Professional Indemnity Forum – Eighth Conference

From Accountants to Biscuit Bakers and Lawyers to Vodka Makers

An Overview of the Functions and Liabilities of Regulatory and Accreditation Bodies and Trade Associations

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Introduction

The purpose of this talk is to give an overview of the functions and liabilities of regulatory bodies, trade associations and accreditation bodies.

Regulations, codes of conduct and accreditation form an ever increasing facet of life in the UK. Some blame Europe for its excessive bureaucracy. Others blame the Americans for teaching us how to be more litigious. But, whoever you blame, regulations and codes are here to stay, and will proliferate in the future.

It was only whilst researching this talk that I realised just how regulated we are. You will all know that Lawyers, Accountants and Surveyors are governed by strict codes drawn up by their professional bodies. But did you know that domesticated ostrich farmers, dried flower arrangers and biscuit bakers have their own codes too?

Even teddy bears are not immune – they have their own body called the British Teddy Bear Association. For this we perhaps can blame the Americans. A quick search on Yahoo! reveals that teddy bear regulation abounds across the water. From Maine to San Diego there are 54,000 trade associations, organisations and clubs spouting out new codes and regulations on how we should treat our bears!

In this talk Emma will be giving an outline of the functions of a number of trade, regulation and accreditation bodies. William will then look at the liabilities these bodies can attract and how this impacts upon Insurers writing cover for these bodies.

LIABILITIES OF REGULATORY BODIES, TRADE ASSOCIATIONS AND ACCREDITATION BODIES

The liabilities which regulatory bodies and trade associations can attract are vast and diverse.

By contrast accreditation bodies tend not to attract a large number of claims themselves. With these I will therefore focus more on a discussion of the adequacy of their codes of conduct and my view of how these will develop in the future.

REGULATORY BODIES

Financial Services Authority

The FSA is the main city regulator whose job it is to protect the interests of investors.

Recently the FSA's attempts at protecting investors has brought it into conflict with the firms it regulates. A prime example of this is the split capital investment trust scandal.

Around 4 to 5 years ago several split capital trusts ran into difficulties causing allegations to run rife of collusion and mis-selling by IFA's. In May 2002 the FSA launched the biggest enquiry in its history into these allegations.

Whilst this enquiry is some way from completion it has already caused substantial problems for the FSA and may in future expose it to liabilities.

The FSA's investigatory authority is contained in the Financial Services and Markets Act 2000. Part 1 of this Act sets out in detail the aims the FSA is meant to achieve. These include increasing market confidence, protecting consumers and reducing financial crime.

The FSA's powers are curbed to some degree by sections 348 and 352 of the Act. Section 348 expressly limits the disclosure of confidential information by the FSA. Section 352 adds teeth to this by providing that the contravention of section 348 constitutes a criminal offence.

The FSA is now facing attack from its members who complain that it has mishandled the split capital trusts investigation and contravened section 348.

The attack on the FSA is based on allegations that the 21 firms involved in the investigation are now widely known even though no conclusions have yet been drawn as to whether they have done anything wrong. As one executive was quoted as saying in the Mail on Sunday, in May 2004:

"Guilty or not, a black cloud could hang over us for three to five years".

It remains to be seen whether the firms in question do take any action against the FSA. Early signs are that they will.

Insurers of personnel working within the FSA will be watching their potential exposure carefully. Contravention of the provisions of section 348 can result in imprisonment or a fine, or both for the offender.

Insurers may take heart that there is a "due diligence" defence under the Act and a further defence which exonerates any person who did not know and had no reason to suspect that the information in question was confidential. It is likely that over the coming months the veracity of these defences will be tested by Insurers.

Civil Aviation Authority

As with the FSA, the CAA is another independent regulator established by Parliament.

The CAA faces potential liabilities from numerous sources. I shall look at three of these: - liabilities arising from failed pilot medical examinations; liabilities arising from the general public and liabilities arising from the regulation of British airspace.

