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PROFESSIONAL INDEMNITY INSURANCE RENEWAL 2011 - THE NEW DYNAMIC

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

Professional Indemnity Insurance Renewal 2011 - The New Dynamic?

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Managing Director of MFL Professional, Kevin McParland takes a look at how Professional Indemnity Insurance renewal has changed in 2011.

In a previous article earlier this year, I posed the question, “The Times, They Are A-Changing - Or Are They?”.

At the time, I saw little opportunity for change in advance of renewal 2011. The Solicitors Regulatory Authority (SRA) had received much complaint from the profession and the Law Society for not acting quickly enough to rid the profession of the ‘bad apples’, i.e. those firms languishing in the Assigned Risk Pool, making claims but not paying premiums. This criticism also embraced concerns about the lack of intervention or intervening too late, to prevent serious financial loss and of course, loss of reputation to the profession as a whole.

The actions proposed by the SRA are:-

- 2011: any firm in the ARP for more than 6 months will be forced to close down. As the firms concerned are likely to be poor ones that should not be trading, this is a positive course of action. It does however leave the insurance market in the position of having to pick up the entire cost of providing “run-off” cover for those firms if, as is likely to be the case, they do not have sufficient resources to pay their “run-off” premium on closure.

- 2012: with virtually all of those poor firms having been closed down and the resultant costs borne in the 2011 insurance year, the profession will be requested to contribute towards the upkeep of the ARP.

- 2013: the ARP will be abolished and insurers will be responsible for cleaning up their own mess, i.e. if any firm on their books in 2013 cannot obtain renewal terms and if no other insurer is prepared to offer terms, cover will have to be extended by 3 months and then the firm will be closed down and the holding insurer will have to provide the ‘run-off’ cover, presumably with or without payment of the premium. This action deals with the insurers’ complaint that they were obliged to pick up the risks they had not been prepared to insure via the back door, as a consequence of the previous ARP arrangements.

Although I do not wish to appear cynical, it remains to be seen whether these proposals will be implemented and acted upon. If you were an insurer deciding on your approach for 2011 renewal, it would have appeared a pretty bleak situation. The imponderables facing insurers were:

- how many insurers would continue to be ‘Approved?’.
- would there be new entrants to the market?
- what would be the attitude of the mainstream insurers - would they be looking to continue to cleanse their books of business? Would their premium rating levels be prohibitive, etcetera?
- in the light of the SRA’s proposals outlined above, what would be the fallout into the ARP, which could have tremendous cost implications for insurers?

At our Question Time Conference in June, Jenny Screech and Mark Carver, the heads of solicitors’ PII for Zurich and Aviva respectively, indicated that the last of these was a major concern to them, given also that there was no financial benefit for the insurance market in 2011 as a result of actions proposed by the SRA. Against this background insurers stepped boldly into the unknown; but will they or the profession be happy with the result? Stranger things have happened. However, my money is staying in my pocket!

Is there ‘A New Dynamic?’. I certainly believe there has been a change in the marketplace. Whether it will be sufficient, whether it will be to the benefit of the profession, and whether it will prove to be sustainable, remains to be seen. To help us make an educated guess, let’s analyse some statistics. In the last 6 years, premium levels for the compulsory cover in accordance with the Minimum Terms have fluctuated as follows:

2011	£255m
2010	£213m
2009	£245m
2008	£216m
2007	£204m
2006	£220m

For the first time, the £250m mark has been exceeded. That was the premium paid by the profession in the last year of the SIF, eleven years previously. A couple of comments are necessary:

- 2010: some Approved Insurers operated a quasi tax-avoidance scheme, using legitimate (but morally indefensible) measures to limit their contributions to the ARP by under-declaring the amount of business they had done. The resultant additional burden fell onto those insurers who played it straight. Most of the loopholes that were exploited have now been closed by the SRA. While it can never be accurately established, it is believed the premium collected but not declared would have produced a true total of £235m, plus.

- 2007 & 2008: Quinn Insurance were very active and in those two formative years were providing cover to smaller practices below cost price in order to build a dominant market position. This was not of course sustainable, with the inevitable consequences. It will be of comfort to former Quinn Insurance policyholders (and the SRA) that the Irish Government appears to have agreed to make a compensation fund available, otherwise many policyholders would be having to fund claims payments from their own resources.

