

Reporting Claims and Potential Claims Under Professional Liability Insurance Policies

The subject of this Practice Notes was originally an AIA Best Practice by the same author

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Introduction

Before a design professional decides whether or not to report a professional liability claim, or circumstance out of which a claim might arise, he or she must understand the definition of a claim, circumstance and what is required of them under their policy. The pros and cons of reporting or not reporting a claim are more fully explored in this Practice Notes.

Why Firms Neglect to Report Claims

From an insurance provider's point of view, it seems that design firms faced with a claim (or a potential claim) too often come close to jeopardizing their professional liability insurance (PLI) coverage. Many firms resist calling their insurance provider to report the matter or ask for advice. Their reasons tend to fall within one of four categories:

1. Ignorance. They do not realize what their policy requires of them when they are presented with a claim or possible claim.
2. Fear. They fear the black mark on their claim history more than they fear the claimant.
3. Denial. They believe that ignoring the problem will produce the best result.
4. Resolve. They have read their policies, understand the risks, embraced that the issue exists and after this careful analysis, choose not to report.

Know Your Terminology

Claims

It is critical that insurance policyholders understand their duties, responsibilities, and benefits under their PLI contract. One of the duties is to report all claims promptly.

What defines a claim? Most policies refer to it as a “demand for money or services.” So the telephone call from the angry client asking you to pay for damages they believe they have suffered as a result of your professional services would rise to the definition of “claim” under most policies.

Why is this definition important? Remember, you must report claims promptly. Failure to meet your obligations under the insurance policy may jeopardize your coverage.

Possible claims

It is important to know how your insurance policy defines a “claim” versus a “possible claim.” Possible claims typically do not rise to the definition of “claim” but could become one. Policies generally define possible claims as “a circumstance from which you reasonably expect that a claim could be made.”

Are you required to report these instances to your insurance company? Maybe. Most policies read, “if you report a circumstance,” but some state, “you must give written notice.” The circumstance provision in most policies goes on to say that if you follow the reporting requirements, “then any claim that may subsequently be made against you arising out of such circumstance shall be deemed to have been made on the date the insurance company received written notice of the circumstance.”

With some policy forms, firms have a fair amount of discretion on whether to report a “circumstance,” unlike the requirement that you promptly report all claims. Keep in mind that most PLI policies for design firms are claims-made, which means that insurance coverage is not retroactive to an unreported occurrence.

Intricacies of PLI Policies

Virtually all PLI policies for design firms are written on a claims-made basis, whereas most other commercial insurance policies are written on an occurrence basis. A claims-made policy that is in effect when a claim is made will pay for losses regardless of when the event giving rise to the claim occurred (subject to limitations). Under an occurrence-based policy, even an expired one, a claim can still be made against it if the policy was in force when the event giving rise to the claim occurred.

Four conditions for coverage

Generally, a professional liability claim must meet four conditions to be considered for coverage:

1. You must have a current policy at the time a claim is made against you.
2. The services that led to the claim must have been performed after your retroactive date—the earliest date a wrongful act is afforded insurance protection.
3. You must report the claim to the insurance company in writing during the policy term (or within some relatively short window of time thereafter, usually 30 or 60 days).
4. You may not have prior knowledge of the claim, or you may not have reasonably anticipated that the claim would be made similar to a potential claim-producing circumstance. No coverage is afforded for a claim or circumstance that you knew about prior to the start of the: 1) policy term, or in some cases, 2) your uninterrupted insurance history with a single insurance company.

Some policies offer a “prior knowledge” exception

Some policy forms soften this “prior knowledge” condition by adding that coverage is considered if, as found in the CNA policy, “on the knowledge date” indicated on your policy, “no officer, director, principal, partner or insurance manager knew or could reasonably have expected that a claim would be made.”

This “knowledge date” is the first date you began uninterrupted coverage with that particular insurance company. You did not violate your policy if you did not know about the claim or circumstance before you started with that insurer—provided you had no gaps in coverage. Some other PLI providers do not offer this enhancement, so their “prior knowledge” restriction applies year by year, not insurance company by insurance company.

