Welcome to this, the first edition of The Willis Index for solicitors. The Index will be a regular barometer of market conditions which, by way of regular surveys, will identify trends in pricing and scope of coverage in relation to Solicitors Professional Indemnity Insurance. It will also provide comment and issues relating to risk exposure and risk containment.

The Willis Group is a global business extending through 300 offices and employing 14,500 people in over 100 countries. Our diverse array of clients, located in 180 countries, comprise 30% of the UK FTSE and over 10% of Fortune 1000 companies.

In the United Kingdom and Republic of Ireland we have extensive regional presence though Willis branch offices and a network of independent brokers.

As part of group strategy, Professional Indemnity Insurance has been identified as an area of specific development and Willis Professional Risks has been the fastest growing business in this sector. Our team has doubled in size in the last 18 months and we are embarking on an expansion plan which will put Willis Professional Risks on the map in your locality.

For solicitors, we are focusing our skills and resources in developing new markets and new products and we will keep you updated on the launch of these in the coming weeks. Our focus is on you and to satisfy and to provide cost effective and innovative solutions to meet your requirements and to provide the highest standards of service.

Our belief is that many firms continue to subsidise the losses of poorer performing practices and Willis will demonstrate how this situation can be overcome by announcing a new facility for the 1 October 2005 renewal date.

This new facility will apply to firms with 2 to 14 partners and a good claims experience.

For larger firms, whether international, national, city based or regional. Willis continue to provide bespoke services backed by proven success in this sector. We therefore urge you, when considering your professional indemnity renewal not to make a decision without talking to us first.

If you would like more information on our services please contact:

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Market Conditions

The Insurance Market Peaks – so what’s in it for solicitors?

Profits for 2004 of £1.36 billion have been announced by the Lloyd’s insurance market despite a £1.2 billion bill for storm damage in the United States and the worst ever year for the insurance industry for losses from natural catastrophes. However, many observers will be surprised at the fact that underwriting profit for the Lloyd’s marketplace was a modest £340 million and that the balance of profit was derived from investment income.

Lloyd’s has reduced capacity for the second successive year for 2005 in an attempt to ensure that it continues to write only profitable business, rather than chasing volume. However there is no doubt that new capacity in the market has caused premium reductions although many market observers believe that the Lloyd’s franchise department seems to be turning a blind eye to this reality. The 2005 reinsurance season has been a determining factor in market capacity and although reinsurers and the actuaries of Professional Indemnity (PI) insurers are demanding stable rates for renewal business, there is a much more relaxed approach to rating for new business. As the PI market is finite, in that there are a limited number of clients, this approach is illogical in that the incumbent insurer has to uphold pricing for a renewal whereas a competing insurer can undercut on pricing. In reality, this results in an overall spiralling down of premium cost based on change of insurer. It is not an environment which sends strong messages to clients to retain continuity of insurer.

Of the respondents to the Legal Risk survey 13.5% of solicitor firms changed primary insurer at 1 October 2004. Willis predict that this is likely to increase at the 2005 renewal.

There are currently 62 syndicates writing insurance at Lloyd’s. Of these, only seven are listed as Qualifying Insurers of The Law Society of England & Wales primary Solicitors Indemnity Rules 2004. Of the remaining 16 Qualifying Insurers, 14 are actively underwriting.
Those who are sitting on the fence will be urged to either become actively involved or to withdraw.

The total premium contribution under these arrangements with effect from 1 October 2004 was £242.7 million. This figure is not dissimilar to the contribution to the Solicitors Indemnity fund in its final year (1999/2000). With growth in revenue of the profession and inflation, it can therefore be argued that the Qualifying Insurer scheme is providing a cost effective solution for the transfer of risk out of the solicitors profession.

However, with over 75% of the current premium income in the hands of six insurers, there is a real concern that the withdrawal of one or two of these insurers could create a capacity crisis.

Claims statistics on the solicitors primary scheme, and for excess layers, are closely guarded by each insurer and fully developed loss records are only now becoming available to each of them due to the ‘long tail’ nature of claims in this class. The reality of the situation is that certain insurers will have made satisfactory profits, whereas others would have experienced losses on their solicitors account.

