

STATEMENT 1.306
GENERAL GUIDANCE
GUIDANCE ON REASONABLE STEPS
TO BE TAKEN FOR PII PURPOSES

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1. Introduction

CPA practices should take all reasonable steps to protect themselves against claims arising out of their professional services.

In the case of Corporate Practices, the Corporate Practices (Professional Indemnity) Rules require compulsory professional indemnity insurance for applicants for, and holders of, current corporate practice registration certificates. While these Rules lay down the minimum level of cover that should be required, as a practical matter, the cover of the compulsory insurance may not be adequate for some applicants, and existing corporate practices. Professional advice from insurance brokers or other advisers should be obtained in order to consider what is an adequate type and level of cover for the practice.

This statement provides guidance on such steps as may reasonably be taken by a practice to assess its Professional Indemnity Insurance requirements in order to meet claims against them. For convenience, this guidance refers to "firms" but it applies equally to relevant members and corporate practices. The nature and size of the practice will influence the degree of attention paid to the various aspects of this guidance but it is intended to be of use and relevance to all practices in respect of all their practice work.

2. Assessment of Risk

Before considering the nature of the protection which is required to cover potential liabilities, a logical approach to risk assessment should be adopted. A firm should carry out such an assessment and take any appropriate action on a regular basis, and at any time when the composition of the firm or its client base changes significantly, giving consideration to the following:

- (a) The possibility of being sued should anything go wrong and of the possible quantum of such a claim:
 - (i) client by client, having regard to whether the work is ongoing or one-off;
 - (ii) client by client, having regard to the maximum potential exposure to stakeholders in the client;
 - (iii) generally, talk through your conjectures, worries and problems with your partners or colleagues.
- (b) evaluation of new and existing clients in terms of:
 - (i) instructions received, nature of work to be carried out and cooperation necessary to complete tasks in a timely and accurate manner;
 - (ii) credibility of management;
 - (iii) quality of accounting, financial and management controls;
 - (iv) type of business;
 - (v) risks of sanction, bribery and money laundering;
 - (vi) geographical exposure;

- (vii) rules and regulations of the industry.
- (c) awareness of general economic climate:
 - (i) rate of company insolvency;
 - (ii) types of business experiencing difficulty;

Translate general impression of climate into specific understanding of clients;
- (d) delegation of risk assessment matters to responsible partner/director;
- (e) capacity in terms of quality and quantity of staff.

3. Mitigation of Risk

Upon identification of a client as creating a potentially high risk:

- (a) evaluate ability to mitigate risk in terms of procedures;
- (b) decide whether to retain client;
- (c) institute safety procedures e.g. second partner/director review.

4. Other Factors

- (a) Bear in mind the need to cover:
 - (i) all firm's current staff, including sub-contractors and consultants;
 - (ii) all firm's activities, including, for example, joint audit appointments;
 - (iii) past and new partners/directors and predecessors in business;
 - (iv) personal appointment, for example, liquidator appointments.
- (b) Bear in mind the firm's claims history and the need for regular analysis of prime causes of any failure experienced by the firm.

5. Amount and Breadth of Protection

Having carried out the above assessment, the firm will next need to decide how much protection it needs. In making this decision it should:

- (a) consider and attempt to quantify the exposure of the firm, taking into account assessment of risk;
- (b) assess whether current measures of protection are sufficient to meet potential claims and are relatively consistent with those of similar firms using available sources e.g. Interfirm Comparison, information held by insurance broker, information held jointly with other firms in mutual arrangement;
- (c) take expert advice as to how much cover is available and its cost;
- (d) determine sufficiency of firm's own resources to meet claims - availability of both personal and the firm's assets and reserves made to meet known claims;
- (e) exercise judgement as to requisite levels of insurance to meet claims and associated costs and interest.

6. Form of Protection

Having decided how much protection it needs, the firm will need to consider the most appropriate way of meeting its requirements subject to the provisions of the Corporate Practices (Professional Indemnity) Rules in the case of corporate practices:

- (a) **Professional Indemnity Insurance:** Use of licensed insurance broker under Insurance Companies Ordinance (Cap. 41) with experience in this field to arrange appropriate terms offering sufficient limits at acceptable price with sound insurance companies.
- (b) **Self Insured Excess:** Selection of appropriate level of excess based on personal resources including borrowing capacity and the firm's resources. Consider past incidence of claims and ability to meet multiple losses.
- (c) **Captive/Mutual Arrangements:** Reference to expert advice and sound management procedures to ensure continued ability to meet claims.

7. Procedures for Identifying and Monitoring Claims

In addition to taking steps to cover liabilities, the firm should look for ways of limiting the damage from existing and potential claims and ensuring that the likelihood of such matters arising again is reduced as far as possible through:

- (a) regular circularisation of and open discussion between partners/directors and senior employees in order to identify matters which may lead to a claim;
- (b) peer review between partners/ directors and senior employees in relation to matters which may lead to a claim;
- (c) establishment of procedures for notifying claims to insurers and otherwise ensuring that insurance arrangements remain valid;
- (d) regular assessment of claims progress;
- (e) use of expert advisers - insurance and legal, for example, consult insurers before admitting liabilities and/ or incurring professional expenses;
- (f) learning from experience.