

Professional Indemnity glossary of terms

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Index

Aggregation of claims	Intellectual property
Automatic reinstatement	Joint venture liability
Average provision	Jurisdictional limits
Cancellation	Libel and slander
Civil liability	Limit of indemnity
Claim	Liquidated damages
Claims made	Lost documents
Continuous cover	Principals previous business
Contractual liability	Prior claims or known circumstances
Contributory negligence	Professional duty
Costs exclusive limit of indemnity	Professional services
Costs inclusive limit of indemnity	Proportionate liability
Excess	Retroactive date
Exclusive excess	Run-off cover
Fraud and dishonesty	Severability and non-imputation
Governing law	Sub-contractors and consultants
Inclusive excess	Territorial limits
Inquiry costs	Trade Practices Act
Insured costs	Trading debt
Insuring clause	

Aggregation of claims

This refers to a clause that combines two or more interrelated claims covered by the policy, to enable them to be treated as a single loss for the purposes of applying the policy Limit of Liability and deductible or excess. Typically an aggregation clause would provide that all claims arising out of, based upon or attributable to a single act, error or omission or series of acts, errors or omissions attributable to the one source or original cause will be considered a single claim and only one excess or deductible and one Limit of Liability will be applied.

Note: Not all professional indemnity policies include this clause

Automatic reinstatement (also known as Increased aggregate limit of indemnity)

Unless otherwise specified in the policy the *Limit of Indemnity* (see definition) of a policy represents the maximum amount that can be paid in any one policy period.

Some policies, however, include a clause known as an Automatic Reinstatement Clause which allows the *Limit of Indemnity* to be 'reinstated' for new, unrelated claims, should the original sum be depleted by a claim or series of claims that equals the *Limit of Indemnity*.

Depending on the number of reinstatements provided by the policy this clause can provide indemnity for multiple claims during the year where the total of these claims exceeds the policy *Limit of Indemnity*. However, no one claim payment by the insurer will exceed the policy *Limit of Indemnity*.

For example, if the Insured purchases a policy with a \$1,000,000 limit of indemnity, and the policy contains one automatic reinstatement the policy provides cover for claims aggregating up to \$2,000,000 during the period of insurance, subject to any one claim being no greater than \$1,000,000.

Note : Some professional indemnity policies only provide this on an optional basis. Please check the quote or policy wording to ascertain whether the policy contains an Automatic reinstatement clause and the number of reinstatements provided.

Average provision (also known as Co-insurance clause)

This refers to professional indemnity policies which provide a *Costs Exclusive Limit of Indemnity* (see definition). Where the total amount of a claim (including the claimant's costs and expenses incurred in bringing the claim) exceeds the *Limit of Indemnity*, then the Insured costs (see definition) covered under the policy will be calculated on the basis of the proportion which the *Limit of Indemnity* bears to the total amount of the claim.

For example:

In a situation where the insured has a professional indemnity policy with a *Limit of Indemnity* of \$1,000,000 and a claim is made for \$2,000,000 including claimant's costs and expenses with Insured Costs of \$750,000 the amount payable by the insurer under an *Average provision clause* would be as follows:

1. \$1,000,000 in respect of the claim including claimant's costs and expenses; and
2. 50% of the Insured costs of \$750,000, being \$375,000 as the \$1,000,000 *Limit of Indemnity* represents 50% of the total cost of the claim.

This leaves an uninsured amount of \$1,375,000

Note: If the Professional Indemnity policy provides a Costs inclusive limit of indemnity (see definition), then the uninsured amount would be \$1,750,000.

Cancellation

Cancellation is the termination of an insurance policy before the expiry date. Most professional indemnity policies include a cancellation clause providing that cancellation of the policy by the insured be requested in writing. Generally the effective date of the cancellation will be the date of receipt of the written cancellation request by the insurer (unless a later future date is specified). A premium refund may or may not be available to the insured for the cancelled period of insurance. This will depend on the policy terms and conditions.