Medical Supervision

The CAA's medical division boldly states the following:

"An aviation medical requirement must achieve acceptable standards of safety whilst allowing as many as possible who wish to fly to do so…"

If ever there was a mission statement that is destined for a turbulent ride, that is it. Again we see how the CAA, like the FSA, needs to steer a line between protecting the public and its members.

Not surprisingly the CAA is extremely rigorous in the medical standards it sets for pilots. The importance of this has no doubt been emphasised by recent scandals abroad which have cast doubt on the effectiveness of pilot medicals. In 2002 an airline called American West failed to pick up that two of its pilots might be alcoholics. The pilots were narrowly prevented from taking off from Miami airport whilst under the influence of alcohol.

A pilot who fails his or her medical examination is debarred from flying (and thus potentially deprived of the means of earning a living).

It is a measure of the importance attached to pilot medicals and the potentially disastrous consequences of getting it wrong that pilots who do fail medicals have relatively little recourse

against the CAA. The only avenue that is open to them is an internal review and, if the pilot is still dissatisfied, judicial review. The review however is not of the medical opinion itself but rather of the procedures applied by the CAA in the light of the opinion. According to the CAA only two decisions have been successfully reversed via judicial review in the past three years.

Airworthiness

The CAA is also responsible for declaring whether a plane is airworthy and it is this function which will be of most interest and concern to Insurers because of the potential for huge exposure.

In the 1995 case of *Philcox v CAA,* Mr Philcox crashed his plane just a month after the CAA had declared it airworthy.

He brought a claim for damages against the CAA seeking the costs of repairing his aircraft. The Court held that the CAA was not liable. This was for a number of reasons one of which was that it was only Mr Philcox who suffered damage. In an interesting enunciation of a regulatory body's duties the Court held that the CAA was not liable because its duty was to protect the public against the owner's failure, not to protect the owner himself.

However Insurers considering writing cover for a body like the CAA will want to consider carefully the possibility of a large "one off" exposure. If a plane were to come down as a result of a negligent CAA inspection and, for example, members of the public were harmed or killed, then following the logic behind the *Philcox* case a claim running into many millions could result.

Air Space Control

Finally, the CAA has found itself on the receiving end of litigation from companies who object to its attempts at controlling UK air space. In the 1997 case of *H5Air v CAA* a Norwegian company sought to argue that it should be allowed to fly its cargo loaded Cessnas over Britain at night. Even though on this occasion the Court of Appeal disagreed, it is likely that with the EU seeking to encourage free movement between member states, more cases are likely to follow.

The Law Society

The Law Society is an institution facing attack from all angles and one which demonstrates more than any other the dichotomy of protecting its members' interests and protecting the public.

The Law Society is the representative and regulatory body of the legal profession. It is a powerful and multi-faceted body.

The Law Society influences every aspect of a solicitor's life from being admitted to the role to (for the unfortunate few) being struck off.

On its web site the Law Society rather grandly describes how it:

> **"sets the standards that underpin the profession's reputation as the best independent professional advisers".**

The non-lawyers amongst you may well question the veracity of the latter part of that statement!

Be that as it may, the Law Society is a prime example of a regulator which exposes itself to a multitude of liabilities by the sheer number of functions it performs.

The Law Society has attracted litigation and criticism which, as we shall see, may one day lead to the extinction of the Society.

Broadly the Law Society faces challenges from three fronts as follows:

1. **From some of its 92,000 members**

2. **From within**

3. From the Government.

I shall briefly look at these in turn.

From its members:

The primary cause of litigation against the Law Society from its members is the Society's duty to balance the interests of its members against those of the consumer.

The ultimate sanction the Law Society can impose is striking a solicitor off the role, effectively depriving him or her of their livelihood. Insurers providing cover for professional regulatory bodies like the Law Society will be aware that it is under this jurisdiction that some of the most expensive claims arise.

