



PROFESSIONAL INDEMNITY FACTSHEET

What is Professional Indemnity Insurance?

Professional Indemnity Policies protect professionals against claims arising from a breach of their professional duty should they commit (or be alleged to have committed) an act of negligence or made an error or omission. Policies provide cover for damages or compensation awarded against the professional, as well as the legal costs incurred in investigating, defending and if required, settlement of a successful claim. These can be costs either incurred by or awarded against the professional, although they must have the prior consent of the insurer.

Who needs Professional Indemnity Insurance?

Anyone who provides advice, design, training, consultancy or other specialist services is a 'professional' and owes a duty of care to their clients.

A breach of this duty of care can lead to a legal liability to compensate a client who has sustained a financial loss. In addition, either defending or dealing with a claim can incur significant legal cost and these costs may not be recoverable from a claimant, even if the defence is successful.

Professional Indemnity Insurance is compulsory for many traditional professions such as accountants, architects and solicitors and may also be a contractual requirement when tendering for a client's business, but anyone providing a professional service is at risk without insurance.

When is the Duty of Care breached?

A professional is expected to exercise reasonable skill and care in the execution of professional services. It is not expected that the professional acts at all times with perfection, but they must exercise whatever degree of skill and care is reasonably expected of any competent practitioner.

If there is a breach of this duty of care (or an allegation of a breach), the professional may be held legally liable for the results of that breach. This legal liability primarily arises from a breach of contract or a breach of a tortious liability, which typically arises in law from a breach of civil duty through negligence, an infringement of copyright or defamation.

A claimant must firstly establish that they were owed a duty of care by the professional (this will almost certainly be the case), it must be clearly proven that this duty has been breached and finally, they must have suffered financial loss or damage.

What cover is provided by Professional Indemnity Policies?

Standard policies provide cover for claims arising by reason of any negligence, error or omissions (a breach of professional duty), although many policies provide wider cover on a 'Civil Liability' basis to include breach of contract, breach of copyright, breach of confidentiality, libel and slander, loss of documents and dishonesty of employees.



Some professions such as architects, engineers and accountants require specialist types of cover and extensions to meet the mandatory requirements of trade bodies or the customary practice of industry sectors. The extra covers and extensions can be wide ranging involving the likes of defence cover against certain criminal proceedings, contractual liability extensions for technology companies or advice on collateral warranties. In the construction sector, separate Design and Construct (D&C) wordings are issued for contractors with a design liability.

How much Professional Indemnity cover do I need?

Unfortunately there is no easy answer. It may be dictated by contractual or regulatory requirements (although it should be noted that the latter may be a minimum guideline and may not be adequate for your needs). Otherwise, you need to consider factors such as the size of the contract, the possible compensation if things go wrong and the potential costs of defending a claim. That will not be easy, so perhaps the best answer is as much as you can reasonably afford.

The policy will be subject to an indemnity limit (the maximum amount the insurers will pay) and will either be on an 'any one claim' or 'aggregate' basis. Any one claim is, as the name suggests, the limit applied to every claim notified during the policy period, whereas an aggregate limit applies to a specific period of insurance and claims would erode the limit of indemnity 'piecemeal' during the policy year until the limit is exhausted. Some insurers offer an automatic right to reinstate the indemnity limit if it is exhausted by claims.

Another consideration is whether the policy is on a 'costs inclusive' basis, meaning the indemnity limit needs to be sufficient to allow for the legal cost of defending or settling a claim or the more preferable 'costs in addition' basis, where legal costs are paid in addition to the indemnity limit.

Professional Indemnity Excesses

The excess is the first amount of every claim that is uninsured. It should be noted that the excess can either just apply to compensation payments made to a third party claimant or also apply to legal costs in investigating and defending a claim. The latter is sometimes called a costs in addition excess.

Professional Indemnity Extensions

Many insurers will provide extensions of cover which can include loss of documents, compensation for court attendance, libel and slander and dishonesty of employees (fidelity). These extensions are usually subject to a sub-limit and often a lower excess.

What is excluded from Professional Indemnity Policies?