The insurer may only cancel a professional indemnity policy in accordance with the provisions of the Insurance Contracts Act 1984.

Note: Some insurers may charge a cancellation fee of up to the whole amount of the pro-rata return premium.

Civil liability

Some professional indemnity policies provide cover for an insured's 'civil liability' to a third party arising out of the insured's conduct of their professional business or the provision of professional services.

Civil liability is liability of one party to another arising out of civil law, as opposed to criminal law.

There are four branches of civil law:

1. Tort law (the common law torts of negligence, nuisance, and defamation);
2. Contract law (breach of contract)
3. Statutory law (eg the Trade Practices Act)
4. Equity - (a system of law based on the principle of 'fairness' designed to furnish remedies for wrongs which were not legally recognised or for which no adequate remedy was provided by the common law).

A civil liability wording ordinarily covers all four branches of civil law. However, the policy only responds to civil liability for claims arising from the conduct by the insured of the nominated professional services stated in the policy schedule.

Claim

A 'claim' means any demand or notice (verbal or written) made by a third party against the insured for payment under the terms of the professional indemnity insurance policy to compensate them for a loss. A claim may be made by, a writ, statement of claim, application or other originating legal process or by other written or verbal notice.

Note: All professional indemnity policies have a different definition of 'claim'. Please check the policy wording carefully.

Claims made

A reference to a 'claims made' policy refers to a policy which provides access to indemnity for claims made against the insured and reported to the insurer during the period of the policy. If during the period of insurance the insured notifies a circumstance that may give rise to a claim then, because of the requirements of the Insurance Contracts Act that also triggers coverage under the policy.

Claims made cover does not require the incident that gives rise to the claim against the insured to have taken place during the period of the policy.

Continuous cover

Claims made policies generally exclude claims arising from facts and circumstances known to the insured before the start of the policy period. An inadvertent and innocent failure to disclose a known fact or circumstance that gives rise to a claim could result in an uninsured loss.

Continuity clauses address this situation by extending cover under the policy to a claim arising out of a fact or circumstance which could have been but was not notified under a previous professional indemnity policy.

For a continuous cover clause to apply, usually the insured must have been insured under a professional indemnity policy issued by the insurer at the time they first became aware of the fact or circumstance that gives rise to the claim. The claim must have been covered under the previous policy and the insured must have continuously, without interruption held a professional indemnity policy with the insurer until the time when they notify the claim to the insurer.

This cover will usually only be provided where there has not been any fraudulent nondisclosure, or fraudulent misrepresentation by the insured. The insurer's liability is usually limited to the indemnity available under the previous policy.

Contractual liability

This refers to any liability assumed by the insured by contract.

Note: Professional Indemnity policies generally do not cover any liability assumed under contract which is beyond the liability which would have existed in the absence of the contract. This may include any express warranty, guarantee, hold harmless agreement or indemnity clauses.

Contributory negligence

This refers to behaviour or an act of the claimant which indicates a lack of due care on their part and which has helped cause the incident giving rise to the loss or aggravated or increased the loss or damages suffered by the claimant as a result of the incident.

Costs exclusive limit of indemnity

The *Limit of Indemnity* is the maximum amount the insurer will pay in respect of any one claim first made against the insured and notified to the insurer during the period of insurance. A costs exclusive limit of indemnity does not include *Insured costs* within this limit. These costs are in addition to the *Limit of Indemnity* (subject to any Averaging provision). See *Insured costs*.

Costs inclusive limit of indemnity

The *Limit of Indemnity* is the maximum amount the insurer will pay in respect of any one claim first made against the insured and notified to the insurer during the period of insurance. A costs inclusive limit of indemnity includes within this limit *Insured costs*. This means that *Insured costs* incurred in defending a claim reduce the *Limit of Indemnity* available to satisfy the 'indemnity' or compensation amount of the claim. See *Insured costs*.

