Economic conditions are forcing businesses, including professional services firms, to cut costs. Inevitably, spend on professional indemnity (PI) insurance is being scrutinised at a time when challenging fiscal conditions, rising claims and increasing reinsurance rates could impact premiums. To assist your clients with budgeting, it may well assist to provide an overview of current PI market conditions.

Looking firstly at surveyors, notifications and claims against this profession have increased and currently total in excess of £500 million. The majority of claims relate to allegedly negligent valuations for lending. Around 60 per cent of matters are reaching settlement and insurers are experiencing loss ratios above 100 per cent.

Consequently, insurance capacity has reduced for firms that have done valuations for lending, and rates are at between five per cent and 15 per cent, although premiums for all other surveying disciplines are generally competitive.

Anxiety regarding valuations will continue until 2013; six years past the peak of the property market and outside the Statute of Limitations. With some insurers predicting a further rate increase if lenders continue to pursue valuers, the outlook remains bleak, and if interest rates rise it is likely to worsen.

Spotlight on solicitors
There’s been a steep rise in claims against solicitors with an estimated 60 per cent of notifications arising from property related matters. Consequently, conveyancing practices, particularly smaller firms, have seen a steep rise in premiums with some firms paying 20 per cent of fee income for cover. At the time of writing, the addition of capacity through unrated security, particularly in the SME end of the market, suggests that the post-October 2011 Assigned Risks Pool (ARP) may be a fraction of the size of previous years.

Elements of the Law Society Review of Solicitors’ PI will take effect in 2011 and 2012, but one of the major concessions to insurers, the disbandment of the ARP, will not impact until 2013. It remains to be seen whether insurers’ other requests, including the ability to cancel policies where premiums go unpaid and void policies for fraud and misrepresentation, will be met. While this would encourage new capacity, the Solicitors’ Regulatory Authority (SRA) has so far stood firm in the face of demands.

The riskier areas of the legal and surveying industries should be aware that if capital is diverted from the PI market, because of a rise in reinsurance rates resulting from global catastrophes, they will be hit first and hardest.

What about the broking sector?
Rates and terms remain competitive but major insurers have stopped aggressive undercutting which has halted the premium falls of the past five years. New capacity bucks this trend but the cover available is usually more restricted. Insurers are seeing a greater frequency of claims, often arising from underinsurance in respect of property and business interruption and failure to explain warrantees sufficiently. This may lead to a gradual hardening of premiums although it is too early in the cycle to provide clarity.

Premiums for independent financial advisers have fallen by 60 per cent since the market was at its hardest in 2003/4 and new capacity means that competition remains high and rates low. However, the soft market is at odds with economic conditions and the expectation of high volumes of claims arising from investment losses. If the UK economy enters a double-dip recession, PI buying could get a lot harder.

There is also uncertainty about the impact of the Retail Distribution Review on PI rates with a lack of clarity surrounding insurers’ rates for the two categories of advisers; Restricted and Independent. Most advisers want to be categorised as ‘Independent’ but this category could carry a higher risk rating. Some have suggested that unless ‘Independents’ advise on, and document, all available products for every client, they could be liable if any investment they don’t mention out-performs the recommended product.

Subsequently, there may be some benefit in being a less glamorous ‘Restricted’ adviser. Conversely, the fact that the RDR introduces tougher guidelines should, over the longer term, lead to a fall in claims which may impact positively on premiums.

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