For other classes of professional practitioner there is freedom of choice of renewal date. This means a constant evolvement of the market occurs which can be monitored throughout the year. For solicitors, a single renewal date means that commentary between one renewal season and the next is based largely on speculation until such time as the renewal season is in full flow.

Currently, insurers and their actuaries will be assessing their claims experience and, in the coming weeks, setting their guide rates in readiness for the renewal season. This will be followed by a spate of ‘early renewal’ offers which tend to benefit insurers more than insureds. It is estimated that around 30% of firms do not finalise their cover arrangements until the final week of the renewal season and there is strong evidence to support that insurers reduce premium rates in the closing days of the season. This model does not apply to ‘major league’ firms where purchase of high excess layer levels requires more time to put the renewal programme in place.

Speculation has already started as to the rating trends for the October 2005 renewal. Certain insurers and brokers are ‘talking rates up’ and suggesting that these could increase by as much as 30%.

There are two key factors upon which this speculation is based:

1. The increase in the minimum indemnity limit.
2. The impact of claims on the profession and its insurers including TAG litigation.

Zurich Professional, who have the largest proportion of premium income with a 24% market share, are on record of having stated that they are looking for a minimum rating increase of 15% across the profession, irrespective of whether firms are exposed to TAG litigation or not.

Certain brokers have stated that they anticipate rating increases of up to 30% this year with smaller firms, which tend to buy minimum cover, likely to be the most adversely affected.

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There is little doubt that the new capacity in professional indemnity sectors such as the financial lines market has resulted in premium reductions and a broadening of coverage, even though established markets are trying to resist this reality. There are few indications that the solicitors mandatory minimum policy terms will be further extended but there are discussions currently taking place between insurers and the Law Society on the issue of aggregation of the policy excess and indemnity limit (see following article).

It has become common knowledge that the level of compliant cover for partnerships and sole practitioners is increasing from £1 million to £2 million at this year’s renewal. However, it is not yet widely appreciated that minimum coverage for Limited Liability Partnerships will be increased from £1.5 million (of which the first £1 million must be compliant cover) to £3 million on a complaint basis. Again, this should not be cause for alarm as most practices operating as LLP’s will already be buying more than £3 million of cover.

Professional Indemnity remains the third largest overhead for most solicitor firms with the cost ranging between 2% to 5% of turnover.

The perceived benefit of the transfer of cover from the Solicitors Indemnity Fund to the commercial market in 2000 was expected to deliver wider choice. However, for those firms at each end of the spectrum i.e. the top 20 and sole practitioners, the availability of choice of insurers has been limited. 2005 could be the year when new entrants make their presence felt resulting in more choice for all firms and reducing cost despite the increase in mandatory limits and insurers concerns about TAG litigation.

There is speculation that more firms will find themselves at risk of falling into the Assigned Risks Pool but previous concerns regarding the numbers of firms in such a predicament have proved to be unfounded.

Fig. 2. Professional Indemnity premiums cost as a percentage of annual fee income

*Source: Financial management in law firms 2004 – PricewaterhouseCoopers LLP*

The Willis View
Willis are not aware of any major firms that were unable to secure the level of cover that they wanted at 1 October 2004. Other classes of professional risk have shown a willingness to increase indemnity limits in 2005 as changing market conditions have made it more favourable for them to do so. Policy excess levels have also remained stable over recent months.

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The current minimum indemnity limit for firms which are unincorporated – £1 million any one claim – was set over 15 years ago and is beginning to look rather stale. Index-linked, that would be £1.7 million now. Our neighbours in Scotland and Northern Ireland require minimum cover of £2 million and £1.25 million respectively.

Even those statistics are not the end of the story, however, because claims are not index linked. Lawyers who say ‘we only do small claims’ or ‘we only convey low value properties’ are missing the point – the big claims often come from the cases which lawyers failed to recognise as big cases.

Examples are legion, but two handled by the writer suffice to illustrate the point: a £3 million claim from a £25,000 land purchase (environmental issues not picked up) and a multi-million pound claim from a £2,000 personal injury settlement (post-traumatic stress disorder not spotted).

So a new limit of £2 million cover seems eminently reasonable. But like all good things in life, it comes at a cost, and the hidden costs may be more than at first appears.

First, the premium: Insurers are talking of rises of about 15% to cover the cost. For those with £2 million cover or more at present, that of course will be academic as they are already paying for it.