Excess (also known as deductible)

The excess is a policy condition requiring the insured to pay a portion of the loss. Usually this amount represents the first amount which is payable by the insured in respect of any one claim with the insurer paying the balance over that amount up to Limit of Indemnity.

Note: See Exclusive excess and inclusive excess

Exclusive excess

An Exclusive excess does not apply to costs and expenses incurred by the insurer or the reasonable costs incurred by the Insured (with the insurer's prior consent), in defending, investigating or settling any claim. The excess applies to the 'indemnity' or compensation amount of the claim only.

Fraud and dishonesty

Professional indemnity policies will generally exclude cover for claims arising from a fraudulent, dishonest or criminal act.

Note: Many professional indemnity policies however will provide a 'writeback' covering claims made against innocent insureds against civil liability for compensation resulting from fraudulent, dishonest or criminal acts, BUT cover will not extend to the perpetrator of such fraudulent, dishonesty or criminal act. This cover varies significantly across different insurers' wordings.

Governing law

Refers to the place where disputes between the insured and insurer over interpretation of policy terms conditions and performance of policy obligations will be determined. An example of a governing law clause is as follows:

This policy will be governed in accordance with the laws of New South Wales, Australia. Any disputes relating to interpretation will be submitted to the exclusive jurisdiction of the courts of new South Wales, Australia.

Inclusive excess

An Inclusive excess applies to both the costs and expenses incurred by the insurer or to the reasonable costs incurred by the insured (with the insurer's prior consent), in defending, investigating or settling any claim as well as to the compensation amount payable.

Inquiry costs

Traditionally professional indemnity policies only provided cover for claims made by third parties for compensation. Many professionals are also exposed to legal costs in representing themselves at inquiries. Inquiry costs extensions provide cover for the costs of these inquiries.

Under an Inquiry costs clause, if the insured has to attend an inquiry or hearing of a disciplinary nature that is held before an official industry or professional body then the insurer will, pay for the reasonable legal costs and expenses incurred in attending the inquiry if the attendance arises directly from conduct of the insured in carrying out their professional services.

This extension only covers notices requiring the insured's attendance at an inquiry first ordered or commissioned and received during the period of insurance.

Note: The level of cover and amount of cover provided by insurers varies considerably across the market.

Insured costs (or Insured's costs and expenses)

Refers to costs and expenses incurred by the insurer or the reasonable costs incurred by the insured (with the insurer's prior consent), in defending, investigating or settling any claim.

Insuring clause (also known as Operative Clause)

The Insuring clause is the most important clause in any professional indemnity policy. This clause sets out what the policy will cover, who is insured under the policy and on what basis. Professional indemnity insuring clauses are generally very broad. The use of definitions, extensions, exclusions and general conditions within the policy wording will restrict the cover back to the insurer's intention.

Note: It is imperative that you understand the defined terms within any Professional indemnity wording as they vary considerably amongst Insurers' wordings.

Intellectual property rights

This is a term used to refer to the legislative and common laws protecting the exclusive property rights in original creative and intellectual effort including laws on copyright, design, patent, circuit layouts, plant varieties, confidential information, trademark and business reputation (trade practices).

Joint venture liability

A joint venture is generally a contractual agreement joining two or more parties for the purposes of executing a specific business endeavour. All parties agree to share in the profits or losses in this venture according to their respective share.

Joint ventures are regularly unincorporated, but some longer term joint ventures are incorporated.

Where the Insured is part of a joint venture it has a joint exposure in this venture and some Professional indemnity policies will cover only the insured's exposure so long as it coincides with the agreed Professional services description. Also see professional services.

Note: Some Professional indemnity policies only provide this on an optional basis. Please check the quote or policy wording to understand whether this cover is provided.

Jurisdictional limits

Refers to the countries where the policy will respond to claims being made against the insured.

