A Guide to **Legal Malpractice Insurance**

Attorney Protective

a MedPro Group/Berkshire Hathaway company

Introduction to **Purchasing Legal Malpractice Insurance**

Where to obtain legal malpractice insurance - Legal malpractice insurance is usually obtained through licensed independent agents and brokers, although some carriers sell directly to customers. Agents and brokers are licensed through state Departments of Insurance and must meet strict educational and fiduciary requirements in order to obtain and keep their licenses.

The application and underwriting process - Applications include numerous questions regarding an attorney's education, experience and areas of practice (AOPs). Ensuring that the application provides accurate and complete information will help the insurance carrier assess the risk and determine the lowest available premium for your law firm. The more information provided, the more comfortable the insurance carrier will feel with the risk.

Additional factors that can affect premiums – Carriers commonly calculate premiums by using credits (discounts to the premium) and debits (increases to the premium) that are added or subtracted from standard rates to set a premium.

Examples of credits:

- Loss/claims-free – credits offered to law firms who have been loss/claims-free for a certain period of time
- Risk management – credits offered for maintaining certain risk management standards

- Part-time credits – credits offered when a lawyer in the firm practices only part-time
- New-to-practice credits – credits offered to law firms new to the practice of law
- Law firms with good loss history may also qualify for additional discretionary credits

Examples of debits:

- Claims frequency – premiums may be increased when an attorney has had an above-average number of claims made against him/her
- Claims severity – premiums may be increased when a law firm has had a claim or claims with above-average payouts
- Practicing in certain areas of practice (AOPs) – premiums may be increased when a law firm or attorney practices AOPs that have historically produced a high frequency of claims or claims with high severity
- Management control procedures – premium may be increased when a law firm's management control procedures do not meet certain standards

Risk management – Carriers often provide risk management tools that add real value to your policy. Encouraging your attorneys to use risk management can help avoid claims and improve your law firm.

Questions to Ask When Shopping for Legal Malpractice Insurance

What legal services are covered in the policy? Confirm that all of the types of legal services rendered by your lawyers will be covered under the policy including, for example, services provided as a notary public, arbitrator or mediator, title insurance agent, etc.

Who is covered under the policy? Check the definition of “you,” “your” or “insured” to confirm that all those doing work on behalf of an attorney or the firm are covered, including past and present partners, “of counsel” and non-lawyer employees.

What is the financial rating of the insurance carrier? You can look to independent rating companies such as A.M. Best and Standard & Poor’s to determine the financial strength of any carrier being considered.

What other coverage does the policy provide in addition to the basic legal services coverage? Check to see if the policy provides supplementary payments coverage for lost time associated with a claim. Some policies provide this coverage and others do not. Also, confirm that the limits provided are sufficient to cover your lost income and note if the provision provides a separate limit so that the policy limits are not eroded by claims.

When is the deductible owed? Under most policies, the deductible becomes due when the carrier pays the first dollar on a claim. However, if “first-dollar defense coverage” is included or purchased, then the insurer pays those costs before any deductible is owed. If the limits of this first-dollar defense coverage are not reached, you don’t pay a deductible. First-dollar defense coverage can save you money, especially on smaller claims that are settled or dismissed before significant defense costs are incurred.

Are there any provisions that will reduce the deductible amount owed? Some insurance carriers provide you with ways to reduce deductibles (such as a provision that cuts the deductible in half when the claim is contained within the deductible). This can mean real savings for your law firm in the event of a claim.

How many and what kind of exclusions limit the policy coverage? Examine exclusions associated with the policy to determine how they will limit your coverage. All insurers have some exclusions in their policies but some insurers' policies have broader exclusions than others.

Does the carrier offer risk management services and tools that add value to their product? Training and education services can be costly to your firm. Determine if your insurance carrier offers these services without charge as that can equate to substantial savings both now and down the road.

Are defense of disciplinary proceedings covered by the policy? Defending a disciplinary proceeding can be costly. Some insurance policies either provide no coverage for disciplinary proceedings whatsoever or provide insufficient limits to allow for a vigorous defense. Check to ensure that your policy generously covers disciplinary matters so that attorneys and the firm are more fully protected.

Is the insurance provider specialized in lawyers' professional liability insurance? When a provider writes many diverse lines of insurance, such as personal lines, property along with professional lines, then catastrophic events in the other lines, such as a hurricane, have the potential to impact your firm's premium (due to the number of claims that the program has to pay out for the catastrophic event). A specialized insurance provider is typically not impacted by events affecting other lines and therefore neither is your firm's coverage or pricing.

