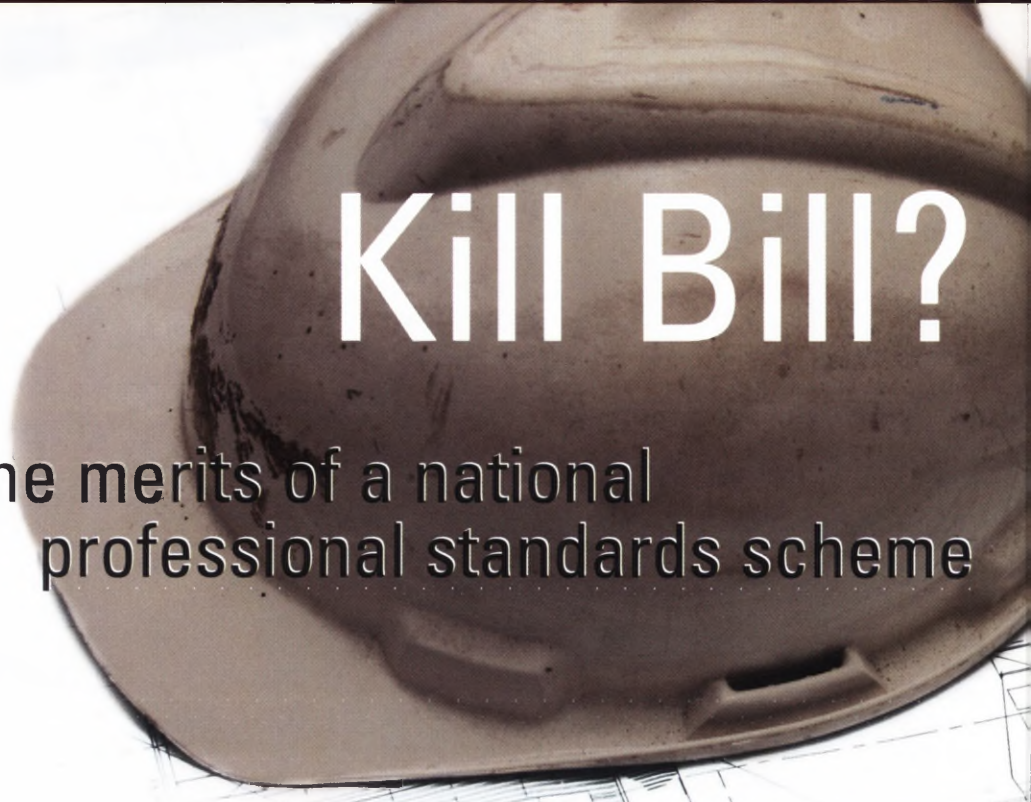

Kill Bill?

Assessing the merits of a national professional standards scheme

By Kirsty Magee

In August 2003, ministers at both a state and federal level agreed to introduce legislation establishing a national professional standards scheme. This national scheme is to be modelled on the *Professional Standards Act* 1994, which is currently in operation in NSW. While a similar scheme was introduced in Western Australia in 1997, all states and territories are now at various stages of implementing their own legislation based on the NSW model.[1]

In addition to the changes being made at a state level, the Commonwealth is also currently considering a Bill to amend several pieces of legislation that it is claimed hinder the effectiveness of the state legislation. This Bill, entitled the *Treasury Legislation Amendment (Professional Standards) Bill* 2003, went before the Senate Economics Legislation Committee which, on May 12, released its report recommending that the Bill be passed.

An analysis of the submissions to the Committee reveals that there is currently a lack of empirical information as to the effectiveness of the NSW legislation. This is compounded by the fact that Australia appears, at present, to be at the forefront of reforms limiting professional liability. It would also appear that this issue has not been the focus of many professional publications. As one journalist observed, these proposed changes have managed to slip by without so much as a 'peep'.[2]

OVERVIEW OF THE *PROFESSIONAL STANDARDS ACT* 1994 (NSW)

The premise underlying this legislation is relatively simple. It appears to involve a trade-off – capped liability for professionals in return for introducing measures to improve standards. These objectives are reflected in s3 of the Act, which states that the aims of the legislation are to limit professional liability, improve occupational standards, and to protect consumers.

