

E-mail: margaret@margaretn.com
Web Site: margaretn.com

15 December 2003

Mrs Percy Ma
CAS(2)3
Council Business Division 2
Legislative Council
3/F Citibank Tower
Hong Kong

Dear Percy,

Re: Item IV: Professional Indemnity of the Law Society of HK

I enclose for circulation to members the attached results of an opinion survey I conducted in October 2003 for information and discussion at the meeting of 18 December 2003 under Item IV.

The survey relates to the two calls on law firms earlier this year for extra contribution to the Professional Indemnity Fund in order to make up for the shortfall caused by the collapse of the HIH Group which was the reinsurer of the Solicitors Indemnity Fund. This unexpected consequence of the Scheme caused great concern among solicitors. In response to their concern conveyed to me, I conducted the opinion survey referred to.

Since the Law Society claims that the power to make these calls comes from the Rules, and also because in the course of the survey many people commented on whether the present scheme should be maintained or changed, the survey results are obviously relevant. The full results can be seen from my website www.margaretn.com. Enclosed herewith are :

Annex 1 : Covering letter for survey dated 7 October 2003

Annex 2 : Summary of results.

Yours sincerely,

Margaret Ng

Encl.
MN/kc

Margaret Ng
Member of Legislative Council
Hong Kong Special Administrative Region

11/F, Rm 116, New Henry House, 10 Ice House Street, Central, Hong Kong
Tel: 2869 8317, 2525 7633 Fax: 2801 7134

E-mail: margaret@margaretnng.com
Web Site: margaretnng.com

7 October 2003

To : All solicitors practising in Hong Kong

Dear Colleague,

Re: Solicitors' Professional Indemnity Scheme (PIS)

Recently, I was approached by a number of solicitors in respect of the heavy burden imposed upon them by the Professional Indemnity Fund. They fear that many firms may have to fold up unless something is done. The matter concerns the profession generally, and profession-wide consultation is desirable, especially if any legislative or policy change is to be contemplated. The attached **Questionnaire** is being sent to all practising solicitors for the purpose of gathering views.

Background

Under Hong Kong law, every solicitor who is or holds himself out to be in practice in Hong Kong must be covered by indemnity. **Section 73A** of the **Legal Practitioners Ordinance, Cap.159** empowers the Law Society Council to make indemnity rules concerning indemnity against loss arising out of claims of civil liability incurred by a solicitor or the employees in his firm. The **Solicitors (Professional Indemnity) Rules** were made for the first time in 1980. They simply required a solicitor to take out and at all times maintain with authorized insurers professional indemnity insurance in accordance with a Master Policy agreed between the Law Society and authorized insurers. Since then, the Rules had gone through changes and revisions.

The current Rules provide for professional indemnity on a common fund basis. The Hong Kong Professional Indemnity Fund Company Limited was set up to operate and manage the Fund. It enters into agreement with insurers to obtain insurance cover for claims made against solicitors and their employees. Every principal of a firm is required to pay a contribution to the Fund calculated according to a formula set out in **Schedule 1** of the Rules on the basis of the number of solicitors in the firm and gross

income. A principal who fails to pay or pay promptly faces immediate threat of solicitors in the firm being disqualified from practice and the firm being closed down by the Law Society.

In September 2001, contributions were increased dramatically by 150% to cover the high insurance premium which resulted from the escalation of claims. This sparked off a controversy at the heart of which was whether the common fund method of providing indemnity should be scrapped in favour of each firm obtaining indemnity from a qualified insurer. The matter was raised before a LegCo Sub-Committee which examined the amendment to the Rules. This eventually led to the Law Society instructing Willis China to carry out a review of the present scheme and possible alternatives. I understand Willis gave a symposium to members on 18 September 2003.

The Present Crisis

The present crisis was engendered by two calls authorized by the Law Society Council in April and July for substantial contributions to make up for the shortfall in the Fund caused by the collapse of the Fund's reinsurer, the HIH Group, in March 2001. Because the Fund can no longer look to HIH to provide cover for anticipated claims estimated to be HK\$461 million, it had to make provisions out of its reserves. According to the explanation of the Company, the Fund would run out by September 2004. The two calls covered only the deficit for the year ending 30 September 2002 of HK\$132,893,268. Further calls are expected to be made to make up for the entire amount. HK\$461 million is a staggering burden to be shouldered by the profession already struggling under tough economic conditions.

