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IN SHORT

RISK - PROPERTY VALUES AND PI INSURANCE

February 2016

PRESENTED BY

*Peter Bates
Blair Dyer*



PRESENTERS



Peter Bates, Registered Valuer at Bates Forensic Valuation Limited, and Lawyer and Valuation Arbitrator at Baker Law, Auckland


Peter's focus is forensic valuation for disputes, statutory valuation purposes and peer review. As an experienced real estate valuer Peter's practice spans significant market cycles and a broad range of property types. He regularly provides expert evidence for mediation, public works, arbitration, WHT, regulatory body, Family, District and High Court, contexts. Peter is dual qualified as a Registered Valuer and Barrister and Solicitor.



Blair Dyer, Professional Liability Manager, Austinsure Ltd, Auckland

Blair assists a wide range of clients with their liability insurance requirements and the 'hands on' management of their claims. His experience, including leading a professional liability underwriting team, gives Blair a unique perspective on the liability exposures you may face. He is a regular presenter to many professional groups on liability issues and practical steps you can take to reduce liability exposures.

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Risk – Property Values and PI Insurance

Peter Bates
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Risk - Property Values and PI Insurance: Peter Bates

- This seminar aims to provide tools for analysis of your own legal practice to better match your profits with your risks.
- Lawyer with around 15 years' land valuation experience.
- Last 5 years focused on valuation evidence and professional complaints and claims (e.g. REAA, NZLS, WHT, DC & HC).
- The intention is not to teach the law. Rather, it is to share forensic valuation, economics and liability management perspectives of legal practice.
- Two key principles: '**Risk-Return-Ratio**' & '**Profit Risk**'.
- Economics will *mostly* be expressed here in terms of principles rather than graphs and equations.



Is the risk of your legal practice worth it? The '**Risk-Return-Ratio**'

The **Risk-Return-Ratio** is a measure of return in terms of risk over time.

- **Consider the rational investor:**
 - For high risk one should demand a high profit.
 - For low risk one should accept a low profit.
 - Eg: Finance companies v banks in the 2007 market.
- **Consider your own firm:**
 - Is your firm a 2007 finance company or an enduring bank?
 - Did you choose your risk profile or simply fall upon the work as work comes?



‘Profit Risk’ (for a law firm)

Where income concentration is such that a loss of a: handful of clients or referral sources; limited number of services; select market; small number of delivery channels, and/or; a few authors can result in significant net income volatility.

- **Two types of ‘Profit Risk’ (factor in both)**

- 1: Risk of loss and;
- 2: Risk of missed return

-Richard CB Johnsson, PhD Economics

Intuitive focus is on loss. Think about your share value halving overnight versus a news headline saying an investment you were considering buying yesterday doubled in value.



Auckland residential property market: “frenzied and volatile”

Time critical, detailed and risky transactions:

- Around 25% value growth p.a. (much of 2014 & 2015).
- Median house prices in many Auckland suburbs = \$1M+.
- Strong immigration, zoning restrictions on land, increasing building costs and shortage of housing stock.
- Desperation for first home buyers, investor buyers, etc.
- Building contracts and turn-key packages (detailed contracts).
- Auctions, multi-offers, back-ups and cash-outs.
- Complicated re-developments and new unit title legislation.
- Low interest rates, low unemployment and speculation.



Auckland residential property market: Median Sale Prices

Month	2011	2012	2013	2014	2015
Jan	\$447,750	\$470,000	\$526,888	\$580,000	\$700,000
Feb	\$457,500	\$464,000	\$525,750	\$620,000	\$686,500
Mar	\$490,000	\$500,000	\$575,000	\$652,000	\$711,000
Apr	\$465,000	\$491,250	\$566,000	\$619,550	\$753,500
May	\$464,000	\$504,000	\$570,000	\$645,000	\$750,000
Jun	\$464,000	\$528,900	\$590,000	\$626,500	\$786,000
Jul	\$470,000	\$518,500	\$585,000	\$645,000	\$757,000
Aug	\$462,000	\$505,500	\$561,500	\$630,000	\$755,000
Sep	\$475,000	\$525,000	\$599,000	\$635,000	\$790,000
Oct	\$472,750	\$545,000	\$590,000	\$655,000	\$780,000
Nov	\$491,000	\$560,000	\$621,400	\$691,500	\$795,000
Dec	\$490,500	\$550,500	\$629,000	\$720,000	\$800,000

see www.barfoots.co.nz

Ease of doing business

World Bank Group 2015 analysis and ranking for New Zealand economy:

