

PROFESSIONAL INDEMNITY INSURANCE

NOT ALL POLICIES OFFER THE SAME COVER

BE CAREFUL OF THE DIFFERENCES WHICH COULD BE COSTLY FOR YOUR BUSINESS

The standards of cover afforded by different Professional Indemnity policies can be as different as “chalk and cheese”. It is therefore important to ensure that you know what you are buying for that significant insurance premium you are being asked to pay. The wrong policy could be as bad for your business as no cover at all.

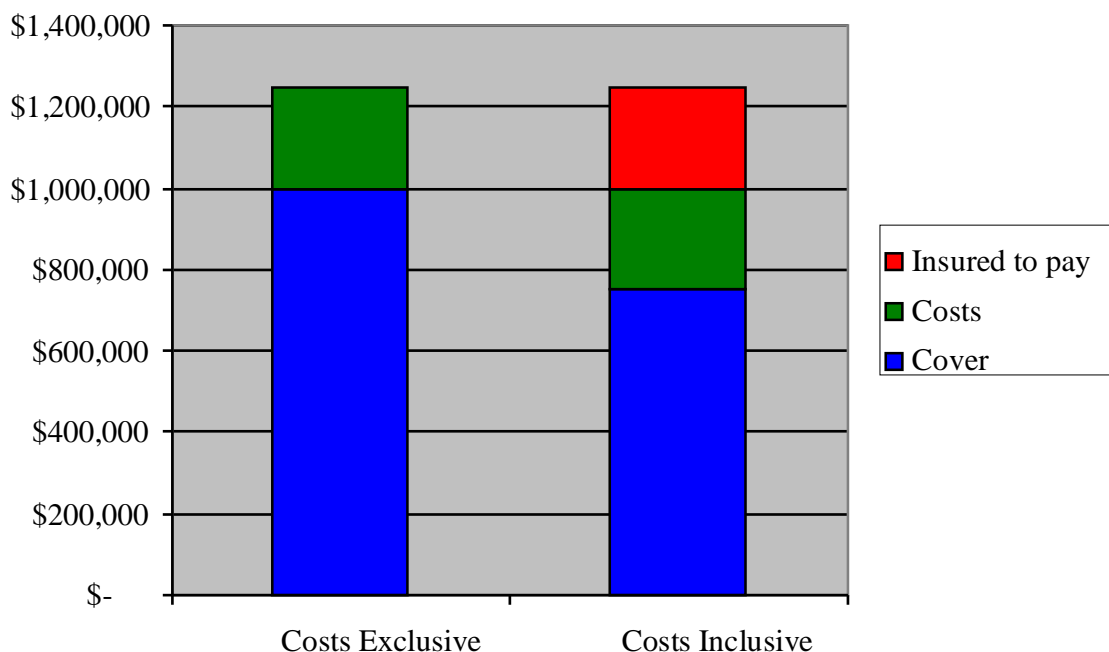
Before you make your decision about which purchase Professional Indemnity insurance policy to purchase you should seriously consider who is providing the product (both the broker and the Insurer), what is covered and how it works. Outlined below are a few of the issues you should consider.

1. A costs inclusive Limit of Indemnity

If a Limit of Indemnity is defence costs inclusive, the amount available to indemnify for compensation payable to a plaintiff and the plaintiff’s costs is reduced by any costs incurred for investigating and/or defending the claim which can place you significantly out of pocket. For example, if your cover is \$1M, costs inclusive, and you have a claim which results in a liability to the claimant for \$1M and costs of \$250,000 are incurred to investigate and defend the claim, then after payment of those costs your available cover to meet the claim is reduced to \$750,000. You will not have cover for the other \$250,000 of the claim, which may have serious financial consequences for you.

Proposed Professional Standards Legislation may make it necessary to purchase cover that is 1½ times the amount otherwise required for policies with a costs exclusive limit so as to overcome this problem. Defence costs exclusive means that the indemnifiable costs of defending the claim are paid over and above the Limit of Indemnity.

The graph below shows the possible differences in payments by Insurance Companies who offer these two different types of cover, assuming other things are equal.



In this example, the difference is a significant \$250,000. There goes any saving you may have negotiated on your premium.

Further, even if it is doubtful whether a claim may exceed the Limit of Indemnity, the mere potential for it to do so by reason of the ongoing costs to defend the claim and/or the size of the claim can create additional costs for you at a time when you least need it and can otherwise complicate the defence of the claim.

