

Consultation paper on the interest rate payable on fidelity fund claims

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LEGAL PROFESSION
Uniform Law

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Call for submissions

The Legal Services Council (**Council**) invites public comment on a proposed rule in relation to the interest rate payable on fidelity fund claims. Submissions can be sent to the Council by email to: submissions@legalservicescouncil.org.au on or before 18 September 2020, and may be published on the Council's website unless you advise us otherwise.

Overview of Part 4.5 of the Uniform Law

The Legal Profession Uniform Law (**Uniform Law**) commenced on 1 July 2015 in Victoria and NSW. The objectives of the Uniform Law framework are to promote the administration of justice and an efficient and effective Australian legal profession through:

- interjurisdictional consistency in the law applying to the Australian legal profession
- ensuring legal practitioners are competent and maintain high ethical and professional standards
- enhancing the protection of clients and the public
- empowering clients to make informed choices about their legal options
- efficient, effective, targeted and proportionate regulation, and
- a co-regulatory framework with an appropriate level of independence for the legal profession.

Part 4.5 of the Uniform Law provides for a fidelity cover scheme, which is a system that provides a source of compensation for clients who have lost trust money or trust property as a result of a default of a law practice. In Victoria, the scheme also covers defaults of approved barristers' clerks. Each jurisdiction is required to nominate a fidelity fund, which is the source of compensation in the scheme, and a fidelity authority, which is the authority responsible for administering the fidelity cover scheme in that jurisdiction.

Part 4.5 sets out requirements relating to the administration of the jurisdiction's fidelity fund and the process for making, investigating and determining claims against the fidelity fund. For example, it requires the fidelity authority to ensure that claims against the fidelity fund are determined independently, at arms' length from the profession.

The fidelity fund is financed by annual contributions made by applicants for, and holders of, Australian practising certificates and Australian registration certificates (but not barristers, government lawyers or corporate lawyers). In Victoria, annual contributions are also made by approved barrister's clerks. The contribution amount is set by the fidelity authority.

If the fidelity authority is of the opinion that the fidelity fund is likely to be insufficient to meet its liabilities, it may postpone, in whole or in part, payments of claims or impose a levy on all lawyers who are liable to pay an annual contribution to the fidelity fund for the relevant financial year, or a class of lawyers so liable that is determined by the fidelity authority. The fidelity authority cannot borrow money for the fidelity fund.

Fidelity fund arrangements in Victoria and NSW

In Victoria, claims on the fidelity fund are determined by the Victorian Legal Services Board, as the fidelity authority. In NSW, the Council of the Law Society of NSW (**Law Society Council**) is the fidelity authority. The Law Society Council has delegated functions in relation to the determination of claims to the Fidelity Fund Management Committee. To ensure the requisite independence and arm's length decision-making, the Law Society Council has appointed a former judge as the Fidelity Fund Presiding Administrator to make recommendations regarding the determination of claims.

Interest payable on fidelity fund claims

Section 243 of the Uniform Law provides for the payment of interest on amounts payable, unless the fidelity authority considers special circumstances apply. Interest is to be calculated from the date the claim was made to the date of notification that the claim has been allowed at a rate of 5%, unless the Uniform Rules provide for a different rate.

The Legal Services Council considers it appropriate to reduce the interest rate payable on fidelity fund claims from the current rate of 5% for the following reasons:

- The current rate does not reflect the rate of return which can be achieved by investing the corpus of the fidelity fund.
- Paying out disproportionately high amounts of interest, particularly on high-value claims, is problematic because it decreases the sustainability of the fidelity fund.
- This would more closely represent the rate of return which claimants might have expected to achieve had the claim been allowed immediately after it was made.
- Applying a formula to calculate the interest payable better reflects the policy reasons for paying interest irrespective of the economic conditions at the time.

RBA formula

The Legal Services Council considers that it would be appropriate for the interest rate payable on fidelity fund claims to be determined by reference to a formula based on the Reserve Bank of Australia (**RBA**) cash rate, plus 1%. The RBA cash rate has been below 5% since December 2008, and is currently 0.25%.

