

Module 8

Professional Liability Loss Exposures

**Professional Liability Loss
Exposures and Insurance**

**Module 8
Chapter 8**

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Objectives

- ☐ Obj I: Legal Foundations of Professional Liability
- ☐ Obj II: Professional Liability Coverage Under CGL Policies
- ☐ Obj III: Common Characteristics of Professional Liability Policies
- ☐ Obj IV: Healthcare Professional Liability
- ☐ Obj V: Financial and Legal Professional Liability
- ☐ Obj VI: Architects and Engineers Professional Liability

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**Legal Foundations of
Professional Liability**

Objective I

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Professional Liability

- ❑ Many types of occupations require professional liability insurance.
 - ❑ Professional liability, malpractice, and E&O are often used interchangeably.
- ❑ Professional liability can be based on:
 - ❑ Breach of contract.
 - ❑ Tort principles.
 - ❑ Statutes and regulations.

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Contract Law

- ❑ Contract law approach to establishing liability is based on the relationship between professionals and their clients.
 - ❑ If a professional fails to perform the services agreed to, a breach of contract occurs.
 - ❑ If the client suffers harm as a result of the breach, the client is entitled to be restored.

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Contract Law

- ❑ Damages recoverable for breach of contract:
 - ❑ Compensatory – intended to indemnify a person for injury or damage sustained.
 - ❑ Consequential – payment awarded to indemnify an injured party for indirect losses.
 - ❑ Liquidated – listed amount in a contract to be recovered if a breach occurs.
 - ❑ Nominal – small amount, such as one dollar.
- ❑ Injured party must prove they suffered a loss as a direct result of the breach.

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Tort Principles

- ❑ Under tort principles, members of a profession are liable for injury from failure to perform with reasonable professional care and competence.
 - ❑ Must be found to have made an error or omission.
- ❑ Reasonable person standard applies under tort principles.
 - ❑ In a contract claim, allegation is that the defendant failed to do something that was required by the contract.

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Statutes and Regulations

- ❑ Statutes and regulations can affect the liability of many professionals.
 - ❑ General application statutes – Racketeer Influence and Corrupt Organizations Act.
 - ❑ Offenses include mail fraud and wire fraud.
 - ❑ Specific application statutes – securities laws.
- ❑ Some laws apply to healthcare professionals.

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Need for Expert Witness Testimony

- ❑ In professional liability suits, the plaintiff must prove the defendant failed to meet the applicable standards of professional conduct.
 - ❑ Without special knowledge, jurors could have difficulty determining if professional used the required level of skill and care.
- ❑ Jury needs to be informed of the standards that pertain to that particular profession.
 - ❑ Standards are established by expert witnesses.
 - ❑ Expert witnesses can state their opinion.

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Need for Expert Witness Testimony

- ❑ Experts are not needed in every professional liability case.
 - ❑ In some situations, a layperson can understand, without the aid of experts, that a professional has committed a negligent act.
- ❑ Experts are also not needed if doctrine of Res ipsa loquitur applies.
 - ❑ The thing speaks for itself.
 - ❑ Applies when injury results that could not have occurred without negligence.

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Practice

- ❑ An amount of damages for breach of contract that is specifically stipulated in the contract as a reasonable amount to be recovered is known as:
 - ❑ A. Liquidated damages.
 - ❑ B. Consequential damages.
 - ❑ C. Compensatory damages.
 - ❑ D. Nominal damages.

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**Professional Liability
Coverage Under CGL
Policies**

Objective II

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Professional Liability Coverage

- ❑ For many professions, the general liability loss exposure is minor.
 - ❑ Lends itself to coverage in businessowners policies that receive little individual underwriting.
- ❑ Many insurers do not want to expand their underwriting to include the personnel needed to underwrite professional liability insurance.

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Professional Liability Coverage

- ❑ Insurers routinely endorse their CGL policies to exclude professional liability.
 - ❑ Even without an exclusion, a CGL policy does not cover many professional liability losses.
- ❑ A CGL policy covers:
 - ❑ Bodily injury.
 - ❑ Property damage.
 - ❑ Personal and advertising injury.