For example, if you were insured with ABC insurance company last year when you became aware of a circumstance but elected not to report it and then renewed your policy with ABC this year and your circumstance turned into a claim, you would likely be without coverage on the loss due to a “Declination Due to Prior Knowledge.”

Know your policy, then trust your instincts

Does this mean you report every problem on every project? No. As professionals, you form a sense of which issues are likely to become claims and which need further attention. States will vary as to the applicable standard in connection with potential claim reporting. For example many states apply an “objective” standard. This means that if the reasonable design professional should recognize that these facts and circumstances will result in a claim, then the matter should be reported to the appropriate insurer.

Trust your instincts. Claims personnel are not on a witch hunt to find reasons to deny coverage, but they will protect their employer’s interest if they find clear evidence you had prior knowledge of a claim and did not report it promptly or if you had prior knowledge of the circumstance or claim before the policy term began.

Fifteen to 20 different insurance companies offer

PLI policies to design firms, and each company has different policy language and claim philosophy. It has become increasingly common, however, for adjusters to follow the letter of their policy obligations because failure to do so on one claim may jeopardize their ability to do so on the next.

To Report or Not to Report?

Now we know the policy requirements. You must report claims promptly, and with some policies, you can decide whether to report circumstances, but failure to do so may jeopardize future insurance protection for the loss.

Your business decisions are a balance, so let’s consider the risks and rewards of reporting a claim. There is only one risk in reporting a claim or circumstance under your policy: the dreaded smudge on your record.

Who sees claims as a black mark? Your insurance company? No, it sees claims all day, every day. In fact, claims are important for evaluating clients—by reported claims or by a noticeable lack thereof.

Will your insurance broker see a claim in a negative light? No, it gives him or her opportunity to provide the services you have paid for in your insurance premium.

Your clients? No. They only see this information in rare cases. Even then, you should be able to weed out reports that never developed into claims.

So who are we left with? You, of course. Will reporting bother you? You bet. It may downright annoy you to have to disclose the claim or incident on applications for the next 5, possibly 10, years. On the scale of risk and reward, however, “annoying” barely tips the balance.

And yes, there could be a financial repercussion from the report you make even before the matter is resolved or paid by your insurer. All insurance companies assess the potential risk presented by a claim. Some make this same assessment on potential claims. The future dollars that your insurance company expects to pay out on a claim for expenses (your defense team and expert witnesses) and payment to the claimant are known as the Reserve. This Reserve information is part of the entire underwriting portfolio that your underwriter will use to evaluate your risk and determine your premium.

Although most insurance companies do not assign a Reserve to circumstances, some do. Most insurers will assign a symbolic Reserve amount (\$1 or \$3) that signals to the underwriting community that the reported matter is indeed only a circumstance.

But if you are with an insurer that does not distinguish between claims or potential claims in their reserving practices, your annoyance factor will skyrocket. If you are faced with the situation where your premium may be partially promulgated based on a mere potential, you should document, document, document when completing your application and creating any additional attachments. And now would be the time to rely heavily on your skilled insurance broker. Remember, however, that we are only talking about circumstances. All claims will have reserves and what is the definition of claim? A demand for money or services. Some insurers treat reserve information as proprietary and are not willing to share it with their insureds. However many states require that this information be disclosed. It is a good practice to secure reserve information, when available, in order to determine whether or not your insurer is over-estimating the value of a claim or incident.

Benefits of Early Reporting

Early reporting has many rewards. Let’s look at an actual situation: An architect called his insurance broker to tell her that a one-ton balcony collapsed adjacent to a recreational pool area. The broker immediately notified the insurance company, who put the design firm in contact with a lawyer to start gathering information and to remind the principal of appropriate responses during the crisis. The insurer then hired a forensic engineering firm, all before the architect even pulled into the parking lot!

In addition, the broker offered her client tips on good public-relations skills when facing the media—still during their drive to the site. The architect was prepared with an alternate solution when his client wanted to sweep up and remove the debris, thereby erasing a critical part of the story should a claim be made later.

Reporting a circumstance or claim should begin your access to the power of your insurer, including its expertise, network of consultants and attorneys, and financial resources. You will not only get valuable assistance with the loss or possible loss, but you also often avoid making a bad situation worse.