Essentially, the Act encourages self-regulation by permitting members of professional associations to cap their respective liability, where they have agreed to improve standards and complaints and disciplinary procedures. To this end, it established the Professional Standards Council ('the Council') with the role of monitoring, and approving 'schemes' to limit the liability of professionals. In order to limit the liability of its members, an association must submit a professional standards scheme for approval, detailing matters such as: risk management strategies, compulsory insurance cover, continuing professional development, and complaints and disciplinary procedures. Once approved, these schemes are legally binding, and require the association to report back to the Council annually. The Council also determines the level of cap to be placed on members, taking into account the history of claims made against members and the overriding need to protect consumers.[3] This method of capping also allows the size of the firm to be taken into account. For example, under the

current scheme administered by the Law Society of NSW, members of small firms are capped at $1.5 million, while larger firms may be capped at up to $50 million. Caps on any members, however, will not affect damages claims that fall below a $500,000 threshold.

The Act has been drafted to enable broad coverage. It encompasses all occupational associations, but excludes claims relating to death, breach of trust, dishonesty, personal injury or a legal practitioner's negligence in acting in a personal injury claim.

According to the *Professional Standards Council Annual Report*, in NSW in 2002/2003 there were a total of 17,741 members of various accounting, engineering and legal associations operating under limited liability schemes. It appears, however, that many professionals have chosen not to take up the scheme.

There is no evidence that plaintiffs are actually pursuing actions under the Commonwealth legislation to avoid the state legislation.

HAS THE NSW LEGISLATION BEEN EFFECTIVE?

There is a significant amount of debate as to the effectiveness of the NSW legislation. Concerns have been raised with respect to the availability of Commonwealth legislative remedies, the legislation's jurisdictional limitations, and the continuing problems that professionals face in obtaining adequate insurance.

Remedies under Commonwealth legislation

It is claimed that the greatest hindrance to the legislation is the ability of plaintiffs to forum-shop. At present, plaintiffs may avoid the legislation by bringing claims for misleading and deceptive conduct under Commonwealth legislation, such as s52 of the *Trade Practices Act*, s1014H of the *Corporations Act*, or s12DA of the *Australian Securities and Investment Commission Act*. These are not subject to capping.

These concerns were reflected in a number of submissions made to the Senate Inquiry into the provisions of the *Treasury Legislation Amendment (Professional Standards) Bill* 2003.[4] The Institute of Chartered Accountants Australia (ICAA), for example, stated that many plaintiffs favoured the Commonwealth legislation not only because of its uncapped damages, but also owing to its broader application, as foreseeability is not a pre-requisite to recovery.[5] The Professional Surveyors' Occupational Association attributed the availability of remedies under Commonwealth legislation to its decline in membership,[6] as did the Association of Consulting Engineers Australia (ACEA).[7]

While concerns regarding the availability of Commonwealth remedies were a common theme among submissions tendered to the Committee, other organisations have argued that such claims are unfounded. The Australian Plaintiff Lawyers Association (APLA), for example, noted that there is no evidence that plaintiffs are actually pursuing actions under the Commonwealth legislation to avoid the state legislation.[8] This view is supported by information currently held by the Australian Competition and Consumer Commission (ACCC).[9] And despite the fact that the legislation has been in operation for the last nine years, offering 'ample opportunity' for plaintiffs to try to avoid it, there is no evidence to this effect.[10]

It would appear that, irrespective of whether the Commonwealth provisions are actually being used to avoid the legislation, the mere perception that this is the case has been detrimental. As demonstrated in the submissions to the Senate Inquiry, many professionals perceive this to be a significant loophole in the current legislation, leading to a fall in membership of schemes.

Jurisdictional limitations

Various professional bodies have claimed that since the *Professional Standards Act* 1994 does not cover work outside NSW, it may be avoided simply by drafting contracts outside the jurisdiction. This has particularly been a problem for engineering professionals[11] and again has been held responsible for the failure to attract more professionals to the scheme. In addition, while members are not able to contract out of their obligations, it is claimed that larger clients are >>

currently able to place pressure on professionals to leave associations, thereby escaping the application of the limited liability schemes. Professionals may be susceptible to such pressure if, as suggested by several associations, there is little differentiation in insurance premiums between members and non-members.[12]

At present, the extent of these claims is unknown, as there is no empirical information available, with the exception of internal surveys conducted by several associations. But there is clearly a widespread belief among professionals and associations that this is a problem, which in itself has hindered the effectiveness of the current legislation.