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Professional Liability Coverage

- ❑ ISO Commercial Lines Manual indicates that businesses requiring a professional liability exclusion include:
 - ❑ Barber shops and beauty parlors.
 - ❑ Computer consulting.
 - ❑ Engineers, architects, and insurance agents.
 - ❑ Medical offices.
 - ❑ Tattoo parlors.
 - ❑ Health or exercise.

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Practice

- ❑ Which one of the following businesses would most likely have professional liability excluded from coverage in its commercial general liability (CGL) policy?
 - ❑ A. Arts and crafts shop.
 - ❑ B. Hardware store.
 - ❑ C. Barber shop.
 - ❑ D. Grocery store.

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Common Characteristics of Professional Liability Policies

Objective III

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Professional Liability Policies

- ❑ Insurers use different types of policies to insure members of each profession.
 - ❑ Most forms are developed by insurers.
 - ❑ Can differ substantially.
- ❑ Professional liability policies are designed to cover claims arising from rendering or failing to render professional services.
 - ❑ Many policies limit their coverage to negligent acts, errors, or omissions.

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Person and Organizations Insured

- ❑ All professional liability policies cover the individual professional(s) named in the policy.
 - ❑ Most policies also cover partners, owners, directors, officers, and stockholders.
 - ❑ Some policies cover employees.
- ❑ A partnership, corporation, or LLC may also be covered.
 - ❑ Some policies only cover organization's obligation to indemnify those who are sued.

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Defense Coverage

- ❑ Professional liability policies ordinarily pay the costs of defending against claims.
 - ❑ Defense coverage typically includes supplementary payments.
- ❑ In some policies, the insurer assumes the right and duty to defend.
 - ❑ Therefore entitled to appoint defense counsel.
 - ❑ In other policies, insurer agrees to pay defense costs but does not assume the right and duty to defend.

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Defense Coverage

- ❑ Sometimes defense costs are payable in addition to policy limits, as in CGL policy.
 - ❑ More commonly, defense costs are included within policy limits.
- ❑ A provision requiring that the insurer obtain the insured's consent to settle is common.
 - ❑ Provision is a specific recognition that the insured has a reputation to protect.

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Defense Coverage

- ❑ Many policies include a hammer clause.
 - ❑ Settlement opportunity clause.
 - ❑ Discourages insureds from refusing to let the insurer settle a claim.
 - ❑ Apply some pressure on the insured to be reasonable in settling valid claims.
- ❑ Some policies provide that if the insured and the insurer do not agree on a settlement, it must be submitted to an arbitration committee.

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Claims-Made Provisions

- ❑ Many professional liability policies cover long-tail claims.
 - ❑ Claims reported after policy has expired.
- ❑ Insurers prefer to use claims-made professional liability policies to match claims with policies.
 - ❑ ISO form offers automatic five-year extended reporting period.
 - ❑ Offers optional supplemental extended reporting period.

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Claims-Made Provisions

- ❑ The option to purchase an extended reporting period is usually available if either party terminates the coverage.
 - ❑ Generally not available if policy is canceled because of nonpayment of premium or fraud.
- ❑ When professionals cease to practice, they no longer need coverage for future acts.
 - ❑ However, they may need tail coverage for claims that are not actually made against the insured until after the insured retires.

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Coverage Territory

- ❑ Most professional liability policies provide coverage for acts committed anywhere in the world.
 - ❑ Suit must be brought in the U.S. or Canada.
- ❑ Some policies allow a suit to be brought anywhere in the world.
 - ❑ Some policies require act to be committed in a more restricted policy territory.

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Exclusions

- ❑ Certain exclusions common to most liability insurance policies are usually also found in professional liability policies.
 - ❑ Intentional injury, pollution, workers comp.
- ❑ Policies for healthcare professionals, architects and engineers do not usually contain an exclusion of bodily injury.

