

## **Professional Liability 101 Common Questions & Answers**

### **Overall:**

The following information is provided as general information, it is not intended nor does it replace a thorough understanding of your own policy or supercede the specific language of any policy. Also remember that Professional Liability policies are not standard, each differs. The terms and definitions presented here may be different from what is contained in a specific policy.

### **What does Professional Liability Insurance cover?**

Professional Liability Insurance protects for errors and omissions committed by you, your partners or your employees in the course of their professional duties where you become or could become legally liable. For example it would cover missed filing deadlines; medical, legal or accounting procedures/engagements that the outcome was less than what was hoped for; or errors made in interpreting the law or applying a statute. It does not provide as a rule general liability insurance or property insurance coverage.

With few exceptions, most commercial and business owners policies exclude coverage for professional acts. No matter how careful you are you are errors (either actual or perceived) do occur.

### **What does Professional Liability Insurance not cover?**

It does not cover slips and falls in an office, destroyed property, advertising injury, or other types of general liability claims. Sometimes there are add-on endorsements to provide some additional coverage for these incidents but these are best covered by your general liability or business-owners policy.

It also does not cover employment practices claims against you, such as wrongful termination, wrongful dismissal or sexual harassment charges. These are best covered by an Employment Practices Liability policy.

### **Why you should purchase Professional Liability:**

Malpractice claims frequency tends to go up when the economy is not doing well. The number of errors or problems did not increase but more business deals go bad and people are looking for ways to become whole again. The problems were already there, but in a declining economy more of the problems come to light.

One of the most important insurance benefits is having the insurance carrier pick up the defense costs and find outside counsel to represent you. Many carriers have claim "Hot Lines" to let you discuss an incident prior to it becoming a claim. And if a claim is filed insurance carriers have pre-selected attorneys that specializes in handling malpractice claims to represent you and if nothing else give you piece of mind that when a problem occurs you are not all alone.

## **Professional Liability 101 Common Questions & Answers**

In addition, when it comes time to pay for an error (actual or perceived), the carrier will step to pay for the problem if needed, without you jeopardizing your personal assets.

### **How much is enough insurance?**

You need to look at your practice and determine your maximum probable loss. Much of this will depend on the type of business you conduct or the type of people that you work with. There may also be a requirement either from a regulatory agency or a business that you do business that you purchase insurance with certain limits.

Look at the likelihood of having multiple losses in one year. Depending on your practice you may have frequency as well as severity issues to cover. If you feel that there is a high likelihood of having multiple claims in a year, make sure that your aggregate limit is high enough to cover these multiple occurrences.

### **What deductible should I purchase?**

First look at what you can afford to come up with unexpectedly. In general the higher the deductible you purchase the lower the insurance cost. But because of how insurance carriers give deductible credits, you may find out that going to the next highest deductible is not a financially sound decision. Take the difference in deductibles and divide by the difference in the cost of the deductibles. This will determine your deductible payback. Here is an example:

Liability Limit	Deductible	Premium
\$100/\$300	\$5,000	\$3,000
\$100/\$300	\$10,000	\$2,000

Difference in deductibles:  $10,000 - 5,000 = 5,000$

Difference in premium:  $3,000 - 2,000 = 1,000$

$$5000 / 1000 = 5 \text{ Year pay back for deductible}$$

If you think that probability of having a claim in less than 5 years is high purchase the lower deductible. If you think that it is low, purchase the higher deductible.

### **What are these other (Add-ons) Coverages?**

What about **Claims Expenses Outside** the limits? Generally the reason that you want to purchase claims expenses outside the limits is to prevent the "Burning" of your liability limit. Professional Liability Insurance defense costs are generally part of the liability limit, so the more it costs to defend a claim; the less is left to settle the claim. As you are being defended you "burn" through your liability limit.

## **Professional Liability 101 Common Questions & Answers**

Understand that **Claims Expenses Outside the Limits** is not an unlimited coverage. It is generally limited to either your limit of liability or some other lower sub-limit. Normally **Claims Expenses Outside the Limits** is capped at no more than \$1,000,000. In the current insurance market environment this coverage is more difficult to get. If you are concerned about this and do not think your underlying coverage is enough, the other alternative to **Claims Expenses Outside the Limits** is to get a higher per claim liability limit.

What about **1<sup>st</sup> Dollar Defense** or a **Loss Only Deductible**? Two years ago, companies were giving this coverage away almost for free, but now it is getting increasingly difficult to obtain this coverage. This only helps if there are claims expenses (defense costs) only and no indemnity payments. If there is an indemnity payment made you are still liable for the deductible. It generally makes more sense to see if you can get this coverage if you are carrying a high deductible. Otherwise, if you are uncomfortable with the deductible being carried, see what the cost of getting a lower deductible would be.

### **What about these Additional Coverages?**

There are a host of different sub-limits and add on coverages, one of the most common is defense coverage provided for disciplinary proceedings. It pays for the defense but not for the fine.

Another is reimbursement expense for you or an employee for the time you spend in helping defend a claim.

