

# Professional liability

Association of Lloyd's Brokers

November 5 2007

# AGENDA

*Greetings and introductions*      Brian Murphy, ALB Vice-Chairman

*Lloyd's update*      Maryanne Swaim, Lloyd's Illinois

*Professional Liability—E&O*      David Sampson, FirstCity

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**BREAK—refreshments will be served in the GAR Rotunda**

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*Insuring Cyber Risks*      Michael Born, Media/Professional Insurance

*Anatomy of a D&O Claim*      Andrea Lieberman, Marsh USA

*Questions and answers*

FirstCity

# Professional Liability—Errors & Omissions

David Sampson

Partner

The FirstCity Partnership Limited, London

# Let's start with insurance humour

- **THIS JUST IN:**
  - The smoke detector industry and the insurance industry are covering up research showing more people are injured every year falling from ladders and stepstools while trying to replace smoke detector batteries than are injured in house fires.
- **Arguing with the Insurance Adjuster**
  - Arguing with an insurance adjuster is like wrestling a pig in the mud.....After a while, you realize he likes it.
- **The Size of the Print**
- **Bold print giveth and the fine print taketh away!**

# What is Errors & Omissions insurance?

Errors and omissions insurance is coverage that protects those people that give advice, make educated recommendations, design solutions or represent the needs of others. The original name, Errors and Omissions came from "doing something they shouldn't have done (an error) or not doing something they should have done (an omission)".

## Are there are other names for E&O Insurance?

E&O insurance is also known as professional liability, malpractice or professional indemnity insurance.

# What is the difference between E&O coverage and General Liability coverage?

- General Liability is intended to cover physical injury to people or physical damage to things (your product causes physical injury to the user of your product or your client trips over your foot and breaks their leg—the old slip and fall).
- E&O is intended to protect you, the consultant or designer, in the event your client alleges that something you did on their behalf was done incorrectly, which resulted in some kind of financial loss or business interruption to your client. Service contracts between the parties can help to limit your real liability, but the big expense in this kind of claim is the legal defense to prove your true liability or innocence. E&O policies are designed cover many of these defense costs and ultimately the final settlement if you do not prevail.

# Who needs E&O?

Today, many business trades and professions require the coverage. Teachers, consultants, software developers, web page designers, placement services, ISP's, telecommunications carriers, inspectors, realtors, insurance brokers, lawyers, doctors and just about everyone else.

## How do I know if I need E&O coverage?

If your client could suffer financial damages as a result of you or your company's failure or error in the provision of services, your company could be the target of an E&O claim. You can protect your company from the potentially devastating financial damages associated with this type of claim by securing E&O insurance coverage.

# How much does E&O cost?

- **How much does E&O cost?**
  - Many factors are considered in determining the cost, or premium, for an E&O policy. Applications are evaluated on their individual merits as well as their industry segment. Size, length of time in business, claims history, location, number of employees, and risk management procedures are all factors in determining the premium. These factors are then evaluated within the context of the industry segment. For example, web hosters generally have greater exposures than title agents and in today's environment Mortgage Brokers appear to have even more potential exposure. (I believe the mortgage broker is now up with the lawyers and doctors when it comes to increased exposures and of course the increased exposure is reflected in the premium and the deductible usually).
- **What types of companies use E&O insurance?**
  - In today's litigious environment, probably all service providers need E&O insurance. It would be impossible to list all service providers who are exposed to E&O risk.

# E&O coverages explained

- **Professional Liability Insurance (Errors and Omissions Insurance)** is your most critical coverage. Professional liability coverage protects you against loss from a claim of alleged negligent acts, errors or omissions in the performance of your professional services. This might include loss of client data, software or system failure, claims of non-performance, or negligent oversell. Be sure your professional liability policy includes the following key features:
  - **Coverage includes legal defense cost.** Professional liability insurance will pay for any resulting judgments against you including court costs up to the coverage limits on your policy.
  - **Coverage extends to both W2 employees and 1099 subcontractors.** Coverage should protect your company from claims resulting from the work done by 1099 subcontractors on your behalf. (It is important to note that 1099 personnel need their own errors and omissions insurance because your policy does not defend them if they are sued separately or in addition to you.)
  - **Optional coverage for allegations of Copyright Infringement and Intellectual Property Infringement.** Intellectual Property Infringement coverage protects you against claims alleging copyright infringement. Software, systems or processes are some of the most commonly known "intellectual properties."
  - **Personal Injury.** Personal injury protects you against claims of libel, slander, and invasion of privacy.
  - **Worldwide coverage if the suit is brought in the USA.**
- **Professional liability coverage may be described in your contract in this way** "Contractor will maintain at its expense: Professional Liability Insurance in the amount of \$1,000,000 including coverage for errors and omissions caused by Contractor's negligence in the performance of its duties under this agreement

# Claims scenarios covered by Professional Liability insurance

- A software design error causes an MRI machine to be rendered inoperable, allegedly causing loss of profit to the hospital.
- A client contracts with a software consultant to develop a software system. The contract contains specific benchmarks for speed and other requirements. These benchmarks are not reached, allegedly as a result of the negligence of the consultant. The consultant is sued in negligence, breach of contract, and negligent misrepresentation for loss of profit.
- While transferring data from a legacy to web based system, a database is compromised, resulting in the loss of valuable corporate sales information.
- A software developer is sued when, during the execution of a contract to build an Internet application for a company, the developer is allegedly negligent in the staffing of the project, which resulted in an alleged breach of contract.
- Real Estate Broker - a prospective purchaser sued a real estate broker when the transaction failed due to close at the last minute due to difficulties associated with their purchase financing. The purchaser ended up losing the non-refundable deposit for failure to close. The key allegations against the broker were for misrepresentation of the availability of deposit funds prior to the money going into escrow.

