

**For discussion
on 22 November 2004**

LegCo Panel on Administration of Justice and Legal Services

**Professional Indemnity Scheme
of the Law Society of Hong Kong**

The object of this paper is to provide an update of the Administration's position relating to the review of professional indemnity insurance since the last meeting on 28 June 2004.

2. A meeting was held between the Law Society and the Administration on 21 July 2004 to discuss the two options proposed by the Law Society and the way forward. Subsequently, the Administration consulted the Commissioner of Insurance on the two options. On 3 August 2004, the Administration set out its position in respect of the options proposed by the Law Society.

Legal requirements

3. The terms of the Professional Indemnity Scheme are set out in subsidiary legislation, made by the Law Society, with the prior approval of the Chief Justice, under the Legal Practitioners Ordinance (Cap 159). Any amendment to those terms is similarly a matter for the Law Society with the prior approval of the Chief Justice.

The Administration's position

4. The Department of Justice is aware of the financial burden that the current arrangements have placed on solicitors, and accepts that this burden needs to be reduced. The Administration is, therefore, not opposed to a change in the scheme, provided that consumers are adequately protected in the event of any insurer becoming insolvent. We also do not consider it to be essential that any future scheme should make solicitors the insurers of last resort. However, we consider that

consumers should not be subject to a large degree of risk of non-recovery in the event of an insurer's insolvency.

Back-up schemes

5. Ideally, any new scheme should be supported by some form of protection in respect of such insolvency. However, the Law Society considers that both a specific policyholders' protection fund and "insurance on insurance" are either unachievable or prohibitively expensive. There is currently no general policyholders' protection fund in Hong Kong, although one may be established in a few years' time.

6. In these circumstances, the Administration informed the Law Society that it had the following comments on whether either of the two options being considered by the Law Society would provide adequate protection to consumers in the event of insurer insolvency.

Qualifying Insurers Scheme ("QIS")

7. A QIS would expose a consumer to the risk of a complete loss if his or her solicitor's insurer went insolvent. This is because a single insurer would provide cover for each solicitor. We do not consider that this would provide adequate protection for consumers. As presently advised, we would not support the introduction of such a scheme.

Master Policy

8. A Master Policy, under which there were, say, four insurers would, in the event of the insolvency of one insurer, only expose consumers to the risk of a 25% loss of cover, set at \$10 million per claim. This would therefore provide better consumer protection than a QIS.

9. If other safeguards could be provided, we would consider supporting such a scheme. In that respect, we have suggested that any Master Policy should –

- (1) guarantee a minimum payment of \$2 million per claim (by way of a retention);
- (2) involve at least four nominated insurers;
- (3) require those insurers to take out re-insurance.

10. We have also suggested that consideration be given to requiring all participating insurers to be authorized (licensed) in Hong Kong and, therefore, subject to the supervision of the Commissioner of Insurance.

The Law Society's EGM

11. We understand that, at an EGM held on 16 November 2004, the majority of members of the Law Society present voted in favour of a QIS. As is stated in paragraph 7 above, we do not consider that a QIS would provide adequate consumer protection.

12. If the Law Society decides to proceed with a QIS, the Administration hopes that it will build into the scheme some mechanism for providing consumers with protection in the event of insurer insolvency. At present, the details of the scheme, the response of the insurance market, and the protection that may be afforded to consumers in the event of insolvency, are not known. At this stage, therefore, the Administration cannot say that it will support the creation of a QIS.

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