British Insurance Brokers' Association

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BIBA Response to HMRC Consultation - Raising standards in the tax advice market: professional indemnity insurance and defining tax advice'

Thank you for meeting with BIBA and some of our leading Professional Indemnity ("PI") insurance brokers earlier this week.

A summary of our main position following the meeting is explained here:

Our understanding of the issue

BIBA members report that the majority (over 70%) of tax advisers, (tax lawyers, tax accountants, IFAs) will have PI insurance already, perhaps as part of their professional body requirements as a member of the Institute of Chartered of Accountants or the Chartered Institute of Taxation.

However, we realise there are around 10,000 firms[1] that give tax advice who may not be a member of a professional body. Consequently, many of them may not have arranged PI insurance, which potentially leaves customers with no insurance 'safety net' for financial redress where there has been an instance of an error or omission and the firm is otherwise unable to discharge its potential liability.

We also understand that there is a second issue behind the move which is that the imposition of an insurance requirement may have the direct effect of improving the standards of work being undertaken.

The PI market context - availability of cover

HM Treasury and the Financial Conduct Authority are acutely aware of the extremely challenging 'hard' market for PI Insurance, with availability worse than it has ever been, with insurers having exited the market and premium rates up several hundred percent and the position is only set to get worse.

To impose a compulsory requirement to have a particular level of PI cover could create a threshold condition that could potentially not always be achieved by all firms and thus leave some firms unable to obtain the minimum cover, which would lead to their eventual sale or failure.

[1] Source HMRC who report that half might be uninsured.

To mitigate this risk, we would propose that HMRC require only a low minimum threshold requirement in line with the requirements of the professional bodies as well as a notice period of at least one year before this compulsory cover came into force.

PI is sold on a 'claims made' basis. This has numerous implications but there are two principal factors we would highlight:

(a) Because these firms have chosen to trade for some time 'uninsured', they will find it very difficult, if not impossible, to secure insurance protection against their historical activity. Insurers will need considerable comfort and premium in order to take on a decade of risk for which the insurance market has had no premium. It seems highly likely that any policies provided to this group would come with restrictions (a so-called "retroactive date") that would mean they would only have PI cover for work undertaken after the new policy came into force.

(b) 'Claims made' policies mean there is a requirement for 'run off cover'. We would urge caution in regard to any requirements around run off cover at the launch stage. Run off cover is generally regarded as unattractive business, particularly so for firms who have no significant history of buying PI cover. The imposition of particular requirements could significantly reduce market appetite. This may be best revisited after the initial requirement for any basic cover is introduced, perhaps as a step two later on. Insurers normally exclude retroactive exposure or, if they cover it at all, will charge a significant additional premium. Our concern is more of a moral hazard in that these firms deliberately chose to trade without PI.

If a tax adviser has no professional body membership and is a sole trader, it is likely they will find it harder to access insurance. However, those with an attractive CV - e.g., a former senior HMRC employee would find it easier than a part time unqualified layman who wants to start a new venture. We seriously doubt the ability of the market to offer cover for the latter.

Limits

We would suggest limits that reflect the current requirements from the professional bodies would be a good starting point to ensure a smooth transition.

Causes for concern:

Tax advisers are a high-risk area of accountancy and appetite for those already insured in this sector is already quite limited. Securing market appetite for these firms and their particular profile will be extremely challenging and it is far from certain they will be able to easily access cover.

We are concerned about the potential for the insurance market to be seen as a quasi-regulatory body, for a number of reasons:

(a) As cover will be less widely available, some firms may seek to 'blame' the insurance industry for their failure to meet the threshold requirement. This will be seen as an 'insurance industry' failing, rather than a failure to set the right conditions from the outset.

(b) The insurance industry is inappropriate for regulating others. The insurance sector operates on a system of risk based pricing and different insurers will have different attitudes to the spectrum of different risks across the tax advice sector.