# Claims scenarios covered by Professional Liability insurance

- An attorney represented a client in a divorce action, and was subsequently sued by his client. In her suit, she charged the attorney with numerous errors, including failure to appraise the husband's business and failure to discover the existence of a business-related line of credit on the marital home. The case settled for \$500,000.
- A homeowners association put a lien on the property of a resident because she refused to pay the association dues. When she ignored the lien, the homeowners association foreclosed on her home. An attorney, the insured in this case, provided legal advice to the homeowners association and assisted with the foreclosure action. The resident sued both the homeowners association and the attorney alleging improper notice and seeking punitive and other damages. She also alleged that the attorney conspired with the homeowners association and the other entities involved to deprive her of her property, causing emotional distress. The insured attorney is now a defendant to an action by a adversary of his client.

# Lawyers' Professional Liability

- This is not a presentation that is aimed at lawyers but.....
- No matter what the nature of a law firm's practice, today's law firms are increasingly the target of client claims and lawsuits. This can be the result of unreasonable client expectations, frivolous claims or real errors. As a consequence we the brokers can only recommend that ALL law firms need to buy professional liability insurance with suitable coverages and appropriate limits to protect them from client claims, and most globally now do.
- The insurance market for lawyers professional liability insurance is now extremely competitive, here in the US or Bermuda and also within Lloyds of London.
- Lawyers in my opinion have very different and varied exposures (so they deserve their own section in this presentation).

# Common areas of legal malpractice

- Failure to: For example failure to:
  - Comply with applicable time limitations
  - Investigate | evaluate
  - Prosecute
  - Conduct and/or respond to discovery
  - Adequately prepare and conduct a trial
  - Adequately and thoroughly research the law
  - Appear
  - Unintentional or improper waiver of defenses
  - Erroneous settlement advice
  - Appellate errors
  - Improper handling of client funds
  - Conflicts of interest
  - Failure to effect service of process
  - Errors associated with court orders

And more!!!!

# Your broker can offer E&O quotes for all of these and more

*Professional Liability (Errors and Omissions or E&O) for*

- Financial services including – Investment Advisors, Mutual Funds/Partnerships, Investment Brokers/Dealers, Private Equity and Hedge Funds, Insurance Companies, Insurance Agents/Brokers, Mortgage Bankers/Brokers, Accountants, Actuaries, Financial Consultants, and many related type operations.
- Real Estate-Related including – Real Estate Agents, Real Estate Appraisers, Title Agents, Escrow Agents and other related type operations.
- Medical Related/Medical Malpractice/Managed Care including – Physicians, Healthcare, Managed Care/HMOs/Medical Services and other related type operations.
- Architects and Engineers
- Attorneys
- Media Related including – Advertising Agencies, Authors, PR firms, Multimedia, Printers, Publishers and other related type media operations.
- Consultants, Insurance Brokers / Agents etc, etc.... (any professional service provider)

# E&O Insurance—a good investment or wasted profits?

- The current insurance market is very competitive so the wasted profits would be what I consider a “minimal cost to do business / operate” (spoken like a true broker).
- No matter how carefully and professionally you conduct your business, suits / legal threats against you and your company can come from many unexpected sources. An E&O claim brings with it the potential of heavy costs for the company (and often you the owner personally), both in terms of money and valuable time lost which can lead to lost business in the future. Also, as you all know settlements or awards at trial are generally more severe here in the US and at the end of the day legal defense costs alone can soon mount up.
- And lastly lets not forget the other important related coverages including Crime / Fidelity, EPLI and D&O and often these products can be purchased as a package for your entire operation.

# Insurance humour to finish

- Three guys are deep sea-fishing in the Caribbean. One guy says, "I had a terrible fire; lost everything. Now the insurance company is paying for everything and that's why I'm here in the Bahamas."
- The second guy says, "I had a terrible explosion; lost everything. Now the insurance company is paying for everything and that's why I am also here in the Bahamas."
- The third guy says, "What a coincidence. I had a terrible flood; lost everything. Now the insurance company is paying for everything and that's why I'm here in the Bahamas also."
- The other guys turned to him scratching their heads and looking confused and asked, "Flood? How do you start a flood?"

# The End

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# Insuring Cyber Risks

Michael Born  
Vice President—Claims  
Media/Professional Insurance

ERRORS & OMISSIONS LIABILITY  
MEDIA MISCELLANEOUS TECHNOLOGY CYBER



Media/Professional Insurance



## Introduction

- What are the risks of doing business in the cyber technology age?
  - Professional liability goes digital
- What are the insurance options to protect against these risks?



