

# How to Select an Appropriate Limit of Indemnity

*A Guide to Top Up Insurance*



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## Top-up insurance for solicitors (also known as excess layer insurance) is coverage that is placed above, or in excess of, the compulsory primary indemnity limit set out by the Solicitors Regulation Authority (SRA).

In this paper we highlight a number of factors for Practices to consider when assessing their PII arrangements, and the potential exposures your practice may face. We explore why it is important to select the correct limit of indemnity beyond the compulsory primary layer.

We also address some of the risks involved when considering a reduction in the limit that a practices currently purchases. Ultimately and importantly, it is the leader(s) responsibility to assess what is the minimum level of coverage that is sufficient for their unique practice.

Under the SRA code of conduct O (7.13) it makes this your regulatory responsibility to assess and purchase the appropriate level of professional indemnity insurance (PII) cover for your practice, taking into account potential levels of claim by your clients and others.

It is imperative given the long tail nature of Professional liability insurance that you take into consideration these factors for your practice today but also previously including any practices that you may have succeeded.

As a part of the annual PII review, but also at appropriate intervals during the year, each practice should assess the likely risk and magnitude of an uninsured loss, to ensure that are meeting with your regulatory obligations.

### **Listed below are a number of factors to consider during your assessment, which should help to establish the appropriate level of cover:**

- Your practice's likely level of exposure to claims – influenced by the practice areas undertaken and your typical clients.
- The nature of activities undertaken which could expose your practice to risk, including the nature and level of undertakings accepted.
- The Maximum value possible for single claim, influenced by largest Transaction values undertaken or the entirety of the value of an Estate.
- The total value if a series of claims from related events were to occur (see aggregation clause section).
- Your practice's claims history.
  - Your claims history can provide some insight to the potential future claims especially if there are any particular trends that can be identified. This cannot be completely relied upon as practices need to also consider maximum severity as highlighted in bullet point 3.
- The total amount of money in your client account at any given time.
  - Practices are the temporary custodians of their clients' money and as such your client account can hold a significant money at any given time throughout the year, your PII limit should reflect at the very least the average amount in the account at any given time.
- Benchmark your practices' coverage is consistent with other practices of similar size and profile.
  - At Lockton we are able to assist you, by utilising our unique benchmarking tool.

It is good practice to consider the possibility of a claim being made against you in each and every department, should anything go wrong, along with the worst case scenario in respect of the quantity of such a claim.

Practices should also take into account whether the work is ongoing or on a one-off basis, as well as the maximum potential exposure of the client and other interested parties.

Although a claim would naturally include the core financial loss to the claimant, the settlement may extend to claimants costs in addition. This should be a consideration, as litigation costs could be significant and these would be included within any claim payment that is made.

Some clients, such as local authorities and lenders, may ask for higher limits on certain transactions or when conducting work for them; larger contracts involving sums greater than the compulsory primary indemnity limits need to be carefully reviewed.

If you decide that work to be undertaken for any client potentially creates a higher than average risk, additional premium for top-up insurance needs to be factored into your decision about whether or not to accept the retainer.

### How to Avoid an Uninsured Loss

The purpose of your insurance policy is to transfer risk and for insurers to pay claims. Ideally liability of a practice should be limited to the policy excess (deductible) that you have selected.

Notably, there is a per claim monetary limit under the MTC primary layer cover, which means that unless the practice has purchased sufficient top-up insurance, if one claim exceeds the limit under the policy, the loss may be partly uninsured.

With transaction values ever increasing we are naturally seeing claims figures follow suit and higher than ever before. Below we give examples of how an uninsured loss can arise, and importantly we look at the aggregation clause located with your policy.

### An example of an uninsured loss could be as follows:

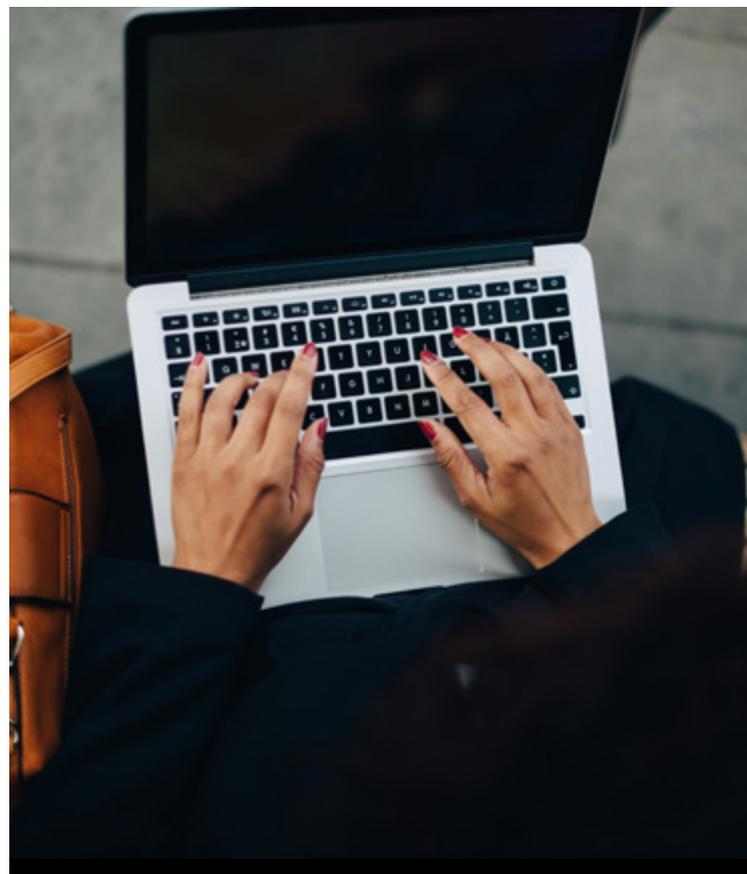
Practice ABC & Co Solicitors is a traditional partnership that purchased the £2m compulsory minimum cover level required under the SRA indemnity insurance rules.