### **When should you shop the insurance?**

While it is usually not wise to “shop” your insurance every year, but people that do shop their insurance generally pay between 10 to 20% less for their insurance than a comparable insured that has not shopped for a number of years. So if you have seen increases in your insurance costs or have not look at other companies in awhile, you could be paying 10 to 20% too much for your insurance. Unlike personal lines insurance, insurance carriers for Professional Liability Insurance have some discretion in the rate being charge for each individual insured.

### **I have never had a claim, why is my insurance going up?**

For almost 10 years the price of professional liability insurance declined steadily as many insurance carriers entered the professional liability market place and attempted to gain market share. Reinsurance rates were generally very cheap and easy to obtain. Approximately 2 years ago, this trend started to change. Certain insureds with specific areas of practice or insureds with claims were starting to find insurance costs going up or not being able to find coverage. The tightening insurance market had already started prior to September 11<sup>th</sup>. After September 11<sup>th</sup>, the insurance markets started to tighten even faster.

## **Professional Liability 101 Common Questions & Answers**

Only one insurer that I know of does not purchase reinsurance (State Farm) because they are so large. All of the others to spread the risk of insuring everything purchase reinsurance. Most reinsurance treaties are annual. As the reinsurers absorb the losses for 9/11 and paid the cost for the cheap reinsurance rates and liberal underwriting of the past, they pass on increases to the primary insurance carriers. The primary insurance carriers have then passed these costs and heightened underwriting standards along to the ultimate consumer, you.

If the declines in the stock market continue through the end of the year, expect another round of price increases and further tightening of the insurance market place as insurance carriers investment portfolios which are counted on to cover some of the costs of insurance have all declined.

### **How can I lower my insurance costs?**

One is to shop your policy with competitors and see if you can save some money. If you do not wish to shop, or even if you shop and cannot find a better deal, look at higher deductibles, eliminating add-ons like **1<sup>st</sup> Dollar Defense**. Resist the temptation to lower your limits. Remember that even if your practice has changed, if you lower your limits, a claim occurred a number of years ago that is reported or made in the current policy year will be settled with the current policy limits and policy terms. A higher deductible payment might “hurt” but an underinsured loss may expose your personal assets.

### **When switching Insurance Carriers, what should I do?**

It is good practice at each renewal to inquire with all partners, principals and employees to make sure that they are not aware of any circumstances that could lead to a malpractice claim. If they are it should be reported to your current carrier, even if you do not change carriers. The same holds true if you are switching carriers, because even if you do not switch carriers, failure to make a timely report of a claim can cause a claim to be denied.

## Professional Liability 101 Common Terms

<b>Admitted versus non-admitted carrier</b>	Admitted carriers are protected by the state's insurance funds in case of a financial default of the insurance carrier. There are payment limits by the state fund and these are usually less than an insured's Professional Liability limits. Non-admitted carriers are not protected by these state funds.
<b>AM Best Rating</b>	Rating agency that provides information about the relative financial strength and claims paying ability of an insurer.
<b>Claims Made Policy</b>	Most professional liability policies are <b>Claims Made or Claims Made and Reported</b> . The insurance carrier that carries the current coverage is liable for the claim when the claim is reported, not when the act occurred. Versus an occurrence policy where the insurance carrier that was on the risk when the act occurred is liability for the claim regardless of when it was reported. The major importance of this is to continue to have coverage for <b>Prior Acts</b> in the future, an insured needs to continue to maintain a <b>Claims Made Policy</b> or have an <b>Extended Reporting Period</b> or <b>Tail</b> purchased to cover the acts in the past.
<b>Deductible-Aggregate</b>	Limits the amount paid by the insured for deductible expenses to the amount shown no matter how many claims are initiated during the policy period.
<b>Deductible-loss only/1<sup>st</sup> dollar defense</b>	With this option the insured only pays the deductible if there is an indemnity payment
<b>Defense outside the limits or Claims Expenses Outside the Limits</b>	A sub-limit that will cover the costs of defending a claim without using the <b>Limit of Liability</b> . Once this is exhausted generally the <b>Limit of Liability</b> is reduced to pay for any additional defense costs.
<b>Excess Insurance</b>	Insurance coverage that pays once the primary insurance is exhausted. It is very important that the primary and excess policies have the same effective and expiration dates.
<b>Exclusions</b>	Defines what is not insured by this policy. You need to read this section carefully as certain policies by exclude a common area of your practice.
<b>Extended Reporting Period or Tail</b>	Commonly referred to as <b>Tail</b> coverage, this provides coverage after a <b>Claims Made Policy</b> expires or is no longer in force for acts that occurred during the time a <b>Claims Made Policy</b> was in-force. You generally have a right to purchase this coverage (within 30 to 60 days) whenever a policy is not renewed. It does not provide any coverage for any future acts.
<b>Following form policy</b>	When one insurance carrier will not provide all of the needed insurance coverage. Other carriers may be willing to provide <b>Excess Insurance</b> to provide the necessary limits. A <b>Following Form Policy</b> uses the terms and conditions in the primary insurance policy to cover and settle losses. This helps prevent uninsured insurance exposures that might result if the policy language between the underlying coverage and the <b>Excess Insurance</b> are different.

