

## Hands up for the COFA?

One of the features of the SRA's new approach to authorisation is the requirement for firms to appoint both a Compliance Officer for Finance and Administration ("COFA") and a Compliance Office for Legal Practice ("COLP").

Whilst many firms will heave a collective heavy sigh at this news, the impact for the more organised practices may not be as painful as first envisaged.

As part of the introduction of Outcomes Focussed Regulation and the new handbook, all firms which are authorised, or who wish to be authorised, need to appoint both a COFA and a COLP. This approach would appear to be part of the SRA's strategy to encourage improved risk management and to try to encourage greater governance in line with businesses that operate in other sectors.

The SRA have published detailed guidance on who can fill both roles although this article will just give an outline of what is in store for any willing COFA...

### Who can be appointed?

Unlike the COLP, the COFA does not have to be a lawyer with a practising certificate but they should be a manager or employee of the practice. In keeping with the importance of

the role, the individual should be of sufficient seniority to be able to carry out the role effectively, and as a result it is likely that partners or senior managers will best suit the appointment. If you have an individual who is particularly keen (and qualified), the same person could be both COFA and COLP although in reality this is only likely to be the case in smaller firms.

### What exactly do they do?

Based on the guidance provided by the SRA, the COFA's main role is to ensure the

practice remains compliant with the obligations of the SRA Accounts Rules. This would involve taking "all reasonable steps" to ensure that managers and employees comply. In practice this will encompass ensuring there is an adequate system in place for the security of client money, or arranging suitable and frequent training on the Accounts Rules for fee-earners and the accounts department.

What is clear from these new rules is that there is a burden of reporting that lies on the shoulders of the COFA. This represents a departure from the current position in that there is a requirement to self-regulate and report breaches to the SRA.



**Continued**

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## Hands up for the COFA? Continued

The draft SRA Accounts Rule 6 refers to compliance with the rules being the responsibility of not only the principals of the practice but also that the duty for compliance extends to the COFA. In addition to this responsibility the SRA Authorisation Rules also state that the COFA must:-

- **report any material failure to the SRA as soon as reasonably practicable**
- **maintain a record detailing any failures to comply, which could then be made available to the SRA on request**

The key questions that arise from this include

- **What exactly is a material failure?**
- **What is reasonably practicable – reporting on a monthly, quarterly, annual or weekly basis?**
- **Should you pass on this record of failures to your Reporting Accountant, and if so what does this mean in terms of the firm's annual Accountant's Report?**

The COFA will need to take steps to ensure that breaches of the SRA Accounts Rules are remedied promptly, which is hopefully the approach that most firms currently adopt. The frequency of reporting does not appear to have been defined although again this would appear to again be at the discretion of the COFA concerned.

One thing is clear amidst the uncertainty surrounding the guidance used by the SRA is that things are not totally black and white! It would therefore seem sensible for firms to be pragmatic in their approach until further guidance is forthcoming or alternatively prepare a written policy regarding the firm's system for self-reporting to the SRA. This would ensure that the COFA's responsibilities are at the very least clearly defined internally.

Once you have decided who your COFA is going to be you need to nominate that person

to the SRA by **31 March 2012**.

This candidate will then be subject to a "suitability test" and if approved by the SRA, will then be authorised from 31 October 2012. It is important that firms start to begin the process of identifying a candidate for the role as soon as possible.

For many firms it may be that there is already an appropriate person who is already carrying out the bulk of these duties albeit their title may be finance partner or finance controller. Where this is the case it is still important that internal systems are reviewed, as well as revisiting the current reporting structure within the firm, to ensure they are sufficient for the COFA to meet his or her responsibilities.

**For further information please speak to your usual WK contact or Tommy White (email: [tommy.white@wilkinskennedy.com](mailto:tommy.white@wilkinskennedy.com)).**

# Who reports?

So we now know that each Solicitor firm, through their COFA, must maintain a record of all breaches of the Accounts Rules, and then report material breaches to the SRA. I can hear you thinking – isn't that the job of the Reporting Accountant? The answer is a reserved No!

The Reporting Accountant is responsible for undertaking those tests set down in the Rules, on a sample basis, and reporting all breaches they identify except the very few that may meet the narrow 'trivial' exclusion from disclosure.

Based on this new approach the COFA will be recording all breaches, and reporting the material ones, whilst the Reporting Accountant is reporting all breaches they become aware of, irrespective of materiality and risk.

So who will be getting value from the Accountants Report? The firm should already be appraised of the breaches before the issue of the Accountants report. The SRA should be aware of material breaches by the time it sees the Accountants report.

