



Attention: Fran Gillon
Intellectual Property Regulation Board (IPReg)
20 Little Britain
London
EC1A 7DH

Sent by email only to info@ipreg.org.uk

2 September 2021

Dear Ms Gillon,

Consultation: Changes to Compensation Arrangements

The Legal Services Panel welcomes the opportunity to comment on IPReg's changes to its Compensation Arrangements given that the scheme will not have insurance coverage after 30 October 2021.

It is unfortunate that the insurance company backing IPReg's compensation scheme provided notification of the withdrawal of coverage at such short notice. In addition, the fact that IPReg is unable to obtain alternative insurance arrangements after 30 October 2021 means that the consumer protection formerly afforded to clients of patent attorneys, patent agents or registered trade mark attorneys is in jeopardy. The Panel appreciates IPReg has taken steps to ensure coverage was extended to allow time to seek views on its proposed measures to deal with this difficult development and put an interim compensation scheme in place.

The Panel agrees that an interim plan for the IPReg compensation scheme is required while IPReg studies relevant evidence and engages additional expertise to devise a long-term solution that ensures the compensation scheme continues to be viable. We also accept that the current arrangements may need to be reviewed and could change. Against this backdrop, it is important to remember that the compensation scheme forms an essential part of the overall system of consumer protection within the regulated legal services sector because it provides a safety net for consumers who suffer losses at the hands of legal service providers who act dishonestly.

Continued Expectation of Data Transparency

Although IPReg has not had any claims on its compensation fund, it would have been useful to review any relevant data available such as the claim histories of other legal services regulators in England and Wales and how its own risk pool differs from theirs. It would have also been useful for the actuary's opinion to set out the comparable data sets that were reviewed in arriving at his opinion. It may also be useful to differentiate between the aims of insurance coverage versus an actual fund where the payment of a discretionary award may be limited by the amount of money

available in the fund. Even in the unfortunate (and urgent) circumstances in which IPReg finds itself, it is important to be transparent with any available data and how they support the regulatory decisions being made.

Consultation question 1

What are your views on IPReg's proposal to establish a compensation fund?

The Panel understands that because IPReg is unable to obtain insurance coverage for the compensation scheme, establishing a compensation fund may be the only viable option for IPReg to continue to provide a similar level of consumer protection. Our overriding concern is that consumers who have fallen victim to dishonest patent attorneys, patent agents or registered trademark attorneys continue to have accessible and meaningful recourse as they would expect from the regulated legal services market. The Panel is encouraged by IPReg taking immediate action to ensure continuing consumer protection for their members' clients and seeking actuarial expertise regarding its proposed interim plan.

Nevertheless, the details of the interim proposal are not clear from the consultation documents. For instance, the £100,000 fund needs to be in place as soon as the insurance policy lapses at the end of October. While it was noted that the funds reserved for the insurance policy premiums, additional costs and claim excesses would be used for the newly established compensation fund, the Panel needs to be assured that the full amount will be available, whether or not additional borrowing is necessitated, as soon as the insurance coverage expires. In addition, the consultation documents suggested that an additional £30,000 would have to be added to the fund in its second year to ensure viability but this amount may change based on actual claims. The Panel would like to ensure that IPReg has a clear plan to finance these changes so that the compensation fund will be there in the event any discretionary awards need to be made.

In addition, the Panel wishes to point out that maintaining a similar version of the current compensation scheme is beneficial to patent and trademark legal professionals as well as to consumers. Beyond providing a safety net for legal services consumers, it means that the entire profession can hold itself out as one worthy of consumers' trust. Consumers procure legal services from IPReg professionals for serious matters which they require assistance navigating. IPReg professionals in turn charge these consumers professional fees based on their training, competence, skills and the protection afforded by operating in a regulated sector. The consumer protection currently provided by IPReg's compensation scheme must be maintained in order for the profession to continue to enjoy the trust and confidence placed in it. While the Panel understand's IPReg's concern over having to increase members' fees, any increase in fees due to ensuring a viable compensation scheme produces a benefit for IPReg members.

The specific details of the interim proposal are examined below.

Consultation question 2

What are your views on the proposed limits of the fund?