If the RBA formula is adopted, the rule would be drafted as follows:

Interest rate for payments

- (1) For the purposes of section 243 of the Uniform Law, the rate of interest is as follows—
 - (a) if the Cash Rate Target is less than 4% as at the relevant date—the rate that is equal to the Cash Rate Target increased by 1 percentage point,
 - (b) if the Cash Rate Target is equal to or more than 4% as at the relevant date—5%.

- (2) In this rule—

Cash Rate Target means the percentage (or maximum percentage) specified by the Reserve Bank of Australia as the Cash Rate Target.

relevant date means the date on which the claim against the fidelity fund concerned was made.

CPI formula

An alternate option would be to determine the interest rate payable on fidelity fund claims by reference to a formula based on CPI, so that the value of the amount payable to the claimant is consistent with the value on the date the claim was made.

If a CPI formula is adopted, the rule would be drafted as follows:

Interest rate for payments

- (1) For the purposes of section 243 of the Uniform Law, the rate of interest is calculated in accordance with the following formula—

$$I = B / A$$

where—

A is the CPI number for the quarter immediately before the date the claim against the fidelity fund concerned was made.

B is the CPI number for the quarter immediately before the date on which the allowance of the claim was notified.

I is the rate of interest expressed as a percentage.

- (2) In this rule—

CPI number, for a quarter, means the All Groups Consumer Price Index number, being the weighted average of the 8 capital cities, published by the Australian Statistician.

Draft Rule

The draft Legal Profession Uniform General Amendment (Interest Rate) Rule 2020 is included at **Attachment A**. This includes both of the options outlined above.

Consultation questions

1. Is it appropriate to reduce the interest rate payable on fidelity fund claims?
2. Should the interest rate payable on fidelity fund claims be determined by reference to a formula based on the RBA cash rate?
3. If the interest rate payable on fidelity fund claims is determined by reference to a formula based on the RBA cash rate, is the RBA cash rate plus 1% appropriate?
4. Should the interest rate payable on fidelity fund claims be determined by reference to a formula based on CPI?



New South Wales

Legal Profession Uniform General Amendment (Interest Rate) Rule 2020

under the

Legal Profession Uniform Law

[The following enacting formula will be included if this Rule is made—]

The Legal Services Council has made the following Rule under the *Legal Profession Uniform Law*.

Chief Executive Officer, Legal Services Council

Legal Profession Uniform General Amendment (Interest Rate) Rule 2020 [NSW]

Legal Profession Uniform General Amendment (Interest Rate) Rule 2020

under the

Legal Profession Uniform Law

1 Name of Rule

This Rule is the *Legal Profession Uniform General Amendment (Interest Rate) Rule 2020*.

2 Commencement

This Rule commences on the day on which it is published on the NSW legislation website.

Legal Profession Uniform General Amendment (Interest Rate) Rule 2020 [NSW]
Schedule 1 Amendment of Legal Profession Uniform General Rules 2015

Schedule 1 Amendment of Legal Profession Uniform General Rules 2015

[1] Rule 89A [Drafting Option 1]

Insert after rule 89—

89A Interest rate for payments

- (1) For the purposes of section 243 of the Uniform Law, the rate of interest is as follows—
 - (a) if the Cash Rate Target is less than 4% as at the relevant date—the rate that is equal to the Cash Rate Target increased by 1 percentage point,
 - (b) if the Cash Rate Target is equal to or more than 4% as at the relevant date—5%.
- (2) In this rule—

Cash Rate Target means the percentage (or maximum percentage) specified by the Reserve Bank of Australia as the Cash Rate Target.

relevant date means the date on which the claim against the fidelity fund concerned was made.

[2] Rule 89A [Drafting Option 2]

Insert after rule 89—

89A Interest rate for payments

- (1) For the purposes of section 243 of the Uniform Law, the rate of interest is calculated in accordance with the following formula—

$$I = \frac{B}{A}$$

where—

A is the CPI number for the quarter immediately before the date the claim against the fidelity fund concerned was made.

B is the CPI number for the quarter immediately before the date on which the allowance of the claim was notified.

I is the rate of interest expressed as a percentage.

- (2) In this rule—

CPI number, for a quarter, means the All Groups Consumer Price Index number, being the weighted average of the 8 capital cities, published by the Australian Statistician.