

# Stop Loss

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## HOW YOUR PREMIUMS ARE CALCULATED

LawCover sets out to collect a certain amount of money each year – the ‘premium pool’. This premium pool takes a number of factors into consideration: by far the largest contributor is our actuary’s projection of the likely claims costs arising from all law practices for the year, followed by the cost of reinsurance to protect the scheme against higher than anticipated or catastrophic claims costs, and the cost of maintaining the scheme as a whole (the administrative, regulatory and compliance costs associated with being an APRA regulated insurance company providing insurance, claims handling and risk management services to the profession). Any surplus generated by LawCover is available to fund future premiums, as occurred in 2009/2010 when premiums were subsidised by 4.5 per cent (see May 2009 *StopLoss*).

### Gross Fee Income vs Head Count

LawCover calculates a law practice’s Professional Indemnity Insurance (PII) premiums primarily on the Gross Fee Income (GFI) generated by the law practice. This is generally accepted globally as a principal indicator of risk for all classes of PII. The claims experience and risk management or practice management certification of each practice are also taken into account. Most law practices can reduce premiums further by selecting a higher excess.

After extensive consultation and with the overwhelming support of the profession, LawCover moved away from the ‘head count’ method of calculating premiums in 2002/2003, in favour of GFI. Prior to 2002/2003, calculating premiums by head count would result in a sole practitioner with no employees earning \$100,000 per year paying exactly the same premium as, for example, a sole practitioner with five employees (paralegal and support staff, not solicitors) earning \$1,000,000 per year. It has remained the profession’s opinion that this is

not an equitable allocation of the overall premium pool. These two examples do not reflect the same level of risk of claims activity and therefore should not generate the same levels of premium.



*Paul McGaben,  
Chief Executive Officer*

LawCover adjusts premiums for each dollar of GFI, rather than relying on a series of ‘income bands’. This avoids the abrupt increases or decreases in premium that may be experienced by practices as they move from one band to another.

LawCover’s approach is more complicated than either the ‘head count’ or ‘income band’ methods but more precisely adjusts premium as GFI moves upwards or downwards. LawCover uses a consulting actuary to review claims experience by GFI and to fit a premium rating curve, moving from the lowest level of GFI to the highest level of GFI, for all insured law practices.

Some examples of premium rates for different levels of GFI are as follows (with clean claims records and risk management/practice management discounts):

| GFI (GROSS FEE INCOME) | BASE PREMIUM (NSW) | DISCOUNTS* | NET PREMIUM | PREMIUM (INCL TAXES) |
|------------------------|--------------------|------------|-------------|----------------------|
| \$100,000              | 8,757.30           | -2,189.32  | 6,567.98    | 7,586.01             |
| \$250,000              | 14,528.02          | -3,632.00  | 10,896.01   | 12,584.89            |
| \$500,000              | 25,332.61          | -6,333.15  | 18,999.46   | 21,944.38            |
| \$1,250,000            | 52,120.38          | -13,030.21 | 39,090.62   | 45,149.66            |
| \$2,500,000            | 81,285.88          | -20,321.47 | 60,964.41   | 70,413.89            |

*\* discounts of up to 25 per cent are available for risk management certification and no or low-claims bonuses*

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# LAWCOVER'S RISK MANAGEMENT PROGRAMS REDUCE CLAIMS COSTS



*Paul McGaben,  
Chief Executive Officer*

LawCover undertakes a variety of risk management activities with the aim of educating practitioners on how to avoid or reduce claims prone situations and therefore professional negligence claims. As a provider of Compulsory Professional Indemnity Insurance (PII), it is in LawCover's interests, and obviously our insured solicitors' interests, to reduce both the incidence and overall cost of professional negligence claims. A reduction of the cost of claims against the LawCover Scheme translates directly into a reduction of the cost of PII premiums for all law practices.

In an attempt to measure the effectiveness of LawCover's risk management activities, we instructed the actuarial firm Finity Consulting to undertake a study of LawCover's risk management activities and to measure the benefits of the activities in financial terms.