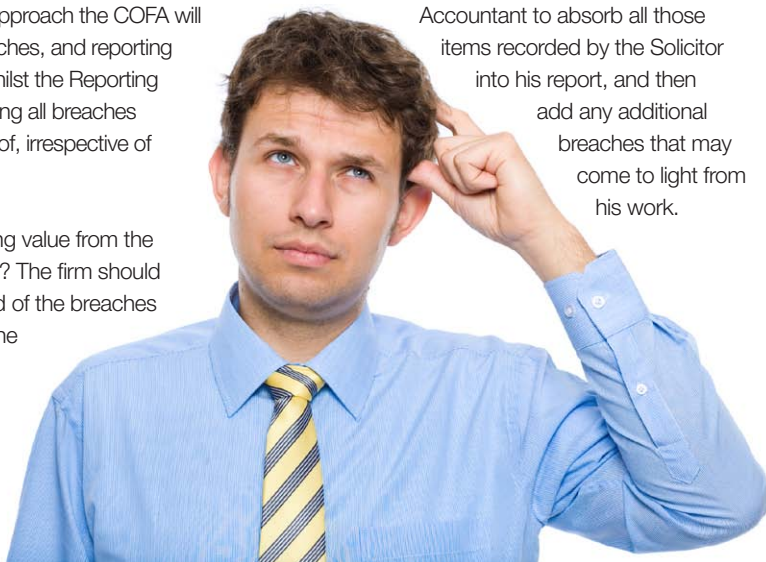
The real value will arise where it is clear that the Solicitor firm has not kept an accurate record of breaches arising, and this becomes evident when the Reporting Accountant submits his report. But how clear will it be?

The Reporting Accountant will now expect to review the record of breaches maintained by the Solicitor, and the reports of any disclosure of material breaches to the SRA. Having done so, because there is little opportunity to filter out minor breaches, it will presumably become commonplace for the Reporting Accountant to absorb all those items recorded by the Solicitor into his report, and then add any additional breaches that may come to light from his work.

In practice, it is likely that the schedule of breaches usually attached to the AR1 form issued by the Accountant will differentiate between those breaches identified (and hopefully corrected) by the Solicitor and those identified from their own work. But if the record maintained by the Solicitor is inadequate or does not include the majority of breaches, there does not appear to be a requirement for the Reporting Accountant to refer to this.

It does seem strange that the SRA have not taken the opportunity to make a change to the role and responsibilities of the Reporting Accountant. Having created an environment which requires self-reporting by the Solicitor, there is logic in expecting the Reporting Accountant to comment upon the firm's compliance with those obligations, rather than compliance only with the Accounts Rules themselves. It is early days at the moment; perhaps more changes are on their way once there has been an opportunity to assess the effect and success of self-reporting – we shall wait and see!

**For further information please speak to your usual WK contact or Bob Johnson (email: [bob.johnson@wilkinskennedy.com](mailto:bob.johnson@wilkinskennedy.com)).**



# VAT Update

## Administration

HMRC have announced a number of changes to the way in which VAT is administered. Details of some of these changes are outlined below:

### 1) Electronic Returns

From 1st April 2012, all VAT returns will have to be filed online and all VAT due is required to be paid electronically regardless of the size of the business.

### 2) VAT payments

It has been reported that mistakes have been made and penalties applied to VAT registered businesses in respect of electronic payments to HMRC on the assumption that the extra seven days grace with electronic payments means the funds need to be paid on the 7th. This is incorrect as the funds must be cleared in HMRC's bank account by the 7th. You therefore should allow at least 3 days for the funds to clear (except if payments are made by Direct Debit).

It is reported that one VAT registered business recently received a 'default surcharge' penalty for over £24,000 for being 2 days late with their payment (i.e. paid on the 7th but did not clear until the 9th), so it is well worth being mindful of these dates!

### 3) Penalties (for VAT returns and payments)

From 2012 (actual date still to be set) a new penalty system will be introduced. This will result in penalties being applied for late filing of VAT returns irrespective of whether any VAT is due (i.e. penalties will still be applied for late filing even if there is a refund due).

### 4) Registration Limits

From 1 August 2012 UK registered companies without a UK trading address will see the threshold for VAT registration reduce from £73,000 to £nil.

Aside from these changes we have also covered in this article a VAT issue which tends to cause confusion for solicitors (and accountants!) – disbursements.

## Disbursements

In relation to the recharge of costs incurred, there is often some confusion over the VAT treatment of costs 'disbursed'. Taking a typical scenario where you pick up some costs on behalf of a client. What about the VAT treatment of any recharge of the costs?

The key point is whether there is a VAT-able supply being made (from you to the client) for a consideration or is it just a case of transferring funds and simply a question of ensuring that the costs are sitting in the right place? With regards to the latter, it may be argued that, rather than being in respect of a supply of services, a recharge is in fact outside the scope of VAT as a disbursement (that is, a payment collected from a customer on behalf of a third party). The circumstances under which payments can be treated as 'VAT free' disbursements are set out below.