ERRORS & OMISSIONS LIABILITY MEDIA MISCELLANEOUS TECHNOLOGY CYBER



# What are the risks of doing business in the cyber technology age?

- **Loss or corruption of data**
  - Your own or others—virus that infects or passes through your system
  - Intentional (rogue employee, hacker) or accidental
  
- **Theft of data (identity theft)**
  - Theft of funds through the use of that data
  - Privacy damages and issues
  - Notification requirements
  
- **Copyright, trademark, defamation**
  - Content of website, blogs, online publications
  - Metatags



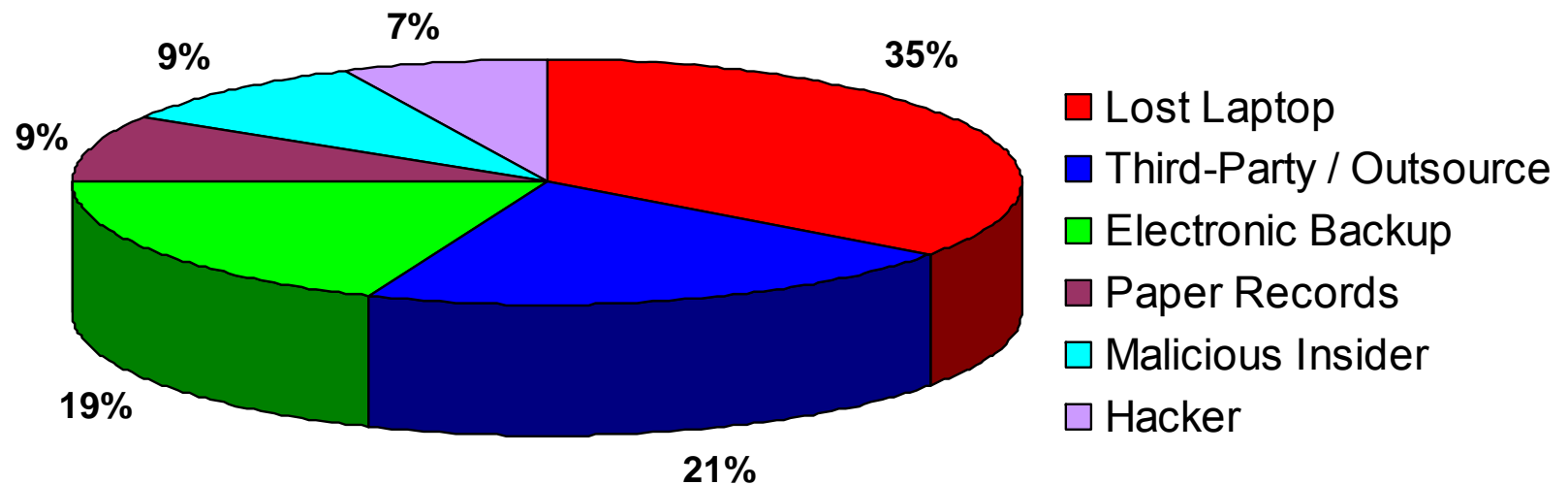
## The cost of cyber mistakes

### Some real world claims examples

- **Competitor's name used in internet search metatag**
  - Court ruled that this was not a trademark violation—but other causes of action remained. Cost to defend: \$5,000,000.
- **Widget Hosting vs. Widget Media**
  - Trademark claim that internet URL (web address) was confusingly similar. Over \$400,000 in damages and legal fees.
- **Blogs**
  - String of defamation lawsuits filed against posters on blogs. The company's own content does enjoy certain First Amendment protections, but can still be the basis for defamation, copyright, unfair competition and privacy claims that are, if nothing else, expensive to defend.