It is difficult for the Panel to take a firm position on the proposed payout limits in the absence of any specific claims data or relevant comparison data. We do appreciate that IPReg has maintained the current individual claim limit and tried to ensure multiple claims could be paid in any given year. However, the current coverage to consumers is reduced and it does not appear that IPReg has provided evidence concerning how this reduction may affect its members' clients. The aggregate claims against one firm that will be covered has been substantially reduced from £250,000 (£225,000 insurance coverage per firm plus up to £25,000 excess funds provided directly by IPReg for a total of £250,000) to £100,000. The total fund available is also drastically reduced from £2.5 million to £100,000 (4%). If the claims were valued at the maximum level, the clients of one firm could only successfully claim four times as opposed to ten times under the current rules. In addition, the entire value of the proposed fund could be potentially wiped out with a very low number of claims or the equivalent to the maximum claims allowed against one firm. Though the actuary believes this is very unlikely, it is important that there is a viable plan for the fund to be replenished should it be depleted.

IPReg provides useful information regarding how its professionals and firms are required to deal with client money held by them. The fact that an IPReg firm cannot hold more than £250,000 of client money unless it has made additional compensation arrangements that have been approved by IPReg is useful context. We note, however, under the current scheme, because IPReg was responsible for providing excess amounts of up to £25,000 on claims, the entire amount that can be held by a firm without additional compensation arrangements is covered by the current scheme.

Furthermore, dishonesty may not only affect the actual amount of money held by an IPReg professional. Taking money for services not rendered would appear to fall under dishonest, not negligent behaviour and the fact that legal services relating to a patent or trademark are delayed may cause additional loss due to the time sensitivity of this legal service. The Panel wants to ensure that any actuarial advice considers the actual losses a consumer is likely to suffer may extend beyond pure monetary theft, including the theft of the intellectual property which a client is attempting to protect.

The actuary has advised on the minimum requirements for a viable fund, but IPReg may want to consider whether that is the specific question that needs to be asked or whether it is what level of consumer protection is needed to provide a meaningful benefit to the profession and consumers that is still affordable. The Panel would like to see compensation fund coverage similar to the current level maintained. In any case, relevant data needs to be sought to ensure that the total fund can provide for claims to be covered in all but the most unlikely scenario. Any adjustments to the compensation scheme, even in the interim, should not unduly prejudice consumers.

Consultation question 3

What are your views on the proposal that this interim arrangement should remain in place until at least the end of 2023?

Given that the insurance coverage expires on 30 October 2021, this would mean that the interim plan would last for at least two years and two months. The Panel notes that the actuary's opinion concerned the first 24 months of the interim plan

and this proposed period extends beyond that. A long term solution that is supported by relevant data and actuarial expertise should be implemented as soon as possible. We appreciate that IPReg wants to take some time to study the problem properly to make sure a viable, lasting and fully funded adequate consumer protection scheme is put in place by the time the interim period is over. However, we wonder if this period needs to be more than 14 months unless specific in depth studies are planned and carried out during this interim period.

Consultation question 4

Do you have any views on our proposal to include in the Guidance that the fund will prioritise individual claimants and will only compensate entities in exceptional circumstances where we are satisfied that hardship has been caused?

The Panel is pleased that IPReg has prioritised individual claimants as the most vulnerable users of legal services are individuals. However, there are other entities that also have lower bargaining power in the market including charities and small businesses which are often in reality not much more than an individual. We have been in touch with charity stakeholder groups whose member charities have benefitted from compensation schemes to recover losses resulting from the dishonesty of legal professionals practising different types of law. Local charities in particular are generally underfunded and could be affected. In addition, in consideration of the area of law being practised by IPReg professionals, many patents and trademarks are pursued by small businesses, often in the start up phase when they do not have easy access to funds. Of course, small businesses that are owned by larger organisations may not fall into this category.

The *Legal Services Act*¹ does not define ‘hardship’ and in fact only contains one instance of the word in subsection 21(2) which states that:

In this Act—
“compensation arrangements”, in relation to a body, means arrangements to provide for grants or other payments for the purposes of relieving or mitigating losses or hardship [emphasis added] suffered by persons in consequence of—
(a) negligence or fraud or other dishonesty on the part of any persons whom the body has authorized to carry on activities which constitute a reserved legal activity, or of employees of theirs, in connection with their activities as such authorised persons, and
(b) failure, on the part of regulated persons, to account for money received by them in connection with their activities as such regulated persons;

In this singular context, the Panel does not see hardship equated with exceptional circumstances but rather with loss in the context of outlining the purpose of compensation arrangements made by regulatory agencies. Our interpretation of the word ‘hardship’ therefore relates to the purpose of the compensation scheme being to provide relief against loss or hardship that has been suffered as a result of a legal professional’s dishonesty or failure to account for money received from clients. As a result, it can be said that the compensation fund provides recourse for persons who have suffered a loss or hardship, nothing more.