Ease of Doing Business Rank	Starting a Business	Dealing with Construction Permits	Getting Electricity	Registering Property	Getting Credit	Protecting Minority Investors	Paying Taxes	Trading Across Borders	Enforcing Contracts	Resolving Insolvency
2	1	3	31	1	1	1	22	55	15	31

- Should this change for 2016 onward?
- What would you expect for registering property, getting credit or paying taxes if you were a:
 - foreign investor;
 - tax advisor;
 - conveyancer, solicitor or legal exec?

Regulatory processes & responses

- 'Brightline' test: forms, advice and consequences.
- IRD numbers and 'Certifier [you]' on title documents.
- Bank account and foreign tax numbers.
- "[IRD] struggling to process tax numbers for offshore investors, with rumours 12,000 are tied up in a bureaucratic –bottleneck" NBR 18.12.2015
- Loan to value ratio (LVR) restrictions introduced.
- LVRs tightened and targeted to Auckland investors (30%!).
- MSD & Kiwisaver forms, processing and timeframe issues.
- Anti-money laundering documentation.
- Post-2007 changes for non-bank lenders FAA and REAA.
- More to come: Income to debt servicing requirements?

Details, details, details...

The increase in professional and administrative time and detail required of law firms increases the circumstances in which errors might occur – increasing law firms' risks.

However, from a client perspective, there is potential for error and frustration with forms and time required to comply and produce information. A client might not qualify, or may owe tax as a result of regulatory changes rather than lawyer error.

This sets the context in which a client might feel let down or frustrated. Expect complaints...

Difficult situations

- Kiwisaver processing too slow for settlement drawdown (NZLS complaint – advise in writing).
- Definition vs circumstances: “main home” advice.
- Unconditional buyer believed “pre-approved” for finance, but was not due to policy change, fine print, or regulation.
- Check registrations and notices for vendors **and** purchasers.
- Law firm mistakes COA for CCC. Result: no claim on Council for negligent issue of CCC. Value - claim against the lawyer.
- Time-barred leaky buildings claims shifts target to latest professionals for a deep pocket claim (PI policy).
- Defective titles, landslips, leaky buildings, etc. Lack of other professional advisors (eg no valuer, or building surveyor): ... expect a higher risk of a claim.

Institutional claims in market cycles

“The collapse in the property market which accompanied the recession at the beginning of the present decade caused mortgage lenders to suffer serious losses. **Unable to recover their advances from the borrowers or by the enforcement of their security they have sought to recover them from the valuers or solicitors** on whose valuations or advice they have relied.

In some cases they have been the victims of a fraud to which the valuers and solicitors have been parties. In other cases, such as the present, they have been **unable to accuse their solicitor of anything more serious than negligence.**”

Bristol and West Building Society v. Mothew (C.A.) per Millett L.J. (pp 438-439)

Law firm considerations

Balancing profit to risk (Risk-Return-Ratio and Profit Risk):

- Time and processes *cautioning clients in writing*.
- Time required by various staff.
- Extent of documentation and detail (records of errors).
- Quantum exposure – high value – high liability.
- Number of potential claimants.
- Lack of other defendants (professionals, Council, etc.)
- Re-allocation of risk outside the firm (eg PI cover).
- Specialisation v general practice and labour supply.
- Durability for market fluctuations and profit opportunities.
- Fees and business relationships.

Tools

- Commerce Act, L&C Act, Conduct and Client Care Rules & fiduciary duties... rules can also be a wise guide.
- Decide if you want to be a high or low risk practice with relatively high or low profit (Risk-Return-Ratio).
- Consider Profit Risk: risk of loss and risk of missed profit.
- **BEWARE THE STAGNANT 'FIXED FEE' OR 'FLAT RATE':**
Ensure fees relate to the liability risk potential, eg:
 - high value conveyancing = higher fee, and;
 - more detail or 'dicey' client, more risk = higher fee, etc.

Tools continued

- Examples of internal profit risk analysis systems:
 - Implement internal conveyancing master-list with sale price included. Monitor exposure to high value real estate and volatile real estate types such as new apartments, subdivision land, or where parties might have a higher risk of default (finance company deals, etc.).
 - Allocate a staff member to confer and analyse where regulatory or other changes may require more time or detail with increased risk of error and consider allocating additional fees for that risk.
 - Monitor circumstances in which complaints and claims arise.