The continued problems of insurance

In spite of the professional standards legislation, professionals still claim to be experiencing difficulty in obtaining insurance.

The ICAA and ACEA have both reported significant problems faced by their members. The ACEA stated that not only had members faced enormous increases, but also that many were faced with 'outright refusal' of professional indemnity insurance, regardless of the cost.[13] It asserts that, in the past two years alone, there has been a 300% average increase for consulting engineers, with engineers in certain specialist areas simply unable to obtain insurance.[14] Similar findings have also been reported by the ICAA, with some members claiming to have experienced premium rises anywhere up to 1,000%.[15]

As a result of such difficulties, it is claimed that an increasing number of professionals have no choice but to continue working without insurance.[16] Consequently, many associations have stated that they are currently considering either reducing or removing altogether their mandatory insurance standards.[17] The difficulties in obtaining insurance are also attributed to businesses closing and professionals leaving their areas, the costs of which are felt not only by professionals but also by the community.[18]

While concerns regarding the rising costs and increasing difficulties in obtaining insurance characterised many submissions, the Senate Committee in its final report acknowledged that, at present, there remains a lack of empirical evidence in this area.[19] Currently, the statistics held by ACCC concern only half of the insurance companies, and are thus not reflective of the insurance market in general.

Despite this lack of formal data, it is certainly arguable that the professional bodies are at present best placed to be aware of the problems regarding insurance, and the fact that their internal surveys have reflected similar concerns suggests that obtaining insurance is a continuing problem, notwithstanding the professional standards legislation in NSW.

AN OVERVIEW OF THE TREASURY LEGISLATION AMENDMENT (PROFESSIONAL STANDARDS) BILL 2003

The Bill aims to prevent forum-shopping primarily by introducing measures to ensure that provisions cannot be avoided by plaintiffs who want to access uncapped damages under Commonwealth legislation. In order to achieve this, it is proposed that amendments be made to the *Trade Practices Act* 1974, *Australian Securities and Investment Commission Act* 2001, and the *Corporations Act* 2001. These amendments will ensure that plaintiffs cannot access Commonwealth remedies where the claim falls within an area covered by state professional standards legislation, and where the professional concerned is a member of an association that administers a limited liability scheme. This reform will also ensure that there is a nationally consistent approach to limiting liability, allowing professional associations to develop one scheme that will satisfy all state and territory requirements.

An increasing number of professionals have no choice but to work without insurance.

THE LEGISLATION, AVAILABILITY OF INSURANCE AND PREMIUM LEVELS

One of the criticisms of the current NSW professional standards legislation is its apparent lack of impact on the insurance problems facing professionals. Proponents of the proposed legislation claim that it will decrease insurance premiums, ensure greater certainty for clients, and improve standards overall.

Will the Bill affect premiums?

Several organisations believe that the proposed Bill will have a number of positive affects on the insurance market, arguing that it will lower professional insurance premiums, and increase the number of professionals holding insurance by providing a greater sense of certainty for potential insurers. It would appear, however, that these assertions are based merely on assumptions, rather than on any empirical evidence.

APLA[20] has stated that there is no direct connection between legislation and the reduction of insurance premiums, as associations are required to negotiate directly with insurance companies. Several organisations have, however, reported difficulties in negotiating insurance premiums. For example, the ACEA has attributed falling membership levels to the lack of differentiation between members' and non-members' insurance premiums. Similar claims were made in a number of submissions from other professional bodies.

The ICAA itself does not support the assumption that the legislation would have a positive impact on insurance premiums. The Chief Executive of the ICAA, in evidence presented to the Senate Inquiry, stated that capping liability itself will not decrease premiums. Rather, premium levels are driven by smaller claims under the $500,000 threshold, which will not be affected by this legislation.[21]

Will the legislation provide certainty for clients?