A claimant successfully concludes litigation against practice is awarded £2.5m in damages for professional negligence. The practice's insurer pays the first £2m in accordance with the terms of the PII policy.

The partners of ABC & Co Solicitors are jointly and severally liable to meet losses that arise from wrongful acts of omissions arising from the practice's ordinary course of business. This includes the uninsured component of the claim. This means the partners are liable to meet the outstanding £500k of the claim.

**Solution: Unfortunately, for ABC & Co, Retrospective coverage for a claim is not available.**

It is important to note that you do not wait until your renewal to address, additional coverage can be sourced at any time throughout the year. No practice is immune from claims and we are witnessing a trend whereby severity of claims is increasing.





## Aggregating Clause

The SRA's minimum terms and conditions (MTC), is the prescribed policy form that every Participating Insurer must provide to all Practices.

Whilst this coverage under the MTC is broad, it does contain an aggregation clause which potentially allows for two or more claims to be treated as a single claim, if they are linked by a unifying factor of some kind. If you were to have a series of linked claims, it could be both a positive and negative implications for your practice.

The positive is that you would only have one excess (deductible) to pay, but the potential negative situation that potentially arises far outweighs this, as depending upon the severity of the loss it could result in you being under-insured.

The aggregation clause was tested in the Supreme Court, in the case of *AIG Europe Limited vs Woodman and others*. This reinforces the idea that law firms should, when assessing risk, be aware of the potential for multiple claims arising from certain types of error. What this highlights is that aggregation firmly remains an entirely fact specific exercise of judgment.

In determining whether claims should be aggregated, the courts will not look exclusively from the viewpoint of one party or another but will make a judgment, as they did in this case, 'objectively taking the transactions in the round'.

Further information of the case can be found [here](#):

In light of this, we strongly recommend that firms consider the aggregation clause when assessing their excess layer requirements and what is an appropriate level of cover.

## Friday Afternoon Fraud

With the ever-increasing risk of cyber-attacks and 'Friday afternoon fraud', it is prudent to review how much money is held in a client account at any given time. Should this exceed your current indemnity limit, you can leave yourself exposed to an uninsured loss.

*For more information, please find our guidance [here](#):*

## How Long Should Top-Up Cover be Maintained?

It is recommended that the minimum period excess layers are kept in force is six years after the completion of work, but as limitation is sometimes greater than this, you should maintain coverage for as long as you feel is appropriate.

### Further important considerations when looking to reduce top up cover:

**Latent exposures:** The nature of the cover is on a 'claims made' basis and discovery of negligence will be the trigger point, rather than the date of when the negligence occurred). You should ensure all historical higher value transactions are assessed.

**The nature of activities undertaken** which could expose your practice to risk, including the nature and level of undertakings accepted. Be mindful of any contractual agreements whereby you have agreed to hold a specific limit of cover. Any reduction in cover could lead to a breach of contract with that client.

**Loss of opportunity claims.** This is usually where we see the higher value claims succeed. When looking at your exposures, it should not just be limited to the purchase/sale value, but also any Investment values. These could be far higher than anticipated!



### Looking Ahead

Our in-depth analysis of the renewal season highlights a continued shift in excess layer pricing which is largely due to a reduction in capacity and record breaking claims. We have seen a number of excess layer providers no longer elect to write this business or impose restrictions in their policy wordings which are inconsistent with the SRA Minimum terms and conditions. With premiums on the rise and evidence to suggest it will harden further it is incredibly important to maintain your limit of indemnity. If forecasts prove correct and there is potential of the economy entering a global recession following the Covid 19 outbreak, your insurance policy may well be in the firing line. Having addressed the aggregation clause above it will be imperative to avoid Under Insurance.

Underinsurance is naturally of even greater importance due to the heightened exposure if the practice is a traditional partnership where partners can be held personally liability.

It is prudent to highlight, despite these increases, the price of additional top up coverage is still a modest rate against your fee income and when in comparison to your peers in other professions (such as IFAs or Construction) it is still competitively priced.



### How Lockton can Help

Options are limited particularly for the working layer, which is the first excess layer above the compulsory primary limit of Indemnity. As mentioned above, it is important to note that not all top-up policies provide the same cover. General differences are often based on jurisdictional restrictions, such as US/Canada restrictions or exclusions, cancellation clauses, fraud exclusions, etc.

Crucially, if you would like to check your current coverage out or you feel you do not have sufficient cover, you do not have to wait until your insurance renewal is due to obtain excess layer insurance.

Contact the Lockton Solicitors team on **0330 123 3870** or your Lockton Account Executive today to find out more about top-up cover or to establish how to get quotations for your practice.

### For more information please contact:

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