Management

Policy decision

Frank Maher on what to consider at this autumn's professional indemnity insurance renewal

The majority of law firms will be renewing their professional indemnity insurance (PII) on 1 October. This article looks at what they can expect, what steps they need to take, and some issues they should keep in mind both now and for the future.

The market

For most firms, the general view is that this will be a relatively benign renewal, as it was last year. Many firms will prefer to stick with their existing insurer: in practical terms, though not in law, loyalty reduces the risk of insurers taking coverage points if something slips through the net on disclosure or reporting of claims or circumstances which may give rise to claims.

However, some firms may find that their insurer is not offering terms. Elite covered many PI firms, and it announced in February 2016 that it was withdrawing from the solicitors' PII market, due to reducing premium rates, increased propensity to fraud on solicitors' client accounts and the proposed increase in the small claims market affecting personal injury firms.

There will always be some firms with problems on renewal – usually claims-related, but sometimes there are other risk factors, such as disciplinary investigations, experience of a rogue partner or employee, or changes in the practice altering its overall risk profile (such as a new higher risk practice area, or an ill-advised acquisition of another firm).

Insurers may also keep a weather eye on the financial wellbeing of PI firms, with all the problems they have faced in the past few years through changes in costs regimes, small claims, the impact of the *Mitchell* decision, and referral arrangements. The concern for insurers is that the firm may hit troubled waters and close, potentially leaving the insurer to provide the six years' automatic run-off cover without the premium being paid.

Firms with problems such as these should obtain advice on how to proceed at an early stage. The writer has seen many firms in this position over the years who have submitted multiple applications before finally seeking help when the options have been all but eliminated, making it very difficult to find a solution; although one somehow seems to have been found in the end, it has involved much hard work and extra cost that could have been avoided.

Should you use a broker? When the open market started for PII in 2000, the best advice was to appoint one broker and let them do the work. The position has become slightly more complex, particularly for smaller firms, with the emergence of schemes for which only certain brokers have access. But that does not preclude seeking advice from a specialist broker on a fee-paying basis, and this is particularly desirable for firms with a problem history of the type referred to above.

If you are going to appoint a broker, it must be a broker with expertise in solicitors' PII. You need a broker with first-hand experience, not one who is merely serving as a post-box to a communicate with a London market broker, as experience shows that much can be lost in translation.

Do not buy on price alone, important though that is. You are buying peace of mind, and the claims handling is an important part of the package. Around one in six firms had dealt with their insurer on claims in the year prior to 1 October 2015, though this rises to 1 in 2 for 11-25 partner size firms.

The Law Society's 2015-16 PII survey (http://goo.gl/EoYToF) showed that 37% of the firms surveyed reported having taken out a policy outside the traditional 12-month duration. Many of these will have been 18-month policies. As noted at the outset, the market is expected to be benign, so in the

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writer's opinion it is unlikely that rates will fall in future. There are plenty of reasons why they might rise, so buying in to a longer policy secures the rate for a longer term. It also means that the impact of any adverse claims experience will be deferred for a little longer. And it means a little less paperwork – perhaps a renewal process twice every three years rather than three times.

The proposal

There are some changes to the SRA Minimum Terms and Conditions as a result of the Insurance Act 2015, which comes into force on 12 August 2016. The changes will increase the standard of disclosure. The effect is to require firms to make a 'fair presentation of the risk' to insurers, in particular requiring disclosure of circumstances an insured ought to know (ie. which would be revealed through a reasonable search of information available to them).

The writer has long advocated asking *all* staff to complete a disclosure form (which may be electronic), ideally on a quarterly basis with one shortly before renewal. It should be in plain English and contain a reminder of the need to notify in between the circulars. It is not sufficient to ask only partners, or only fee-earners. The obligation extends to all staff. It may be that support staff are aware of key information which is critical to the firm's risk of which fee-earners may be unaware, or which the latter may be concealing.

In one case in which the writer was involved, a junior solicitor was handling a multimillion pound clinical negligence claim with inadequate supervision. She knew she had missed a critical time limit and issued an application to the court, but kept it to herself, hoping the application would succeed. The firm then renewed its insurance, failing to disclose the matter (which would have been covered without difficulty if it had been notified to the current insurer pre-renewal). The application to the court failed, and there was no prospect of resurrecting the client's claim. The new insurers took the point, and although they are required under the SRA Minimum Terms and Conditions (MTC) to deal with the claim, the four partners were left with personal liability to reimburse the insurer. Ultimately, they paid £600,000.

However, note that section 3 of the Act provides that the disclosure of material circumstances must be made in a manner that would be reasonably clear and accessible to a prudent insurer, so it is not an option to hide material disclosure in a large pile of data.

Expect to see questions in the proposal form regarding the steps you have taken to address cyber risks: client account frauds have become a major cause of loss. The Law Society's PII survey reported that '[almost] a quarter of firms report having been targeted by scammers in the last year, larger firms much more so'. This is not solely an IT question: training all the staff is also critical – again, not just fee-earners, but all support staff too. The management must lead on this – nobody is exempt. Online training is inexpensive and may pay for itself many times over.

Note that the PII policy will not cover the firm's own losses arising from a cyber incident. This might include theft of the firm's money, the cost of putting systems right and notifying clients, and even fines imposed by the SRA or the Information Commissioner. Some PII insurers offer extensions for cyber cover and standalone policies are also available. However, this is an emerging market, there are no standard wordings, and policy wordings should be considered carefully as there is wide variation in cover, some providing very limited protection.

Level of cover

Outcome 7.13 in the SRA Code of Conduct 2011 requires that 'you assess and purchase the level of professional indemnity insurance cover that is appropriate for your current and past practice, taking into account potential levels of claim by your clients and others and any alternative arrangements you or your client may make'.

Many firms overlook the risk of multiple claims arising from similar causes being subject to a single policy limit under the provisions of the 'aggregation clause' in the policy. This might arise where the firm has a series of claims arising from a disaster, or perhaps even a series of related industrial disease claims. Another example might be a failure in the firm's own systems, such as a defective computer program used for valuing claims.

Coverage disputes

To put the question of disclosure on the proposal form into context, the writer's firm is seeing far more claims by insurers against law firms seeking reimbursement. This can be due to non-disclosure in the proposal form, or late notification of circumstances or claims to insurers. By way of example, the writer is currently defending one such claim for approximately £400,000 arising from a late reporting to insurers of circumstances. Again, this was a case where the fee-earner was hoping to resolve the problem but was unable to do so either promptly or during the policy year in which the firm discovered the circumstances. Because of the wide benefits under the MTC, insurers had to settle the claim - but are seeking to recover reimbursement of most of the claims payments from the partners.

Mergers and acquisitions

Finally, as many PI firms may be thinking about merging or selling out, it is important to keep in mind the 'successor practice' provisions, which can make a firm liable to insure the risk of another firm in certain circumstances where the latter has closed and some business has been transferred. In one case in which the writer was involved, a relatively small firm failed to consider the risk when taking over another practice, and ended up with a £1m premium and a £1m excess on claims. Had they sought advice before they did the deal, they could still have acquired the practice and avoided that.

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