Tools continued

- Consider your PI policy:
 - ensure appropriate PI cover for type of work and quantum of liability;
 - regularly review cover relative to business practice, and;
 - train staff to be aware of what is now covered and the firm's policy in relation to such risk exposures.
- Consider and review at what price point you would be better to price your firm out of work and take other work with a lower risk profile (the 'walk away' approach).
- Make a simple risk-sensitive fee scale (so staff can tell clients).

Example 1 of a fee scale in the context of real estate risk:

Real Estate agents: see www.barfoots.co.nz

Residential sales commission rate calculation (GST exclusive):

On the first \$300,000
of the purchase
price* 3.95%

On the balance of the
purchase price* 2.0%

Minimum commission
rate of \$8,000 + GST

Selling price	Barfoot & Thompson commission	Typical Auckland commission*
\$300,000	\$13,628	\$13,683
\$400,000	\$15,928	\$17,238
\$500,000	\$18,228	\$20,025
\$750,000	\$23,978	\$26,232
\$1,000,000	\$29,728	\$32,438
\$1,500,000	\$41,228	\$44,852
\$2,000,000	\$52,728	\$57,265
\$3,000,000	\$75,728	\$82,091
\$5,000,000	\$121,728	\$131,744

Example 2 of a fee scale in the context of real estate risk:

A valuation company's residential
real estate valuation fees at 2003:

"Minimum fee: \$380 excl GST

Formula: Up to \$300,000 - \$380
plus GST. Thereafter \$5 plus GST per
\$10,000. Or \$50 plus GST per
\$100,000 up to \$5,000,000.

Urgency: Add \$100-\$200 plus GST."

**At 2016: \$650,000 base @ 0.001%
+ risk and time fees + GST and disb.**

Value	Fee excl GST	Fee incl GST
\$300,000	\$380	\$427.50
\$350,000	\$405	\$455.63
\$400,000	\$430	\$483.75
\$450,000	\$455	\$511.88
\$500,000	\$480	\$540.00
\$600,000	\$530	\$596.25
\$700,000	\$580	\$652.50
\$800,000	\$630	\$708.75
\$900,000	\$680	\$765.00
\$1,000,000	\$730	\$821.25
\$1,250,000	\$855	\$961.88
\$1,500,000	\$980	\$1,102.50
\$1,750,000	\$1,105	\$1,243.13
\$2,000,000	\$1,230	\$1,383.75
\$2,250,000	\$1,355	\$1,524.38
\$2,500,000	\$1,480	\$1,665.00
\$2,750,000	\$1,605	\$1,805.63
\$3,000,000	\$1,730	\$1,946.25
\$3,500,000	\$1,980	\$2,227.50
\$4,000,000	\$2,230	\$2,508.75
\$4,500,000	\$2,480	\$2,790.00
\$5,000,000	\$2,730	\$3,071.25

Risk reduction – assumptions

- A building surveyor's and registered valuer's advice often reduces a lawyer's risk exposure.
- The bank says you don't need a valuer? Trustee's duties...
- Loss may be more than full price or market value. Some properties have nil or a negative market value - *Jerard v Paxton and Paxton* [2014] NZHC 2493. See [31], [32], [45].
- Parties should not be advised by lawyers to proceed based on dated external advice. Changes mean more work and risk (eg: requiring authority delays in PWA compensation - you should seek updated valuation advice with fee & costs).
- External advice should be clear and well supported. Eg: land valuation advice in: *Messenger & Anor v Stanaway Real Estate Limited* [2015] NZHC 1795. See [105] to [111].

Externalization of risk (PI)

Consider your professional indemnity insurance cover and whether your day to day practice matches your intended transfer of risk to the insurer:

- Work for family not covered by PI?
- Working both sides (transfer into company or settlor to trustee) not covered by PI?
- Former employee not covered by PI policy wording?
- Defence costs covered by PI? *Steigrad v BFSL 2007 Ltd - SC*
- Regulatory body cover appropriate? Just \$100,000?
- Cover consistent with liability risk exposure (rising values)?
- Policy cover jeopardised / voided by conduct or ToE?
- Do your staff know which work is not insured?

Adaption v status quo?