The wording of Professional Indemnity Policies will vary from insurer to insurer, but most have a number of standard exclusions. These typically include the following:

- Injury to employees (ie risks covered by Employers Liability Policies)



- Injury to third party persons or damage to third party property unless arising from a breach of a professional duty (ie risks generally covered by Public and Products Liability Policies)
- Dishonest, fraudulent or malicious acts, although most insurers will provide cover if such acts are committed by a current or former employee, so long as a principal, partner or director was not involved or condoned the act.
- Circumstances (potential claims) that the professional was aware (or ought reasonably to have been) existed prior to inception of cover.
- Most fines and penalties, including penalties or liquidated damages arising from contractual agreements, that exceed statute or common law
- Pollution, asbestos or toxic mould, although specialist policies are available for those working in these sectors.
- Intellectual Property Rights, other than the unintentional breach of confidentiality or copyright
most insurers exclude cover for work undertaken outside certain geographical limits and claims brought outside certain legal jurisdictions, although some will provide worldwide cover
- War, nuclear and terrorism risks
- bankruptcy of the professional

Some of the above exclusions can be covered (possibly subject to a sub-limit) via specialist policies or subject to negotiation.

What does 'claims made' basis mean?

Professional Indemnity Policies issued in the UK are underwritten on a claims made basis and only provide cover for claims made (and reported to the Insurer) during the period of insurance. In practical terms this means the claim will fall on the policy in force at the time that the professional first becomes aware a claim may be made against them, rather than when the alleged error or breach of duty of care actually took place.

Because a claim may not manifest itself or be reported to the professional for many years after the work took place, it is essential professional indemnity insurance is kept in force even after retirement or the closure of a business. Further information is detailed in the 'run-off' cover section.

When should a potential claim be notified?

A claim is generally deemed to have been made when the professional first becomes aware of circumstances that could lead to a claim against them. This is known as a 'circumstance' and could be anything from a verbal criticism to receipt of a formal statement of claim from a client.

The interpretation of when a circumstance occurs is the most common source of dispute between Insurer and policyholder. It is often difficult to differentiate between what seems a minor issue that can be rectified quickly and something more serious. However, if a circumstance is not notified to the insurer at the correct time, they may refuse to deal with the claim for late notification.



Here, the exact wording of the policy may be crucial and will usually require you to notify circumstances that either 'may' or are 'likely' to give rise to a claim. 'May' has been deemed to be more than a 20% chance of developing into a claim, whereas 'likely' is more than a 50% chance. There are two schools of thought as to which is better. 'Likely' is less onerous from a notification perspective, however, an insurer may refuse to accept the notification if they do not agree that a claim is likely. This can cause complications, whereas insurers will generally accept 'may' notifications. Complicated? Yes, so the best advice is that insurers should be informed even if it is considered that the claim is without merit and the professional's actions are beyond reproach. Don't fall into the trap of worrying that your premium will increase if you notify a potential claim. These concerns are generally unfounded as insurers tend to react to actual claims rather than notifications and expect policyholders, especially larger companies to have some notifications.

Once a circumstance have been notified, it should be noted that many insurers have a condition that the claimant is not made aware of the existence of the Professional Indemnity Insurance (unless it had to be disclosed as a condition of the tendering process to obtain the work).

How long does a potential liability exist?

A claimant may lose the right to bring an action if proceedings are not commenced within certain periods, known as limitation periods. These can be complicated with various exemptions, but a summary is as follows:

- Personal injury – a claimant will lose the right of action if proceedings are not brought within 3 years from the date of injury, however, in respect of minors the limitation period does not start until their 18th birthday and for patients being treated under the Mental Health Act, until they are discharged as a patient. The limitation period runs from the date the injury is sustained or from the date the claimant is aware of the injury.
- 'Latent Property Damage/Defects' – the time runs from the date the damage first began or 3 years from discovery of the damage, whichever is longer, but never longer than 15 years.
- Other torts or civil liabilities – action must be brought within 6 years.

In view of the length of time available to a claimant to bring a claim, the professional should not only maintain Professional Indemnity Insurance, but also give consideration to retaining files and documentation, i.e. evidence that may assist in the defence of a claim.

Whilst limitation periods offer some help in restricting a professional's liability, they are also a reason why a professional may be obliged to sign collateral warranties, particularly in the construction sector. Collateral warranties generally extend a limitation period by deed of contract, typically to 12 years.

What is 'run off' cover?

Run-off cover is Professional Indemnity Insurance for a firm that has ceased trading. It is needed because of the claims made basis of Professional Indemnity Policies and is



mandatory for many professions, but also a sensible precaution to protect all firms that have been sold or closed to provide cover for work carried out prior to when the firm ceased trading. Claims can materialise many years after the work has been undertaken and because of the limitation periods, a professional will retain a continuing responsibility (and liability) after a business has closed, even if the firm was a limited liability company.