What if our architect had told his client, “Don’t worry, I’ll take care of it” before his negligence was established, thereby possibly accepting financial risk without insurance coverage? Every claims adjuster has sad stories like this to tell. This is most common when a design firm receives a subpoena for testimony before being made a party to the action. Feeling they are fulfilling their civic obligation, they freely discuss matters with opposing counsel in what they may later consider an unwise fashion after they are joined in the claim and find that their casual, on-the-record comments harm their own case. Early advice from the claim adjuster can be invaluable.

Even if, later on, this policyholder discontinues their insurance or purchases coverage or options that are less favorable than they currently have, this claim will be covered under the terms and conditions of the

policy in place on the date the circumstance was reported to the insurance company.

Even if you are not obligated to report a circumstance according to your policy requirements, you may still report it. By doing so, you will have more options to choose from at your next renewal. You may not ultimately decide to switch to a different insurance company, but you should have the freedom to do so. Unless the matter is reported, you are not free to consider other insurers, lest a claim arise with the new insurer from an unreported circumstance of which you were previously aware.

If you are about to undertake the careful analysis of the pros and cons of failing to make a report, you should include one more important piece of information. Does your insurance company include a financial incentive for reporting a circumstance before the claim develops?

Free Pre-Claims Assistance

Yes. You read that right. Free. Many insurance companies waive your deductible payment for any expenses they incur to avoid future damages from the circumstance you report.

When We receive Your written notice and We, at Our discretion, incur Claim Expense to undertake measures to avoid any Damages as result of the reported Wrongful Act or Pollution Incident, We will waive the applicable Deductible.

Some insurance companies will even pay these expenses on their tab and not use them to deplete your available limit of liability.

Look for this language in your policy:

... payments made under this section are our costs, are not subject to the Deductible and are in addition to the Limit of Liability shown on the Declarations. Until the date a claim is made, we may pay for all costs or expenses we incur, at our sole discretion, as a result of investigating a circumstance that you report in accordance with [your policy].

And for those firms that believe that ignoring the problem will make it go away, sometimes you are absolutely right. But sometimes you are not. If you take this risk and you are wrong, you may have compromised your insurance coverage. Keep in mind that early reporting of a matter to the insurance company to avail yourself of their resources does not necessarily mean engaging the claimant in discussions. You and your insurance adjuster may mutually decide that the best course of action is to lay low until other action is necessary.

Applications and Representations

The question of reporting a claim or potential claim (circumstance) is not simply a matter of what is required under the policy. Remember that you will be completing an application for each coverage renewal. If you remain with your current insurer you might not be required to respond to the claim and circumstance questions. If you do respond to these questions, however, you will need to disclose whether or not a claim has been made and whether or not circumstances exist out of which a claim might arise. You go through this process with every renewal.

If you are required to complete these questions and fail to disclose a claim or circumstance, your insurer might have the basis to not only deny coverage for the unreported matter but might also be in a position to rescind the policy. This is because claim and circumstance information is material, and failure to report it can be a material misrepresentation.

And when you read your application, you might find that it isn't only your personal knowledge of a claim or potential claim that is being sought. Some forms require that you "inquire" of all members of the firm. While another may ask if you or any other principal, partner, officer, director, insurance manager or

shareholder have knowledge. And your application might give you a list of what you need to include, reasonably aware of or not. These lists generally include acts, errors, omissions, unresolved job disputes, accidents or other circumstances that are or could be the basis for a claim under the proposed insurance. A skilled broker can reduce the impact of a reported claim or circumstance but will be of limited assistance when faced with a coverage problem created by a material misrepresentation.

Lessons Learned

As we can see, it is important to

1. Read your policy to understand the definition of claim and circumstance; your duties in the event of a claim; your rights in the event of a circumstance; and how prior knowledge of a claim or circumstance will affect your coverage.
2. Report claims promptly.
3. Consider your options when faced with a circumstance.
4. Use your insurance broker, professional groups, colleagues, and legal counsel as resources.
5. Before renewing your PLI policy, check with your partners and employees for possible knowledge of a circumstance and follow your policy duties for reporting it.

