

January 2, 2020

Important Notice to all Policyholders: Claims Expense Deductible

Effective April 1, 2020 Pro-Demnity Insurance Company will begin applying a Claims Expense Deductible (CED) to a small number of Policyholders. The CED will impose a new deductible on the Expenses involved in defending a claim, commencing at the point where the claim must be defended, whether through mediation, litigation, or other legal means.

This deductible – which is explained in more detail below – is intended to reduce the overall claims costs incurred by Pro-Demnity, thereby helping to control the ongoing increases in rates. The impact of this measure will take a few years to be felt, given the average timelines for claims litigation. But ultimately, it will help to spread the cost of a claim more evenly among all practices – the insurance premiums of the many paying for the losses of the few.

Why this deductible is being applied

The intent of this endorsement is two-fold:

1. To better apportion the costs of defending high frequency claimants, since when individual firms incur repeated costly claims, all policyholders are unfairly affected;
2. To help those firms in this small group understand that their claims frequency is high and to encourage them to take action to address that issue. This may be accomplished by a) increasing their fee structure to recoup some of the expected deductible they will have to pay (therefore, moving the cost onto the project and off of the rest of Ontario architects), b) helping them to change their risk management approach perhaps by limiting their liability in contract, or c) by other means or combinations of means.

Pro-Demnity was created to ensure that all architects qualified to practise in Ontario would have guaranteed access to professional liability insurance on an affordable, fair and equitable basis. Commercial insurers were, and are, unable to offer this guarantee. A further requirement was that there would always be funds available to defend against and, when necessary, to pay for any actual or alleged errors or omissions for which architects may be responsible.

This arrangement enables architects to undertake projects without jeopardizing their financial survival and ensures the public and building owners that there are funds available to correct deficiencies. This system allows innovation and growth that would otherwise be restricted or curtailed.

The process by which Pro-Demnity provides insurance and sets its rates is very simple: we collect enough premium each year to pay for all the losses of that year. There is no magic involved. Although over the short-term, we may see various highs and lows in the cycle, in the long-term, the money we pay out cannot be more than the money we bring in. With over 30 years of claims data, we can make well-educated estimates and predictions of claims frequency (how many) and severity (i.e. how big) for average situations.

All architects may become the subject of a claim, which is why the law requires all architects to have professional liability insurance. As your insurer, we know that claims (real or alleged) are an inevitable part of the overall design and construction process. It is increasingly apparent, however, that a small group of practices (less than 1%) has attracted a significant number of claims – well above the average. Over a 10-year period, these practices have accounted for 18.4% of all claims (by number) and an average of 13.9 claims per policyholder. Since expenses – not actual damages – represent by far the largest component of our claim costs, and since each claim incurs new expenses (whether or not our policyholder is deemed liable), we know that claims frequency is an indicator of how expensive a firm is to insure. We calculated that this same small group of frequently litigated practices had, over the same 10-year period, received significantly more in claims payments than they had paid in cumulative premiums.

What the deductible means and how it works

For the affected firms, the Claims Expense Deductible (CED) will be applied to any claim where “*Legal Defence*” is required to allegations made against the architectural practice as follows:

- 50% payable to Pro-Demnity upon the commencement of a defence for the architect;
- 50% payable to Pro-Demnity at the start of discoveries, examinations or a pre-trial.

“*Legal Defence*” means that Pro-Demnity has received any of the following: a) a Statement of Claim, b) notification of motions pursuant to an active statement of claim, or c) notification of the beginning of other legal proceedings that require a formal legal response. This definition applies to litigation, mediation, arbitration or any other stages at which a lawyer’s involvement is required.

The CED applied will range from \$10,000 to \$50,000 based upon policyholder revenue.

The CED will not apply to claims for which we have received notification from the policyholder but for which no *Legal Defence* has begun.

Who will be affected?

For the 2020-2021 policy period, the CED will be applied to fourteen (14) practices, at the time of their next renewal on or after April 1, 2020.

To identify this group, we employed the following process:

- We reviewed the history of all claims for the past 10 complete underwriting years, discovering that, in total, 405 policyholders had 1,058 claims, representing just over a quarter of all policyholders.
- We noted that, of all 405 policyholders with claims, 142 have had claims payouts that exceed their total premiums paid.
- We then reviewed these 142 practices and focused on the “top” 30 practices in detail, for potential application of the CED. Of these, 16 were removed from the list because they were either three years claims free and/or they had fewer than five claims over 10 years.
- We determined that the remaining 14 policyholders will have the CED applied commencing with their next renewal after March 31, 2020.

The names of the affected firms will be kept confidential. Affected practices will be notified as their next renewal (April 1, 2020 or after) approaches.

Going forward

Each year, Pro-Demnity will review all claims and will identify any additional policyholders who will have the CED applied. All policyholders for which the CED will apply will be notified as part of their renewal process. Once the CED is applied, it will remain until the account no longer qualifies (three years claims free and/or less than five claims in the previous 10 years) for three consecutive years, measured at the renewal date.

What the CED is and is not

The CED is not a tool for identifying good or bad architectural practices. The list of firms affected includes many that are respected and well-run. It happens that they do projects that are often complicated, large and challenging. We are not trying to tell architectural practices to stop doing those projects.

Instead, we are saying that these projects should be priced to include the costs of the inevitable claims that will arise from them. It is much fairer for its owners, developers and ultimate end-users to bear the costs of these claims, rather than all Ontario architects doing so.

Our underlying intent – and greatest hope – is that the CED will heighten awareness of risk management and such “boring subjects” as signing wise contracts that limit and control your liability, as well as proper project documentation which makes it significantly easier and less expensive to defend you, and engaging engineers and other professionals with their own valid and adequate insurance.

And to the very few companies on this list that seem to have decided that having multiple claims is an OK way to do business, we are simply saying that it is time for you to start paying the costs of your business model yourself.

Most importantly, we know that the CED is a tool not a solution. The increasing claims activity faced by architects is the result of complicated forces: an overcrowded legal system, the imposition and acceptance of unfair contracts, and the increasing propensity of lawyers to sue everyone they can think of (perhaps mistaking quantity for quality), to name a few.

As your insurance company, Pro-Demnity’s primary commitment remains the continued assurance that all Ontario architects have access to professional liability insurance that is affordable, fair and equitable, now and in the future.