

# PI MARKET FOR PROFESSIONALS

**Renewal terms for professionals will be driven by four factors in 2009: general insurance market conditions, the Professional Indemnity market dynamics, the profession involved and the individual firm's underwriting profile. The first factor can be a powerful driver for change and is capable of producing the most dramatic changes from year to year. So it is important to understand this element, which will help to set expectations and determine renewal strategy.**

A mixture of anecdotal evidence and publically announced information gives us an impression of the current market conditions and prospects for 2009 and 2010. Despite general expectations of rate increases at the beginning of 2009, conditions in most insurance classes, including PI, currently remain stable.

There have been increases in certain areas – property catastrophe, FI and some D&O classes. Generally, however, underwriters have been moderating their views about the timing of rate increases. Globally, the market hardening that was anticipated has failed to materialise. For example, in March in the US P&C rates declined 8% over the prior year.

Why is this happening, contrary to most predictions?

There are a number of factors contributing to this:

- **Reinsurance:** Some commentators predicted that reinsurance would drive increases. In fact, reinsurance prices for PI seem to have been flat or perhaps moved up 1% or 2%. Insurers' lower reliance on reinsurance than in the past means that, unlike other insurance classes, reinsurance will not be the prime driver.

- **Insurers' results:** Typical results came from Allianz reporting a 0.8% overall rate increase in Q1 2009 with a combined ratio of 98.5%. This latter figure would certainly be below an ideal industry target but is not a market turning result.

- **AIG** continues to dampen pressure for premium increases with aggressive pricing but they have lost some market share.

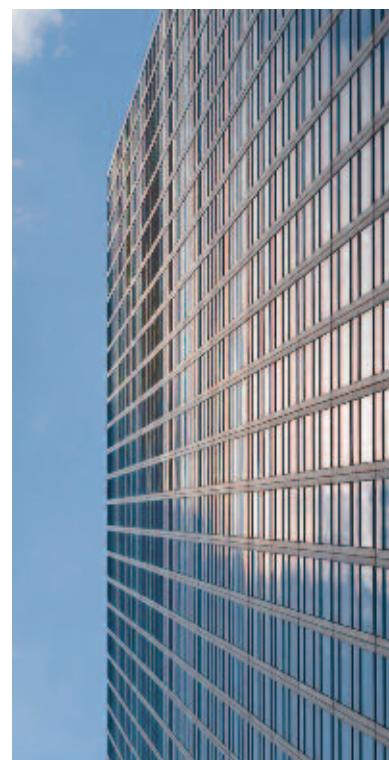
Capital and capacity therefore remain intact. In fact, damage to insurers' balance sheets has come predominantly from the investment side. Looking forward, there are some pointers towards change:

- New capital has flowed into Lloyd's, signifying a perceived improvement in trading conditions.
- Larger reinsurers, e.g. Munich Re, announced reduced commitments to recession prone classes.
- In the results season insurers and reinsurers predicted more favourable trading conditions, expecting more rate increases in more classes.

We anticipate that industry financial performance pressures will continue to put upward pressure on rates.

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# EXPECTATIONS

## FOR SOLICITORS

For this year, the general view is that if there is no change in exposure the premium will be flat.

In our discussions with excess insurers that will provide capacity for this year's renewals, one insurer expressed the view that excess layers were 30–40% under-priced. Such judgements are difficult to substantiate due to the benign claims environment. The view is based on the size of total premium income relative to limits purchased. The competitive pricing of excess layers is thus due essentially to insurers not having to pay claims at these levels. There have been high profile cases, such as the Football League's £142 million claim against Hammonds and Levicom's £44 million claim against Linklaters, but actual exposure to insurers has not materialised.

For this year, the general view is that if there is no change in exposure the premium will be flat. Some insurers reaffirmed our view that reinsurance will not be a crucial driver. Regarding premiums for 2009, flat rates could mean that insurers would look for premium increases to

reflect firms' revenue growth. The supply and demand dynamic and the amount of capacity being sought will influence overall programme pricing.

We believe our advice to pursue early renewals in 2009 has proven to be sound and firms that employed that strategy are likely to be satisfied with the terms obtained thus far. We expect pressure from excess markets to increase prices but anticipate that firms with good loss records and professional presentations will be able to obtain flat premium renewals.

For 2010 the situation is unclear. There is a chance that property and credit related claims will be made and mature in the next 12 months adding to general industry pressures and creating more challenging conditions than this year. We are monitoring those pressures and will report in future newsletters.

## FOR ACCOUNTANTS

The professional indemnity market for most non-Big 4 Accountants is benign, with rates remaining low and coverage wide. In particular, small and medium sized firms that do not work in areas perceived to be high risk, such as insolvency, are enjoying very competitive premiums and low excesses.

The most significant premium and rate adjustments that followed the last hard market have in the main already been made and large scale reductions are unlikely. Many Insurers would like to see rates rise in this sector as they anticipate increasing claims cost as a result of the recession, but insurers are finding any increase difficult to achieve owing to ample capacity.