¹ *Legal Services Act* 2007, c. 29.

Consultation question 5

Do you consider that there are any diversity issues that we need to take into account?

According to the Panel's most recent Tracker Survey, legal users from minority ethnic backgrounds are less likely to be confident that the legal services provider they used would keep their money safe² but we are not certain why this is the case. We do not have data on how different groups are variously affected by legal professional dishonesty. This may be an area to study when the interim compensation scheme is in place.

Consultation question 6

Do you have any comments on the proposed drafting changes?

In the Proposed Compensation Arrangements Rules, the definition of "micro, small and medium sized enterprises" was deleted, however, IPReg may want to reconsider excluding all small businesses from the compensation scheme, especially micro and small businesses, for the reasons stated above. If some small businesses retain the ability to claim from the compensation scheme, some appropriate definition will need to be adopted.

It is unclear why Rule 5 on eligibility is entirely deleted with only pure discretion allowed substituted. If IPReg would still like to remove all small businesses from eligibility to make a claim under the compensation scheme, this change alone can be made. Explicitly setting out the rules for eligibility provides notice to consumers and the profession alike and also encourages objectivity in the administration of the fund so that every claimant is treated the same way. Simple adjustments to the eligibility criteria could be made for the interim period.

Under Regulation 19, it is not clear why any mention of a compensation scheme is deleted in its entirety. A new Annex B can replace the current Annex B when a new compensation scheme is devised but only minor adjustments are needed in the interim period.

Consultation question 7

Are there any other matters that you would like to bring to our attention?

Finally, looking into the compensation scheme in more detail during the interim period will allow for an opportunity to review the current compensation arrangements in their entirety. IPReg may choose to consider whether any protection should be offered to consumers who find themselves having incurred a loss due to IPReg professionals not having PII coverage as required. Currently 7.1(b) specifically bars compensation in such an instance.

In addition, some of the rules listed under Rule 7 are not consistent with one of the statutory objectives of legal services regulation being access to justice.³ It almost

² See Question #85 in Tracker Survey Data, 5 July 2021 (Legal Services Consumer Panel) found at <<https://www.legalservicesconsumerpanel.org.uk/what-we-do/research-and-reports>>.

³ Subsection 1(1)(c) of the *Legal Services Act 2007*, c. 29.

defeats the purpose of providing a compensation scheme for consumers if you first require them to outlay significant money to try to enforce a claim in court against a dishonest IPReg professional. Beyond added cost (which could be crippling if the person has already suffered loss or hardship), IPReg is forcing a victim of legal professional dishonesty to engage another legal professional to go after the dishonest one. Beyond monetary, time and confidence barriers to instituting an action, it adds insult to injury. Even though the current drafting does not always make this mandatory, it should be noted that this type of hurdle could be used to negate access to the compensation fund, which not only disadvantages consumers but also IPReg members because ensuring swindled consumers are protected benefits the entire profession. Furthermore, Rule 7.3 allows IPReg to sue in the name of the applicant to the compensation scheme without stipulating that any monies recovered above the claimant's compensation and any additional costs incurred should be turned over to the claimant. Such a feature is reasonably expected of a scheme whose whole purpose is to provide relief to persons who have been negatively affected by the dishonesty of their IPReg professional.

The mutual benefits of the compensation arrangements to both professionals and consumers must be the central concerns for IPReg in deciding how to proceed. The Compensation Arrangement Rules must continue to provide these benefits over the long term. The Panel strongly encourages IPReg to make every attempt to gather all the relevant evidence it can find in order to ensure a potential claims picture that is as accurate as possible. In addition, further actuarial expertise may have to be engaged to ensure the scheme continues to be viable and adequately funded over time.

In conclusion, the Panel would also like to make a wider point about the need for the sector as a whole, led by the Legal Services Board, to consider a comprehensive review of the compensation fund arrangements. The Panel is of the view that ideas such as 'pooling' funds across the regulators are worth exploring, as doing so may spread the risk and thereby potentially reduce costs, especially if the funds accumulate over time.

We remain open to providing further comments on any new proposals and hope you find these comments helpful. Please contact Heidi Evelyn, Consumer Panel Associate, with any enquiries.

Yours sincerely,



Sarah Chambers
Chair
Legal Services Consumer Panel