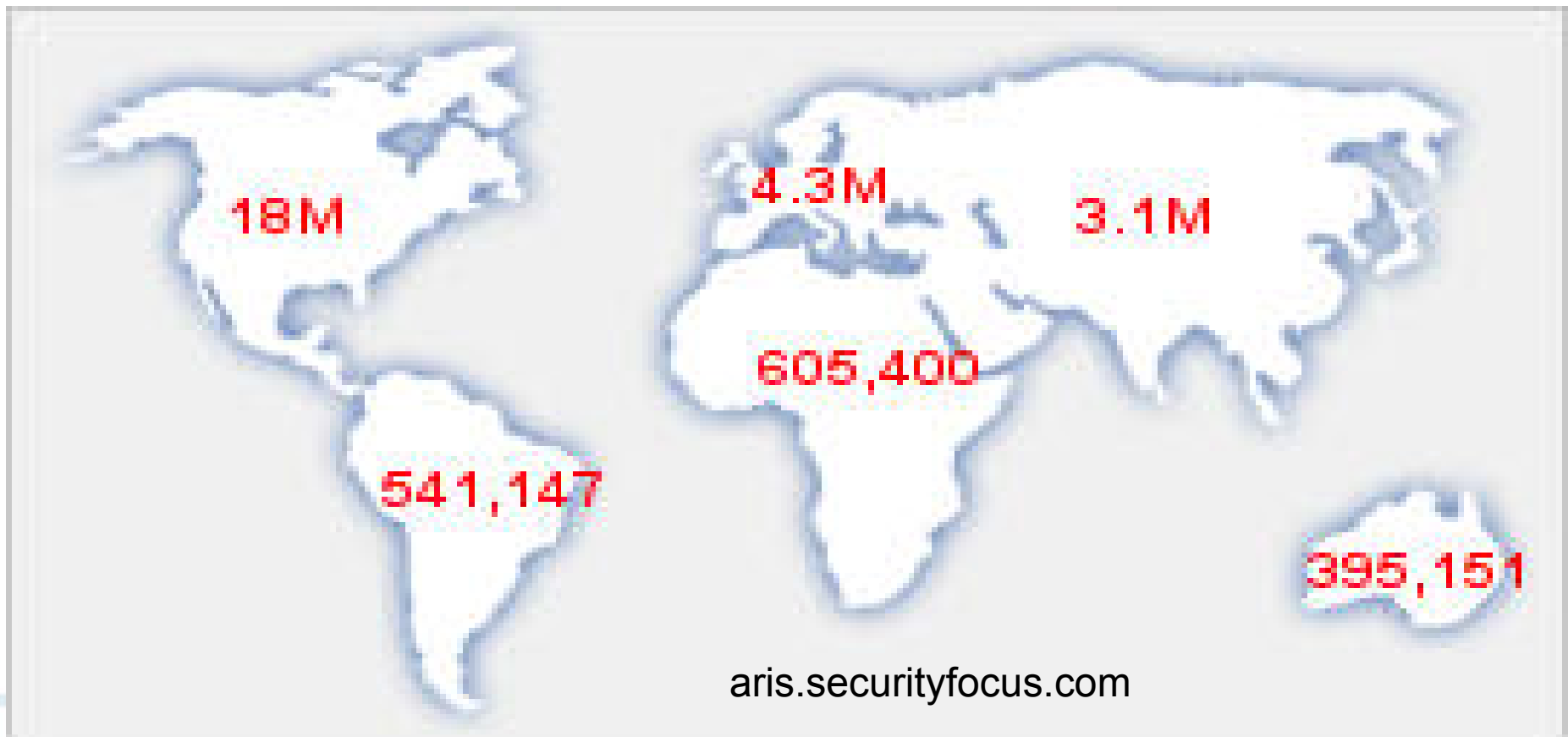


## Privacy risks—where is the danger





## Global cyber security events during a 24 hour period last week (27 million total)





## Even more scary numbers

- **10 million**
  - Estimated number of identity thefts per year
- **\$50 billion**
  - Cost to consumers and businesses from identity theft
- **76%\***
  - Number of companies that experienced one or more database/website/email “security events” in the past 12 months
  - In order from most to least common “security events”
    - Automated attacks (viruses, worms, malicious code)
    - Unauthorized access to and use of information
    - Spyware
    - Illegal generation of spam email
- **27%\***
  - Percent of security breaches committed by insiders
- **\$740,000\***
  - Average financial loss for those security events that caused financial loss

\*CSO Magazine 2006 E-Crime Watch survey



## New state and federal regulations effecting data security

- The first ever data security breach notification law was enacted in California on July 1, 2003. Since then, 39 states have or will pass similar laws and the federal congress has introduced numerous bills.
- At the heart of these laws is the requirement that companies storing personal information must promptly notify persons whose information may have been accessed by an unauthorized person.

In a recent survey of 9,000 people who received data breach notifications, 60% said they had or were considering terminating their relationship with the company.



## Third party liability provisions

- Oral or written publication of material that slanders or libels a person or organization or disparages a person's or organization's goods, products or services
- Oral or written publication of material that violates a person's right to privacy
- Infringement of copyright, title, slogan, plagiarism, piracy, or misappropriation of ideas under implied contract
- Infringement of trademark, trade dress, trade name, service mark or service name, title or slogan
- Failure to prevent a party from unauthorized access to, unauthorized use of, tampering with or introduction of malicious code into data or systems



## Privacy/mitigation coverages

- Crisis management / public relations / extra expense in the wake of a computer attack or accidental loss or release of customer (and employee) data
  - *The cost of a public relations campaign (advertising, press releases, public relations consultant in the wake of a **computer attack** or loss or release of personal information*
  - *The cost of preparing and sending personal notification to a person or party whose private personal information may have been improperly accessed, lost or stolen*
  - *The cost of credit monitoring*

- The average cost of a data breach is \$182 per lost customer record
- The average total cost per breach is \$4.8 million



## Other first party coverages

- Cyber extortion
  - Demand for payment of funds to avoid a **computer attack** against the **insured**
  
- Business interruption
  - Expenses, in excess of the **insured's** normal operating expenses, to restore the **insured's** computer system after a **system failure**
  - **Lost income** incurred by an **insured** during this **restoration period**
  
- Data restoration
  - Reasonable costs to restore any data lost as the result of a **computer attack** or the cost of reaching a determination that the data cannot be restored



## Where to get more information

- [www.mediaprof.com](http://www.mediaprof.com)

- Rob Bowers

Assistant Vice President and Product Manager – Cyber and Technology  
Media/Professional Insurance

(816) 292-7548

[rob.bowers@mediaprof.com](mailto:rob.bowers@mediaprof.com)