Will professional standards legislation achieve greater certainty for consumers by requiring professionals to have adequate insurance?[22] The argument is that, while in some cases receiving less, plaintiffs will at least obtain some form of compensation for their loss. This view appears to have been accepted by the Senate Committee in its final report.[23]

There is, however, no guarantee that compulsory insurance in itself will provide certainty for consumers or clients, as it remains unclear whether the legislation will improve the availability or adequacy of insurance obtained by professionals. In fact, many organisations have claimed that if changes do not occur within this area, they may be forced to reduce their mandatory insurance requirements.[24]

Is there a relationship between capping and professional standards?

Whether there is a *necessary connection* between the legislation, capping, and the improvement of standards is unclear. One of the conditions of a scheme being approved by the Council is that the association must demonstrate that it has put in place measures to improve standards; for example, through risk management strategies. But the reality is that many associations – having experienced difficulty in obtaining adequate insurance – have already implemented such measures, in order to protect themselves against the threat of litigation.[25]

UNCAPPED LIABILITY AS A DETERRENT

Various submissions put to the Senate Inquiry claimed that professional standards legislation will reduce the valuable deterrent against poor professional behaviour that uncapped liability currently provides.[26] For example, the Australian Bankers Association claimed that removing the fear of a large claim of damages may subsequently lower the quality of professional work.

In a counter-claim, Professions Australia contended that the fear of failure would remain, as certain firms will still be detrimentally affected by damages claims of $20 or 50 million.[27] In addition, it was noted that the majority of damages claims will *not* be affected, as the majority average damage claim is currently $23,248,[28] well below the $500,000 cap proposed.

However, in the author's opinion, it is not these smaller claims that serve as an effective deterrent for bad behaviour by professionals. By far the most effective deterrent is the threat of a huge payout which has the potential to cripple individual professionals and their firms.

IS THE PUBLIC LOSING OUT TO THE PROFESSIONALS?

Professional standards legislation has been described as an attempt to balance the interests of professionals against the interests of clients or consumers.[29] But is the balance that has been struck appropriate, or is it in fact tipped too far in favour of professionals?

It appears that the legislation may have several implications for clients. One of the most significant effects, it is claimed, is the shifting of risk from the professional to the consumer, which some submissions described as a shift 'from the person best placed to manage the risk to the person least able to manage the risk'.[30] This is likely to impact not only upon the individual plaintiff, but also the public, as it is inevitable that in circumstances where the wronged party cannot absorb the loss, it will eventually flow though to the community.

It has also been claimed that capping will primarily benefit larger firms, and thus those advocating its introduction are acting purely in their own 'self-interest'.[31] If the cost of claims against solicitors in 99% of claims is indeed less than $100,000, then the decision to cap liability is effectively based on fewer than 1% of claims.[32] In Rush's view, allowing capping in the favour of both professionals and larger firms not only comes at the expense of clients, but could also potentially undermine legal credibility itself.

While clearly many commentators believe that the legislation will diminish consumer rights, others have attempted to point out its benefits. For example, Marden posits that the legislation is, in fact, about 'consumer protection'. She claims that while the legal profession has previously tended to focus on the business of the profession, the introduction of professional standards legislation will 'shift the focus to encompass outcomes for the community'.[33]

In general, however, professionals are likely to benefit to a much greater extent than clients through limited liability. >>

Any 'side-benefits' – in terms of improved standards – appear to be outweighed by the potential risk that clients may have to bear, and may anyway have been introduced irrespective of the Bill.

CONCLUSION

Several factors have hindered the effectiveness of the NSW *Professional Standards Act* since its enactment in 1995. Most notably, concerns have arisen in respect of the availability of Commonwealth remedies, jurisdictional limitations and the apparent inability of the legislation to have any substantial effect on the insurance problems faced by professionals. While there is a lack of empirical data to support this view, it appears that the mere perception of these problems by professionals has had detrimental effects on the take-up of schemes.

Additionally, while the proposed professional standards legislation has the potential to address the jurisdictional limitations of the current legislation, its capacity in general to address the problems concerning professional liability remains debatable. The main concern is the 'inherent uncertainties'[34] attached to these reforms. There is presently *no* evidence as to the ability of professional standards legislation either to reduce insurance premiums or enhance professional standards. More importantly, however, there are significant concerns regarding the consequences of removing uncapped liability as a deterrent for bad behaviour, and the potential risk that would consequently shift to clients.