Solicitors faced with being struck off have, not surprisingly, sued the Law Society seeking reinstatement and damages for the loss of their practices and the harm done to their professional reputations.

The armoury that these solicitors have at their disposal is ever increasing as lawyers acting for struck off solicitors seek new and inventive way to challenge the Law Society.

In January 2003 in the case of *Holder v The Law Society* Mr Holder almost succeeded in being allowed back on the roll by arguing his striking off was in breach of the terms of the Human Rights Act. Unfortunately for him, whilst the Court at first instance agreed, the Court of Appeal did not.

Another example is one where the Law Society faced proceedings for libel. It is part of the Law Society's function in protecting the public to identify fraudulent solicitors and to weed them out of the profession.

Weeding the rot from the profession is a laudable goal. Getting it wrong, however, tends to be expensive and spectacularly embarrassing!

In September 2002 the Law Society published details of a solicitor who had supposedly been charged in connection with a £7Million fraud and been struck off. In fact the solicitor had been guilty of neither.

The solicitor himself received "a very substantial sum in damages and costs" together with a very public apology.

It is perhaps not surprising that the Law Society sometimes gets it wrong in matters of solicitors' dishonesty. Some of the judicial guidance on the tests to apply are not easy to follow. The 2004 case of *Bultitude v The Law Society* is a prime example. In this case it was found that the solicitor should not have been struck off even though he had acted "with conspicuous impropriety that amounted to dishonesty". The solicitor's saving grace was that he had "not tried to conceal his dishonesty".

From within:

The Law Society has also faced challenges from within.

You will have heard of the high profile claims pursued against the Law Society by Kamlesh Bahl, the former vice president of the Society.

Ms Bahl was forced out of the Law Society in March 2000 after being found guilty of bullying.

It is beyond the scope of this talk to look into that case in any detail. Suffice it to say that Ms Bahl's resignation has led the Law Society into a veritable soap opera of litigation with accusations and counter-accusations of victimisation, bullying, libel, harrassment….you name it!

Whether Kamlesh Bahl succeeds or not, her case is a timely reminder that the most powerful regulators in the country are far from immune to the squabbles and skirmishes of everday life. It is also a timely reminder to Insurers of regulatory bodies of the expense of litigation. As at December 2002 the Bahl case had run up costs of around £2M. With the litigation ongoing and further appeals looming this will probably have doubled by now and could easily treble in the future.

From the Government:

Institutions like the Law Society which are created by statute can face the ultimate liability which is having their regulatory authority removed entirely.

In its report published in July 2003 and entitled "Competition and Regulation in the Legal Services Market" the Department for Constitutional Affairs concluded that the current regulatory framework for lawyers in England and Wales was "outdated, inflexible, over-complex and insufficiently accountable or transparent".

It would be difficult to phrase a more damning indictment.

David Clementi, the Prudential Plc Chairman and former Governor of the Bank of England, has been tasked with undertaking a wide ranging independent review of the regulation of legal services in England and Wales. This is due for completion by December 2004. At the very least substantial reform of the existing structure is probable and this may well include the establishment of an entirely new independent regulator.

With the Lord Chancellor chiming in his views on a regular basis that the Law Society is failing to meet its targets for dealing with complaints against solicitors, it is difficult to see how the Law Society can survive as a regulatory body in anything like its current form in future years.

The ACCA and the RISC

I shall deal only briefly with these regulators.

Like the Law Society the ACCA and the RICS proscribe rules and codes of conduct for their respective professions. Also like the Law Society they are vulnerable to attack from their members when they get it wrong.

An unusual case which does merit a mention is that brought by Mr Bankole against the ACCA in 1995. Mr Bankole sought to sue the ACCA for negligently marking his accountants' examination papers.

The Court of Appeal declined jurisdiction and helpfully suggested that Mr Bankole might try re-sitting his exams instead.