Evaluating an Insurance Carrier's **Financial Strength**

Ratings – The financial strength rating of a carrier is one of the most important indicators of financial strength. A.M. Best is the leading independent analyst of the insurance industry. It analyzes the financial and operating strength of insurance carriers and awards ratings that range from A++ to F. To learn more about the A.M. Best rating system, visit www.ambest.com. Other rating organizations assess the financial strength of carriers, including Standard and Poor's, Duff & Phelps, Moody's and Weiss Research. Some basic factors used to determine financial strength include:

Surplus – A carrier's surplus is the amount by which a company's assets exceed its liabilities. Since projecting future claims costs and establishing reserves (assets backing the estimated liabilities) to cover such costs is not an exact science, a healthy insurance company routinely maintains a cushion (surplus) above its reserve amount. If losses exceed reserves, the cushion protects the company and its insureds from insolvency. A healthy surplus serves to provide strength and to maintain fiscal integrity in the face of adverse loss experience that is not actuarially anticipated and is an important barometer of the financial health of an insurance carrier.

Loss Reserves – Loss reserves are the value of assets set aside by a carrier to cover future indemnity payments and expenses for both known and unknown claims.

Ratios – Financial ratios commonly used to assess the financial health of insurance carriers are:

- Ratio of net written premiums to surplus – indicates the carrier's ability to assume additional risk. Regulators suggest a ratio of between 1 to 1 and 3 to 1, all other things being equal. The lower the ratio, the less leveraged the carrier, so look for carriers with lower net premium-to-surplus ratios.
- Ratio of loss reserves (indemnity plus loss adjustment expenses) to surplus – indicates the company's ability to cover unanticipated reserve deficiencies. Again, a lower ratio indicates the carrier is less leveraged, and regulators recommend this ratio not exceed 4 to 1.
- Loss ratio – this ratio represents the total amount of incurred losses (indemnity payments plus loss adjustment expenses) expressed as a percentage of earned premium. In other words, this ratio depicts the percentage of every dollar of premiums collected that is used to defend and pay claims.
- Expense ratio – the total amount of operating expenses expressed as a percentage of earned premium. Lower ratios mean the carrier is not spending too much in expenses.
- Combined ratio – the total amount of incurred losses and operating expenses expressed as a percentage of earned premium. A combined ratio of more than 100% in any given year indicates an unprofitable year and a need for some type of adjustment to reduce the combined ratio and return to profitability.

A little about **Attorney Protective**

Attorney Protective's program

- Underwritten by National Liability & Fire Insurance Company, a Berkshire Hathaway insurance company
- A.M. Best rating of A++ (the highest rating available)

The Attorney Protective program offers access to one of the broadest policy forms available.

- Visit www.attorneyprotective.com to see a list of our program's unique coverage highlights. Remember that coverage provisions often vary significantly from one insurance program to another. It's important to compare the coverage details before making a decision.

Attorney Protective provides our insured law firms with valuable and relevant risk management solutions including:

- Free webinars throughout the year (approved for CLE in most states)
- Exclusive access to our online AttPro Best Practices Database
- Unlimited access to our risk management hotline
- A quarterly risk management newsletter

Attorney Protective provides valuable claims expertise.

A claim can be traumatic. It can be far less traumatic with someone by your side who knows the territory intimately. Our claims team is made up of seasoned claims managers who will be your ally during a claim, and we hire the best defense counsel available to defend you. You can count on us to deliver when it matters most.

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The Attorney Protective program offers legal liability insurance through select agents. Please visit www.attorneyprotective.com/apply and click on your state to request a premium estimate from an appointed broker, or call (877) 728-8776.

Legal Malpractice **Insurance Terms**

Admitted Carrier – A carrier licensed and authorized to write insurance in a particular state using rates, rules and forms that have been approved for use by that state's Department of Insurance. These entities are subject to the highest level of regulatory oversight and scrutiny.

Annual Aggregate Limit – For Claims-made policies, the annual aggregate limit is the maximum amount the carrier will pay for all covered claims first made against the insured during a given policy year. For Claims-made and reported policies, the annual aggregate limit is the maximum amount the carrier will pay for all covered claims first made against the insured and reported to the carrier during a given policy year.

Assessable Policy – A type of insurance policy that allows the carrier to make assessments against insureds over and above the original premium charged to assure sufficient reserves and capital surplus are maintained.

Cancellation – The termination of an insurance policy either by the carrier or the insured prior to the expiration of the current policy term. State law generally sets out the required notice and acceptable reasons for cancellation or non-renewal of legal malpractice policies by the carrier, including: non-payment of premium, mutual consent of the parties, fraud or material misrepresentation, revocation or restriction of the attorneys' licenses, or an increase in the hazard insured against.

Claim – An express, written demand upon an insured for money or services as compensation for civil damages.

Claims-made Policy – A type of policy that offers coverage for a claim arising from a legal service that not only occurred on or after the retroactive date (as set forth in the Declarations Page of the policy), but also was first made against an insured during the policy period.

Credit – A discount applied to the policy premium based on underwriting criteria.

Debit – An increase applied to the policy premium based on underwriting criteria.

Declarations Page – Issued by a carrier along with the insurance policy, this document states basic information about the policy, including: policy period, types of insurance coverage, limits of liability, premiums due and coverage restrictions.

Demand Trigger – A type of Claims-made policy provision that requires a claim actually be made against an insured during the policy period for coverage to apply.

Endorsement – An amendment added to an existing policy modifying its terms.