Until the extent of these concerns can be determined by formal empirical evidence, the potential consequences for clients and the many unresolved questions in this area warrant a cautious approach by the legislature. ■

> Professionals are likely to benefit to a much greater extent than clients through limited liability.

Notes: **1** At the time of writing, the Victorian Professional Standards Act 2003 has been passed but not assented to; the Professional Standards Bill in Queensland and South Australia are currently in the House; the Professional Standards Bill in Northern Territory is going to public comment; while the ACT has just started preparing its Professional Standards Bill, Professional Standards Council <http://www.lawlink.nsw.gov.au/lawlink/professional_standards_council>. **2** Ackland R, 'One-size plan still squeezes the little people', Sydney Morning Herald, 21 March 2004, <http://www.smh.com.au>. **3** Marden B, 'High aims for professional standards legislation', Law Institute Journal 77 (11), 2003, p33. **4** Hereinafter referred to as 'the Senate Inquiry'. **5** Institute of Chartered Accountants Australia (ICAA), Submission to the Inquiry into the Treasury Legislation Amendment (Professional Standards) Bill 2003, March 2003 <http://www.aph.gov.au>. **6** Professional Surveyors' Occupational Association, Submission to the Inquiry into the Treasury Legislation Amendment (Professional Standards) Bill 2003, March 2003 <http://www.aph.gov.au> **7** Association of Consulting Engineers Australia, Submission to the Inquiry into the Treasury Legislation Amendment (Professional Standards) Bill 2003, March 2003 <http://www.aph.gov.au> **8** Australian Plaintiff Lawyers Association, Submission to the Inquiry into the Treasury Legislation Amendment (Professional Standards) Bill 2003, March 2003 <http://www.aph.gov.au> **9** Transcript of Evidence, 29 March 2004, cited in Senate Economics Legislation Committee, Provisions of the Treasury Legislation Amendment (Professional Standards) Bill 2003, May 2004, <http://www.aph.gov.au> [hereinafter referred to as Senate Report]. **10** Senate Report, Ibid, p33. **11** Association of Consulting Engineers Australia, above n7. **12** Professional Surveyors' Occupational Association, above n6. **13** Association of Consulting Engineers Australia, Policy Position Statement: Professional Indemnity, <http://www.acea.com.au> **14** Association of Consulting Engineers Australia, above n7. **15** Institute of Chartered Accountants Australia, above n5. **16** ACEA, above n7. **17** ICAA, above n5. Note, however, that this does not apply to legal practitioners in NSW who are required to have indemnity insurance in order to practice under the Legal Professional Act 1987 (NSW). **18** ACEA, above n7, and ICAA, above n5. **19** Senate Report, above n9 at 11. **20** Australian Plaintiff Lawyers Association, above n8. **21** Senate Report, above n9 at 41. **22** This is discussed by Powell, 'Moves to Cap Lawyers Professional Liability', Bulletin 21 (6), 1999, p6. **23** Senate Report, above n9 at 22. **24** ICAA, above n5; ACEA, above n7. **25** Attorney-General, National Competition Policy Review of the Professional Standards Act 1994, Ch 5 <http://www.lawlink.nsw.gov.au>. **26** Ibid. **27** Professions Australia, Submission to the Inquiry into the Treasury Legislation Amendment (Professional Standards) Bill 2003, March 2003 <http://www.aph.gov.au> **28** Australian Competition and Consumer Commission, Public Liability and Professional Indemnity Insurance, monitoring report, January 2004, pp21-2, cited in the Senate Report at p19. **29** Hill D, 'Capping of Liability of Professionals', Australian Corporate Lawyer, 1995, 5(1) at 23. **30** Australian Competition and Consumer Commission, Submission to the Inquiry into the Treasury Legislation Amendment (Professional Standards) Bill 2003, March 2003 <http://www.aph.gov.au> **31** Rush J, 'Legal Services Market, Competition Policy, Limitation of Liability, Multi-disciplinary Practices: A Contrary View', Victorian Bar News 111, 1999, p59. **32** Ibid, at p60. **33** Marden B, above n3. **34** Gietzmann M & Quick R, 'Capping Auditor Liability: The German Experience', Accounting, Organizations and Society, 23(1), 1998, p81.

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