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Practice

- ❑ Which one of the following statements is correct regarding professional liability insurance policies?
 - ❑ A. They all provide coverage for employees of the professional organization.
 - ❑ B. They typically contain a provision requiring the insurer to obtain the insured's consent to a settlement.
 - ❑ C. They allow an insurer to turn over the claim to an arbitrator if the claim is not settled within the policy period.
 - ❑ D. They typically limit coverage to those acts committed in the U.S. or Mexico.

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Healthcare Professional Liability

Objective IV

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Legal Foundations

- ❑ Some of the highest-risk professional liability classifications are within the healthcare field.
 - ❑ Healthcare professionals have specific liability exposures.
- ❑ Medical professionals and facilities can be held liable for negligence when a patient is injured.
 - ❑ Healthcare professionals must exercise the level of skill that a reasonable person would exercise under the same circumstances.

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Legal Foundations

- ❑ A plaintiff must establish the standard of care applicable to the medical treatment at issue.
 - ❑ Must also establish a causal connection.
 - ❑ Most courts require expert testimony.
- ❑ Most states have effectively established a national standard of care.
 - ❑ Implies rural practitioners have the same training and exercise the same judgment as urban practitioners.

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Legal Foundations

- ❑ Practitioners and facilities can be held vicariously liable for negligence of employees.
 - ❑ Business entities can be held vicariously liable.
- ❑ Practitioners can also be held liable for acts of hospital employees.
 - ❑ “Captain of the ship” (borrowed servant).
 - ❑ Under this legal theory, hospital employees are considered temporary servants of the operating surgeon.

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Legal Foundations

- ❑ Sovereign immunity can protect governmental entities from liability claims.
 - ❑ Charitable immunity historically extended the same immunity to not-for-profit hospitals.
 - ❑ Many hospitals are for-profit entities and would be ineligible for charitable immunity.
- ❑ Some states have Good Samaritan laws.
 - ❑ Protect those who render assistance at the scene of an accident without compensation.
 - ❑ Doesn’t apply to gross negligence.

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Informed Consent

- ❑ A physician must obtain the consent of the patient before performing surgery.
 - ❑ Except under emergency conditions or in unanticipated situations.
- ❑ Must also explain potential risks associated with the surgery or treatment.
 - ❑ Informed consent is also required for various procedures performed by hospital staff.

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Informed Consent

- ❑ To obtain informed consent, physician must disclose to the patient:
 - ❑ Nature of the patient's condition or problem.
 - ❑ Nature of the proposed procedure.
 - ❑ Risks associated with the procedure.
 - ❑ Anticipated benefits of the procedure.
 - ❑ Alternatives to the procedure and the risks associated with them.

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Risk Management Techniques

- ❑ Healthcare risk management emphasizes root-cause analysis.
 - ❑ Focuses on systems and processes to identify improvements that will decrease the likelihood of such occurrences in the future.
- ❑ Healthcare organizations adopt a variety of risk management techniques.
 - ❑ Some professionals and organizations use avoidance as a risk-control technique.

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Healthcare Liability Insurance

- ❑ Healthcare professional liability policies cover liability for injury resulting from rendering of, or failure to render, professional services.
- ❑ Professional services can include:
 - ❑ Acts performed in the course of treatment.
 - ❑ Postmortem procedures.
 - ❑ Service as a director or chief of a hospital.
 - ❑ Service on a formal accreditation board.
 - ❑ Good-faith reporting of improper conduct.

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Healthcare Liability Insurance

- ❑ Some policies split coverage into two insuring agreements:
 - ❑ First agreement covers individual healthcare professional(s) named in the policy.
 - ❑ Second agreement covers the entity of which professionals are stockholders or partners.
 - ❑ Entity coverage is provided only when claim arises out of the acts of the practitioners.
- ❑ Some policies also cover employees.

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Healthcare Liability Insurance

- ❑ Coverage territory for is usually worldwide, provided the claim or suit is brought within the U.S. or Canada.
- ❑ Some policies include very few exclusions, such as:
 - ❑ Criminal acts.
 - ❑ Contractual liability.
 - ❑ Workers compensation.
 - ❑ Professional services rendered by others.

