



WHEN IS ADEQUATE, ADEQUATE?



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MFL

Professional Partnerships

INSURANCE BROKERS

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Martin Jackson, Director of MFL Professional Partnerships, asks: 'When is an adequate level of Professional Indemnity Insurance, well, adequate?'

We live in a society which is increasingly compensation minded and anyone who has had to defend a negligence claim will know it can be an extremely worrying experience with potentially crippling costs.

Additionally, a client commissioning the professional service from a business has the right to expect their work to be covered by PII.

In recent years there's been a number of real-life situations where businesses, particularly micro SMEs, have maintained insufficient levels of cover and instances of claims have arisen where the total amount claimed has well exceeded the limit of indemnity, subsequently forcing these firms to go out of business. Not only has their livelihood gone but there's also the serious possibility of a damaged reputation.

Where the responsibility lies?

Today, a number of regulatory bodies, clients or agencies insist on mandatory minimum limits of insurance in their terms of business. But when this is not the case, which can be a common occurrence specifically on smaller domestic contracts, then where does the responsibility lie?

As a professional you are expected to use your judgement and experience to ensure you maintain an 'adequate level' of Professional Indemnity Insurance cover. Some professional bodies state that 'Adequacy' is to be determined between the client and on advice from their insurance broker, taking into account all types of work the member is liable for. This should include both the level of cover and the length of time it should be maintained, which could vary dependent on the type of contract entered into by the parties concerned.

So with no specific amounts dictated, how do you determine what level of cover is 'adequate'?

Considering unique factors

Unfortunately, there's no magic formula for calculating the limit of indemnity. However, there are a number of factors which should be taken into consideration and which will be unique to each business.

For those unsure as to what constitutes the adequate level of PII cover they need, they should seek the advice of their PII broker.

It's important to ask yourself: 'What is the extent of loss that might result from a mistake on any particular project?'

In order to give some food for thought, the size and complexity of projects undertaken by businesses should be taken into account as well as remembering that in most cases, a Professional Indemnity claim will be made up of:

- Own costs (depending on the quality of cover, this should be payable in addition to your limit of indemnity)
- Third Party Claim (damages)
- Third Party Costs

It should also be taken into consideration that claims can include costs associated with personal injury, loss, damage, delay, demolition, expert witness costs and additional costs.

It's not just the limit that should be taken into consideration, however:

- the basis of the wording – ensure it is a 'Civil Liability' wording, a policy which is based on 'neglect, error or omission' doesn't cut it these days;
- the limit of indemnity should be 'any one claim/each and every claim';
- legal defence costs should be paid by insurers in addition to the limit of indemnity. As costs tend to represent two thirds of the claim, you want to protect what limit you have to make sure it will meet the claims.

Considering the above, it can be appreciated how easy a limit of indemnity of £100,000 can quickly disappear, even £250,000 is pretty thin these days.

It could be argued that in today's professional climate, full-time businesses should be carrying a minimum level of £1,000,000, especially as purchasing this type of insurance has become much more accessible in terms of premium and coverage than at any time over the last 20 years or so.

Ensuring adequate, is adequate

So, what if you operate on a much smaller scale and your annual fee income is say, less than £10,000? Even a modest project can give rise to a significant claim.

As an example, a construction project worth £25,000 gave rise to a potential claim of £135,000. For a consultant, who had a fee income below £5,000 and a limit of indemnity of £100,000, might have appeared reasonably covered, but in practice this was shown to be woefully inadequate.

Even those individuals who support community based projects and do not seek to charge fees, still have a duty of care to their client. They are still exposed to potential liabilities and would still need to consider their requirement for adequate cover.

Employees also need to be aware that if appropriate insurance is not in place for the firm, they could still be held personally responsible for losses at some time in the future as highlighted in the 2001 case *Merrett v Babb*. It is therefore important for employees to satisfy themselves appropriate cover has been put in place and is maintained. Anyone who isn't confident that they're secure can purchase extra cover accordingly.

Insurance against such eventualities is a necessary requirement of any professional practice and you can and should use it as an important marketing tool to set you apart from many of your competitors.

Covering potential claims

While this article has been written with an element of 'construction' bias, it is important to note that the following conclusions can apply to a whole host of professions:

1. If you're offering or providing services directly to clients (including friends or family, paid or unpaid), dependent on your regulatory/professional body, it may be mandatory to obtain and maintain an adequate level of PII.
2. Review the projects undertaken and ask yourself: 'Have I got adequate PII cover? What's the extent of loss that might result from a mistake on any particular project?'
3. Remember PII claims are made up of a range of potential costs including, third party legal costs, third party costs associated with personal injury, loss, damage, delay, demolition, expert witness costs. Your defence costs (dependent on the quality of cover) should be picked up in addition to your limit of indemnity.
4. Where you're unsure what constitutes an adequate level of PII cover you should seek the advice of your PII broker.
5. Finally after all the above, probably the best advice is to buy the highest level of cover you can reasonably afford.

For further information contact MFL Professional Partnerships today:

Direct Dial: 0161 236 2532

Fax: 0161 236 2583

Email: info@m-f-l.co.uk

Web: www.m-f-l.co.uk

MFL Professional Partnerships Barlow House Minshull Street Manchester M1 3DZ
Main Switchboard 0161 236 2532 Fax 0161 236 2583 Email info@m-f-l.co.uk Web www.m-f-l.co.uk

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