Among the small to medium firms which felt the most critical impact, there is now a feeling that their survival is a matter of indifference to their profession and the community.

Many questions have been raised. First, the sharpened question of the common fund system; second, whether the Law Society Council was right in deciding to make the calls under **paragraph 2(5)(a) and (b) of Schedule 1** of the Rules which has never been invoked before; third, the operation and management and transparency thereof of the Company; fourth, the whole question of the right balance between the extent of protection for the public and the burden on a solicitors' practice.

What is to be Done?

1. There is a strong feeling among some that there is something fundamentally wrong with the scheme as understood and operated by the Law Society Council, because it makes solicitors insurers of last resort for each other. This is because when an insurer collapses, as HIH did, liability arising from claims will have to be shared among practitioners to the full extent. No other profession in Hong Kong practises under such an indemnity scheme. HIH happened. It can happen again. If HK\$461 million is a staggering burden for 500 firms to share, there is

nothing to guarantee that this is the ceiling or that there is a ceiling at all. Can public interest fairly and reasonably require this of the legal profession?

If this is the position, then the solution is in changing the Scheme by reviewing and amending the law. The Rules have been changed and revised before. Change of circumstances justifies a new amendment. What changes should be made is a matter for discussion and debate.

2. Some members believe that the Law Society Council's interpretation of the Rules and the legislative scheme may not be right, because the Legislature could not have contemplated such an event as the collapse of the reinsurer, and could not have intended that in those circumstance, the Fund should still be maintained by making up the loss from contributions under paragraph 2(5)(a) and (b) of Schedule 1 of the Rules.

Under Hong Kong's system, the way for an authoritative interpretation to be obtained lies in judicial review. The Department of Justice also has a role in terms of legal policy. Real public interest requires a scheme which is viable, and fair to both the consumer and the practitioner.

3. There has been a suggestion that, whatever the long term solution, immediate relief is needed to give the profession a breathing space. For example, a subsidy or loan obtained from the government to cover the anticipated shortfall. In the case of a loan, repayment is to be made in full by a temporary surcharge levied on solicitors' billings.

Such expenditure from public funds would require the support of the government and approval of LegCo's Finance Committee. The level and method of surcharge will not be readily agreed among the profession. Further, temporary relief may be achieved more directly by the Company not making further top-up calls on members for the time being.

The Questionnaire

Please fill in the attached questionnaire and return it to me by **20 October 2003** so that I can take early action. The overall results of the questionnaire will be made public, but your identity and your firm's will be kept strictly confidential if you indicate that this is your wish.

Yours sincerely,

Margaret Ng

Attch.

Questionnaire on Solicitors Professional Indemnity Scheme (PIS)

Please return this Questionnaire on or before 20 October 2003 to Margaret Ng at Room 116, New Henry House, 10 Ice House Street, Hong Kong (Fax No.2801 7134/ 2179 5190).

		Yes	No	No View
Q1.	Do you agree it is wrong for solicitors to be exposed to unlimited liability in order to make up for the entire shortfall in the Professional Indemnity Fund brought about by the collapse of the reinsurer?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Q2.	Do you agree the PIS as currently operated is unfair and unreasonable in that it effectively makes solicitors responsible for each other's liability as insurers of last resort?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Q3.	Do you agree the Solicitors (Professional Indemnity) Rules should be reviewed immediately to remove the objections in Q1 and Q2 above?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Q4.	Do you agree that, in any event, the calls made are not justified by the Solicitors (Professional Indemnity) Rules, and that the Fund should be allowed to collapse?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Q5.	Do you agree demands for contributions from solicitors to meet the shortfall in the Fund, whatever the amount, due to the collapse of the reinsurer is justified because it is the profession's responsibility to maintain the Fund so as to ensure that claims by the public are met?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Q6.	Do you agree that the present hardship faced by the profession is caused by unfortunate circumstances, and that there is no need to change the PIS?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Q7.	Do you agree that, to give everyone a breathing space, no further calls for topping-up contribution to the Professional Indemnity Fund should be made at least for the coming year?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other remarks/ Suggestions :				

