Are there any circumstances in which professional indemnity insurers will indemnify insured persons in respect of a loss of fees?

This was the broad question which confronted the Court of Appeal in *RSA v. Tughans* [2023] EWCA Civ 999, and the unanimous answer was Yes. The case is of interest both because of the result and because of the importance accorded by the Court to the policy underlying compulsion on professionals to have at least a specified minimum level of professional indemnity insurance.

At the relevant time, the Belfast solicitors' practice known as Tughans was a partnership (there is now Tughans LLP). The solicitors were obliged to maintain insurance on a form required by the Law Society of Northern Ireland pursuant to the Solicitors Indemnity Insurance Regulations 2014. The insuring clause of the policy provided that:

> "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 ..."

Although the requirements for the insurance of solicitors in Northern Ireland are separate from those applicable in England and Wales, the concept will be familiar to eyes in England and Wales, where the SRA Minimum Terms require that there be insurance which:

> "... must indemnify each insured against civil liability to the extent that it arises from private legal practice in connection with the insured firm's practice ..."

but contains exclusions, particularly the fraud or dishonesty exclusion, which permits the exclusion of

> "... liability of the insurer to indemnify any particular person to the extent that any civil liability or related defence costs arise from dishonesty or a fraudulent act or omission committed or condoned by that person, except that:

"(a) the insurance must nonetheless cover each other insured ..."

Cover is provided to individuals, and the cover is arranged on the basis that those individuals who behave dishonestly or condone dishonesty are not covered but those who are personally innocent, but liable to a third party either on the basis of partnership liability or on the basis of vicarious liability, are covered.

It is obvious that the words "any civil liability" are wide.

An arbitrator, and then the Courts, had to consider a particular issue as to whether Tughans' insurers would, on facts which were assumed, be obliged to provide indemnity for a third party's claim, which included a claim for damages consisting of the fee which had been paid to Tughans. The question what the full facts were remained to be determined, in both criminal and civil proceedings.

What was not in doubt was that in connection with a transaction which involved sale of assets for €1.6 billion Brown Rudnick LLP ("BR") had entered into an agreement which would entitle it to be paid a Success Fee of £15million; BR also entered into an agreement which provided for Tughans to be paid £7.5m by BR in the event of that Success; Success occurred; BR paid Tughans that fee ("the Tughans Fee"). At that stage matters "unravelled" for the Tughans partner concerned, who in due course resigned from the partnership and became the subject of a report to the Law Society of Northern Ireland, and later became the subject of criminal charges which have not yet been determined. Two relevant sets of civil proceedings have followed:

(A) (the later in time), BR sues Tughans (1) as assignee of its client in the asset sale and (2) in its own claim;

(B) an arbitration in which Tughans sought to establish rights of indemnity against their insurers.

BR alleges that the Tughans partner concerned made negligent or fraudulent misrepresentations to it / its client which induced it to make the agreement under which the Tughans Fee was payable and/or to pay that Fee; its own claim is based on various causes of action including alleged breach of contract. Its damages claims include a claim for the amount of the Tughans Fee. The contract with Tughans has not, however, been rescinded.

In somewhat convoluted circumstances, the issue arose and was determined in the arbitration whether, if the BR claim succeeded, innocent Tughans partners would be entitled to indemnity in respect of that part of the award to BR which represented the Tughans Fee. The arbitrator (Mr Michael Brindle K.C.), the Judge and the Court of Appeal have all held that they would.

The essence of the insurers' argument was that if BR were to succeed, it would follow that in substance Tughans never became entitled to the Tughans Fee, and so could suffer no loss in having to return it. So, it was said, (1) it was not the purpose of a professional indemnity policy to pay solicitors a sum representing profit costs to which they had never been entitled, and (2) for Tughans to be held entitled to cover would violate the principle of indemnity (that is to say, that indemnity insurance provides indemnity in respect of a loss).

The principal basis of decision of the Court of Appeal [paragraphs 40-43] is that, the contract of Tughans not having been rescinded, they had done what was necessary to earn the Tughans Fee, and what they had received was in law and equity theirs. Any award of damages would constitute a loss for the purposes of a professional indemnity policy, even if the damages were or included the amount of the Fee.

The judgment went on to review matters more widely. Two matters of general importance were immediately emphasised:

1) That the wide expression of the insuring clause is consistent with the "function of compulsory PII insurance for solicitors". The rationale of compulsion was explained by Lord Brightman in the leading speech in *Swain v. The Law Society* [1983] A.C. 598 at p.618 (in the writer's view the rationale is applicable to all professions which require members of the profession in question to have such insurance). (The first aim is to protect those external parties who deal with the professional; the second, to protect the professional against the financial consequences of mistakes of the professional, partners and staff (and, one may add, of fraud of partners and staff.)

2) That the [dishonesty] exception makes clear that for an individual insured who has not themself committed or condoned fraud, the fact that the fraud of another has given rise to liability is no bar to cover (for which both the third party claimant and the innocent partner have a commercial need).

Then, considering the policy wording and the indemnity principle:

1) A solicitor who has earned a fee suffers a loss if deprived of that fee by a liability claim [paragraphs 61-68].

2) To hold that the policy did not provide cover for the element of the claim would produce a result inconsistent with the policy identified in *Swain v. The Law Society* if the solicitors were unable to meet the claim from their own resources. (While the public policy there identified does not require unlimited insurance, the fundamental aim is public protection (wise clients checking that their professionals carry adequate insurance) [paragraph 69].)

3) Likewise, it would produce a result inconsistent with the additional basis for compulsion, which is to protect partners and employees from their own and others' negligent mistakes and fraud [paragraph 70].

4) The insurers' construction was inconsistent with the composite nature of the insurance, i.e. that the insurance provided a large number of individual insureds with rights against the insurers:

   "Any individual partner is liable for the whole of the partnership liability to BR, and may not be able to recoup the balance from the other partners"

   The Court pointed out that this liability was not proportionate to the individual's benefit from the fee earned (particularly in a large practice) [paragraph 71].

Ultimately, these matters are matters of interpretation of what insurance terms emerge from negotiation between professions and insurers, but at any given stage the existence of industry-standard terms will produce standard results across the profession; and there is no apparent reason why the position under the Minimum Terms in England and Wales would be different from that in the *Tughans* case.

This decision is important for showing the effect, for insurance purposes, of the professional having earned the fee; for the Court's regard to the rationale of compelling professionals to have indemnity insurance - a suggested interpretation which actually conflicts with that rationale is most unlikely to be accepted; for the Court's regard to the significance of a policy of this kind being composite, providing insurance to a number of individual insureds; and for the testing of suggested interpretations by consideration of the consequences of insolvency.

The decision does not mean that if a professional institutes proceedings for a fee and is met with a successful defence of, e.g., equitable set-off, to a claim, the insurers will have to pay the fee [paragraphs 81-82]. The interesting point is made that where the fee *is* paid by the party which subsequently claims all individual partners are exposed to the whole of the damages claim for the amount of the fee, whereas if the fee has *not* been paid any individual insured has only suffered to the extent of losing out on a proportion of the gross fee.

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Disclaimer: this article is not to be relied on as legal advice. The circumstances of each case differ and legal advice specific to the individual case should always be sought.