

## A GUIDE TO PROFESSIONAL INDEMNITY INSURANCE

This provides a brief summary of the cover provided. The actual policy wordings should be reviewed for specific details of coverage.

### Professional Indemnity Insurance

A policy providing indemnity to professionals against claims made against them resulting from legal liability to others for loss or damage arising out of professional negligence, error or omission in advice, specification, design, service or duty on the part of the professional

Specifically coverage is provided for:

- Settlements by or judgements against the business and/or professional person arising out negligent advice or services.
- Legal costs and expenses associated with the defence of legal action.

Extensions to the basic coverage provided may be provided for:

- Defamation
- Liability arising from a previous business or occupation
- Loss of Documents
- Breach of Confidentiality
- Automatic Reinstatement of Policy Limits
- Liability or loss through dishonesty by employees

Specifically, the policy excludes physical loss or damage (i.e. property damage), which is generally covered under Public Liability insurance.

### **Who is Protected?**

Coverage is provided to the named insured and extends automatically to any:

- Subsidiary.
- Organisations controlled and actively managed.
- Director, employee, partner or shareholder of the Insured, in that capacity.
- Person or organisation to whom the Insured has promised to arrange insurance (but only with prior agreement of the insurer).
- Any newly acquired organisation, which the Insured notifies to the insurer.

Coverage is provided to The Insured as declared in respect of:

- Its own negligence
- The negligence of its predecessors in the business
- The negligence of its employees
- The negligence of any person, partnership, company or firm acting on its behalf.

## **Business**

Cover is only provided in respect of the business activities detailed in the policy schedule. Therefore, any additional activities that may commence during the policy period need to be notified to the insurer immediately, otherwise no cover is provided

## **Claims Made Insurance**

Professional Indemnity insurance provides cover on a 'claims made' basis. This means that you are protected against claims that are made against you, and then notified to the insurer, during the period of insurance. This enables companies to select limits of indemnity each year to keep pace with the likely cost of damages.

## **Claims Reporting Requirements**

It is important that any claim or circumstances that you become aware of that may give rise to a claim (regardless of when the original cause or event giving rise to the claim occurred) is notified to the Underwriter immediately, and prior to the expiry of the policy period. Failure to notify will prejudice your rights to indemnity under the policy.

### **1. Claim**

A claim is when another party had advised you, either verbally or in writing, that they will make a claim against you, will take legal action or will sue you. It generally involves a demand made by a third party on the Insured for compensation.

### **2. Circumstance**

A circumstance that may give rise to a claim is a subjective matter. As a general guide the circumstances must be such that:

- There is an indication that a claim will be made against the Insured; or the Insured has reason to suspect that they have done something wrong or that there would be merit to a claim being made, or

- A threat is made either verbally or in writing that another party will take legal action against you, or
- It can be any circumstance that could eventually lead to a claim being brought against you.

Whether or not circumstances are such that they may give rise to a claim depends on the facts of the particular case

### **3. Claim Notification to the insurer**

Notification to the Insurer must be adequate, meaning that the Insured must provide proper particulars of the circumstances, which may give rise to a claim in order for the advice to be accepted as a notification under the policy. A general indication that things are wrong and claims are likely is not enough for the Insurer to accept a notification.

Generally if the Insured can provide the following, proper notification will have been achieved:

1. What happened to make the Insured believe there is a circumstance
2. Why the circumstance has the potential to give rise to a claim
3. When the event occurred
4. Who the potential claimant is
5. Where the alleged mistake occurred

### **4. Why notify a circumstance?**

Circumstances should be notified because once a circumstance has been properly notified to the Insurer, cover is preserved under that policy period for any valid claim that may later arise from that circumstance. This is the case, even if the claim arises after the policy has expired.

Failure to notify a circumstance during the period of cover can cause indemnity problems.

### **5. When do claims have to be notified?**

The best time to report a claim or circumstance is immediately you become aware of it.

## Some useful definitions

### **Automatic Reinstatement**

When the annual insurance limit is exhausted by claims, the policy automatically reinstates the limit. Usually restricted to one automatic reinstatement, but sometimes more can be negotiated.

### **Breach of Fiduciary Duty**

Arises when your client argues that your involvement in a project has influenced your advice to them.

