Julian Dobson SOLICITORS

Insolvency Lawyers

Solicitors and Statutory Trust

The recent case of The Law Society v Pathania [2019] EWCA Civ 517 dealt with a solicitors' practice that was intervened. The statutory power to intervene in a solicitors' practice is given to The Law Society whose powers are exercised by the Solicitors Regulation Authority (SRA). Where intervention takes place the Statutory Trust applies to all sums of money held by or on behalf of a solicitor or his firm. The effect of the Statutory Trust is one which insolvency practitioners must be aware of when dealing with solicitors' practices.

How does the Statutory Trust arise?

This happens where The Law Society ("Society") passes a resolution to intervene in a solicitors practice. The grounds for intervention can be summarised as follows:

(a) suspected dishonesty

(b) failure to comply with accounts rules;

(c) bankruptcy and

(d) to protect interests of clients/beneficiaries

Following a resolution being passed Paragraph 6 of Part II of Schedule 1 of the **Solicitors Act 1974** as amended provides:

"6 (1)…any sums of money…and the right to recover or receive them shall vest in the Society….

(2)...all sums of money held by or on behalf of the solicitor or his firm in connection with;

(i) his practice or former practice

(ii) any trust of which he is or formerly was a trustee…."

To what sums of money does the Statutory Trust apply?

The courts have considered on a number of occasions exactly what monies or assets may be covered by the Statutory Trust. In **Dooley v The Law Society 23 November 2001** the Judge held that the right to recover unpaid fees of a solicitor either before or after intervention did not vest in The Law Society as "sums of money" under Para 6(2)(a).

Lightman J commented:

> *"the right to recover sums due from former clients to the solicitor remains vested in the solicitor and the solicitor can alone commence and pursue proceedings for recovery of the debt".*

That said, recovery made in respect of such debts will automatically vest in the Society. Pending receipt, the solicitor is prevented from dealing with the debts ie, by sale or assignment.

The Dooley amendment

It was a result of **Dooley** that the statutory provisions were amended in 2007 to provide a new Paragraph 6(A) giving the Society the right to recover debts due to the solicitor.

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The Legal Services Act 2007 added an additional paragraph 6(A) which provides:

" (1)...any rights to which this paragraph applies shall vest in the Society….

(2) This paragraph applies to any rights to recover or receive debts due to the solicitor or his firm in connection with his practice or former practice

(3) Any sums recovered...shall vest in the Society..."

It was commented in **The Law Society v Pathania** that whilst there was a statutory amendment to reverse the effect of Dooley this seemingly had never been used because in a typical intervention the administrative effort involved in identifying and pursuing debts would be too great.

The Law Society v Pathania - the facts

Intervention

On 28 May 2009 The Law Society passed a resolution and intervened in the practice known as Newlands on the grounds of suspected dishonesty.

Bankruptcy

Subsequently on 29 June 2010 Mr. Pathania was made bankrupt. A year later Mr. Pathania was discharged from his bankruptcy following which he took assignments from his trustee in bankruptcy of the right to sue for various loans that he had made through his practice prior to intervention.

Loans from client account

Mr. Pathania had made some 18 loans to various parties out of funds held in his firm's client account. Some of the loans had been repaid by Mr. Pathania but some remained to be recovered following intervention.

Under one of the loans Mr. Pathania obtained judgment against a Mr. Sharif for £9,250 in respect of a loan that had been made to him. Subsequently Mr. Pathania alleged that Mr Sharif's solicitors had misappropriated the sums intended to satisfy the judgment, and Mr. Pathania claimed against the Compensation Fund.

The case was heard on Appeal and the question was:

Did the words *"all sums of money held by or on behalf of the solicitor or his firm"* include:

(a) monies paid out of the client account in breach of trust before intervention if not repaid and even if repaid

(b) the chose in action represented by the 10 remaining outstanding loans or

(c) only monies held in bank accounts or that were immediately accessible to the solicitor?

In an earlier case of **Rose v Dodd [2005] EWCA Civ 957** it was held that the object of intervention was to safeguard the interests of the public.

It did not, however, empower the Law Society to:

> *"take the practice over, to continue to carry it on by providing legal services to clients of the firm or to close it down. The ownership of the assets and goodwill of the practice are unaffected by the intervention and could be disposed of notwithstanding the intervention. Client files and client money are a different matter."*

In the case of **The Law Society v Austin [2013] EWHC 3002 (Ch)**, the Law Society intervened in a practice which had received purchase monies of £400,000 and before intervention had dispersed half the amount of its client account.

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The Law Society sought to recover the monies from the defendants on the grounds that they were constructive trustees. This was based on the argument that it was a personal claim having vested in the Law Society as a result of the intervention. On that occasion the Court rejected the idea that sums of money represented by a constructive trustee type claim would vest under the Statutory Trust.

The decision in Pathania

The Court held that intervention did not entitle the Society to recover loans previously made out of the firm's client account. However, should any of the loans be repaid then they would by caught by the Statutory Trust.

Conclusion

The decision in, **The Law Society v Pathania** confirms that "sums of money" only includes monies that are immediately accessible to the solicitor or his firm and do not extend to the right to recover monies that may have previously been paid out of the firm's client account whether in breach of duty or otherwise. The right to recover book debts belonging to the practice i.e, ordinary debts is now vested in The Law Society although The Law Society are unlikely to avail themselves of this power

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Author: Julian Dobson

1 Frederick Terrace, Frederick Place, Brighton BN1 1AX
Tel 01273 766 355 Fax 01273 766 350 **email: info@juliandobson.com Web: www.juliandobson.com**