## Professional Liability 101 Common Terms

<b>Hammer Clause</b>	This is the clause contained in many <b>Insuring Agreements</b> that states that even though the insurer will not settle a claim without the insured's consent, the insurer's exposure to the loss is limited to the amount that would have been paid if the insured had taken the insurer's recommendation. In other words, if an insured does not accept the insurer's recommendation, then the insured is liable for any additional costs.
<b>Innocent Insured</b>	Most policy exclude coverage for deliberate or criminal acts. This coverage protects the other partners or principles from the deliberate acts of another employee or partner if the others had no knowledge of the actions.
<b>Insuring agreement</b>	The <b>Insuring Agreement</b> defines what and who is covered and the responsibilities of all parties.
<b>Limit of liability-aggregate</b>	The maximum indemnity and claims expenses amount that the insurer will pay for all claims reported during the policy period
<b>Limit of liability-primary</b>	The maximum indemnity and claim expenses that the insurer will pay for any one claim or incidents that are considered one claim.
<b>Named Insured/Who's Insured</b>	This is one of the most important definitions in any policy. It defines who is an "insured" and who is considered insured. These definitions differ from one policy to the next and it is very important to read your particular policy to determine if all operations are covered as expected.
<b>Policy period</b>	Most <b>Professional Liability</b> policies are annual, but some are multi-year. This is the time between the effective date and expiration date of the policy.
<b>Prior Acts</b>	Acts that occurred prior to the current policy period may not be covered unless the current policy has a <b>Prior Acts Date</b> prior to the occurrence of the act or shows no <b>Prior Acts Date</b> .
<b>Prior Acts Date or Retro Active Date</b>	This is the date that if an act occurred prior to this date, even if it is reported during the policy period the act is not covered. It is very important to maintain your <b>Prior Acts Date</b> once established to prevent gaps in coverage.
<b>Prior Acts Date-Retro Date Inception</b>	This generally occurs during the 1 <sup>st</sup> year of a <b>Claims Made Policy</b> . This is when the <b>Prior Acts Date</b> equals the <b>Policy Effective date</b> . With a policy that the <b>Prior Acts Date</b> equals the <b>Policy Effective Date</b> there is no coverage for any acts that occurred prior to the effective date of the current policy even if reported during the policy period.
<b>Prior Acts dates- Individual versus Firm (Entity) versus Career Coverage</b>	A policy may have a <b>Firm Prior Acts</b> date or <b>Individual Prior Acts</b> dates or offer <b>Career Coverage</b> . One is not inherently better than another; it depends on the desire of the firm or practice and the circumstances. It is important to understand the difference: <ul style="list-style-type: none"> <li>• <b>Firm Prior Acts:</b> Everyone in the firm is covered by the same prior acts date.</li> <li>• <b>Individual Prior Acts:</b> Each individual in the firm has a different prior acts date.</li> </ul>

## Professional Liability 101 Common Terms

	<ul style="list-style-type: none"> <li>• <b>Career Coverage:</b> Regardless of the firm prior acts date each individual has coverage for all covered professional acts. Many firms choose not to want to expose their policy to prior acts of people that join the firm or practice at a later date. Others want to offer this coverage to all professionals.</li> </ul>
<b>Rate guarantees for Multiple for Multiple Years</b>	Some insureds will include a per-person or some other rate guarantee subject to certain conditions. These have almost disappeared in the past year.
<b>Reinsurance</b>	Almost all insurance carriers purchase <b>Reinsurance</b> to cover the policies they write. With <b>Reinsurance</b> a primary insurance carrier is able to spread its ultimate exposure of any one loss or group of losses.
<b>Step Rating</b>	Most <b>Claims Made Policies</b> are <b>Step Rated</b> . During the first few years of a policy the exposure increases as the policy covers more and more <b>Prior Acts</b> . The rate tables for most carriers reflect this and over a 3 to 10 year period the policy premiums will increase as it goes through the rating step years. Once the policy becomes fully rated, then the only changes in premium should occur because of claims history of the individual or the insurance carrier; changes in the areas of practice of the professional; and/or changes in the general insurance environment.
<b>Surplus Lines</b>	<b>Non-admitted or Surplus Lines</b> insurance policies are generally sold through Surplus Lines Agents that are responsible to the state to pay the premium taxes and fees normally paid by an admitted carrier. Also the Surplus Lines Agent is the point of service should a dispute arises with the non-admitted carrier.
<b>Warrants versus Representations</b>	Many insurers attach a copy of the insured's application to the policy. This makes it part of the policy and "Warrants" the statements made as being absolutely true. Representations are those made by an insured that true to the best of their knowledge. The difference can be important if an insured has not done due diligence in check with all parties in a practice to make sure that all information is properly reported.