Personal data : Confidentiality requested

Name of Solicitor :					
I am a principal	<input type="checkbox"/>	assistant solicitor	<input type="checkbox"/>	consultant	<input type="checkbox"/>
Name of Firm :					
Sole proprietor:	Partnership (2-5):	Partnership (6-15):	Partnership (over 15):	Partnership (without stating the no. of partners):	
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Inquires : Please call Wendy Yip at 2869 8317 or email at margaret@margaretnng.com

Results of the Questionnaire on Solicitors Professional Indemnity Scheme (PIS)

		Yes	No	No View
Q1.	Do you agree it is wrong for solicitors to be exposed to unlimited liability in order to make up for the entire shortfall in the Professional Indemnity Fund brought about by the collapse of the reinsurer?	646 (96.4%)	19 (2.8 %)	3 (0.4%)
Q2.	Do you agree the PIS as currently operated is unfair and unreasonable in that it effectively makes solicitors responsible for each other's liability as insurers of last resort?	647 (96.6%)	18 (2.7 %)	5 (0.7%)
Q3.	Do you agree the Solicitors (Professional Indemnity) Rules should be reviewed immediately to remove the objections in Q1 and Q2 above?	652 (97.3%)	7 (1.0 %)	10 (1.5%)
Q4.	Do you agree that, in any event, the calls made are not justified by the Solicitors (Professional Indemnity) Rules, and that the Fund should be allowed to collapse?	488 (72.8%)	59 (8.8)	116 (17.3%)
Q5.	Do you agree demands for contributions from solicitors to meet the shortfall in the Fund, whatever the amount, due to the collapse of the reinsurer is justified because it is the profession's responsibility to maintain the Fund so as to ensure that claims by the public are met?	54 (8.1%)	577 (86.1 %)	36 (5.4%)
Q6.	Do you agree that the present hardship faced by the profession is caused by unfortunate circumstances, and that there is no need to change the PIS?	13 (1.9%)	629 (93.9 %)	25 (3.7%)
Q7.	Do you agree that, to give everyone a breathing space, no further calls for topping-up contribution to the Professional Indemnity Fund should be made at least for the coming year?	602 (89.9%)	25 (3.7 %)	40 (6.0%)

Distribution of comments in categories

Categories	Note	No. of comments
(a)	That the common fund system under PIS is objectionable and unfair	22
(b)	That PIS should be replaced by a system under which firms can get their own insurance	46
(c)	That adjustments should be made to PIS to allow different contributions for different types of practices	11
(d)	That the present level of indemnity required (\$10 million) is unreasonable	9
(e)	That compulsory insurance/indemnity should be replaced by voluntary insurance and obligatory public disclosure	6
(f)	That PIS should be replaced by a system of levies on	11

	transactions	
(g)	That PIS be scrapped/ immediately reviewed	40
(h)	That the shortfall calls should be accepted	3
(i)	That the shortfall calls are objectionable and unfair	35
(j)	That the shortfall should be met by government subsidy	9
(k)	Miscellaneous Of which,- (k1)Comments on Law Society and /or on the management of the Fund - 17 (k2)That the solicitors should be able to practise as limited company/limited liability partnerships - 9	50

Total no. of questionnaires sent (on 10 October 2003) : **5467**

Total no. of questionnaires returned (as at end of October 2003): **670**

The breakdown of respondents by position in the firm

Principal/Partner	370(55.2%)
Assistant Solicitor	171(25.5%)
Consultant	100(14.9%)
Others	8(1.2%)

The breakdown of respondents by size of firm

Sole Proprietorship	109(16.3%)
Partnership (2-5 partners)	306(45.7%)
Partnership (6-15partners)	105(15.7%)
Partnership (over 15 partners)	69(10.3%)
No. of partners not provided	13(1.9%)