Event – An accident. Typically, all injuries arising from (1) the same or related acts, errors, or omissions or (2) the continuous or repeated exposure to substantially the same errors is considered one event.

Ex-Date – The anniversary of your current policy.

Exclusion – A policy provision setting forth a specific loss or risk the policy does not cover.

Exhausting/Reducing Limits Policies – Some policies include defense costs within limits. This means that for every dollar spent to defend an insured, the limits of coverage are reduced by a dollar. For example, if a policy contains an exhausting limits provision and has limits of $500,000 and the carrier incurs defense costs in the amount of $400,000, then $100,000 of the limits is left to pay claims.

Extended Reporting Endorsement (Tail Coverage) – Applicable to Claims-made policies, this coverage allows the insured to report claims first made after a policy termination date. However, such claims must result from an event that occurred on or after the retroactive date, but prior to the policy termination date. Some carriers waive the additional premium for this coverage in the event of an insured's death, disability or permanent retirement.

Hammer Clause – A policy provision that reduces the available limit of liability if the insured refuses to provide consent to settle a claim. Under a hammer clause, the carrier is typically released from any exposure beyond the amount the claim could have been settled for had the insured given consent.

Incident – An event the insured knows or reasonably should know is likely to result in a claim.

Incident Trigger – A type of Claims-made policy provision that does not require that a claim actually be made against an insured to trigger coverage, but rather requires only that the insured reasonably anticipate that a claim is likely to result from an otherwise covered incident. Claims-made policies with this provision are often referred to as "incident trigger" policies.

Indemnity – As used in this informational document, indemnity is generally intended to mean the payments made by an insurance carrier on behalf of its insured to cover loss arising from liability claims for which the insured has become responsible and for which the insurance policy issued by the carrier provides coverage.

Limits of Liability – Policy limits set the maximum dollar amount a liability policy will pay on behalf of an insured to cover claims that are made against that insured for liability resulting from negligence and other covered acts (if any). Limits are usually stated as a per occurrence/claim amount and as an annual aggregate amount. The per occurrence/claim amount is the amount the carrier will pay for each covered occurrence/claim arising during one policy period. The aggregate limit represents the total amount the carrier will pay for all occurrences/claims arising during one policy period. For example, if an insured has a policy with limits of $1,000,000/$3,000,000, and the carrier pays a $500,000 claim that arose during the policy period, the carrier will pay only up to $2,500,000 more in claims with respect to the same policy period.

Non-Admitted Carrier – A carrier that is not licensed to do business in the jurisdiction in question but which may otherwise be approved or permitted to do business there. Generally, the rates, rules and forms of such carriers are not approved by the Departments of Insurance, and they are not required to follow the stringent rules and regulations that an admitted carrier is required to follow. Generally, surplus lines carriers are the most common type of non-admitted carriers, although other non-admitted types include Risk Retention Groups (RRGs) and captives.

Non-Renewal – Termination of a policy at the expiration of a policy term by the decision of either the carrier or insured.

Legal Malpractice **Insurance Terms** (cont.)

Prior Acts Coverage – Similar to an extended reporting endorsement or tail coverage, this coverage allows the insured to report claims arising from events that occurred after the retroactive date, but prior to the effective date of the insured's current policy. Prior acts coverage is offered by a law firm's new carrier when coverage is purchased under a new policy. In contrast, tail coverage is provided by the prior carrier and allows the reporting of claims after the expiration of coverage with that carrier.

Retroactive Date – Generally listed on the Declarations Page of a Claims-made policy, this is the date after which an event must occur to be eligible for coverage under the policy.

Risk Management – A systematic approach used to identify, evaluate and reduce or eliminate the possibility of an unfavorable deviation from the expected outcome of legal services. The primary purpose of risk management is to prevent injury to, and the loss of assets of, clients due to negligence or perceived negligence.

Risk Retention Group (RRG) – An RRG is an insurance entity formed under one state's law but, pursuant to federal law, may operate in any state after formal registration in those states. The registration process is simple when compared to the requirements placed on an admitted carrier. Because RRGs operate outside the regulations and oversight applicable to admitted carriers, their rates and forms are not reviewed or approved by the states' Departments of Insurance. Risk Retention Groups are generally owned by their members.

Substandard Risk – A person or entity that fails to meet standard underwriting criteria. In order to secure coverage (often only found in the surplus lines market), these insureds must pay higher premiums and/or be subject to special coverage restrictions.

Surplus Lines – Sometimes referred to as Excess and Surplus (E&S) insurance, surplus lines insurance is coverage secured through a non-admitted surplus lines insurance carrier. Surplus lines carriers are typically not regulated by states' Department of Insurance and do not file rates, rules or forms (other than for informational purposes). The coverage available through a surplus lines carrier is typically limited to those coverages that are not available from an admitted carrier and cannot be accessed merely to secure more favorable pricing.

Tail Coverage – See definition of "Extended Reporting Endorsement."

Underwriting – The process by which the carrier evaluates policyholder risk, including the application of applicable credits and debits, and determines if non-renewal is warranted in cases where the risk no longer meets acceptable underwriting guidelines.

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