### **Claim Settlement Expenses**

The expenses incurred in the investigation, assessment and settlement of a claim - including direct (eg court costs, legal fees) and indirect costs (eg expenses of the claims department).

### **Deductible / Excess**

The amount of loss that is to be borne by the party insured prior to being able to claim on the policy. There are two types of excess - costs inclusive and costs exclusive.

- **Costs inclusive** – means that the excess applies to the legal costs involved in defending a claim.
- **Costs exclusive** – means that the excess does not apply to legal costs.

### **Duty of Disclosure**

You have a common law duty to disclose all material facts before entering into, renewing or altering a contract of insurance. If you fail to do so, or if any material facts are misrepresented, the insurance could be made void.

### **Hold Harmless Agreement**

A clause in a contract that prevents or limits your right to sue another party for recovery of a loss. In such circumstances, your insurers will be unable to exercise their recovery rights (subrogation). These agreements must be disclosed to your insurers, or your insurance could be rendered void.

## **Limit or Limit of Liability**

The maximum amount an insurer will pay under a particular policy coverage.

## **Material Fact**

A material fact is one that would influence a prudent insurer in accepting or rating a risk. Your common law duty of disclosure applies only before each contract is entered into, renewed or changed, but some policies have a condition that extends the duty throughout the period of insurance.

Your duty of disclosure does not include facts which are common knowledge, nor does it include facts already known to your insurer, or which ought to have been known to your insurer in the ordinary course of business.

## **Retroactive Date**

The date from which cover is provided for negligent acts, errors or omissions. Acts prior to the retroactive date are not covered.

## **Solvency**

Ability of a company to meet its liabilities as they fall due.

## **Subrogation**

The right of an insurer to recover from a third party who is wholly or partially responsible for a claim paid or payable by the insurer.

## Claims Philosophy

Each insurer varies on how they handle claims, but the following is a best practice procedure that insurers should follow:

**1. Assessing liability and devising a strategy for resolution** of the claim as quickly as possible. If a policyholder is liable to make good a loss, insurers move to settle the claim economically and confidentially. In so doing, insurers recognise that policyholders should have the maximum opportunity to preserve the commercial relationship with their injured clients.

**2. Preservation of the reputation of policyholders** through the forceful defence of unmeritorious claims is important. Insurers understand that reputation is the cornerstone to commercial and professional policyholders.

**3. Utilising only quality legal advisors.** Insurers should not compromise the defence of claims by using budget lawyers. Only "first class" litigation lawyers and barristers should be deployed; specific individuals that have consistently provided a superior level of advocacy and representation.

**4. Proactive claims management** is important from an insurer. Intervening appropriately in respect of a claim or potential claim improves opportunities to restrict or improve upon the adverse consequences flowing from a problem or sometimes avoid liability altogether.

**5. Working in harmony with policyholders.** There may be other related issues or processes occurring concurrently with the defence of a claim that need to be handled sympathetically. There might, for example, be adverse publicity that a policyholder wishes to rebut or control. There could be some competency or disciplinary process underway in respect of an employee implicated with the claim. Or even perhaps a formal investigation by a government agency or professional body.

**6. Promoting early resolution of claims** through Alternative Dispute Resolution processes – particularly Mediation.

## Risk Management

The more insurance claims that an organisation experiences, the more difficult insurance becomes to arrange. Insurers can increase premiums, increase excesses,

reduce insurance cover or, at worst, withdraw cover altogether. It is impossible to eliminate claims totally, but with good risk management procedures, an organisation can greatly reduce their exposure to claims or circumstances that may lead to a claim.

### **Contracts**

- Restrict or eliminate your liability wherever possible
- Never accept liability or provide a hold harmless agreement without first of all having it accepted by your insurer.
- Transfer the risk to other parties wherever possible.
- Ensure that your insurance brokers view the contract for any insurance implications.
- Ensure that your legal advisers view your contracts before signing.
- If anything unusual, refer to Mahony & Company – e.g. unusual insurance requirements, assuming role of Principal Consultant, having to insure other consultants, activities other than your normal activities etc.

### **Once contract has commenced**

- Do your job properly
- If something is supposed to be done, make sure it is!
- Be meticulous and punctual in your duties.
- Cross all the T's and dot all the I's.
- Keep good written records of all discussions, telephone calls etc with client, suppliers, other consultants.
- Report any circumstance that may lead to an eventual claim against you.