TRADE ASSOCIATIONS

As with Regulatory bodies, Trade Associations face a multitude of potential liabilities which Insurers need to be aware of before agreeing to write cover. As we will see, however, the extent of potential liabilities varies greatly between Associations depending on the type of service they offer and the types of trade covered.

The Biscuit, Cake, Chocolate and Confectionary Alliance

I shall start by looking at a Trade Association governing something close to all out hearts – namely biscuits and chocolate.

The BCCCA is a powerful body which controls a UK manufacturing sector worth over £7 billion.

In terms of the potential liabilities I would like to focus on one topical issue, namely childhood obesity.

Obesity affects 1.7 billion people around the world and is the subject already of litigation in the USA against fast food manufacturers. Two lawsuits have been issued against McDonalds and KFC. Neither has made substantial headway yet. However if the tobacco litigation in the US is anything to go by this could be the beginning of long and protracted litigation.

There is some way to go yet before we are likely to see obesity related litigation over here. If claims are made they will in the first instance be against the manufacturers themselves. Even here prospective claimants will face huge hurdles establishing a causal link between, say, advertising and obesity.

However there has to be a real chance that if UK confectionary manufacturers are targeted in litigation then claims will also follow against trade associations like the BCCCA. This will be particularly so if they endorse an "ideal" level of sugar in certain product which is then found to be too high. The warning signs are already there. The World Health Organisation suggests sugar should not account for more than 10% of energy in an average diet. The BCCCA and other trade associations contend for a 25% average.

The BCCCA is not shy for a fight. It has publicly pronounced that there is no proven link between obesity and consumption of confectionary. On its web site the BCCCA takes the line that eating biscuits is "fun" and that "cakes and confectionary are nutritious". The site does go on to concede that eating too much of these things is a bad idea but I wonder whether in years to come the BCCCA will come to regret its forthright approach.

We shall have to wait and see but meanwhile Insurers considering writing cover for confectionary manufacturers and their trade associations and may choose to cast a wary eye to what is happening in the States.

The Gin & Vodka Association

So from chocolate and biscuits to gin and vodka.

The Gin & Vodka Association is a trade association dedicated to protecting the image of UK produced gin and vodka.

The GVA website rather pointlessly asks the user to confirm that they are over 18 before allowing access to the site. Quite how that prevents a five year old from pressing the appropriate button is a mystery.

The age restriction of the web site is however an acknowledgment that there may be troubled waters ahead for the GVA and similar associations.

Again the US is providing the lead in alcohol related litigation. As of 1st March 2004 four cases had been issued in the US against alcoholic beverage producers. Broadly these cases are all based on allegations that the companies in question purposefully marketed their products to underage youth. The relief sought in one case is punitive damages of $4 billion.

There is no indication as yet on whether these actions will succeed. One portent might be that the Claimants in two of the cases seemed to have little difficulty in signing up the same lawyers that dealt with the successful tobacco litigation. Perhaps they know something we don't.

It is a quantum leap to suppose that, even if the US litigation succeeds, there will necessarily be similar litigation over here either against the brewers or trade associations like the GVA. Again the law over here on establishing duties and causation will present a formidable hurdle.

If at all it is likely that the brewers who advertise direct to the public would be targeted in future litigation rather than a trade association like the GVA. Indeed the GVA when asked professed themselves to be unconcerned with the US litigation. The GVA stated that its website does little more than provide interesting facts about gin and vodka and its function is to encourage members to subscribe to codes of practice to regularise standards across the Indusrty.

It is in my view unlikely that the GVA will become exposed to substantial future liabilities. Perhaps aware of these potential bars on a successful future action the GVA blithely recommends on its web site a number of ways of mixing powerful gin and vodka cocktails!

Nevertheless, out of an abundance of caution, insurers considering writing cover in years to come for brewers or their trade associations may wish to take a quick glance across the Atlantic to see if anything did come of that $4billion claim.