Questions and conflicts:

- Allocation of true costs – should one legal service subsidise others? Sometimes? When? Review?
- Tougher times may inspire claims.
- Rational self-interest and professional responsibility.
- Would you rather go out of business by overcharging or under charging? Is this flippant, or is it worth considering:
 - what of your clients if your firm goes bust?
 - what of access to justice and continuity of legal services?

PI Insurance: Blair Dyer

Are Auckland PI claims different?

- Issues with multiple titles – apartments etc.
- Unclear titles or lack thereof
- Leaky Buildings – (*what is next*)
- Loss of Profit/Revenue/Opportunity
- Time Pressures
- Larger claims

“Yes I feel there are differences”

PI Insurance

Does Auckland raise PI risk?

- Notification problems
- Negligence vs Omission
 - Professional duty vs professional services
- Relation Property
- NZLS complaints
- Managing Expectations

“Increased likelihood of claim activity”

Adequacy of PI Limits

Average Limits have not changed in 20 Years

Despite

- Inflation estimate. 49%
- Limitation Act 2010
- Section 9 Insurance Law Reform Act
- Increase in property value (*reduction in coverage*)
- Larger mortgages, lower interest rates

Suitability of PI Insurance

Are PI policies consistent with Auckland issues?

- Conflict of interest conditions
- Leaky Buildings
- Other property related exclusions
- Contractual/assumed liability
- Cut & Run provisions
- Claims in excess of limit
- Settlement of claims

“Greater potential for the ‘grey’ at claim time”

What to do?


You should consider?

- Increasing Limit of Indemnity
- Request for higher limits (from lenders or clients)
- Key Decisions
 - Broker vs Insurer/Cover
 - Cover vs Premium
- Read your policy
 - Understand relevance to your business,
 - Does it match your risk/profitability profile
- Run-off Liability

Questions



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Risk – Property Values and PI Insurance

Peter Bates
Blair Dyer

February 2016

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RISK – PROPERTY VALUES AND PI INSURANCE

Peter Bates
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Introduction

All law firms are exposed to risk. Work undertaken should be managed to ensure that the income generated is worthwhile in terms of that risk. The following aims to provide tools for aiding such decisions. The intention is not to teach the law. Rather, it is to share the forensic valuation, economics and risk management perspectives of legal practice to better match profit with risk. Economics will largely be expressed here in terms of principles rather than graphs and equations with a focus on two key principles: '*Risk-Return-Ratio*' and '*Profit Risk*'.

Assessing Risk

The *Risk-Return-Ratio* can be used to measure the return achieved on work in terms of the risk involved in completing that work over time. In short, it can be used to determine if the income generated is worthwhile once it is off-set against the risk to which it exposes the firm. For example, a rational investor undertaking a high risk project will expect to make a large profit, while an investor in a low risk enterprise will be content with a lower profit. This is evidenced by the position of finance companies in contrast with the position of banks in the 2007 New Zealand credit-investment market.

With this in mind firms should review their practices to determine their risk profile. In terms of risk, is the firm a 2007 finance company or an enduring bank? The answer to this is often closely related to the firm's attitude to taking on work and the systems around completion of work. Is all work simply accepted as and when it comes? Or, does the firm have set systems in place for identifying risk levels and determining the most efficient way to manage types of work in terms of profit and risk exposure over time.

Profit Risk particularly relates to the risk that profits may be lost or not made. Thus, it can be recognised in two key forms: 'risk of loss' and 'risk of missed return'.¹ Both of these factors should be included in the law firm's risk assessment process. The intuitive focus is on loss. Think about your share value halving overnight versus a news headline saying an investment you were considering buying yesterday doubled in value.

Consider the impact on the firm's profits in terms of income concentration. For example, having only a small number of clients or referral sources, a limited number of services, a select market, a small number of delivery channels, and/or only a few authors can contribute significantly to net income volatility. Where a firm only works for a small number of large clients, it is easy to imagine the consequence of losing a single client.

Take, for example, the risk involved in operating in the frenzied and volatile Auckland residential property market. The Auckland residential property market has seen around 25% value growth p.a. (2014 and 2015 – with some softening / moderation in late 2015)

¹ Dr Richard CB Johnsson, *A Simple Risk-Return-Ratio*, 25 July 2010, www.richardcbjohnsson.net.

with the median house prices in many Auckland suburbs now sitting at \$1,000,000 or more. With strong immigration, zoning restrictions on land, and increased building costs added to a shortage of housing stock, working in such a market necessarily entails work that is time critical, detailed and risky.