The table below shows the activity level across the Approved Insurer market:

Insurer	2011 Position	2011 %	2011 Premium £
XL	1	18.288%	46,762,283
Hanover Re	2	12.514%	31,999,015
QBE	3	11.782%	30,126,660
Travelers	4	11.602%	29,667,782
Zurich	5	9.411%	24,063,685
Chartis	6	8.870%	22,681,580
Allianz	7	5.773%	14,762,795
Libra	8	3.495%	8,938,026
Alpha	9	3.363%	8,600,000
Aviva	10	3.333%	8,521,532
ERIC	11	3.260%	8,335,419
QBE DAC	12	1.714%	4,381,818
WRB	13	1.467%	3,750,000
Liberty	14	1.333%	3,409,074
Enterprise	15	1.145%	2,927,000
First Title	16	1.075%	2,750,000
RSA	17	1.073%	2,744,598
Chubb	18	0.342%	875,000
Pembroke	19	0.159%	406,247
Lemma	-	-	-
SIMIA	-	-	-
Aspen	-	-	-
A G Dore	-	-	-

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Insurer	2011 Position	2011%	2011 Premium £
Quinn	-	-	-
ACE	-	-	-
Catlin	-	-	-
Hiscox		-	-
Newline	-	-	-

TOTAL	£255,702,518

Notable points are:-

- 19 insurers have written business in 2011 (or 18 if QBE and QBE/DAC are considered one market);
- Pembroke and Chubb are not seriously contributing, just serving historic connections;
- XL has increased premium take by £18m, which could be regarded as madness in the current situation. Insurers who have chased the holy grail of market share have tended to get their fingers burnt and either departed the scene or had to spend years trying to realign their books of business to restore profitability;
- XL and Hanover Re are anomalous in that both have been aggressive in chasing business in the last two years. They are now likely to feel the impact of claims and may well have to take corrective action next year. The likes of QBE, Travelers, Zurich Allianz, Aviva, RSA and latterly Chartis have already done this and are possibly at a stage of being able to compete more effectively next year.
- There should be some concern about the following markets:

  Alpha - Premium £8.6m
  ERIC - Premium £8.3m
  Enterprise - Premium £2.9m

The above do not appear to carry any financial rating.

Firms who have placed cover with these insurers can only hope that they are still around when claims crystallise and are due for payment.

Insurance brokers should have warned firms of the potential pitfalls. As at the 28th August 2011, the last 6 years' ARP figures were as follows:

Year	Number In	Premium Due £	Premium Paid £	Total Claims Reserve £
2005	33	0.927m	0.412m	3.378m
2006	32	0.522m	0.271m	3.173m
2007	28	0.308m	0.236m	14.740m
2008	169	4.941m	2.164m	49.446m
2009	279	6.128m	3.071m	39.454m
2010	309	12.132m	4.269m	19.949m

- these figures make no provision for the additional cost of providing run-off cover to firms that became defunct, which is substantial;
- at the time of writing, the exact statistics for 2011 had not been issued. However, it is anticipated a further 48 firms will have been placed in the ARP, which would be considerably fewer than had been expected;
- the claims costs for 2009 and 2010 are by no means fully developed at this stage;
- the figures for the last 3 years' claims reserves are quite staggering. On current projections the impact is that the Approved Insurers, over and above claims paid on behalf of their legitimate clients, have to find a further £109m to cover claims made by firms which none of them chose to insure; the eventual cost could well be more. Many in the profession feel the firms causing these claims should have been closed some time ago.

In conclusion:

- the premium rise in 2011 could have been much steeper;
- some insurers are turning the corner but others have yet to experience the pain of irresponsible underwriting. There are however some positive signs for 2012;
- while the SRA can breathe a sigh of relief in that the renewal round has been completed, this relief may be temporary. The means by which the number of firms falling into the ARP was kept down is that many firms escaped the ARP only by securing cover from insurers with no financial rating. As the average gestation period for claims to evolve from initial notification to becoming payable exceeds two years, many claims will not become due for payment until after the renewal round in 2013. If any insurer becomes insolvent by then, the profession's Discretionary Compensation Scheme may pick up some claims but there will be no automatic insurer of last resort, ie the ARP, to provide cover. Affected firms will have to find an insurer prepared to cover them, the result being that firms may not get their claims paid; may not be able to find alternative cover; or at the very least, may have to pay a further and possibly more expensive premium to a new insurer.

Surely the time has arrived for the SRA to introduce financial criteria when approving participating insurers (after all there are only a limited number) and to stop gambling with the reputation and livelihood of the profession and with the protection available to its clients.

Last and no means least and I know this is a repetition of what I have said many times before, firms will have to make themselves into better risks, not only from an insurance perspective but also to manage the myriad changes engulfing the profession at the moment.

Kevin J McParland
Managing Director
MFL Professional

For further information, contact a member of the MFL Professional team:

Direct dial: 0161 236 2532