Payments may be treated as disbursements if all the following conditions are satisfied:

- (a) You acted for the client when paying the third party.
- (b) The client actually received and used the goods or services provided by the third party.
- (c) The client was responsible for paying the third party.
- (d) The client authorised you to make the payment on his behalf.
- (e) The client knew that the goods or services would be provided by a third party.
- (f) Your outlay is separately itemised when invoicing the client.
- (g) You recover only the exact amount paid to the third party.
- (h) The goods or services paid for must be clearly additional to the supplies made to the client.

It is usually condition (b) above that prevents expenses from being treated as disbursements for VAT purposes.

A key point is whether the costs were originally invoiced to you or the client. If this is the case, then the better view is likely to be for you to recharge the costs plus VAT to the client. You will then be able to reclaim the VAT charged on the invoices from the third parties which is off-set against the output VAT charged to the client. The position is then 'VAT neutral' for you. Your client may then be able to reclaim the VAT charged by you as input VAT, although this will depend on the client's own VAT profile.

**For further information please speak to your usual WK contact or Andy Dawbarn, VAT Partner (email: [andy.dawbarn@wilkinskennedy.com](mailto:andy.dawbarn@wilkinskennedy.com)).**



## VAT Penalties

Late filing of returns (electronically) will result in a penalty as follows:

- **1st Default: Warning (and enters 12 month penalty period) then**
- **2nd Default: £100 penalty**
- **3rd Default: £200 penalty, up to £400 per quarterly return**

Furthermore additional penalties will be applied for returns over 6 months and 12 months overdue based on the liability, plus further penalties for those who "deliberately" withhold returns of up to 100% of any liability.

Late payment (made electronically) will result in a penalty as follows:

- **1st Default: no penalty but "penalty period" starts for a period of 12 months, then**
- **2nd Default: in the next 12 months, penalty calculated at 2% of tax due**
- **3rd Default: 2%**
- **4th Default: 3%**
- **5th and subsequent default: 4% of tax due**

# Changes to the Solicitors Accounts Rules

We are fast approaching October, a significant month of change for solicitor practices across the country. We can be slightly more assured however when looking at the changes to the Accounts Rules as there are only a few amendments and one could possibly argue that they are somewhat more helpful rather than restrictive!

In this edition of WK Law we will discuss two changes to the rules.

## Client Account Signatories (previously Rule 23)

The revised rule has removed the long list of authorised signatories and the onus is very much on the firm to put in place a procedure to cover who should sign on a client account. Firms will need to implement a procedure or review their current procedures in order to adhere to this revised rule.

The procedures to be implemented should cover who is permitted to sign on a client account but be mindful as there are still certain people who are not appropriate persons. Care should be taken when selecting signatories as matters such as whether or not that person is part time or full time or how close they are to client matters should be considered.

The signature may now be in electronic format subject to safeguards and controls. It is not yet clear as to what 'safeguards' are acceptable. When using online banking we currently have passwords and/or individual codes – but it is unclear from the rules whether this be an acceptable electronic signature.

## Interest (previously Rules 24 and 25)

Up until now interest has been payable to clients on one of two bases; if monies have been maintained on a separate designated deposit, the net interest has been credited to the client. If funds remain on a general ledger account, the client is entitled to a payment in lieu of interest, the amount of which is determined by a pre-determined table. Interest need not be paid from a general client account however, if the amount is less than £20.

This rule has been updated and there is now a requirement for the interest to be paid 'when it is fair and reasonable to do so'. There will no longer be a distinction between designated client accounts and general client accounts.

Firms must therefore adopt a written policy on the payment of interest. The policy should be fair and it must also be drawn to clients attention prior to any work commencing – most likely on engagement of each matter.

It is likely that firms will be able to retain a de-minimis policy if there is one already in place, for example the £20 as discussed above.

If however it is considered 'fair and reasonable' to pay all interest received on the client account to your clients then an appropriate system should be designed which will enable a simple and easy method to calculate interest. This is important as it could well turn into a burden if for example you were to calculate interest on a line by line basis on a matter listing over well

over 30 pages! The good news is that there are many accounting packages which already calculate the interest per client for you.

## Electronic Bank Statements

At the time of going to print the draft rules allow firms to obtain and retain electronic copies of bank statements, rather than paper statements.

As we all move towards the paperless office practices could consider storing other information electronically, such as bills, as this is permitted under SAR 32 (15). The stipulation to this is that the information must be capable of being reproduced quickly in printed form, and be available for at least 6 years.

There are also many slight amendments to the rules, so it is well worth making sure you and your staff are up to speed with all the changes taking effect in October and enrolling them on any courses or refresher courses as necessary.

**For further information please speak to your usual WK contact or [Jemima Jones \(email: jemima.jones@wilkinskennedy.com\)](mailto:jemima.jones@wilkinskennedy.com).**



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