The nature of the current market increases the desperation of first home buyers and would-be investors. This motivates the purchase of properties under building contracts and turn-key package arrangements, often necessitating detailed contracts. Such a frenzied market also changes the nature of purchase arrangements due to the prevalence of auctions, multi-offers, back-up offers, cash-out clauses and complicated re-developments. In recent years this has been further complicated in some cases by regulatory and legislative changes, such as the new unit title legislation. With low interest rates, low unemployment and speculation, the more detailed arrangements require considerable care. These, often time consuming, factors create more risk for law firms.

Ease of Doing Business

In 2015, the New Zealand economy was ranked second in the world for ease of doing business and first for both ease of registering property and getting credit.² What would the impact be if this were to change for 2016 onward? What ranking would be expected for registering property, getting credit or paying taxes if you were a foreign investor, tax advisor, conveyancer, solicitor or legal executive?

Changes to regulatory processes and the required responses to these changes have also increased the professional and administrative time and detail required of law firms. The changes may affect the forms and processes to be completed by the firm itself, or may affect those of third parties involved in the transactions. For example, it is reported that the IRD was rumoured to be: “struggling to process tax numbers for offshore investors, with rumours 12,000 are tied up in a bureaucratic bottleneck”.³

Either way, increased complexity equates to increased risk for the law firm. For example, when processing transactions, a law firm now has to take into account (directly or indirectly):

- the ‘Brightline’ test and associated forms, advice and consequences;
- IRD numbers and ‘Certifier’ displayed on title documents;
- bank account and foreign tax numbers;
- loan to value ratio (LVR) restrictions, which have been introduced in recent years;
- LVRs tightened and targeted to Auckland investors (30% equity required!);
- MSD and Kiwisaver forms, processing and timeframe issues;
- anti-money laundering documentation;
- post-2007 changes for non-bank lenders, the Financial Advisors Act 2008 and the Real Estate Agents Act 2008, and;
- more regulatory impositions might come, such as income to debt servicing requirements.

² World Bank Group, www.doingbusiness.org/rankings, last accessed 5 February 2016.

³ National Business Review Online, www.nbr.co.nz, 18 December 2015, *Tax red tape delays hit foreign investors, hot stocks to watch, Auckland city squeezed*, last accessed 5 February 2016.

The increase in professional and administrative time and detail required of law firms increases the chance of error – increasing law firms’ risk. However, from a client perspective, there is potential for error and frustration with forms and time required to comply and produce information.

A client might not qualify, or may owe tax, as a result of regulatory changes rather than lawyer error. This sets the context in which a client might feel let down or frustrated and increases the likelihood of complaints. A myriad of difficult situations can arise from seemingly simple transactions.

Although few may wish to admit it, practitioners can, and do, find themselves in very difficult situations. Some are of the lawyer’s own making, while others are not. For example:

- A client complaining that a lawyer did not adequately advise that Kiwisaver processing can be too slow for settlement drawdown (exemplified in a recent NZLS complaint).
- Dealing with a frustrated unconditional client who was “pre-approved” for finance, but due to policy change, fine print, or regulation in fact is not.
- Failure to fully check registrations and notices for purchasers *and* vendors.
- Mistaking a Certificate of Acceptance for a Code Compliance Certificate (CCC) where a contract is subject to a CCC (result: no ability to claim against Council for negligent issue of a CCC).
- Advising on the new “main home” definition in unique circumstances (for example, where two adjoining properties are held and used together as one primary residence).

As more leaky building claims are found to be time-barred this can shift the target to the latest professionals for a deep pocket claim. This is due to their Professional Indemnity insurance policy cover (PI cover). A higher risk of a claim should also be expected in instances of defective titles, landslips, leaky buildings, etc. especially where there is a lack of other professional advice. Other professionals, such as valuers or building surveyors, may identify issues that could affect the purchaser’s decision to proceed. In these instances, the risk to the lawyer is substantially reduced, as the issue was known pre-settlement. Often settlement will not proceed where other professionals have identified defects or risks with a property. This means a purchaser client is less likely to experience loss which might otherwise leave them looking for a party against whom to claim.

The potential risk of an institutional claim will often relate to the market cycle with volatile markets leading to increased risk. For example⁴:

“The collapse in the property market which accompanied the recession at the beginning of the present decade caused mortgage lenders to suffer serious losses. **Unable to recover their advances from the borrowers or by the enforcement of their security they have sought to recover them from the valuers or solicitors** on whose valuations or advice they have relied.

