

## Professional Liability Insurance is Different and Special

May 1, 2020

The COVID-19 crisis has imposed significant change on many parts of society, the economy, and business. One thing it has not changed, however, is the fundamental difference between Pro-Demnity's Professional Liability policies and most other Property and Casualty (P&C) policies you may purchase as an individual or business.

Fundamentally, all insurance is an attempt to offer protection to policyholders today for unknown claims that may arise tomorrow. As such, the price for insurance represents the insurance company's best estimate of the cost of defending and handing those claims, usually based on actuarial analysis and historical experience. As the insurance company's estimate of risk (and its associated costs) rises and falls, rates and premiums will rise and fall over time as well. This fundamental link between the cost of the risk assumed by an insurance company and the prices it charges for its insurance policies has also not been changed by this crisis.

What has changed for some insurance is that the estimated cost of the risk covered by a policy has changed. For auto insurance, as an example, people staying at home and greatly reducing their driving is changing the expected claims that will arise, and auto insurers are reclassifying drivers (from commuting to pleasure-use, for example), thereby reducing premiums. For other types of insurance, the current crisis is unlikely to change expected claims costs.

To understand why this is so, it is important to consider the differences in the essential nature of various policies and how they affect the risk and the cost of that risk covered by your insurance.

### How is Professional Liability Insurance different?

Professional Liability insurance – also known as Errors & Omissions (E&O), Professional Indemnity (PI), and occasionally as Malpractice insurance – are typically **Claims-Made** policies. Every policy issued by Pro-Demnity is Claims-Made. The policies most of us are familiar with (i.e. home, auto, office, general liability, etc.) are **Occurrence** policies.

#### Claims-Made Policy

An insurance policy that covers claims first presented during the current policy term arising from incidents which happened during the same policy year *or for any previous year going back to the retroactive date.*

Fundamentally, a Claims-Made policy covers everything that has happened in the past or current year that triggers an allegation of wrongdoing in the present policy term.

#### Occurrence Policy

An insurance policy that pays for incidents that occur during the policy term, regardless of when a claim is filed in the future.

Fundamentally, an Occurrence policy covers everything that occurs during this policy period that triggers an allegation of wrongdoing in the future or current year.

## How does this affect Underwriting & Pricing?

Claims-Made policies underwrite *based on past activities*, since they are what trigger most claims that will be presented in this policy term. For Pro-Demnity, this is why we use the average of the last three years' revenue from our policyholders as the basis upon which to charge premium: it is those projects (and the ones before them) that will trigger most of our claims. Contrasting this with your home or auto insurance – or even your Commercial General Liability (CGL) and office property – where the risk being charged for is only the events of the current year. An increase or decrease in the use of your auto, for example, triggers an immediate change in your rating because it makes an immediate change to the risk being covered by this year's policy.

In the current environment, this means that insurers can adjust your office property and CGL premiums to reflect that there are few or no people on the premises, they can reduce your auto premium to reflect that you are not commuting to work, etc. For Pro-Demnity, the past has not changed, and our risk exposure is as high as it was at the start of the year. Given the historical trend of adverse economic times causing an increase in allegations of wrong-doing – people in dire straits seek to find money wherever they can find it – it could be argued our risk exposure is increasing daily.

## How does this affect our action/reaction in the current situation?

Our insurance costs are real, and the cumulative risk of all past projects which could lead to a claim in the current period does not lend itself to flexibility in changing or waiving current premiums.

To ensure financial security and stability, we purchase reinsurance and these costs must be paid by us regardless of whether the policyholder has paid their premium. To properly defend and protect architects, we use industry leading experts and specialized lawyers, both internally and with our preferred panel of law firms. All of this work continues throughout the crisis.

It costs us about \$18 million to operate our company: \$13 million or so for claims, \$5 million to run the company. This means we pay about 72% of our revenue on claims, versus 56.9% for the average P&C insurer in Canada in 2018.<sup>1</sup> We also suggest taking a read of Pro-Demnity's [2020 Plan Update](#) which further outlines the impact of claims and legal expenses on overall rates and premiums.

## What else makes Professional Liability Insurance special?

Professional Liability insurance stands out from all other P&C products as it is designed to shelter your livelihood and reputation. It extends financial protections to you as a professional, to your architectural design business, and to your heirs and successors.

## What makes Pro-Demnity special?

Pro-Demnity was created solely to serve Ontario architects. As part of our mandate, we have an obligation to remain fiscally sound, resilient and robust so that all participating Ontario architecture practices benefit. We protect and defend your livelihood as a professional and the reputation of your architectural practice.

Looking after architects, as individuals and as a profession, is why we exist: your success is our success. We are here to help you enhance your practice risk management acumen, minimize the costs and time of claims, and optimize the valuable benefits and coverages that are already included in your Pro-Demnity policy.

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<sup>1</sup> Insurance Bureau of Canada, [2019 Facts Book](#), page 9.