Secondly, the hidden cost: the change to the so-called ‘aggregation clause’. An insurer takes on almost unlimited exposure when it insures a law firm under the Law Society’s Minimum Terms and Conditions, because at present it insures the firm for £1 million (plus defence costs) ‘any one claim’. So, as often as you have a claim, you have £1 million cover. Not so under the new rules. The price to be paid for the increase in cover – in addition to the increase in premium – is a tightening up of the definition of ‘any one claim’.

The reason for most of the changes is a decision of the House of Lords in Lloyds TSB General Insurance Holdings Ltd and others v The Lloyds Banks Group Insurance Co [2003] UK HL 48. That was a case arising from pension misselling – the question was whether they should all be added together, or aggregated, and treated as one claim with one excess. They were small claims and it suited the insured if they were aggregated, but the House of Lords held that they were separate claims.

The new definition means that many more claims may be added together in calculating the new £2 million indemnity limit. Briefly, this new definition provides that claims will be added together if they arise from one act or omission, one series of related acts or omissions, the same act or omission in a series of related matters or transactions, or similar acts or omissions in a series of related matters or transactions. The final twist of the knife comes with the provision that all claims against one or more insured arising from one matter or transaction will be regarded as one claim – not a point which arose in the Lloyds TSB case.

It is not hard to see how this may cause real hardship. One in 13 firms currently faces claims by the insurers of The Accident Group. Many of those have no aggregate limit on the number of excesses and would clearly benefit under the new rule if insurers apply it to the excess calculation as well as the overall limit of indemnity.

But the issue extends to the limit of indemnity too, so imagine if you had a defective rent review clause in your firm’s precedent. You used it for several clients, possibly resulting in several claims – insurers would doubtless argue all
should be added together with one indemnity limit. Not a problem, you may think, if you only do small property matters, but think about the consequences if you had even a dozen claims for £250,000. Add the claimants’ costs to them and it is easy to see how you could go way over the indemnity limit.

Nor is it only a problem for the small firm. Top up insurers are likely to follow suit, and even the large firms with £100 million cover or more may face similar difficulties.

There has always been an aggregation clause, but it rarely had much effect in practice. Even worse, the additional provision which had nothing to do with the Lloyds TSB case may impact quite often. This is the provision that all claims against one or more insured arising from one matter or transaction will be regarded as one claim.

The real problem emerges, however, when you look at the main changes, which could mean several different clients’ claims being added together with one limit of indemnity – although you can limit your liability to individual clients contractually, what you can’t do is limit liability across your entire client base. You can’t tell an individual client that there is only, say £2 million, to spread between him and all your other clients if things go wrong.

So firms need to consider carefully what else they are doing to protect themselves. Opportunities are there – a good, properly thought through set of contract terms, perhaps limited liability partnership, and, above all, a properly structured risk management system.

Risk management is not simply an annual visit by one partner to a seminar on the subject, it needs a strategy to implement a process right through the practice, with buy-in from everyone – partners, fee earners and support staff. The writer dealt with a £3 million claim from a letter in the wrong envelope, so include your post-room staff too!

The Willis Group recently announced that it has strengthened its expertise in the field of solicitor’s professional indemnity with the appointment of Trevor Moss.

Trevor joins Willis after seven years with Alexander Forbes where he was in charge of the Solicitors/International Professional Indemnity Division.

Speaking about his decision to join Willis, Trevor said “I decided for career reasons to seek a new challenge. Willis is a fantastic brand in the global insurance broking arena and was looking to develop its Professional Risks division throughout the United Kingdom. This provides a real opportunity to deliver creative thinking and develop this important market sector, Willis Professional Risks are a great team of people with a strong reputation for delivery”. He joins as an Executive Director in London.

Roland Avery, Managing Director of Willis Professional Risks says “We welcome Trevor on board, his experience and management skills make an ideal match for our ambitions to increase our market share and deliver great service to all our clients. His knowledge, particularly in relation to solicitors’ professional indemnity insurance, will see us developing further in this sector.”

Richard Bucknall, Group Chief Operating Officer of Willis says: “Trevor’s appointment is part of a continuing process of recruiting and retaining the best people in the insurance market to deliver quality to our clients and we welcome him as part of a rapidly developing team.”