Design firms spend much time and money to acquire a PLI policy. What does it do for you? Sure, it offers peace of mind, and ideally allows you to meet your client's insurance requirements. But what is it really for? To pay claims and claim-related expenses.

Resources

For More Information on This Topic:

See also "Insurance Coverage" by Lorna Parsons and Ann Marie Boyden, Hon. AIA, *The Architect's Handbook of Professional Practice*, 13th edition, Chapter 12, page 331.

About the Author

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Appendix

A Guide to Claim and Potential Claim Reporting

Step 1.

Figure out if what you have on your hands is a claim or a circumstance.

Definitions of claim:

Claim means a demand for money or services, naming you and alleging a wrongful act or pollution incident.

Claim means: 1. a written demand against any Insured for monetary damages or non-monetary or injunctive relief, or 2. a civil proceeding against any Insured seeking monetary damages or non-monetary or injunctive relief, commenced by the service of a complaint or similar pleading, including an appeal therefrom.

Claim means an oral or written demand for monetary damages from any party whose intent it is to hold you responsible for any wrongful act or pollution incident in performing professional services. Claim also means your knowledge of circumstances which could reasonably be expected to give rise to such demand.

Claim means a demand for money or services, naming the Insured and alleging a wrongful act. A claim also includes the service of suit or the institution of an arbitration proceeding against the insured.

See these differences? Some policies will require the reporting of an oral demand for money. Some policies impose the same reporting demands on you whether the matter is a possible claim or a claim.

Stop. If the matter at hand meets your policy's definition of a claim, read Step 2, otherwise, checkout Step 1.A.

Step 2.

In the event of a claim, look for what your insurance company expects you o do next. Here are some examples.

Your Duties if there is a Claim

If there is a claim, you must do the following:

1. Promptly notify us in writing. This notice must be given to us within the policy year in which the claim is made or within 60 days after its expiration or termination. All claims reported during any extended reporting period shall be considered as having been made during the last policy year this Policy was in effect. If the claim is made during any applicable extended reporting period, then notice must be given to us within such extended reporting period. Notice of a claim must be sent to the attention of either of the following:
 - a. [insurance company name]
 - b. [managing general agent name]
2. Specify the names and addresses of the persons making a claim against you and provide us with information on the time, place, and nature of the claim.
3. Immediately forward to us all documents that you receive in connection with the claim.
4. Fully cooperate with us or our designee in the defense of a claim, including but not limited to

assisting us in the conduct of suits or other proceedings, settlement negotiations, and the enforcement of any right of contribution or indemnity against another who may be liable to you. You shall attend hearings and trials and assist in securing evidence and obtaining the attendance of witnesses.

5. Refuse, except solely at your own cost, to voluntarily make any payment, admit liability, assume any obligation, or incur any expense without our prior written approval; and
6. Pay the Deductible amount when due. After you report a circumstance or a claim is made and you have the right under any contract to either reject or demand arbitration or other alternative dispute resolution process, you shall only do so with our prior written consent.

In general: report the claim including details on the claimant and allegations; send along any supporting documentation; cooperate with your insurer; don't admit liability or incur any expenses without checking with your adjuster; and pay your deductible.

Your insurance policy outlines these obligations to safeguard your insurer's ability to protect your mutual interests. Note that you must promptly notify your insurer. You must immediately forward all documents you receive in connection with the claim to your insurer. And you must refuse to voluntarily make any payment.

Another policy form adds the following obligation:

Other than what is required by law, refrain from discussing the facts and circumstances of any Claim with anyone other than legal counsel representing the Insured or representatives of the Company.

So look for the answers to these questions in your policy form:

- 1). If you receive notice of a claim at the end of your policy term, are you allowed additional time to report the matter?
- 2). To whom do you make the report?
- 3). What information are you required to provide?
- 4). What are your obligations to your insurance company during the claim process?

Now you have been helped along your policy way. You have a claim and you have reported it. Or you have elected not to report it in spite of the risks to your financial protection.