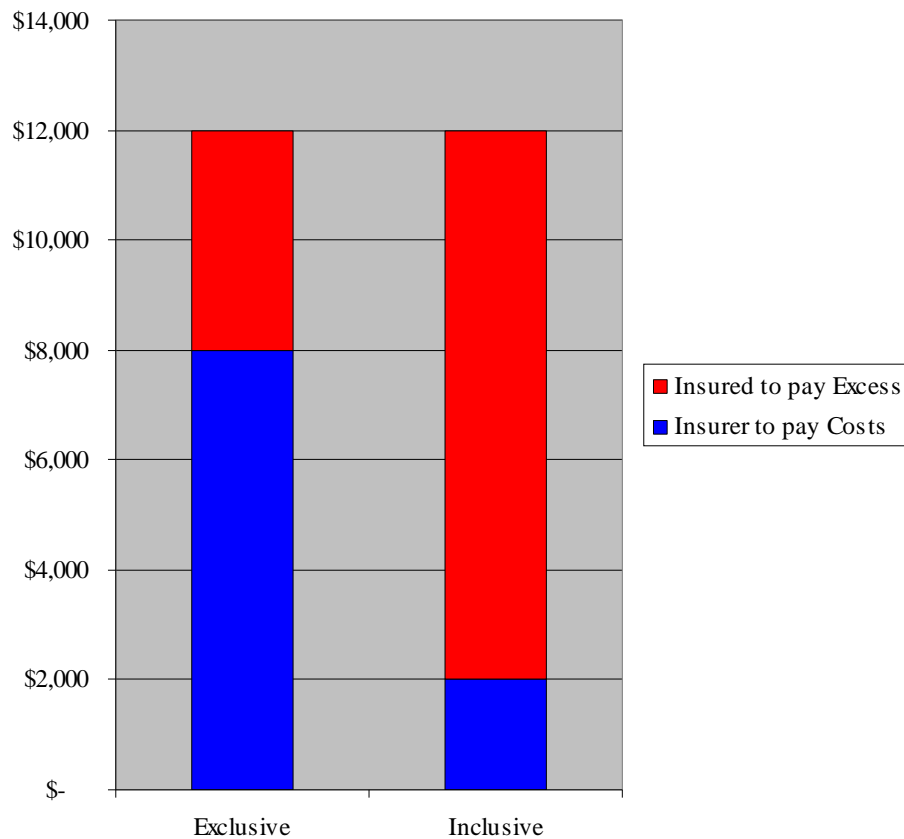
2. A costs inclusive Excess

How would you feel about having to pay your excess even if no payment is made to the claimant? If the excess on your policy is costs inclusive, then this is exactly what could happen.

When your excess is costs exclusive you only have to pay that amount if a payment is required to settle with the plaintiff.

The graph below shows the effect that these two excess types can have on your cover, other things being equal.

In this example, a claim is made against the practice which results in a settlement payment of \$4,000 after the Insurer incurs cost and expenses of \$8,000. The cover is \$500,000 with an excess of \$10,000.



In this example, you would have to pay \$6,000 more simply because of a costs inclusive excess. Even this difference could exceed any premium saving you may have received.

3. Cover for all of your work

There are a number of restrictions, limitations and exclusions on policies that can affect the cover you have for certain of your activities.

Don't leave it until you have a claim to find out that some of your work is not covered. Get written confirmation of cover for all of the work you are doing. Some of the activities which could be worth investigating about the extent to which you will be covered include:

- √ Audit work,
- √ Investment Advice,
- √ Financial Planning,
- √ Mortgage/Finance Broking,
- √ Insolvency,
- √ Mergers and Acquisitions or buying or selling businesses,
- √ Migration,
- √ work for Deceased Estates and
- √ Insurance.

4. Part IV A

There are a number of policies currently being offered which exclude Part IV A or Tax minimisation claims.

5. Professional Standards Legislation

A number of products currently available to Accountants may not satisfy the requirements for cover when the proposed Professional Standards Legislation is implemented and may need to be changed. This might even necessitate a change of insurer. You should seek specific advice about this.

6. Other

There are a number of other issues that should also be looked at but not all of them may be important to you, such as:

- i) **How many reinstatements of the Limit of indemnity are being provided?**
 - this varies from policy to policy. The preference is for unlimited reinstatement of the Limit of Indemnity and this will be necessary for PSL. Other options include no reinstatements, one, two and sometimes three reinstatements.
- ii) **Does the policy include unlimited retrospective cover?**
 - any limitation on your retrospective cover could affect cover for some or all of the work you may have done in the past. The impact of any such limitation needs to be carefully considered.
- iii) **Does the policy provide cover for any previous business that you may have operated?**
 - some don't. This could affect the cover you thought you had against a claim that may be made against you in connection with a previous business.
- iv) **What extensions are being offered and what sub-limits might apply to them?**

- the variations are numerous. The normal extensions likely to be available include:
 - § Libel and Slander,
 - § Loss of Documents,
 - § Dishonesty,
 - § Fidelity,
 - § Trade Practices Act,
 - § Outgoing Principals,
 - § Incoming Principals,
 - § Inquiry Costs and FICS.

Some of these may be automatic if the policy provides cover for any civil liability. Sub limits on some of these extensions can range from \$50,000 to \$500,000. Any other extensions being offered may be a bonus.

v) **In what jurisdictions and territories are you covered by the policy?**

- the general standard would be to cover anywhere in the world excluding USA and Canada. Some policies may limit cover to Australia and/or New Zealand only whilst some others will extend to cover worldwide without restriction.

vi) **Will the policy cover any firm that you may acquire or merge with at any future date?**

- there may be cover but there may also be a requirement in the policy stipulating that you will have to advise your insurer within a specified period and pay an additional premium for such cover to continue. You should confirm the position if you intend to merge or acquire a firm.

If you're not sure about any of these cover issues then you should discuss the offer you have been given with the broker of same. As a general rule you should then ensure that any advice provided is confirmed in writing.

The above material is only general in nature and not intended to be specific to the reader's circumstances. The reader should therefore seek independent advice from a broker or solicitor before making any decisions or relying on the information provided.