There is strong competition, as anticipated claims deterioration for accountants has not materialised, and many insurers are seeking to refocus their portfolio away from more contentious areas such as Surveyors and IFA's. In the longer term it may be prudent to plan for rate and premium increases. Insurers are experiencing an increase in the number of accountants' notifications by approximately 20% when compared to the same period as last year.

Many suspect that the expected recessionary type claims may simply be delayed as firms react first to business management issues before trying to pursue advisors to recover losses.

Within the next 12–18 months it is likely that audit work for a firm that has subsequently gone into liquidation or been found to be fraudulent will come under scrutiny and claims may result. Similarly, areas such as tax advice may come under pressure as the government gives renewed focus to tax analysis and collection. If these types of recessionary claims develop, firms should be prepared for increased premiums and higher excesses for high risk activities.

Insurers are yet to feel the impact of Madoff and Stanford but they are increasingly requesting that supplementary questionnaires relating to Institutional Fund Management and Private Client Portfolio Management be completed as part of the renewal process. There are some exclusions appearing relating to Madoff and Stanford.

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## FOR SURVEYORS

**There is unlikely to be any improvement in insurer sentiment if there is further deterioration in claims for this sector, as expected by the insurance market.**

Recent rate increases in the Surveyors' sector have been caused by claims experience that has been deteriorating markedly since 2007. This position has worsened dramatically in the last 12 months with insurers noting an increase both in the number of notifications and also the average value of loss. As a result, Professional Indemnity insurers are reviewing their involvement in this class.

Two insurers have withdrawn from the Surveyors market in the last 12 months. And those that remain have particular concerns relating to survey and valuation activities. Only 3-4 insurers currently remain active in underwriting firms that specialise in this area.

Some insurers are maintaining a holding pattern by only renewing existing business and not writing any new business. Insurers who continue to underwrite in this area are reducing the amount of policy limit they are willing to commit and increasing excesses for work considered to be high risk.

At this stage, there is no evidence that the recent increases in rates are sufficient to attract new insurers or for existing insurers to increase their involvement.

There is unlikely to be any improvement in insurer sentiment if there is further deterioration in claims for this sector, as expected by the insurance market. There remains the possibility that some insurers will review their involvement in this class and consider scaling back their involvement even further. This lack of competition in this sector makes further rating increases seem inevitable and it is likely that some firms may find themselves unable to secure RICS compliant insurance.

Firms that are exposed to survey and valuation work or those with a poor claims record should be prepared for a difficult renewal season in 2009 and 2010 with the prospect of the further hardening in rates and increases to excesses. For practices with very limited exposure to survey and valuation work, competition between Insurers remains strong and rates competitive.

## RISK ISSUES

Looking beyond market conditions for professionals, what issues are on the minds of corporate buyers of insurance? Airmic (Association of Insurance and Risk Managers) chief executive John Hurrell was recently interviewed by 'Reinsurance' magazine.

He expressed the views of his members in a number of areas. The main concern was the market changes and how dramatic pricing, capacity and coverage changes might be. He pointed out that most members were less able to assimilate price increases and were equally concerned about capacity and cover restrictions.

Insurer ratings and the lack of information were cited as frustrations. Their members are looking for more from their broker and would like to see the rating agencies play a bigger role.

Buyers will be obliged to consider more self insurance options. Captive plans will be dusted down. Airmic has a major project for 2009 on risk appetite and will be looking at best practice for risk retention decisions and how an organisation's risk appetite informs its risk management policy. Those with captives will be looking at Solvency II trying to understand its ramifications.



# OUR SEMINARS

We will be hosting seminars covering current insurance, risk and risk management issues.

Our most recent seminar on July 2 looked at technology risks. A leading IT risk management consultant and other speakers explained the risk perspective of insurers and the cover available. The seminar provided an understanding of the risks associated with IT systems, the risk management framework and available insurance solutions.

Later this year we will hold a seminar on captives, addressing questions such as how to evaluate their value to you, capital requirements, set up, ongoing cost and logistical issues. We will tackle topical issues relating to those subjects.

# MARKET UPDATES

This is the first of our quarterly newsletters. We will address issues of current interest related to the professional indemnity insurance markets, the risk landscape and related insurance programme issues for professional service firms. If there are any items you would like us to cover please let us know and we will try to include an article.

## MEET THE TEAM



### Terry Caden

Terry has 30 years insurance experience principally advising on risk financing and design of Professional Indemnity programmes for international professional firms. Prior to joining Willis, Terry worked for Minet and its successor Aon, dealing with the Professional Indemnity programme for the Big 4 accounting firm. Terry subsequently joined Marsh and dealt with a variety of professional firms including law firms, management and property consulting firms. Terry has conducted Strategic Risk reviews for a variety of professional firms in the U.K. and U.S.

### Qualifications

Fellow of Chartered Insurance Institute, and MBA from the Cass Business School in London.

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