The study has focused on the following major risk management activities:

- Risk Management Education Program (RMEP);
- Practice Advisory Service (PAS); and
- Adverse Risk Category (ARC)

and on measuring the size and frequency of claims for law practices participating in those activities over time and making comparisons with the LawCover average.

## **Risk Management Education Program**

Attendance by all principals of a law practice at relevant RMEP courses has been shown to reduce claims against the practice by 25 per cent in claim size and 10 per cent in the number of claims. This translates to an estimated saving to the LawCover Scheme over the last seven years of around \$1 million per year.

## **Practice Advisory Service**

The PAS is a voluntary risk management consulting service offered to law practices that have higher than average claims costs.

Nineteen practices have participated in the service since 2003. Of the law practices that have participated in the PAS, loss ratios (that is, the ratio of claims costs to premiums collected) have improved dramatically – from over 600 per cent to less than 100 per cent. Finity Consulting estimates a reduction in claims of \$1.5 million per year as a result.

## **Adverse Risk Category**

Law practices in the ARC (ARC criteria for the 2009/2010 insurance year is available on the LawCover website at [www.lawcover.com.au](http://www.lawcover.com.au)) have average loss ratios 7.8 times higher than the rest of the profession. LawCover requires ARC practices to undertake risk management remediation and imposes significant premium loadings for those practices that refuse to participate or enact suitable recommendations.

The ARC has been in operation since 1 July 2008 and 26 law practices have been selected to participate. While it is too early to accurately determine savings to the LawCover Scheme from these practices successfully returning to a 'non-ARC' average, Finity Consulting estimates the savings may be as high as \$6 million per year.

The size of the savings depends on the extent of the loss ratio improvement and the speed at which change can be achieved. LawCover is working closely with ARC law practices to help improve their risk management practices.

LawCover remains committed to reducing the cost and frequency of claims, and therefore the overall cost of PII premiums for all insured solicitors.

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## **HOW YOUR PREMIUMS ARE CALCULATED** *continued from previous page*

### **Why are LawCover premiums different to other States?**

Premiums vary from State to State for two major reasons. First, each State determines its premiums on the claims experience of solicitors in that State and second, each State calculates premiums for individual legal practices using different rating methods (for example, head count or income bands as discussed previously). The different incidence and cost of claims in each State is driven by the particular commercial, social and legal environments of that State.

### **How do we reduce premiums?**

First and foremost, all solicitors in NSW must continue to strive to reduce the incidence and cost of claims, the effect of which will reduce the premiums charged to the profession. As the article above shows, LawCover's risk management services have been proven to reduce both the size and frequency of claims.

For more information on risk management education and how your law practice can reduce the risk of claims, visit the LawCover website at [www.lawcover.com.au](http://www.lawcover.com.au)

# THE LAWCOVER CLAIMS PANEL



*Peter Driessen  
Chief Claims Solicitor*

Potential claims or circumstances and simple unlitigated claims are handled in-house by LawCover's claims solicitors. Litigated claims and more complex unlitigated matters are referred to LawCover's Claims Panel solicitors.

The Claims Panel as a whole has the capacity and resources to cater for the largest and most complicated matters notified by insureds as well as specialisation in the areas of law that more frequently give rise to claims. The Panel also caters for the many sole and small practices that make up the New South Wales profession.

There are currently ten law practices on the LawCover Claims Panel. The law practices on the Claims Panel reflect the different sizes and nature of the law practices that notify claims, and the claims made against them. This allows LawCover to provide an optimal service to those practitioners facing a claim.

## **How the Claims Panel handles a claim**

Each Panel practice has a team dedicated to doing LawCover work. Claims are referred only to the team, which is lead by an experienced partner who is responsible to LawCover for performance, adherence to the LawCover retainer agreement and compliance with LawCover's reporting requirements.