If jurisdiction is limited to certain named countries then the policy only responds to claims in those countries. If it is 'worldwide excluding North America' then the policy responds to claims anywhere except in North America.

A typical 'worldwide excluding North America' jurisdictional limits clause, would provide cover for claims made against the insured anywhere in the world, except for claims brought in a North American court, or that arise from a judgment or order of a North American court.

Note: Not all Professional indemnity policies provide "Worldwide excluding North America" jurisdictional limits.

Libel and slander (also known as defamation)

Defamation refers to the publication of statements or material which may have the effect of lowering the reputation of a person in the eyes of others. The statement may be made orally (slander) or in written form (libel). Any living person, small business (employing fewer than 10 people) and non-profit organisations may sue for defamation. Corporations are restricted in suing for defamation but directors and senior managers of corporations may sue as individuals.

Note: Professional indemnity policies generally cover unintentional acts only.

Limit of indemnity

The limit of indemnity is the maximum amount the insurer will pay for compensation and claimant's costs and expenses arising from any one claim and all claims in the aggregate made by the insured under a policy during the period of insurance. Also see Automatic reinstatement, Costs inclusive & Costs exclusive limit of indemnity.

Liquidated damages

An amount of damages which has been contractually pre-determined in the event of a breach of that contract. In a contract a liquidated damages clause must be a genuine pre-estimate of the loss that will be suffered by the innocent party as a result of a breach. This agreed sum must not be in the form of a penalty as this will be unenforceable.

Note: Covers in respect of liquidated damages vary across Insurers wordings. Please check the relevant wording.

Lost documents

A Lost documents clause will provide cover for the costs associated in the replacement or restoration of documents which have been destroyed, damaged, lost or mislaid (some insurers may also cover any direct consequential loss).

Documents can mean deeds, wills, agreements, data, electronic records, maps, plans, records, written or printed books, letters, certificates, written or printed documents or forms of any nature (excluding any bearer bonds, coupons, bank or currency notes or other negotiable instruments) which is the property of the insured or for which the insured is responsible.

Note: The level of cover and amount of cover varies considerably across Insurers. Please check the policy wording.

Principals previous business

Principals previous business clauses offer cover to the insured principal for wrongful acts committed by them whilst conducting the same professional services in a prior partnership or company.

For example, an insured who was a partner in an accounting firm and then set up their own accounting firm, they would need to obtain a Principal's previous business extension to ensure they were covered for any claims arising out of work undertaken as a principal in the previous firm.

Note: this is not generally a standard feature of professional indemnity policies. It is usually available upon request via endorsement.

Prior claims or known circumstances

Claims made policies generally exclude claims arising from facts and circumstances known to the insured before the period of insurance. Just like any other form of insurance, a professional indemnity policy is intended to cover unforeseen circumstances / events only.

The Prior claims or Known circumstances exclusion is a clarification that any prior claims or known circumstances to the insured are not covered by the policy.

Professional duty

A professional (any person who exercises and professes to have a special skill) owes a duty of care to a client or third party in the performance of their professional work. This duty may be owed in tort (any civil wrong doing) and in contract.

Note: Generally a professional indemnity policy wording which covers a breach of Professional duty only (see Insuring clause of wording to check) is less broad than a Civil liability professional indemnity policy wording as it must be proven that the claim arose out of breach of professional duty owed.

Professional services

Professional services are the insured's business activities which are covered under the professional indemnity policy. The Professional services description is usually defined manually by the insurer in the quotation supplied. Professional services can be defined within the policy wording and generally occurs when the policy wording is tailored for a specific profession.

Note: it is important that the Professional services description in a professional indemnity policy matches the activities performed by the insured.

Proportionate liability

The principle of proportionate liability requires that the liability of a wrongdoer, who is a concurrent wrongdoer, be limited to the proportion of the loss or damage which is considered to be a just and reasonable reflection of that wrongdoer's responsibility for the plaintiff's loss.