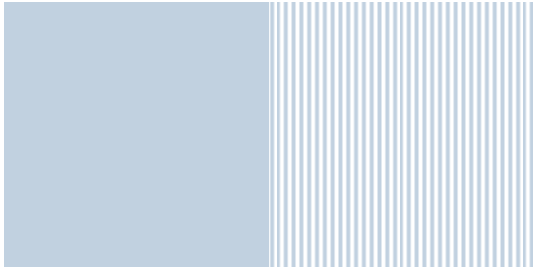
MARSH



MARSH MERCER KROLL  
GUY CARPENTER OLIVER WYMAN

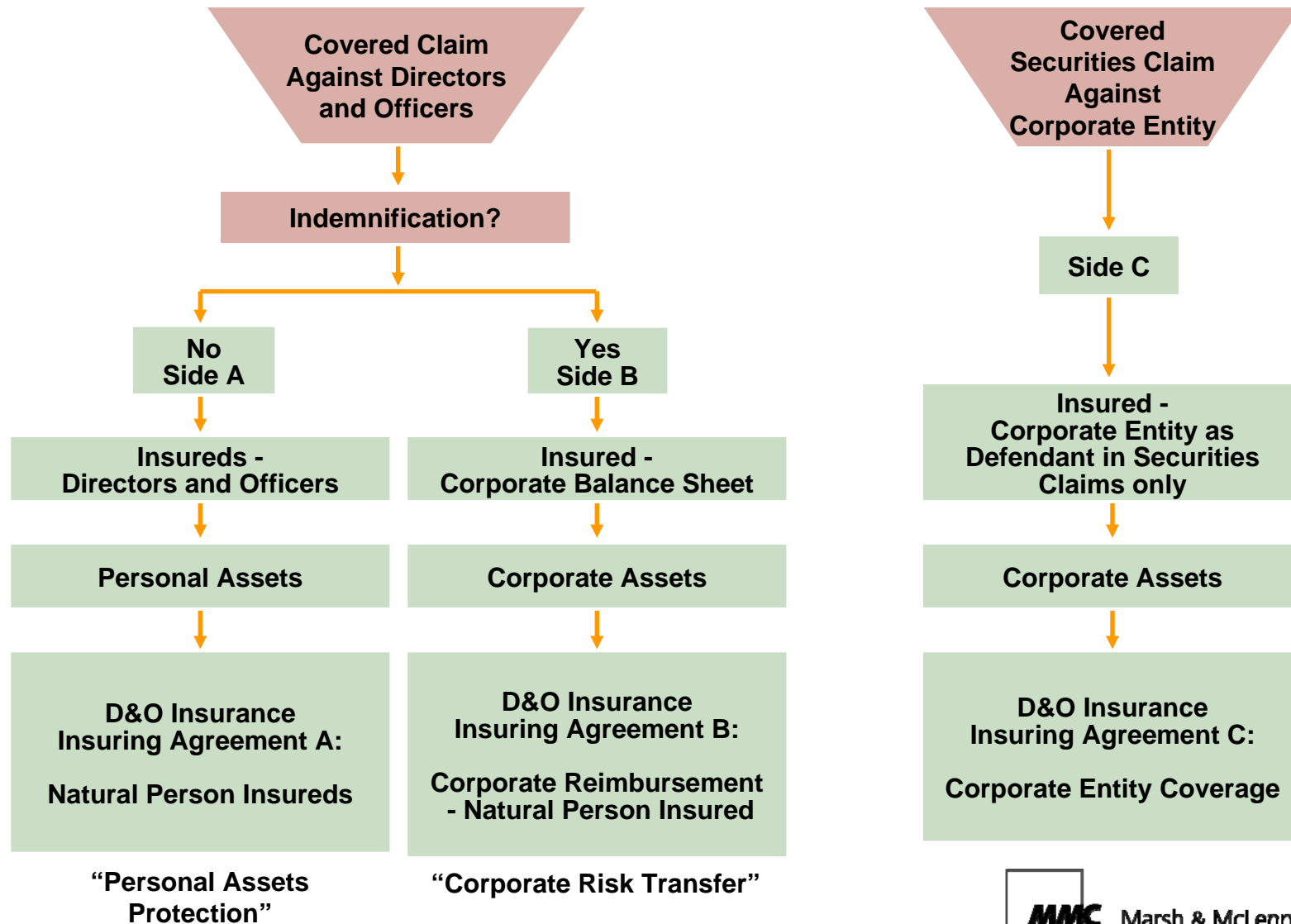
# Anatomy of a D&O Claim

Andrea D. Lieberman, Esq.  
Managing Director  
Marsh USA



# Overview of the D&O policy

# Overview of the D&O policy



# What / who is covered

- Claim
  - a written demand for monetary damages or non-monetary relief
  - a civil proceeding commenced by the service of a complaint or similar pleading
  - a formal civil administrative or civil regulatory proceeding commenced by the filing of a notice of charges or similar document or by the entry of a formal order of investigation or similar document
  - a criminal proceeding commenced by the return of an indictment



# What / who is covered (continued)

- Wrongful act
  - Any error, misstatement, misleading statement, act, omission, neglect, or breach of duty actually or allegedly committed or attempted, by a director or officer, individually or otherwise, **in his/her capacity** as director or officer of the named entity.
  
- Insured
  - All past, present and future directors and officers of the corporation and its subsidiaries. “Subsidiary” generally extends to an organization in which **more** than 50 percent of the outstanding voting stock representing the right to vote, or has management control of the corporation or its subsidiaries.



