New SRA Accounts Rules – what you need to know

The Legal Services Board has recently approved sweeping regulatory reforms proposed by the SRA under its Looking to the Future programme. The changes are expected to be effective from April 2019.

Included within the changes is a new set of Accounts Rules. The new rules are shorter, less prescriptive and much more outcomes-focused. All of the old timescales (14 days, 2 days, etc) have been removed, and firms will be given the freedom to decide on their own time frames. The rules also give firms the option of using Third Party Managed Accounts (TPMAs), instead of holding money in client account.

The SRA has said that it expects most firms to carry on doing what they have always done when handing client money, at least to begin with. It is not quite as easy as that though, as many firms will need to make some changes to current procedures.

Key points to note include the following:

1. The new rules run to just 13 rules over six and a half pages, compared to the current 52 rules, several appendices and over 80 pages.

2. All of the rules are considerably shorter than they are now. For example, the current rule 20 (withdrawals from client account) has been reduced from nine sections and six guidance notes to three short paragraphs. The current part 3 (interest) has been condensed from four rules and 22 guidance notes to just two sentences.

3. All of the old guidance notes to the rules have been removed. Initially, the SRA promised to issue up to 15 toolkits to help guide firms through the changes, then it said it would not be issuing anything at all, and now the SRA is promising something, but we don't know when, or what it will look like.

4. The SRA had initially proposed a new definition of client money, so that money received in advance for fees and disbursements for which the firm was liable would have to be held in office account. Following widespread objection, the SRA changed its mind on this one, although the new rules do allow firms to hold these funds in office account where they are the only client monies that they hold, and provided they inform clients in advance. The SRA believes that this will allow some firms to operate without a client account in future.

5. Money received from the Legal Aid Agency for costs can in future be held in the office account.

6. Cease to hold audits will no longer be required when firms cease trading or change status, unless the SRA request one. That said, it is not entirely clear what this means, as in our experience many changes of status take place at a firm's normal year end, and therefore there is rarely an additional "cease to hold" audit anyway.

7. A significant change relates to transfers for fees and disbursements. Currently, the rules allow firms to transfer money from client account to reimburse themselves for amounts spent or incurred on disbursements without first issuing a bill. Under the new rule 4.3, firms will have to give a bill of costs, or other notification of costs incurred, to the client or paying party before they can transfer funds from client account. The SRA's definition of costs includes disbursements.

8. The concept of professional disbursements has been removed. It seems that all disbursements will be treated in the same way in future.

9. The concept of agreed fees has also been removed. Currently, money received for an agreed fee can be held in office account, even if a bill has not been raised. In future, the money will need to be held in client account until a bill is raised, unless the firm can take advantage of the change in point 4 above.

10. The new rule 8.3 formally requires the COFA or a manager of the firm to review and sign off the client account reconciliations. It also states that any differences on the reconciliation should be investigated and resolved promptly.

11. Another big change relates to client's own accounts. Currently, these are subject to just a few of the Accounts Rules, mainly in relation to record keeping and obtaining bank statements. In future, firms that operate client's own accounts will need to reconcile them every five weeks. It is not entirely clear what firms are supposed to reconcile the balances to though, as in our experience it is unusual for client's own accounts to be recorded on client ledgers.

12. The new rules permit the use of TPMAs for the purpose of receiving payments from or on behalf of, or making payments to or on behalf of, the client in respect of regulated services. In actual fact, firms are already able to do this if they wish.

13. Finally, the current exemption limits for not needing an Accountant's Report are unchanged in the new rules. However, the definition of statement or passbook balance for the exemption test has been changed, and will in future include balances held in any joint accounts or client's own accounts operated by the firm. This could mean that firms that are currently exempt will not be exempt in future.

What should firms do in advance of the new rules?

With the removal of all of the current timescales, firms need to give some thought to what could work best for them and their clients. They also need to consider whether to adopt the current rules (with suitable changes) or come up with their own approaches. Areas to consider include the following:

1. Banking of client monies received. Moving from same or next working day to "promptly". What does this mean, particularly if a firm has several offices, or there is no local branch to pay money into?

2. Transfer out of office money paid into client account. Moving from 14 days to "promptly". Again, what does this mean?

3. Transfers for costs. The new rule doesn't specifically give any timescale for these, but moving away from the current 14 days could be detrimental to cash flow. Also, what changes will be required to comply with the new requirement to raise a bill in advance of taking money for paid disbursements?

Key to all of this will be having documented systems and controls, so that everyone (particularly new joiners) is fully aware of the firm's procedures. This will also be important for reporting accountants, who will need to familiarise themselves with their clients' processes. At the moment, most firms are broadly the same, but this could all change from next year.

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