Next issue: meet the team.
The regulatory shake-up and its impact on risk management

Lord Falconer’s general endorsement of the Clementi recommendations, gives the Government the impetus to implement reforms designed, they say, to make the UK legal system the most liberal in the world. There is however a certain irony that the proposals will also make the UK legal profession one of the most regulated.

What is the likely reaction of the insurance market to these changes and how will they impact on scope, cost and availability of professional indemnity insurance for solicitors? This article raises as many questions as it proposes solutions. However, it does indicate the potential enormity of the topic and its possible impact upon the profession.

Reactions to the white paper will depend as much on “when” changes will take effect, in relation to the insurance cycle, as to “how” the insurance market perceives the impact of the changes on the risk profile of the profession. In other words, timing is as critical as substance in terms of insurers’ appetite to continue insuring the professional risk exposures of lawyers.

Interestingly, there is some precedent in that one Australian Law Society saw the proposed withdrawal of its pivotal role of regulating members and negotiating with insurers as a major detriment to both the profession and consumers.

It is also evident to insurers that the recommendations of the Clementi review create a markedly different landscape and will require new entrants to the profession and existing practitioners to gain additional knowledge in terms of their education and training.

Key aspects of Clementi’s recommendations which will impact on insurers views are:

**Regulation** – The extent to which a single overseeing regulator, the Legal Services Board, will allow the provision of legal services beyond the existing ‘closed shop’of practitioners and to what extent there will need to be commonality of insurance arrangements.

**Complaints** – The establishment of the Office of Legal Complaints will bring with it enhanced powers to make awards without undue reference to professional negligence and without financial limit. Complaints and formal claims against solicitors and their insurers are currently running at high levels, will insurers be prepared to insure additional losses in the guise of awards?

Clementi is adamant that the complaints issue must be tackled and states that “research shows that complaints arise as much from poor business service as from poor legal advice. If certain lawyers continue to reject the notion that they are in business, such complaints will continue until they are indeed out of business”. The demise of a firm is as likely to result from insurers’ declinature to offer professional indemnity insurance coverage as it is from clients’ complaints to the regulators.
The Regulatory Shake-up continued

Risk Management – Clementi envisions equal emphasis to be placed on practice management and systems of legal business as on the status and knowledge of each practitioner. Firms will also need to increase their complaints procedures significantly and risk management will take on a higher profile as the proposals require complaints procedures to comply with clear standards prescribed by the regulator. Demonstrating compliance will be easier for those firms with Lexcel or other externally assessed quality standards as these will be taken as evidence of compliance.

We anticipate a process for competency and risk reduction taking the form of that outlined in figure 3. In the event that this model becomes a common standard, insurers may well be encouraged by the prospect of reducing claims frequency and, as a result, feel more able to reduce premiums.

Alternative Business Structures – The advent of the Legal Disciplinary Practice (LDP) will create certain challenges for the insurance market, not least in terms of assessing risk and premiums and finding a suitable policy wording to cover the multifarious activities of such entities. Nevertheless, these challenges pale into insignificance compared to the considerations that will need to be addressed should lawyers eventually be allowed to practice as part of Multi-Disciplinary Practices (MDP’s).

Insurers will also be alive to the fact that external investment into law firms could increase exposure to claims from conflict of interest issues.

In conclusion, there are a number of challenges that will need to be addressed to enable insurers to feel comfortable insuring a newly structured legal profession but as these changes are intended to drive out poor performance from the profession the overall view should be a positive one.

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LLPs – A Risky Business?

The insurance market and certain of its solicitor clients have identified two areas of professional risk associated with LLPs which are not covered by the current Professional Indemnity coverages, these are:

- Management Liability covering risks similar to those faced by directors of limited companies.
- Personal Assets Cover, to protect an LLP member responsible for committing a Professional Liability action, where his or her personal assets are at risk and where the LLP’s PII cover and assets are exhausted.

However, with little legal precedent available to establish the extent of exposure and untested policy wordings, are these policies worth the paper they are written on? For opinion on these issues refer to the next edition of the Willis Index for Solicitors.

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Breaking News

Willis has been named the “2005 European Commercial Broker of the Year” as voted by more than 3,000 risk and/or insurance managers or directors of multinational companies across 12 European countries (Belgium, Denmark, France, Germany, Italy, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland and the UK.)