

HONG KONG SOLICITORS INDEMNITY SCHEME

REVIEW OF INSURANCE ARRANGEMENTS

Review Report

28th November 2003

Willis

~~In Australia when a major airline became insolvent, Ansett, the Australian Government imposed a A\$10 levy on all air tickets sold to set up a fund to pay accrued employee benefits such as holiday pay, long service leave and superannuation. There are many examples of such financial strategies, where the public, or the interest of a particular section of the public, is compromised because of insolvency.~~

It has been suggested to us by a number of solicitors during our consultation process that any such levy ought to be tied to the value of the property concerned. We do not favour that course because it is complicated, and it will not allow an accurate assessment of how much HKSIF can plan to collect when it otherwise collects contributions.

Between 1997 and 2003 property prices in Hong Kong were in a freefall dropping by 60%. Published reports indicated that 168,500 homes were in negative equity. According to the Managing Director of Knight Frank Hong Kong, house prices in Hong Kong have turned around. Prices increased by 6% in the quarter ended 30th September 2003. The number of commercial property transactions doubled to 11,000 in October 2003 alone. The Government has introduced an initiative whereby a person who invests the equivalent HK\$6 million is entitled to automatic Hong Kong residency which normally takes 7 years. This is causing an upsurge in the number of buyers. Mortgage rates are competitively low with some banks offering mortgage rates of 2.5% below the current rate.

To tie any levy to the value of property would make the process cumbersome and not necessarily any fairer. The liabilities such a levy would fund are past liabilities, being recovered from clients because a business cost was not passed on to the clients in earlier years. Disclosing the passing on of that business cost is the only result of a levy. It ought to be passed on to the client in fees charged, disclosed or not.

3.8.5 Registration System – Land Titles Bill

We considered a great deal of information relating to the pending introduction of a registered title system for interests in land in Hong Kong. We consider that the introduction of a registered title system will have benefits in reducing liabilities in the long term for conveyancing claims that are related to a solicitors failing to investigate or identify a defect in the title (interest in land refers not just to ownership but an interest as a mortgagee). Those type of errors, account only for 10.48% of conveyancing claims.

Under a registered title system mistakes such as breach of undertaking, conflict of interest, delay, failure to answer requisitions, failure to conduct searches, fraud, late stamping, loss of documents and missed timed limits will still continue. Any benefits from the introduction of a registered system on the insurance scheme are not likely to be apparent until all of the land in Hong Kong has been brought under the registered system. We do not know the estimate of that period, but it may be at least the period that it takes for one generation to pass family land holdings to the next.

The introduction of the system however, does potentially create greater risks for solicitors and therefore greater liabilities for HKSIF, or any other insurer. As currently proposed the legislation requires a solicitor to certify that the applicant who registers an interest has a good title to that interest. Upon registration, title becomes indefeasible, subject to fraud and forgery.

Solicitors will therefore be increasing their potential liability as the class of persons to whom they become liable will be greatly extended and the period over which that indemnity might arise will be greatly increased. There is no proposal to establish a fund to compensate people who lose out on an interest because of registration. When the Torrens Land Title system of registration was invented in 1886 the existence of a compensation fund and a levy on every application to register any interest was imposed. In the absence of such a fund the adoption of the registered title system is likely to result in greatly increased liabilities for insurers of solicitors in Hong Kong for ten to thirty years after introduction of the system.

If the promoters of the Land Titles Bill cannot be persuaded to introduce such a fund some other funding of the liabilities or insurance is an imperative. If HKSIF continues to be the provider of indemnity to the Profession, excluding any liability arising from first bringing an interest in land under the registered system would not provide adequate protection to the public. In our view any such liabilities however, must be quarantined from the rest of HKSIF and funded differently. There are mechanisms to achieve this but because the legislation has not been passed and our efforts to find out when it will come into operation has resulted in us being informed that it may not come into operation in 2004 we do not elaborate on them.

If and when the registration of title land does becomes law in Hong Kong and if HKSIF continues to be the provider of indemnity insurance for certifying a title ought to be funded both by the practitioner concerned and the interest being registered. Those interests include financiers registering mortgages and other securities.

Contributions ought to be calculated differentially for this service (risk banded) and a penalty deductible applied. We have not recommended this course generally for liability arising from conveyancing transactions because the existing liabilities relate to transactions in past years and it is now too late to impose an extra business cost on either the solicitors conducting conveyancing transactions or their clients for transactions that have occurred in past years.

We mention in passing that we have seen two proposals from First American Title Insurance Company. The proposal to provide insurance of the title will not assist HKSIF insurers as under the proposal, is not proposed to surrender a right of subrogation against solicitors (and HKSIF) with respect to losses arising from defects in titles.

This means that if any loss arose from a defect in title as a result of negligence of a solicitor the title insurance company could claim the equivalent of that loss back from the solicitor and that solicitor's insurer or HKSIF.

Another proposal with respect to all conveyancing liabilities from all types of errors has been put to the Society. If the Society was inclined to follow that route there is no reason why it cannot do so itself by its own segregated insurance arrangements rather than through a commercial insurer. It is to be noted that in Ontario the Legal Practitioners Indemnity Company has a separate captive through which it offers title insurance in competition to commercial title insurance companies. The insured under these schemes is not the solicitor but the owner of the legal interest who pays the premium. Because the cover is offered by a captive insurer that is owned by the Law Society of Upper Canada which also owns the captive operating the professional indemnity cover for solicitors any rights of subrogation between the two are waived.

~~3.8.6 Low Fees on Conveyancing Transactions~~

During our consultation it was suggested to us that the rising conveyancing claims was partly due, or at least contributed to, by a charging of fees for conveyancing transactions which were economically unviable. This is not an insurance issue until a correlation between low fees and claims is shown.

To determine whether there is a connection or correlation between the charging of low fees and the claim, needs a detailed analysis of the facts of each claim compared with the fee charged on the transaction and other factors that might vary such as size of firm, staff ratios or the nature of the error. We have not been able to have access to any of the claims files as they would have identified firms against whom claims had been made. Our information is limited to statistics.

If there is any correlation between the two, which can only be determined by the Claims Committee HKSIF Limited and Essar, we recommend that a penalty deductible be applied to any such claim. It must be borne in mind that under a claims made policy work done in one