

## **INCORPORATION OF SOLICITORS' PRACTICES**

In 1995 the Government published a Consultation Paper on Legal Services which contained arguments in favour of allowing solicitors to incorporate their practices. (Para. 10.11 et seq.) The Consultation Paper suggested that the shareholders of such a practice would only be liable to the extent of the unpaid nominal capital of the shares which they owned. Compared to a partnership in which each of the partners is liable to the full extent of his partnership and private assets for any liability of the practice incurred by the partners or employees, incorporation is, on the face of it, an attractive proposition.

In consequence of this the Law Society supported the proposal and in due course amendments were made to the Legal Practitioners Ordinance through the Legal Services (Miscellaneous Amendments) Bill which passed into law in the end of June 1997. Those amendments were slightly unusual in that they provided the authority to enable solicitors to incorporate but left it to the Law Society to provide the rules under which incorporation was to take place.

Immediately after the change of sovereignty there was a collapse of the property market, the effective abolition of scale fees and a general economic recession. There were other more pressing livelihood issues occupying the Law Society at the time and an absence of any demand from members for rules to be promulgated to enable them to incorporate. Accordingly there was not the highest priority given to the drawing up of rules for incorporation.

However the Law Society undertook research on the issues relating to incorporation particularly in overseas common law jurisdictions including England & Wales, Australia, Canada, South Africa, Northern Ireland, New Zealand and Singapore although many such jurisdictions had marked differences from practice in Hong Kong. For example legislation in certain states in Australia allows providers of professional services to limit their liability. There has been a misconception that incorporation would enable a solicitor to limit all liability towards his client both in contract and in tort.

Having taken the advice of leading London counsel on this point the Law Society has been advised that the existing legislation does not permit solicitors to avoid liability to their clients in tort. Given the present state of the legislation in Hong Kong the reality is that a solicitor may be able to limit his contractual liability to a client of the corporation in the absence of any contractual personal duty to or fiduciary relationship with the client of

the corporation but unless he genuinely has no knowledge or involvement in the negligence of his partner/co-director he will remain jointly and severally liable with his co-director solicitors to the client. Consideration might well be given to placing a statutory cap on the tortious liability of solicitor directors with indemnity cover at least to that limit. This is the position in New South Wales where a Professional Standards Scheme applies and Western Australia is about to follow suit.

Recently we have ascertained that legislation is under discussion in Western Australia to enable solicitors to incorporate. Similarly in New South Wales where incorporation under the Legal Profession Act has existed since 1991 there are moves to enable practices to incorporate under the Corporations Act thus removing the anomaly that currently exists whereby solicitor corporations are not subject to the provisions of company law in the State. We understand that federal law in Australia permits the incorporation of bodies such as law firms and it has only been state law which has prevented law firms from incorporating with limited liability.

Having decided in principle on the most appropriate format for incorporation of a Hong Kong solicitor's practice the Law Society Council resolved to put out to tender the work of drafting the rules. In December 1998 an invitation to tender was circulated to all law firms and in mid January 1999 Messrs. Deacons, Graham & James were appointed. The firm proceeded to carry out further research on incorporation of practices and received up to date information from a number of overseas jurisdictions. A detailed comparative report on the legislation in other jurisdictions was submitted to the Law Society in June 1999 and the Society's working party met to consider the specific instructions to be given to the solicitors for drafting the rules. Detailed instructions were given in December after publication in Singapore of the Legal Profession (Amendment) Bill and in March the first draft was made available to the working party. Following consideration of the first draft at meetings of the working party further instructions were given and a second draft was submitted to the Law Society in June 2000. That draft was also discussed at length and further comments made as a result of which a third draft was received on 24 November. That draft is now under consideration and subject to some minor amendments will shortly be submitted to the Chief Justice for his approval and thereafter to the Law Draftsman.

Consideration of the issues has involved detailed discussion on the way in which solicitor corporations will conform to existing practice rules including those relating to the Hong Kong Solicitors Professional Indemnity Scheme, compliance with rules of conduct and regulatory matters all of which are intended to ensure that the way in which the profession conducts its business is maintained for the benefit of the public

yet allows solicitors greater flexibility in the manner in which they run their practices. A significant number of issues have had to be discussed and decided upon in order to achieve these ends. These include specific provisions to meet the likely demand for incorporation from sole practitioners who constitute more than 50% of the total number of firms in Hong Kong.

In England & Wales the Limited Liability Partnerships Bill received the Royal Assent in July 2000 and regulations are in the course of preparation which will lead to the first such bodies being incorporated in early 2001. It is the belief of many that LLPs constitute a more effective means of conducting a legal practice at the same time providing adequate safeguards to the public. However until they are seen in operation in England & Wales we are unable to advise as to whether this is an appropriate format for use in Hong Kong.

15th December 2000

The Law Society of Hong Kong