What is retroactive cover?

Retroactive cover is cover for work carried out prior to the inception of a policy and is an extension offered by most insurers for companies who may have initially traded without Professional Indemnity Insurance. An additional premium is charged to 'back date' cover for the period prior to inception of the policy and the ideal is to have a retroactive date from when the company (or their predecessors) first traded, although some insurers will only go back 'so many' years or provide cover for a specific contract. The policy will either have a specific retroactive date or if it is shown as 'none', retroactive cover will apply from when the company started trading.

When switching Professional Indemnity cover from one insurer to another, the new insurer will generally provide the same retroactive date that applied to the previous policy.

How do I arrange Professional Indemnity cover?

Insurers traditionally required a full proposal form before they would provide a quotation at inception of a policy or prior to each renewal. Nowadays, particularly for smaller or what insurers consider to be lower risks professions, many insurers have tried to make the process of arranging Professional Indemnity Insurance as easy as possible and only require a brief proposal or 'risk profile', which may be online. Insurers generally produce a 'statement of fact' from the information provided, however, this statement will usually include a number of generic assumptions and it is vital all information is checked before submitting the form or application to a broker or insurer.

For more complicated or higher risk professions, most insurers will require a full proposal form and for new ventures, insurers often require up to date CVs (curriculum vitae) for the main directors or partners detailing their professional experience and a business plan.

Whatever form or application is completed, it is also vital that all the professional's activities are notified to insurers and there is an ongoing duty to notify during the period of insurance, if activities subsequently change.

Under the new Insurance Act 2015 policyholders have a duty to provide a 'fair presentation of risk' to the insurer and those that fail to do so risk not being insured if a claim occurs.

Design and Construct Policies

It has become common place for contractors to incur a design liability, either by offering an in-house design service or through a design and build contract where, whilst the design work is sub-contracted, the contractor retains a contingent liability.

Design and Construct (D&C) Professional Indemnity Policies provide cover in respect of claims arising from negligence or error or omissions committed in the conduct of their



'professional activities'. These professional activities are the areas that would be undertaken only by or under the direct control of a properly qualified professional in a traditional construction project.

Design and Construct Professional Indemnity Policies do not provide cover for the normal activities and duties of a building or engineering contractor that are covered by Employers and Public Liability Policies. Faulty workmanship is not covered; it is only for claims made arising out of the 'professional activities' and cover is confined to the specified insuring clauses of design or specification, supervision of construction or installation, feasibility study, technical information calculation and surveying. Supervision of the professional activities will be covered, but not where a contractor is supervising their own or sub-contractors' staff in their capacity as contractors.

Policies will provide cover for liability that the contractor may incur as a result of negligence by professional consultants to whom work has been sub-contracted, but will usually be subject to the professional consultants maintaining their own professional indemnity insurance for a certain minimum limit of indemnity. Even if this is not a requirement, it is certainly best practice to check cover is in force and some insurers will also require a written contract to be in place between the two parties.

Design and Construct Policies usually provide extensions of cover for loss of documents, libel and slander, collateral warranties (but see the notes about express warranties or guarantees below), adjudication costs in accordance with the Housing Grants Construction & Regeneration Act 1996 or defence costs associated with the Construction (Design and Management) Regulations.

Exclusions in Design and Construct Policies are similar to standard professional indemnity policies, however, particular attention needs to be taken with contractual liability. Generally, policies do not cover liability which would not have existed in the absence of the contract or agreement, but collateral warranties can extend a contractor's liability to a third party beneficiary of a project (one not party to the original contract) and contain fitness for purpose obligations, such as express warranties or guarantees. If these warranties or guarantees are absolute obligations, they usually go beyond the standard of care expected from a professional, which legally has a 'reasonableness' test and can put a contractor in breach of contract, even if they have not been negligent. Such contractual commitments and any resulting liquidated damages or penalties may not be covered by insurers or where work is subcontracted, may mean that liability cannot be passed onto the actual professional who did the work.

Some insurers provide a collateral warranty checking service as an additional policy benefit, where specialist solicitors will check warranties on a contractor's behalf, to identify contract clauses that go beyond the scope of their professional indemnity coverage.

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