# What / who is covered (continued)

- Loss
  - All amounts incurred in defense of a claim as damages, judgments, settlements and defense costs, including pre- and post-judgment interest
- Does not include
  - Any non-indemnified amounts for which the Director or Officer is absolved from liability
  - Matters uninsurable under applicable law
  - Punitive, exemplary and multiplied portion of multiple damages (all unless expressly stated to the contrary)
  - Taxes, fines and penalties (all unless expressly stated to the contrary)



# Exclusions

- What is excluded from the coverage?
  - The exclusions are most easily explained by splitting them into three categories
    - Exposures that are better insured elsewhere
      - Fiduciary, BI/PD, Professional Liability
    - Exposures/activities that are uninsurable by law
      - Deliberately fraudulent/illegal remuneration
    - Exposures that are outside the intent of the D&O policy
      - Insured v. insured, pollution



# D&O claims environment

# Claims by allegation

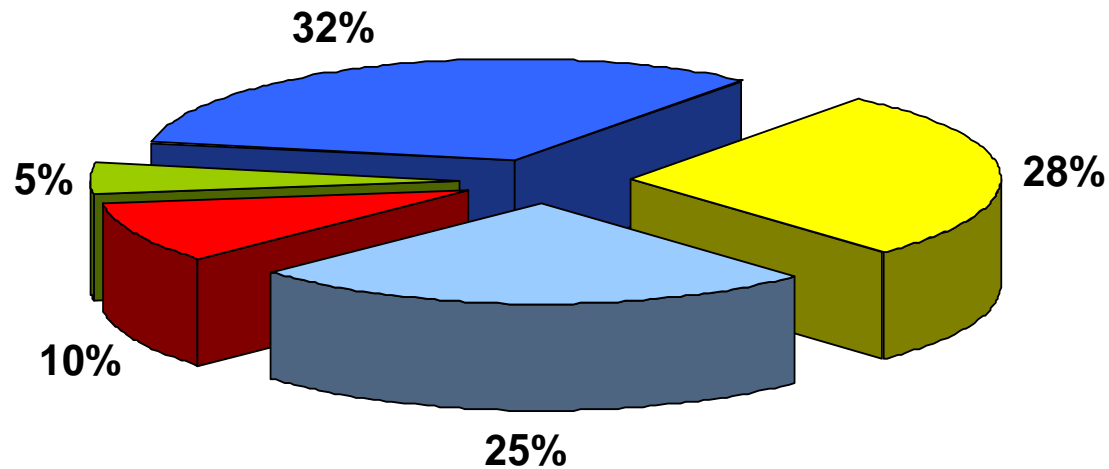
- Shareholders
  - Inadequate/inaccurate disclosure
  - General breach of fiduciary duty
  - Use of inside information
  - Stock or other public offering
  - Merger/acquisition activity
- Employees
  - Discrimination
  - Wrongful termination
  - Harassment/humiliation
  - Failure to hire or promote



# Claims by allegation (continued)

- Competitors/suppliers
  - Anti-trust
  - Contract dispute
  - Copyright/patent infringement
- Customer/clients
  - Discrimination
  - Dishonesty/fraud
  - Contract dispute
- Government
  - Anti-trust
  - SEC
  - Dishonesty/fraud

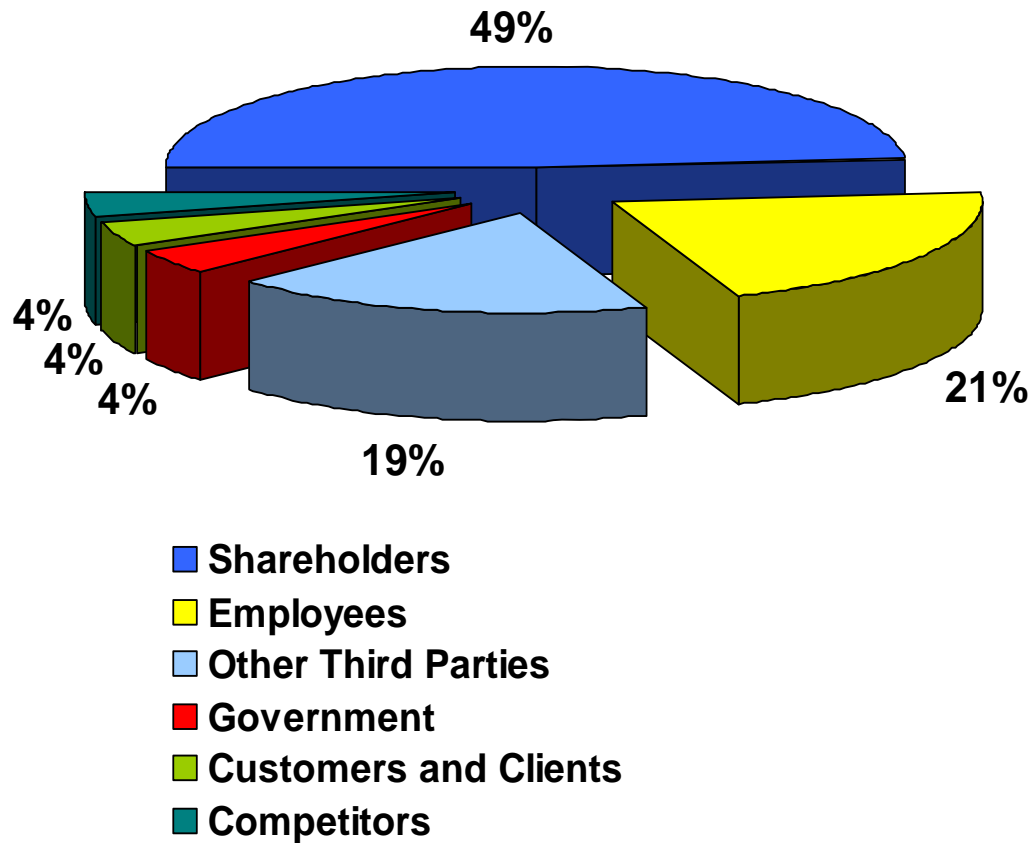
# Claimant distribution for private companies