(c) This impacts on the hope that insurance will drive quality. Although we hope there will be an improvement in the quality of tax advice given if this change is made, this is by no means any guarantee. Whilst most insurers will have basic ‘hygiene’ tests that insureds must meet, which include reasonably robust quality systems, pricing is largely determined by the composition of work being undertaken, the claims environment and the macro-economic state of the broader insurance market. Whilst logically the requirement to have (and pay for) insurance should drive quality, in the hope that improving the quality of work will reduce insurance cost, the two do not necessarily go hand in hand. Extremely diligent firms can have catastrophic claims which means they are objectively a ‘bad’ risk, whereas firms with relatively loose quality control systems might have none and therefore be (wrongly) perceived as a ‘good’ risk. The insurance industry simply does not underwrite in sufficient granular detail to be able to influence firms in the way you might think. Moreover, as is the case now, even the most diligent firms can be severely impacted by factors which are outside their control.

It will take significant resource from within the insurance sector to take on several thousand new tax adviser clients and this is another reason why sufficient notice before implementation is required. Equally, the Prudential Regulation Authority will want to see that insurers hold sufficient capital to be able to take on these additional risks.

Ultimately, it is highly probable some small or high risk previously uninsured firms giving tax advice may be unable to secure suitable insurance.

There will also be the potential for a number of unrated, poorly capitalised overseas insurers to temporarily enter the market and fail (as we have seen in other sectors, like solicitor’s PI insurance[2]) and we would strongly suggest early conversations are held with the PRA and FCA about insurer security in this sector. Whilst Brexit may have reduced the risk, there is nothing stopping what is known as ‘reverse solicitation’ whereby the tax adviser approaches an unrated/poorly capitalised overseas insurer for their cover, as it is cheap.

We also want to make it clear from the start that the PI Insurance products may pay for fees, certain penalties, and interest but it would NOT normally pay for the actual unpaid tax alleged.

What would help

If tax advice was defined by legislation, it may make the job of insuring firms easier.

Insurance, however, is not the complete solution. As we have seen with other extremely challenging parts of the professional PI market, the maxim that anything can be insured for a price simply no longer holds true. There are some risks which are, for want of better words, ‘too dangerous’ for the market to want to provide cover for. We fear that this cohort of firms may fall into that particular basket. In trying to secure insurance for these individuals – which we believe is the right thing to try to do – you must try and ensure that the requirement for insurance goes hand in hand with other factors. These were the ‘environmental factors’ we spoke of on the call. We would suggest you explore ways to bring forward requirements for these firms such that:

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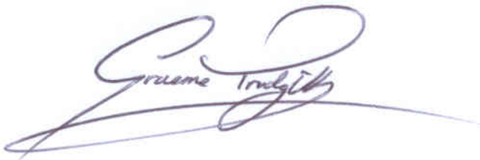
[2] https://www.sra.org.uk/sra/news/press/sif-extension-2021/

The SRA has decided to extend the Solicitors Indemnity Fund (SIF) by a further year, owing to difficulties solicitors are having trying to get PI cover that includes a run-off period.

(a) A system of registration is brought in so that we know ‘who’ the individuals are and what services they are going to undertake.
(b) As part of registration, a system of recognised qualifications and CPD are compulsory in order to be able to offer services which fall under the definition. This would not only raise standards, but it would also improve the insurability of the firms and market appetite.

I hope you find this feedback helpful, and we would be happy to discuss further.

Yours sincerely



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About BIBA

The British Insurance Brokers' Association (BIBA) is the UK's leading general insurance intermediary organisation representing the interests of insurance brokers, intermediaries, and their customers.

BIBA membership includes around 1800 regulated firms, employing more than 100,000 staff. General insurance brokers contribute 1% of GDP to the UK economy; they arrange 67% of all general insurance with a premium totalling £65.1bn and 81% of all commercial insurance business. Insurance brokers put their customers’ interests first, providing advice, access to suitable insurance protection and risk management.

BIBA receives hundreds of thousands of enquiries per year to its Find Insurance Services, online and via the telephone, which are directed to insurance broking firms.

BIBA is the voice of the sector advising members, Government, regulators, consumer bodies and other stakeholders on key insurance issues.