In some cases they have been the victims of a fraud to which the valuers and solicitors have been parties. In other cases, such as the present, they have been **unable to accuse their solicitor of anything more serious than negligence** [emphasis added].”

⁴ See decision giving context of *Bristol and West Building Society v. Mothew* [1998] Ch1, per Millett L.J.

In a changing market, law firms should carefully consider balancing risk and profit (in relation to both Risk-Return-Ratio and Profit Risk). This should include consideration of the time and processes involved in cautioning clients in writing, as well as the overall time required by various staff. Law firms should consider the extent of their documentation and the level of detail (potential records of errors).

The quantum exposure should be calculated bearing in mind that high value often equals high liability. When assessing risk also consider the number of potential claimants – is there a lack of other defendants (professionals, Council, etc.). Also, consider the durability of the firm's structure in terms of market fluctuations and profit opportunities, fees and business relationships. Further, consider how risk can be re-allocated outside of the firm (by PI cover) and the implications of specialisation versus general practice and labour supply.

PI Insurance

When determining the risks and rewards associated with working in the Auckland property market particular attention should be paid to how this 'risk' impacts on professional negligence claims against the legal profession.

With conveyancing claims or claims involving property, such as relationship property, that involves the Auckland market, the more prominent characteristics include issues with:

- multiple titles – body corporates, commercial and residential property;
- unclear title or lack of title;
- leaky buildings;
- loss of profit, revenue and opportunity;
- timing pressures, and;
- greater levels of compensation sought.

It would appear that, in general, the Auckland market does negatively impact on claims against the legal profession. Such claims of negligence are likely to:

- involve more complexity;
- be for larger amounts;
- be more costly to resolve, and;
- present more issues for obtaining insurance cover.

It is, therefore, critical that firms review their PI cover and the approach taken to this vital risk mitigation tool. Start with two key questions:

- who will be your insurance broker and why, and;
- who will be your insurer and why?

Tools for Reducing Risk

First decide whether the firm is to be a high or low risk practice with relatively high or low profit (Risk-Return-Ratio). Consider Profit Risk: the risk of loss and risk of missed profit. With this in mind, beware the stagnant 'fixed fee' or 'flat rate'. Ensure fees relate

to the liability risk potential and adjust to meet the context of changing liability and risk profiles, such as increasing real estate values.

Fiduciary duties, legislation and regulations such as the Commerce Act 1986, Lawyers and Conveyancers Act 2006, Conduct and Client Care Rules 2008 (especially r 4.1 and r 9.1) provide some restrictions on fees but also can be a natural guide to risk assessment. Other good resources such as the Eurojuris International Risk Management Manual⁵ can give useful guidance for self-assessment of risk.

High value conveyancing should equate to a higher fee, and more detailed transactions or ‘dicey’ clients, which involve more risk should equate to a higher fee. Consider and review at what price point the firm would be better to be priced out of work and take other work with a lower risk profile (the ‘walk away’ approach).

Make a simple risk-sensitive fee scale (so staff can tell clients). The slides which are associated with this paper show examples of fee scales used by real estate agents and valuers who also deal with professional liability in the real estate market. In both cases there is a minimum or base fee which might relate to the cost of administrative support and other basic processes. The fees then increase in relation to the sale price or likely value of the property. For valuers, there are additional fees for more complicated property types or urgency. Agents would usually charge in addition for certain advertising. Thus we have an adjustable fee scale which can provide a useful example for Auckland law firms.

Internal profit risk analysis systems could include, for example, implementing an internal conveyancing master-list which includes the sale price and risk profile. This way, the firm can monitor exposure to high value real estate and volatile real estate types such as new apartments, subdivision land, or where parties might have a higher risk of default (finance company deals, etc). A staff member can be allocated to confer and analyse where regulatory or other changes may require more time or detail with increased risk of error. The firm can then consider allocating additional fees for that risk. The firm should also monitor circumstances in which complaints and claims arise.

When focusing on risk assessment, a key aspect is addressing existing assumptions. For example, the bank says you don’t need a valuer. Is this in fact correct? What about Trustee’s duties? There are many highly relevant trustees’ duties⁶ (such as investing prudently and taking advice). In practice a building surveyor’s and registered valuer’s advice may serve to protect the client but often reduces a lawyer’s risk exposure.