- Employees
- Other Third Parties
- Shareholders
- Competitors, Suppliers & Other Contractors
- Customers, Clients, Consumer Groups

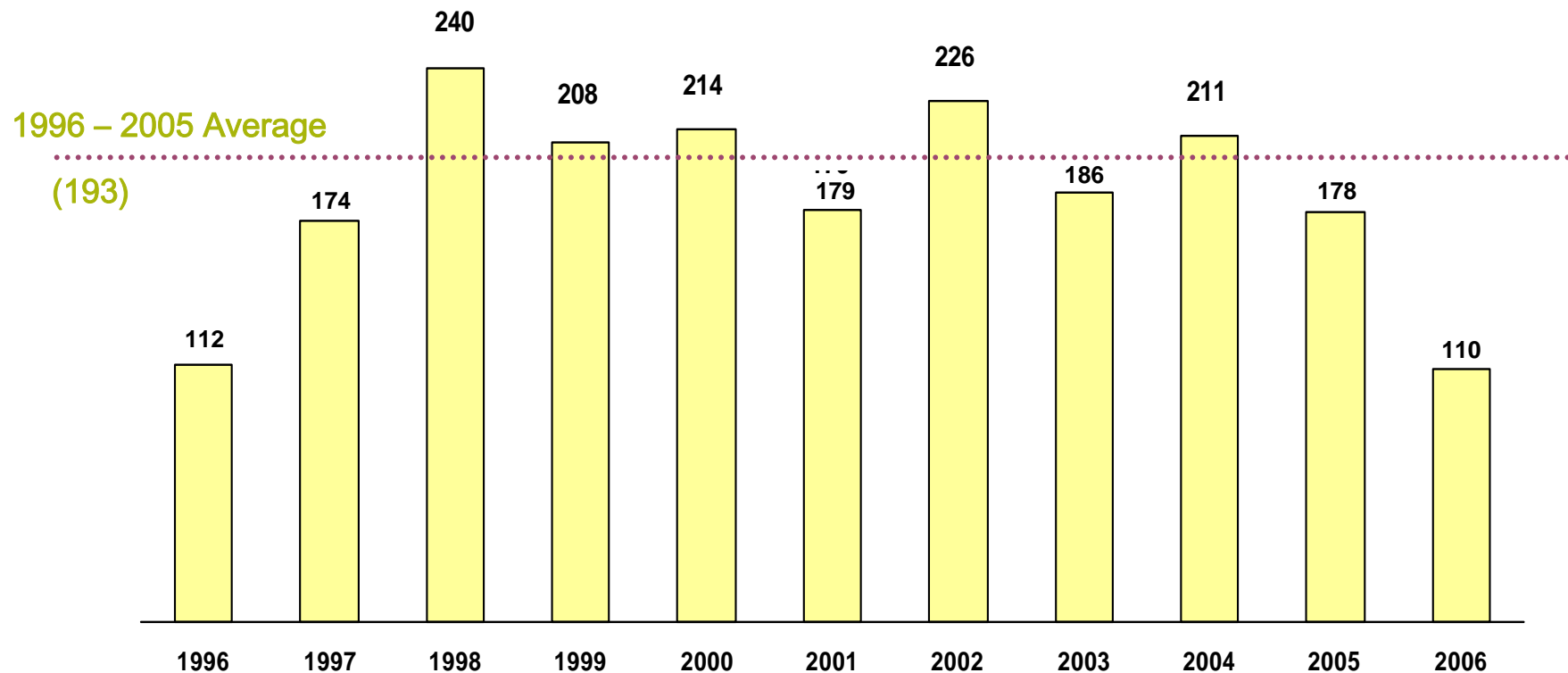
Source: 2006 Towers Perrin D&O Survey

# Claimant distribution for public companies

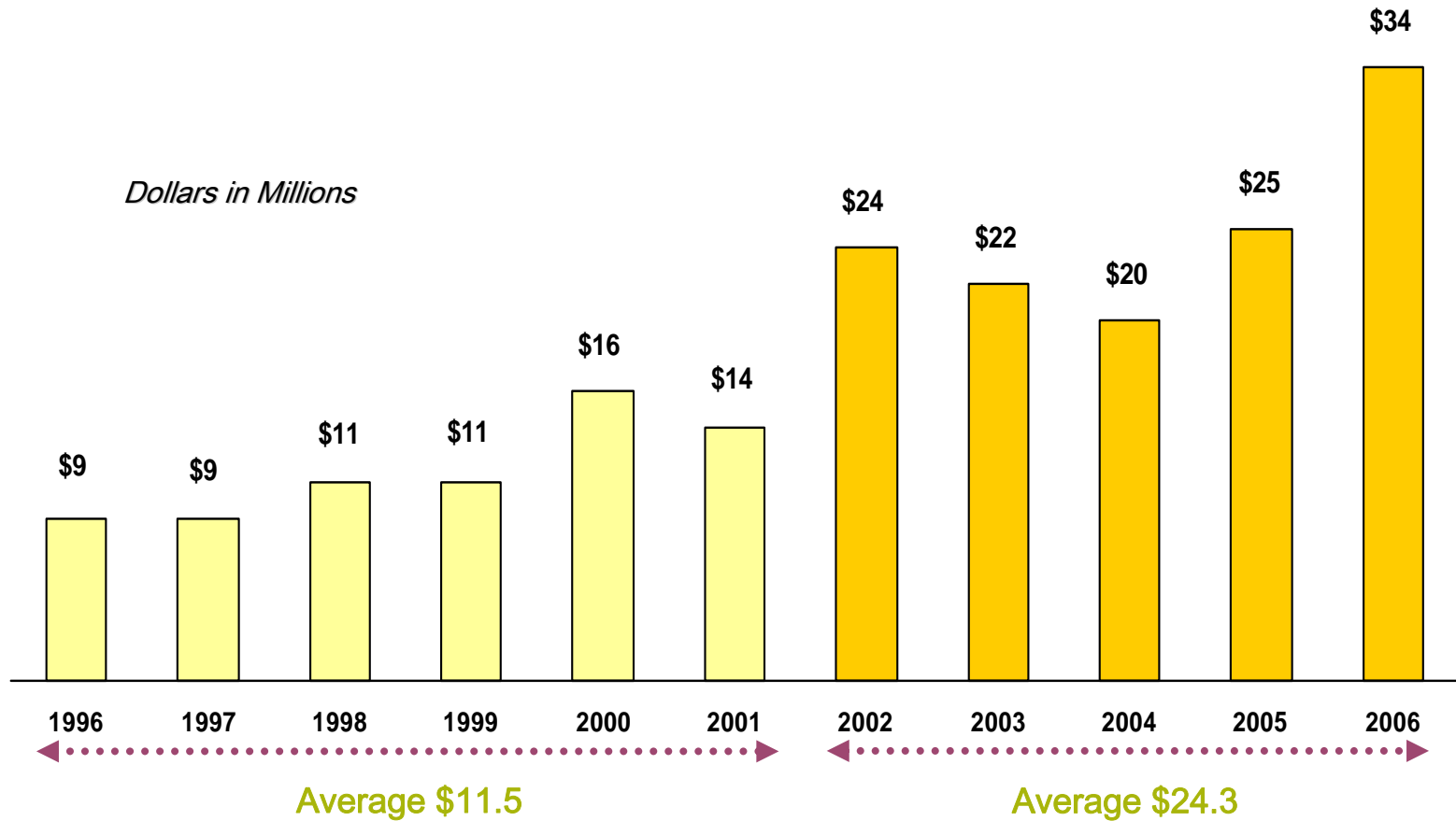


Source: 2006 Towers Perrin D&O Survey

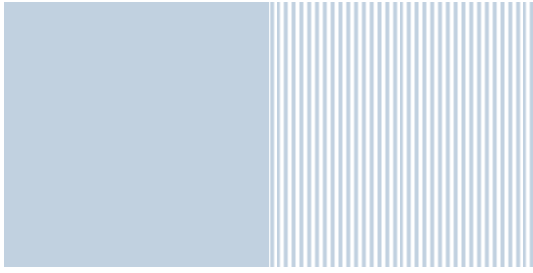
# Number of class action filings 1996–2006



# Average settlement value 1996–2006



**NOTE:** The average settlement values exclude the 2000 Cendant, 2005 Worldcom, and the 2006 Royal Ahold, AOL Time Warner, and two Nortel Networks settlements.



# Lifecycle of a D&O claim

# Lifecycle of a D&O claim

- Notice and reporting
- Defense counsel—selection and management
- Communication with carriers
- Reservation of rights letters
- Settlement

# D&O claims—notice and reporting

- Notice and reporting issues
  - Claims made/claims made and reported
  - Reporting requirements
    - As soon as practicable
    - Definite time period following policy expiration
- Definition of claim
  - Lawsuit
  - Written demand
  - Administrative/regulatory proceeding
  - Criminal proceeding
- Notice of circumstances/potential claims



# D&O claims—defense counsel

- Defense counsel selection issues
  - Duty to defend v. duty to indemnify
  - Panel counsel requirements
  - Expertise and rates
  - Multiple firms
  - Litigation management guidelines
  - Advancement/allocation of defense costs
  - Interim funding agreements
  - Legal fees review/audit



# D&O claims—reservation of rights

- Reservation issues
  - Rationale behind issuance
  - Deadline to issue
  - Typical coverage defenses
  - Responses to reservation letters
  - Issues particular to duty to defend policies



# D&O claims—communication with carriers

- Carrier communication issues
  - Duty to cooperate
  - Coordination and distribution
  - Duties to primary v. excess carriers
  - Privilege issues

# D&O claims—settlement

- Settlement issues
  - Consent
  - Allocation
  - Depletion of underlying limits
  - Demand within policy limits

# D&O claims—additional considerations

- Severability
- Rescission
- Priority of payments
- Restitution and disgorgement
- Side A coverage

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## Questions



Marsh & McLennan Companies