must notify their insurers and the SRA and of course the bank who should be encouraged to resolve the problem.

This issue should be included on the firm's Risk Register and a contingency plan put in place. Is there access to a pre-arranged bank loan? Does one of the partners have ready funds to lend to the practice until insurers meet the claim? Also a regular review of your internet banking passwords and security procedures would be recommended. Prevention is better than cure in such circumstances. ■

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