Under proportionate liability there is no right of contribution between wrongdoers as such because each can only be required to compensate the plaintiff for their proportion of the loss suffered.

Retroactive date

The Retroactive date of a policy is the date after which acts, errors or omissions of the insured are covered; any act, error or omission occurring before that date will not be covered. That is, any act, error or omission arising from professional services provided after the Retroactive date will be covered under the policy. Retroactive cover extends cover under the policy to acts, errors or omissions that occurred prior to the inception date of the current policy period.

Policies can be underwritten with two types of retroactive dates.

- a) Unlimited retroactivity - where the policy will cover a claim made and reported during the policy period relating to an act, error or omission, regardless of when the act, error or omission occurred; Or
- b) A "dated" retroactivity clause - where the policy will cover a claim made and reported during the policy period relating to an act, error or omission that occurred after the retroactive date.

Note: If a Retroactive date is imposed, insureds should be aware of this limitation of cover.

Run-off cover

Professional indemnity policies are usually claims made and notified policies. This means that in order to trigger the policy the claim must be made against the insured and reported to the insurer during the policy period. Companies or individuals ceasing business still have exposure to claims being made after their business ceases arising from their previous business activities.

Run off cover provides cover for unknown claims made and reported following expiration of the professional indemnity policy arising out of acts, errors or omissions occurring during the period of Run-off insurance cover.

Note: Some Professional indemnity policies will provide automatic run-off cover up until the end of the policy period of insurance should the policy be cancelled during the policy period. Further run-off cover can then be purchased by the client for multiple years thereafter. Some insurers may only consider run-off on a year by year basis, whereas some insurers can offer multiple years of run-off cover in a single policy.

Severability and non-imputation

This policy term applies where there is more than one insured under a professional indemnity policy.

This clause protects an innocent party insured under the policy where there has been a failure of another insured to:

- comply with their duty of disclosure under the Insurance Contracts Act 1984; or
- comply with any obligation, term or condition of the policy.

This clause will also protect an innocent insured where another insured undertakes any dishonest, fraudulent, criminal or malicious act so long as the innocent party had no prior knowledge of these acts.

The effect of the clause is that cover will still be available to the innocent insured despite the failure of the other insured party.

Sub-contractors and consultants

Insured's often use the services of sub-contractors or consultants to provide specialised services. In doing so, the insured may be found to be vicariously liable for the acts and omissions of those sub-contractors and consultants performing work for or on behalf of the insured.

Professional indemnity policies generally provide cover for the insured's vicarious liability arising out of the professional services provided by the subcontractor or consultant. Indemnity will generally not be extended to cover the liability of the sub-contractor or consultant who committed the act, error or omission.

Note: Where requested, insurers may consider extending cover to the sub-contractors or consultants. Ordinarily the sub-contractor or consultant should be required to hold and maintain their own separate professional indemnity policy.

Territorial limits clause

Territorial limits clauses restrict cover to claims resulting from the conduct by the insured of professional services in certain countries. A narrow Territorial limits clause will restrict cover to operations in certain named countries. A broader territorial limits clause may cover conduct of professional services worldwide.

Ordinarily a Territorial limits clause will exclude professional services of the insured performed in North America, provided to persons in North America or subject to the law of North America.

Trade Practices Act

A Trade Practices Act clause provides cover for misleading and deceptive conduct in breach of the Trade Practices Act 1974 (Cth) (TPA). The object of the TPA is to enhance the welfare of Australians through the promotion of competition, fair trading and provision for consumer protection. In so doing the TPA regulates how corporations act in trade or commerce.

Note: Professional Indemnity policies generally do not cover any civil or criminal penalties provided for by the TPA.

Trading debt

A trading debt is a debt(s) incurred as a result of the undertaking of the insureds business or trade. As trading debts are generally not compensatory in nature and professional indemnity policies are intended to deal with claims for compensation, claims for trading debts are generally excluded from cover under a professional indemnity policy.