

Focus on engagement letters

(Lecture B1184 – 11.24 minutes)

This article identifies what can go wrong with engagement letters and how you can reduce the chances of things going wrong. In addition, the article will briefly consider issues relating to liability caps and "distance selling".

Retainer Issues

A common cause of claims relating to engagement letters is not understanding the scope of the retainer between the adviser and the client.

It is important to clarify who you are acting for to clarify to whom a duty of care is owed, what that duty is, what the client is responsible for and what the adviser is responsible for.

An accountant might act for a company and have an engagement letter for the company, but what happens when the Directors ask for advice in their personal capacity? Such advice would need a separate engagement letter. There is a need to consider: Who is my client? Who am I acting for?

It is important to think about: What am I doing and what am I not doing? This needs to be made clear. Without a clear engagement letter, there is a significant risk that a Court will hold that the retainer is wider than you might expect.

For example, if you are acting on a transaction in a tax scenario, are you advising on the tax consequences of a transaction, or are you advising on the most tax efficient way of structuring the transaction? If the engagement letter doesn't make it clear, you may find that you are liable for failing to advise on a more tax efficient structure.

What about where you are preparing Tax Returns for a client, based on the information he provides to you? Are you obliged to audit or verify that information? The engagement letter needs to be clear.

What if there is more than one adviser? What is your responsibility, what is the responsibility of the other adviser? Responsibilities may overlap or other tasks may be omitted from the two letters. It is important to ensure that all aspects are covered.

Fees

It is important that the fee structure is clear, that the client knows what he is paying for, and what is covered and not covered within the fee quote.

What if the work undertaken expands? The client needs to know if the fee quoted will be increased and why. Any increase in fees should be notified and agreed in advance of the work being undertaken.

Unenforceable Engagement Letters

If the engagement letter is not valid, so if it hasn't been agreed by the client, you can't prove that the client received it, or the appropriate notice under the Consumer Contracts Regulations hasn't been sent, then the engagement letter may not be enforceable and any terms contained therein, including any liability cap, will not apply. Appropriate systems need to be in place to ensure that the engagement letter is enforceable and that there is clarity as to the terms of the agreement entered into between the adviser and the client.

Reducing the chances of things going wrong

It is important that you have a system when you open a file to automatically:

- issue an engagement letter;
- check that the client has received it; and
- chase up the return of that engagement letter.

Don't create the task to chase the engagement letter at the point that you send out the engagement letter, as the ones that don't get sent out will fall through the gap.

It's worth having an automatic diary review every six to 12 months, to think about whether or not the engagement letter needs amending for additional work that has been agreed. It is all too easy to forget to do this.

To ensure that the client has received your engagement letter, send it with a covering letter asking them to do something else, like to pay money on account. When the money comes in, this provides your evidence that they did receive your letter asking them to sign the engagement letter. If for some reason they fail to sign the actual letter, you do at least have an audit trail that they received the letter and have not objected to it.

The engagement letter should state on it which terms of business have been used. Don't just say "enclosed terms of business". The terms of business need to have a date on them so that it is clear which version of the terms of business have been used.

Think carefully about when to review and reissue the engagement letter. For each client, consider when this would be appropriate. Annual clients can be reviewed annually but for other clients it might be more appropriate to review it for each transaction.

Liability caps

You need to have a system in place that allows you to alter the cap. One of the factors the Court will take into account in determining whether or not the cap is reasonable, is the fact that the cap can be changed depending on the client's circumstances.

Ideally the cap should go into your covering letter and not within the terms of business. This demonstrates that the cap can be changed. Highlight the cap in bold to bring it to the client's attention and think about the level of the liability cap but don't go too low! In determining whether a cap is reasonable, a Court will consider:

- Client's ability to pay;
- The parties' abilities to insure; and
- The ability of the parties to negotiate.

The lower you go, the more likely that cap is likely to be held as unreasonable, resulting in it being struck out by the Courts and an unlimited liability resulting.

Is a 'Multiple of fees' a reasonable approach? Is this an adequate representation of the risk? The level of fee may indicate the extent of duty, but doesn't usually indicate the level of quantum that may apply so a multiple of fee is vulnerable to being struck out for being unreasonable.

Distance selling

It is important to consider at matter level, not client level, whether the client for that matter level is a consumer and, if so, whether the contract is a distance or "off premises" contract. If so, the appropriate notice will need to be sent to the client. So for each matter you must consider whether you have met the client.

If the appropriate notice is not sent, it may be a criminal offence, but can also render the contract unenforceable. This means the liability cap, if any, contained within the contract is unenforceable and it may be impossible to recover any fees incurred in relation to the transaction.

Fees

If your engagement letter has a fee included in the engagement letter for the transaction, have a fee alert at, say, 75% of the way through the work. If at that point, you are not almost at completion, think about why not.

- What has caused the fee to overrun? Is it that you've spent too long and if so, why have you spent too long?
- Is it that the matter has become more complicated? If so, explain to the client, issue a new engagement letter, or a revision to the engagement letter. The way the client will be expecting a higher bill.
- Is it that somebody in the firm is not experienced enough, spending too long and lacks expertise? If so, you can write off the time, supervise that individual, ensure they are suitably trained and so avoid a claim.
- Is it that the client is becoming difficult? What is causing the difficulty with the client? Look to manage any issues before the client complains.

If a new/revised engagement letter is needed, issue it before you issue an invoice for the higher fee to the client, so that no issues arise with the client.

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