Stress Therapists

All this talk about litigation is very stress-inducing, so where better to go next than the Association of Stress Therapists.

Britain loses over 90 million working days per year because of stress. A 2003 report commissioned by the TUC suggested that long term work stress has the equivalent effect on the human body to putting on 40lb in weight. Employers increasingly face claims from employees who say their health has been affected by workplace stress. In the face of this some employers have turned to Stress Therapists both to cure those already affected by stress and to provide preventative advice to those at risk. Not surprisingly Stress Therapy is one of the fastest growing professions in the Country.

The AST is the trade association for stress therapists. Conscious of the potential for litigation against its members it insists that all members are covered by professional indemnity insurance.

In theory a trade association like the AST is vulnerable to legal claims. As is evident from the rise in medical litigation, when so called "cures" do not work, the lawyers are often the first port of call. This is the case for both main line medicine and complementary treatments like stress therapy. If a stress therapist is sued then he or she may seek to bring a claim against the AST for endorsing or recommending a particular treatment.

It is perhaps for fear of litigation that the AST website is an incredibly bland and uninformative document. One heading entitled "how to beat stress" offers nothing more than a suggestion that relaxing and getting plenty of sleep might help!

The AST refused to be drawn on whether they were concerned about the possibility of being drawn into claims involving their members. Their website, in my view, however speaks volumes.

British Dried Flower Association

The BDFA pronounces itself as a valuable source of information for purchasers of dried flowers.

This might leave it open to a claim for negligent mis-statement if it gave wrong advice resulting in economic loss.

Commendably, despite many hours of fruitless search, I have not found a single case in which the BDFA is a named party. Perhaps flower growers have more important things on their minds than litigation or perhaps the BDFA is indeed the valuable source of information it claims to be!

The Rugby Union Society of Referees

There are numerous associations around the country governing the conduct of rugby referees. Most counties and cities have their own refereees associations. These deserve a brief mention for two reasons. First, in order to cheer English sporting hearts by showing a slide of the great Jonny Wilkinson. Secondly to illustrate how regulators and associations can fall victim to changes in the law which can leave their insurers painfully exposed. Nowhere is this more true than in the case of rugby.

Many of you will recall the 1996 case of Ben Smoldon who suffered crippling injuries when a scrum collapsed in a junior match. He subsequently took legal action against the referee of the match who was a member of the Staffordshire Rugby Union Society of Referees, Mr Smoldon was successful and was awarded substantial damages.

In 2002 a case was brought against the Welsh Rugby Union by a Mr Vowles who had been paralysed during an adult rugby match. Mr Vowles succeeded in arguing that the WRU was responsible for his injuries on the basis that they had failed to ensure that the referee properly protected the players.

Before the Smoldon and Vowles cases most referees, their associations and insurers would never have anticipated these types of claims. It is a useful reminder to insurers to keep an eye on where the next developments in litigation may be. Rugby is not the only game which exposes its players to dangers which could be avoided by proper refereeing. From football to ice hockey the potential for future claims is vast.

ACCREDITATION BODIES

With regulatory bodies and trade associations I have focused on the legal liabilities these bodies themselves might attract.

With accreditation bodies I am going to shift the focus slightly to look at how these bodies seek to protect the public. Generally this is done through codes of conduct for their members and in some (but not all) cases insisting that their members have professional indemnity insurance.

What will become clear is that there is a vast disparity between the standards accreditation bodies apply to their members. Whilst some have rigorous codes of conduct and insist on their members being fully insured, others are little more than a register which a member can join without any form of vetting or compulsory insurance cover.

I shall start by giving an overview of the effectiveness of various accreditation bodies. I shall then deal briefly with the changing landscape for the future.

Effectiveness of Accreditation Bodies

There are a number of accreditation bodies which regulate their members very tightly. Prime examples are SAVA (accreditation for surveyors and valuers), and Corgi (gas appliance installers).