STEP 1.A

Definition of circumstance

But if your issue at hand does not meet your policy's definition of claim, what are your rights/obligations for reporting circumstances? What you will find is that some insurance policies make this report optional and others make reporting it, or in fact reporting it promptly, a condition to future coverage on the matter.

For example, one policy indicates:

If you report a circumstance for which there may be coverage under this Policy.. (bold added for emphasis).

While another policy says:

If the Insured first becomes aware during the Policy Period of: (1) an actual or alleged Breach of Professional Duty or circumstance arising out of Professional Services or (2) a Pollution Condition arising out of Covered Operations which is reasonably likely to result in a Claim, **the Insured must give written notice to the Company**... If such written notice is received by the Company prior to the end of the

Policy Period, any Claims subsequently made against the Insured arising out of such conduct shall be deemed for the purpose of this policy to have been made on the last day of the Policy Period (bold added for emphasis).

Clearly, failure to report the matter when you “must” can impair coverage should the circumstance develop into a claim at a later date.

If you must report the circumstance, go on to step 2.A. If your report is optional, go to step 2.B.

STEP 2.A

Reporting a circumstance

Locate your policy obligations for circumstance reporting. Here are a few samples:

It is a condition precedent to the coverage afforded by the policy that the written notice shall contain the following information:

1. The actual or alleged Breach of Professional Duty or circumstance or Pollution Condition which is the subject of a potential Claim;
2. A description of the Professional Services rendered or Covered Operations performed by the Insured which may result in the Claim;
3. The date(s) of such conduct which may result in the Claim; and
4. A description of the injury or damage that has or may result in a Claim;
5. The identities and address of any potential claimant(s);
6. The anticipated location(s) of any such potential Claim;
7. The circumstances by which the Insured first became aware of the potential Claim.

If all of the above information is not so provided or is, in the reasonable judgment of the Company, deemed inadequate, the Company shall inform the Insured that any Claim made after the Policy Period relating to the written notice will not be deemed to have been made during the Policy Period.

The addition of the above paragraph is not universal, but this insurance company’s intention is to discourage firms from submitting a laundry list of every fathomable issue, reasonably expected or not, before the end of the policy term in a misguided attempt to memorialize all possible coverage. Professional Liability myth has this happening before a firm elects to discontinue one of these claims made policy forms.

Another insurance company adds this condition:

The notice of the potential claim must include the following... an explanation as to why the Insured believes the claim may be made and the date that the Insured first became aware of such possible claim...

Your homework list will mirror that for claim reporting, namely:

- 1) If you receive notice of a circumstance at the end of your policy term, are you allowed additional time to report the matter?
- 2) To whom do you make the report?

3) What information are you required to provide?

So now, if you must report the circumstance, report it.

Now you are in the home stretch. You have either decided to report the circumstance or not. If you will not be reporting the matter at this time, you have one last bit of your policy to read.

Step 2.B

Do you get another chance to report the claim later?

Remember that some insurance companies do not require you to report circumstances. It is at your discretion. But the catch is, **all** insurance companies offering you a new policy (and sometimes even the insurance company you are currently insured with) will exclude coverage for claims or circumstances that you were aware of before their newest policy's effective date. Read your policy.

With the following provision, even if you remain with this insurer from year to year, you must report each circumstance during the policy period in which you are made aware of it.

For this coverage to apply, all of the following conditions must be satisfied:

2. **Prior to the Effective Date of this policy**, no officer director, principal, partner, insurance manager or risk manager of the Insured had knowledge of the actual or alleged Breach of Professional Duty or Pollution Condition or circumstance likely to give rise to a Claim under this policy (bold added for emphasis).

Or you may see the following language that implies that you have until the end of your relationship with them to report the circumstance. It would be wise, however, to have first completed your check on the definition of claim and circumstance and on whether or not reporting of the matter is required or optional.

We will pay damages which you become legally obligated to pay and claim expense, as a result of claim(s) first made against you and reported to us in writing during the policy period... provided that:

3. **Prior to the inception date of the first policy issued to You by Us and continuously renewed by Us**, You had no reasonable basis to believe that such Wrongful Act or Pollution Incident had been committed or that a Claim would be made against You alleging such Wrongful Act or Pollution Incident (bold added for emphasis).