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Practice

- ❑ To obtain informed consent, the physician is required to disclose to the patient information regarding:
 - ❑ A. Available insurance to cover hospital or clinic charges.
 - ❑ B. The costs associated with the proposed procedure or treatment.
 - ❑ C. The patient's legal rights and remedies if the treatment is unsuccessful.
 - ❑ D. The nature of the patient's condition or problem.

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**Financial and Legal
Professional Liability**

Objective V

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Legal Foundations of Liability

- ❑ Financial professionals include accountants, attorneys, insurance agents, and brokers.
 - ❑ Policies for financial and legal professionals cover liability for financial harm resulting from errors and omissions.
- ❑ Professional liability claims can be based on:
 - ❑ Statutes.
 - ❑ Breach of contract.
 - ❑ Tort principles.

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Statutory Liability

- ❑ Employee Retirement Income Security Act (ERISA) of 1974.
 - ❑ Sets minimum standards for most private-industry pension and health plans.
 - ❑ Requires fiduciary responsibilities for administrators.
 - ❑ Requires administrators to provide additional plan information to participants.
 - ❑ Gives participants a grievance process and the right to sue for breaches of fiduciary duty.

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Statutory Liability

- ❑ Sarbanes-Oxley Act (SOX) of 2002.
 - ❑ Enacted in response to corporate scandals.
 - ❑ Imposes additional requirements on accountants, auditors, and attorneys.
 - ❑ Created Public Company Accounting Oversight Board to oversee auditors of publicly-traded companies.
 - ❑ Requires certification of corporate financial statements by CEO and CFO.
 - ❑ Subjects officers to criminal penalties for failing to fulfill its requirements.

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Statutory Liability

- ❑ Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.
 - ❑ Most comprehensive overhaul of financial regulation since the Great Depression.
 - ❑ Introduced comprehensive regulation of financial markets.
 - ❑ Contained consumer protection measures.
 - ❑ Demands transparency and accountability for financial derivatives.

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Third-Party Claims

- ❑ A third party can assert breach of contract or a tort claim.
 - ❑ A third party is someone that is not a direct party to the contract.
 - ❑ Third party must prove they were an intended beneficiary of the contract.
- ❑ Example – investor who relied on a misleading financial statement could assert the accountant breached the contract with the organization.

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Bad Faith

- ❑ Allegation of bad faith is a potentially severe professional liability loss exposure for insurers.
 - ❑ Can be asserted because of an insurer's denial of coverage without cause.
 - ❑ Can result in extracontractual damages, punitive damages, or both.
- ❑ Declining to accept a reasonable offer to settle a liability lawsuit can lead to bad faith.
 - ❑ Insurer might be required to pay entire court award even if it exceeds the policy limits.

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Avoidance of Bad-faith

- ❑ Steps to avoid bad-faith awards:
 - ❑ Do not misrepresent policy coverages.
 - ❑ Respond promptly to claimants.
 - ❑ Thoroughly investigate all claims.
 - ❑ Outline reasons a claim is being rejected.
 - ❑ Document what is important in evaluating a claim.
 - ❑ Advise the insured as soon as possible about the possibility of a judgment in excess of policy limits.

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Professional Liability Insurance

- ❑ Insurers develop their own legal and professional liability policy forms.
 - ❑ Separate policies for various professions.
 - ❑ Almost always have claims-made trigger.
- ❑ Insuring agreement covers losses resulting from the insured's professional services.
 - ❑ Clear definition of what is included and excluded is needed for both the insured and the insurer.

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Exclusions

- ❑ Typical exclusions in professional policies:
 - ❑ Bodily injury and property damage.
 - ❑ Dishonest, fraudulent, or criminal acts.
- ❑ Reasons these exclusions exist:
 - ❑ Usual consequence of a financial or legal professional error is financial harm.
 - ❑ These claims are covered under other commercial policies such as the CGL.

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Exclusions

- ❑ Policies can also contain exclusions for:
 - ❑ Claims for liability under ERISA or any securities laws.
 - ❑ Punitive damages or fines.
 - ❑ Claims made by or against a business enterprise not named in the policy.
 - ❑ Liability assumed under a contract.
 - ❑ Claims made by one insured against another.
 - ❑ Loss resulting from investment performance.

