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**Paper for the House Committee meeting
on 29 October 1999**

**Further report of the Subcommittee to study three items of
subsidiary legislation gazetted on 9 July and 20 August 1999**

Purpose

This paper reports on the deliberations of the Subcommittee on the Solicitors (Professional Indemnity) (Amendment) Rules 1999. This is a further report to the one made to the House Committee on 8 October 1999 (LC Paper No. CB(2)34/99-00).

Solicitors (Professional Indemnity) (Amendment) Rules 1999 (the Amendment Rules)

2. The Amendment Rules were made by the Council of the Law Society of Hong Kong under sections 73 and 73A of the Legal Practitioners Ordinance (Cap. 159) with the prior approval of the Chief Justice. The Amendment Rules amend the Solicitors (Professional Indemnity) Rules (Cap. 159 sub. leg.) to -

- (a) exempt the Hong Kong Solicitors Indemnity Fund Limited (the Company) from providing indemnity in respect of claims arising from or are connected with the fact that any computer equipment is not year 2000 (Y2K) compliant;
- (b) provide that the above exemption does not apply to a claim where the computer equipment in question is not owned or operated by the indemnified and the claim arises solely from advice given by the indemnified to his clients in the course of his business of practising as a solicitor;
- (c) provide that the Company may have discretion in each individual case as to whether or not to pay out on a claim arising from or connected with the fact that any computer equipment is not Y2K compliant; and
- (d) make technical amendments to the Chinese text of the principal Rules.

3. The Amendment Rules have come into operation on 20 August 1999 i.e. the date of publication in the Gazette. The Amendment Rules were tabled in the Council on 6 October 1999. The deadline for making amendments to the Amendment Rules is 3 November 1999, or 10 November 1999 if extended by a resolution of the Council.

Deliberations of the Subcommittee

4. Under the chairmanship of Hon Ambrose LAU Hon-chuen, the Subcommittee had a meeting with representatives of the Law Society of Hong Kong (Law Society) to discuss the Rules. The major issues discussed are summarized below.

Hong Kong Solicitors Professional Indemnity Scheme (the Scheme)

5. In response to members' enquiries on the extent of coverage of the original insurance policy, the Law Society has briefed members on the details of the Scheme.

6. According to the Law Society, solicitors practising in Hong Kong have been required to have professional cover for negligence for themselves and their staff since 1980. The Scheme is currently managed by the Company which is wholly owned by the Law Society. The Company has delegated management of claims to the Essar Insurance Services Limited. The Scheme which comprises a mutual fund and reinsurance does not operate as a commercial insurer. A self-insured fund is established under the Scheme with annual contribution from each firm in accordance with the Scheme's rules. With effect from 1 October 1994, the amount of cover provided to each solicitor per claim is HK\$10 million (inclusive of costs). The first one million dollars of each claim is made from the fund and thereafter the remainder of the claim up to HK\$10 million is made from cover provided by re-insurers.

7. The Scheme is governed by the Solicitors (Professional Indemnity) Rules. The Scheme is intended to cover negligence by solicitors and their staff in their practice of the law. It has no provision for cover in respect of civil liability arising from the Y2K problem.

The Amendment Rules

8. In response to members' queries on the reason for excluding the Company's liability for claims arising from the Y2K problem, the Law Society has explained that it has had lengthy negotiations with Essar and the underwriters. It appears to be a common practice that within the insurance industry no cover is provided for a Y2K system failure. One reason for this is that it has always been the policy of insurers to underwrite risks which are fortuitous, i.e. events which are unpredictable rather than inevitable. Y2K is regarded as a predictable event in that problems relating to it have been widely publicized and are avoidable if appropriate precautions are taken. The purpose of the Amendment Rules is to reflect the position that the Scheme was

originally not intended to cover claims in respect of a failure of a firm's office system due to Y2K failure and will continue to be so.

9. The Law Society has also advised that commercial insurers in Hong Kong and internationally who underwrite professional indemnity insurance for solicitors believe that losses caused by or relating to Y2K could be significant. They have therefore taken steps to specifically exclude Y2K risk which is regarded as a predictable event. If amendments were not made to the Rules, the Scheme would probably be the only professional fund which covers claims arising from Y2K system failures.

10. Members have queried the justification for exempting the Company's liability by means of legislation. The Law Society has advised that as the Solicitors (Professional Indemnity) Rules are statutory, any amendments made to the Rules are therefore subject to the approval of the Council of the Law Society by way of a resolution and that of the Chief Justice as well as scrutiny of the Legislative Council.

11. The Law Society has reassured members that the Scheme will not exclude claims against solicitors for negligent advice in relation to Y2K or any other area of practice of the law but only in relation to a failure of the system.

Consultation with the Consumer Council

12. Members attending the meeting have different views as to whether the Consumer Council should be invited to give views on the Amendment Rules. Those who have made the suggestion consider that it is not unusual for committees of LegCo to consult the Consumer Council on proposals which might affect the consumers. Those against the suggestion are of the view that the Law Society has full autonomy in setting its own rules and that its decision should not be subject to the views of other organizations. If not for the fact that the Scheme is governed by statute, it would be exempt from Y2K liability like any other insurers in accordance with the market practice of the insurance industry. The Law Society has questioned whether it is fair that consultation should be made with other organizations in respect of internal rules made by the Society and is concerned about the extent of the consultation. After discussion, members have agreed that the Consumer Council should be provided with detailed background information on the Scheme and should be asked to give its views on the Amendment Rules in the light of the market practice of the insurance industry.

13. In response, the Consumer Council has advised that it is a common market practice of the insurance industry to exclude Y2K problems from the cover provided by existing insurance policies as such system failures are predictable and avoidable. Its stance is that if a Y2K failure has not been taken as a risk factor in the determination of the amount of insurance premium, it is not unreasonable for an insurer to exclude it from the insurance cover. It is however the duty of an insurer to give notice to such effect to the prospective insured well before an insurance

contract is entered into. In the case of the Hong Kong Solicitors Professional Indemnity Scheme, the Consumer Council considers that the same principle should apply.

14. The Consumer Council has made two suggestions. The first suggestion is that the Law Society should advise its members that claims arising from Y2K system failures are not covered by the Scheme and urge its members to check their office equipment and system and ensure Y2K compliance. The Law Society has confirmed that its members were advised that claims arising from Y2K system failures would not be covered by the Scheme. In a letter sent to all senior partners and sole practitioners in August this year, they were urged to obtain a system audit by a competent information technology consultant firm of their choice.

15. The second suggestion is that the Law Society might explore the feasibility of taking out a special group insurance cover against claims arising from Y2K failure of a firm's office system for offer as an option to its member firms. The Law Society has agreed to take follow up action as suggested.

Recommendation

16. The Subcommittee recommends that the Rules be supported.

Advice sought

17. Members are invited to note the recommendation of the Subcommittee in paragraph 16 above.

Legislative Council Secretariat
28 October 1999