On being allocated a claim by LawCover, a Panel solicitor will contact the insured to request the relevant papers or file and arrange an interview to discuss the matter. Wherever possible the LawCover claims solicitor with carriage of the matter will also attend the initial interview. It is important that insured practitioners assist in this process, or at least provide a timeframe within which to provide assistance, so as to keep within the deadlines imposed by the litigation process. The Panel solicitor is also required to provide LawCover with a detailed preliminary advice within eight weeks of initial instructions.

LawCover will usually ask the Panel solicitor to provide advice on the insured's entitlement to indemnity under the LawCover PII policy. Even though the Panel solicitor is retained by LawCover to provide such advice, pending a grant of indemnity the Panel solicitor will assist as far as possible to protect the interests of the insured practitioner in relation to the claim.

At either the preliminary advice stage or otherwise early in the litigation process, the Panel solicitor will advise whether the claim is or is not reasonably defensible, and

recommend a suitable claims management strategy. If the claim is defensible, the Panel solicitor will defend the claim as far as is commercially justifiable. If the claim is indefensible, the Panel solicitor is required to explore an early and proactive resolution of the matter.

Panel solicitors are encouraged to visit practitioners in their offices wherever possible and to be conscious of providing a value for money service. One Panel team, based in Newcastle, provides a city and metropolitan service as well as successfully catering to regional and country needs north of Sydney. The goal of having a versatile Panel is so that LawCover can allocate a claim to those teams with the best resources to handle it in an expert, efficient and cost-effective manner.

The team provides the practitioner facing a claim with the benefit of solicitors (at partner, senior associate and other levels) with many years experience in LawCover work as a significant or major part of their practice who are fully acquainted with LawCover's policy wording and with professional indemnity insurance law. They are also fully conversant with LawCover's claims policies and procedures, which are designed specifically to assist legal practitioners through the claim process.

LawCover endorses the use of Alternate Dispute Resolution methods and requires Panel solicitors to consider the most cost-effective and efficient way of managing a claim including identifying or refining the issues in dispute by way of an issues conference, seeking informal discovery and embarking on a negotiation strategy at the earliest opportunity.

## **LawCover's conduct of the claim**

It is important to remember that whilst Panel solicitors act on behalf of the insured practitioner in defending the claim made against that practitioner, the Panel solicitor acts on the instructions of LawCover pursuant to the terms and conditions of the professional indemnity insurance policy with the insured. A key feature of the policy is LawCover's right to conduct the claim, once notified. In the 2009/2010 policy, clause 12(a) provides that LawCover has "*the conduct of a claim against you [the insured], including its investigation, defence, avoidance, reduction or, subject to clause 16, its settlement*". Clause 16 provides that LawCover, often through its Panel solicitor, will seek the insured's consent on whether to proceed to a defended hearing or to settle a claim; and will do so pursuant to a timeframe.

Constructive input from the insured in the management of a claim is welcome and appreciated. Occasionally

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# LAWCOVER CLAIMS STATISTICS UPDATE AT 30 JUNE 2009

The claims statistics in the pie charts (below and below right) show the cost of claims in total incurred value by area of law for the 2007/2008 policy year (1 July 2007 to 30 June 2008) and the 2008/2009 policy year (1 July 2008 to 30 June 2009), as at 30 June 2009.

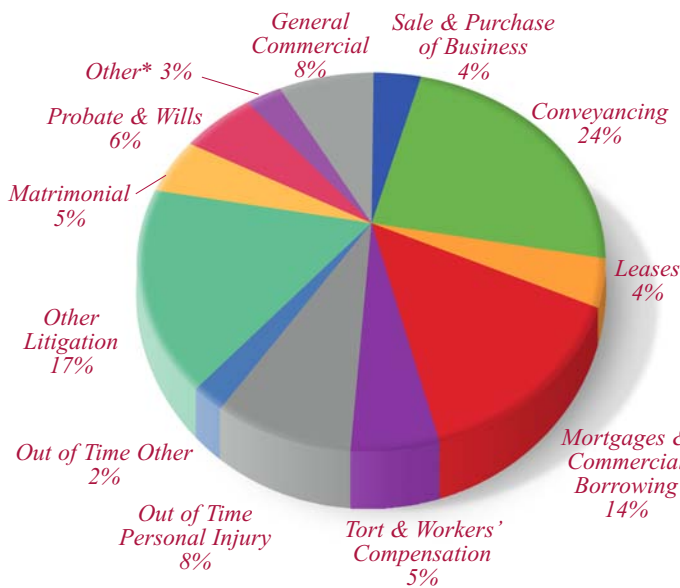
The total incurred is the anticipated cost of each claim comprising the amounts for claim payments, claimants' costs and defence costs. Once the claim has resolved the total incurred is the actual cost of resolving the claim.