It is sometimes assumed that a lawyer’s risk exposure is likely to be only a percentage of the total contract price. However, the loss suffered on a property may be more than full price or market value. Properties can later be found to have nil or a negative market value.⁷

External advice should be current and fit for the purpose for which it is sought. Parties should not be advised by lawyers to proceed based on dated external advice. Changes mean more work and risk (for example, where a requiring authority delays in public works compensation). Updated valuation advice with fees and costs should be sought. External advice should also be clear and well supported.⁸

⁵ www.eurojuris.net, last accessed 5 February 2016.

⁶ See for example, Trustee Act 1956, ss 13B, 13C, 13E, 13F and 13G.

⁷ *Jerard v Paxton and Paxton* [2014] NZHC 2493 - See [31], [32], [45].

⁸ See, for example where, one of the expert witnesses could not support a stated land value in: *Messenger & Anor v*

Another key tool is the externalization of risk such as through PI cover. PI insurance cover should be assessed to ascertain whether the day to day practice matches the intended transfer of risk to the insurer. The firm should also be clear on what exactly is covered under the policy. PI cover should be appropriate for the type of work and quantum of liability. Firms should regularly review PI cover relative to business practice. Staff should be made aware and kept up to date with what is covered and the firm's policy in relation to such risk exposure.

Where law staff are unfamiliar with insurance policies, they might proceed based on assumptions. Such assumptions could leave the firm without cover in the event of a claim. Law firms should ask, for example, if a lawyer in the firm does work for a family member will this be covered? If the firm is working for both sides, for example, when transferring property into a company or from a settlor to a trustee, is this covered? Be clear on whether the policy wording covers *former* employees for work done while at the firm.

In the wake of *Steigrad*⁹ ascertain whether defence costs are independently covered. Is the regulatory body cover appropriate? If it is the typical \$100,000, it might not be sufficient if expert witnesses, appeal and / or judicial review are needed. Ensure that staffs' conduct and wording for documents (such as terms of engagement, undertakings and supply agreements) do not inadvertently void PI cover. Finally, assess whether the PI cover is consistent with the firm's liability risk exposure (rising values) and ensure that staff know which work is, and which work is not, insured.

Conclusion

As is appropriate for professional practices, the hard questions and issues need to be dealt with by largely autonomous professionals in the day to day business of law. The nature of professional 'risk' is such that there can be apparent conflicts, yet simultaneously apparent complements of purpose or effect. It is the practitioner who must first decide what is appropriate for the circumstances. Should one legal service subsidise others? Sometimes? When? Review?

Tougher times may inspire claims. Rational self-interest and professional responsibility can appear conflicting but also have a common interest. A degree of self-interest can preserve the firm and ensure the viability of available legal services. One could ask: Would you rather go out of business by overcharging or under charging? This may seem a flippant question. However, it is worth considering what harm there might be to clients if a firm goes bust and what of access to justice and continuity of legal services?

It is hoped that the issues and tools highlighted in this paper may enhance legal practice and reduce risk in fast paced 'frenzied and volatile' legal practices.

Stanaway Real Estate Limited [2015] NZHC 1795. See [105] to [111].

⁹ See: Law Reform Act 1936, s9(1) and the full series of *Steigrad v BFSL 2007 Ltd* decisions up to the Supreme Court, culminating in allowing the two appeals (SC 19/2013 and SC 21/2013): Summarised in the 23 December 2013 Supreme Court of New Zealand Media Release: "*The appellants in both appeals submit that they have a statutory charge over the insurance moneys payable to the directors in respect of their claims, with the effect that defence costs cannot be paid under the policies if to do so would deplete the funds available to meet the directors' liability if eventually established... The Supreme Court has, by majority (comprising the Chief Justice, Glazebrook and Anderson JJ) held that the statutory charge covers whatever the amount of liability to the third party eventually turns out to be. Reimbursement to the directors of their defence costs is not within the statutory charge. It is immaterial under the statute that the contractual obligation to pay the directors' defence costs arises when the costs are incurred and that liability on the claim for damages is not yet determined or payable. The effect of the charge is that payments under the insurance policy to meet the directors' defence costs can be met only at the peril of the insurer when there is insufficient insurance cover under the limit of the policy to meet both insurance obligations.*"



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2
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1.5
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DATE

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