In the case of SAVA accreditation is undertaken by trained independent assessors and accreditation is only given to surveyors and valuers who subscribe to a detailed codes of conduct, hold indemnity insurance in line with RICS standards and operate an RICS approved complaints handling procedure. This complaints handling procedure extends to anyone to whom a duty of care is owed and sets out stringent minimum requirements which must be met. The guidelines specify for example that the procedures need to be quick, clear and transparent and, if the complainant is dissatisfied with the initial review, there needs to be redress to a form of ADR such as mediation or arbitration.

SAVA will also be the accreditation body for the new breed of specialists called Home Inspectors. The Housing Bill introduced into Parliament on 8 December 2003 proposes the mandatory creation of Home Information Packs. These packs will have to be supplied by sellers of homes to prospective purchasers and will have to be prepared before the property in question is marketed.

Each sellers pack will contain a Home Condition Report which will broadly contain the same information as a standard survey. It is envisaged that the creation of the sellers pack will lead to a demand for around 7,000 Home Inspectors.

The extent of accreditation and regulation in respect of Home Inspectors is still under debate. It is likely to take a similar form to RICS regulation in which case indemnity insurance will be compulsory as part of the accreditation. The likely start date for sellers packs may be as soon as 2007 although this will depend on the appropriate legislation being enacted in time. If indemnity insurance is compulsory, as is likely, there will clearly be a substantial market for insurers writing this type of business.

Insurers looking to get into this market will wish to look carefully at the types of claim which may arise against Home Inspectors. The seller who commissions the report will be concerned about undervaluation since the selling price will be based on the report. As with surveyors there will be a

margin of error within which the report is acceptable (around 10% either way). The danger for Insurers is that a good degree of local knowledge will be required by Home Inspectors if they are to avoid claims. In the event (as is likely) that there is an initial shortage of Inspecors, many may be asked to compile reports on properties outside their geographical expertise. Insurers need to be aware of this danger and may go as far as providing indemnity cover for Home Inspectors which is territorially limited so as to avoid potential exposure.

Registration with Corgi is now a legal requirement for businesses and self-employed people working on gas fittings and appliances. Corgi runs a rigorous scheme of assessment in order for their installers to obtain their competency certificates. These assessments have to be renewed every five years.

Whilst Corgi registration certainly ensures a well qualified and competent installer, astonishingly indemnity insurance for Corgi registered installers is not compulsory, although it is recommended.

Accrediation bodies like SAVA and Corgi therefore offer comprehensive codes of practice and in the former's case compulsory indemnity insurance. At the other end of the scale are accreditation bodies and regulators who offer relatively little protection to the public.

Thus the Confederation of Roofing Contractors provides a ten year guarantee for its members' work but does not insist that companies have insolvency cover. The Domestic Appliance Service Association and the Hire Association Europe do not require any indemnity insurance cover at all.

The Changing Landscape for the Future

As I said at the start of this talk, regulation and codes of conduct are on the increase. We can expect more rather than less.

There is also evidence that members of the public place some store in trade logos and accreditation symbols which they perceive as marks of quality. In a recent Which? survey 70% of those questioned said they were more confident using a company which displayed a trade logo.

The Office of Fair Trading has also cottoned on to this. It now runs a endorsement scheme for codes of conduct. If a given code meets certain customer protection standards the accreditation body or trade association can apply to the OFT for endorsement. Effectively thereby endorsing the endorsers.

This scheme is in its early days at present. However it is quite likely to take hold given the public's perception that trade logos can be a mark of quality. A trade logo accompanied by an OFT approval is likely to have more effect still.

This could well be good news for insurers. Once certain way to curry favour with the OFT is for accreditors and trade associations to encourage their members to have proper complaints procedures and indemnity insurance. It may take some time yet but in years to come the insurers and brokers amongst you may find queues of roofing contractors and domestic appliance installers clamouring for competitive insurance rates!