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Securities Brokers Insurance

- ❑ Securities brokers and dealers professional liability policies.
 - ❑ Insure the firm and registered representatives for claims alleging negligence and errors.
- ❑ Also typically cover firm's liability for:
 - ❑ Selecting products for sale.
 - ❑ Oversight of registered representatives.
 - ❑ Implementation of compliance and supervisory procedures.

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Insurer Liability Insurance

- Insurer professional liability insurance.
 - Often referred to as insurance company errors and omissions (E&O) liability coverage.
 - A major loss exposure for insurers is allegations of bad faith that can result in extra contractual payments.
 - Can cover claims for liability arising from claim handling and safety inspections.
 - May include coverage for punitive and exemplary damages.

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Practice

- The Sarbanes-Oxley Act of 2002:
 - A. Enhanced financial disclosure requirements for privately-held corporations.
 - B. Created a regulatory organization that audits publicly-traded corporations.
 - C. Requires corporate officers to guarantee financial statements do not contain errors.
 - D. Subjects officers to criminal penalties for failing to fulfill its requirements.

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Architects and Engineers Professional Liability

Objective VI

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Legal Foundations

- ❑ Professional liability claims against architects can be asserted by members of the public.
- ❑ More common allegations against architects:
 - ❑ Practicing beyond the scope of the license.
 - ❑ Breach of contract.
 - ❑ Conflict of interest.
 - ❑ Negligent preparation of plans or designs.
 - ❑ Negligent selection of materials/equipment.
 - ❑ Negligent supervision of construction.
 - ❑ Liability to other parties.

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Statute of Limitations

- ❑ Loss exposures of architects and engineers can be affected by statutes of limitations and statutes of repose.
 - ❑ All states have statutes of limitations.
 - ❑ Generally does not begin to run until the negligence is discovered.
- ❑ Statute of repose requires a plaintiff to file a lawsuit within a specific time period after a wrongful act.
 - ❑ Enacted by a number of states.

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Risk Control

- ❑ Hold-harmless agreements are almost universally used as a noninsurance risk transfer technique by architects and engineers.
 - ❑ Standard contracts contain detailed hold-harmless agreements.
- ❑ Standard of care for most professionals is ordinary and reasonable skill.
 - ❑ Some project owners request that contract language be changed to require highest professional standards.

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Architects Liability Insurance

- ❑ Insurer typically pays damages resulting from services as an architect or engineer.
 - ❑ Professional services are usually limited to those services that the insured is legally qualified to perform.
 - ❑ In some cases, the policy also covers the insured's subcontractors.
- ❑ Virtually all policies are written on a claims-made basis, and defense costs are usually payable within the limits of liability.

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Exclusions

- ❑ Policy exclusions are similar to those found in other types of professional liability policies.
 - ❑ Discrimination, punitive damages, or dishonest or criminal acts.
 - ❑ Other exclusions are designed to eliminate overlaps with the CGL, business auto, or workers compensation policies.
- ❑ Coverage is usually excluded for projects where any construction is performed by the insured.

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Other Provisions

- ❑ Policies are ordinarily subject to a per claim limit and an annual aggregate limit.
 - ❑ Deductible normally applies to each claim.
- ❑ Coverage territory is often worldwide.
 - ❑ Suit must be brought in the U.S. or Canada.
- ❑ Many policies provide that disputes between the insured and insurer be settled by binding arbitration.

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Design-Build Projects

- Design-build firm is usually led by a contractor.
 - Either has in-house architects or contracts with independent firms for these services.
- Design-build projects do not fit neatly into standard insurance policy coverage.
 - CGL policy excludes professional liability.
 - Project-specific policies that combine professional and general liability coverage in one policy usually provide a solution.

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Practice

- The roof of a new building collapsed due to lack of structural support. It was determined that the building was constructed in accordance with the architect's blueprint. In an attempt to recover their losses, the building owner could assert:
 - A. Negligent supervision of construction.
 - B. Conflict of interest.
 - C. Negligent preparation of plans or designs.
 - D. Breach of contract.

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