The most obvious feature of the statistics is their relative stability for the various areas of law given that the past two policy periods saw the Global Financial Crisis and downturn in the Australian economy.

The business law and conveyancing statistics (General Commercial, Sale & Purchase of Business, Conveyancing, Leases, Mortgages & Commercial Borrowing) taken together show that these notifications made up 54 per cent of the total incurred in 2007/2008 compared with 49 per cent in 2008/2009. This appears to be largely attributable to a decrease in Conveyancing as an area giving rise to claims and may reflect a downturn in property market activity and the consequent claims that arise.

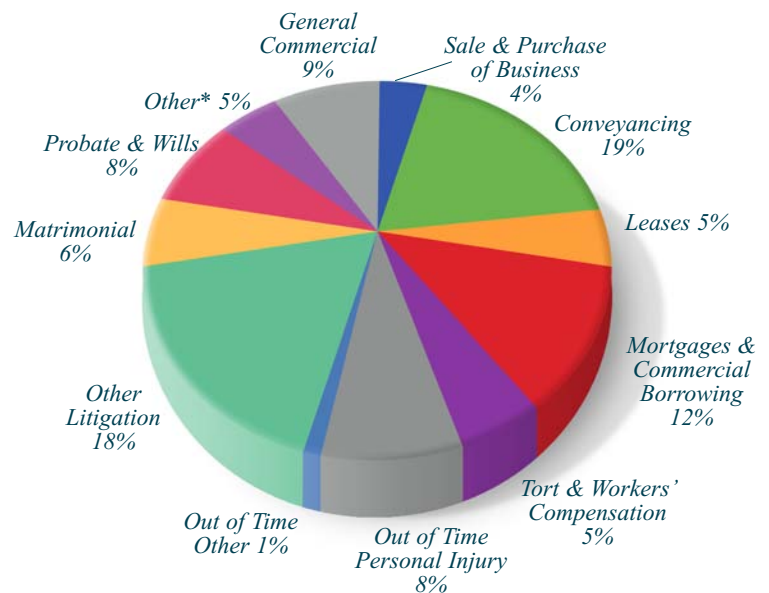
Comparing these statistics with those from earlier periods 2004/2005–2006/2007, the current statistics indicate a significant decrease in Personal Injury related claims including Out of Time claims. These have decreased by more than 50 per cent.

**2007/2008 percentage of notifications  
by Area of Law as at 30 June 2009**



\* Includes: defamation, criminal, revenue & immigration

**2008/2009 percentage of notifications  
by Area of Law as at 30 June 2009**



\* Includes: defamation, criminal, revenue & immigration

## THE LAWCOVER CLAIMS PANEL

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insureds can make demands on the Panel solicitor that are unproductive, unreasonable or unlikely to advance the progress of the claim. Panel solicitors are retained by LawCover to determine the most appropriate strategy for the efficient, timely and cost-effective resolution of a claim in the interest of the individual solicitor against whom the claim has been made as well as in the interests of the LawCover Scheme taking into account the NSW profession as a whole.

Many actual or potential claims can be managed successfully, if they are dealt with quickly. As soon as you become aware of an actual or potential claim, ring LawCover on **02 9264 8855** and ask to speak to a claims solicitor.

Generally, the notification of circumstances will not contribute to or generate a claims loading for a law practice, nor will it impact on a law practice's no-claim bonus. Even notifying a claim of modest proportions may not have an impact on your no-claim bonus.

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