



MARSH



Financial Advice
NEW ZEALAND

A FINANCIAL ADVICE NEW ZEALAND MEMBER PUBLICATION

Understanding Professional Liability Insurance: A Friendly Guide for Advisers



MARSH & MCLENNAN
COMPANIES

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Introduction

Financial Advice New Zealand is very proud of its Liability Programme – a programme developed by Financial Advice New Zealand for its members. The ongoing partnership we have with Marsh and NZI is a key component to this programme and is greatly valued by Financial Advice New Zealand. It is important that we have a cost effective, sustainable, and comprehensive Liability Programme for our members.

This Friendly Guide to Liability has been produced by Marsh, with much assistance from Financial Advice New Zealand, and the insurer NZI. It is designed to enhance your knowledge and understanding of liability insurance.

Please take the time to read this and do retain it as a reference tool. Like all our Friendly Guides, they are designed as working documents – and as feedback is received from members, or it requires updating due to the inevitable changes that occur in our industry, this document will be updated.

For more information on the key benefits of the Financial Advice New Zealand's Liability Programme, please refer to page 16 of this guide: 'Why place your risk with the Financial Advice New Zealand Liability Programme?'.


Purpose of guide on professional liability insurance

This guide is designed primarily to explain the risks associated with providing professional advice, describe how an insurance programme can help minimise these risks to your business, and equip you with some knowledge around what your liability insurance programme should provide you and your business.

It does not replace the terms and conditions applying to any of the insurance products described herein. In the event of a claim, coverage will be subject to the full terms of the insurance policies in place. For a copy of the policy wordings, please contact Financial Advice New Zealand.

For the sake of this guide we refer to advisers without limitation as Life Agents, Investment Advisers, Financial Planners, Mortgage Writers, Consultants and Advisers in the sale of any financial product or advice.

The risk

Professional consulting businesses such as financial advisers and mortgage writers, like any individual providing specialist expertise, are under pressure to perform cost-effectively and responsibly. Professionals are expected to be accountable for their advice.

Disputes over the services provided by a financial adviser are a real possibility, and with changes in legislation the avenue for clients to make complaints or hold advisers accountable has never been more real.

Any potential liabilities that may arise can be financially crippling, and any such complaint can lead to costly litigation, damages being awarded and loss of reputation.

Insurance is not a substitute for good management practices, risk management and disciplines. It is a safety net for those occasions when mistakes and oversights occur – regardless of the controls and safeguards that have been put in place.

How advisers can be exposed

Exposure to the possibility of legal action can occur in a number of ways. Advisers primarily owe a duty of care to their clients; by law this is:

“A financial adviser, when providing a financial adviser service, must exercise the care, diligence and skill that a reasonable financial adviser would exercise in the same circumstances”¹. This duty has become much wider under the new Financial Services Legislation Amendment Act and the Financial Advice Code.

Any loss suffered, as a result of a breach of that professional duty, can form the basis of a claim for damages. This claim might come from a client under the terms of a contract (where the adviser is legally liable for the loss), or alternatively, it might come from third parties who maintain that they have been adversely affected by the advice given.

BEAR IN MIND THAT CLAIMS CAN BE MADE MANY YEARS AFTER THE ADVICE WAS PROVIDED.

See notes on Claims Made Policies.

¹ Section 33 of the Financial Advisers Act 2008, <http://www.legislation.govt.nz/act/public/2008/0091/latest/dlm1584671.html>

Section 1: Professional Indemnity Insurance

What is it?

The purpose of Professional Indemnity insurance is to cover a professional person or company for claims made by a third party alleging financial loss due to a breach of professional duty.

A Professional Indemnity policy includes cover for the:

- claim for compensation; and
- costs and expenses associated with defending such an allegation,

thus protecting you against the financial strain of litigation.

It is the opinion of Marsh, the Financial Advice New Zealand's insurance advisers, that with the level of cover provided by programmes in the market such as the Financial Advice New Zealand's Liability Programme, the exposure to an adviser's business is much greater compared with the price to transfer this risk to an insurer.

BASIC COVERAGE:

Covers legal liability to third parties arising from the provision of professional advice.

THE POLICY IS TRIGGERED BY:

A claim for compensation arising out of the Professional Business.

Operative clauses – What does it cover?

There are two main types of Professional Indemnity insurance policies in the marketplace: Civil Liability and Negligence wordings.

Most Professional Indemnity policies written in New Zealand are Civil Liability wordings; they provide cover for a person's legal liability based on a breach of contract, tort, and breach of statute.

A Negligence wording would only cover actions against an adviser based on the tort of negligence. There is no cover for breach of contract or a breach of statute as covered under a Civil Liability wording.

The operative clause or insuring clause of any policy will state whether the policy is written on a Civil Liability or Negligence wording. A typical operative clause would read:

"The Insurer shall indemnify the Insured for a breach of Professional Duty arising from"

Generally a Negligence wording will differ at this point and read something similar to:

any negligent act, error or omission committed or alleged to have been committed..."

A Civil Liability wording would instead read: *"any Civil Liability"*.

CIVIL LIABILITY WORDING:

Works on the principle "it's covered unless excluded".

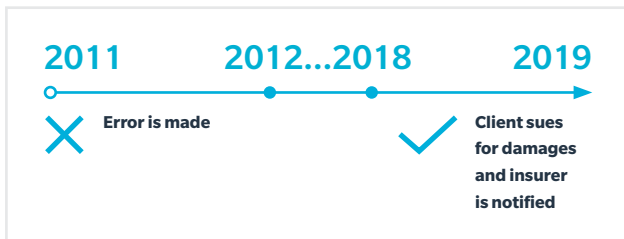
NEGLECTANCE WORDING:

The claimant must allege negligence.

Claims made?

Professional Indemnity insurance, along with the majority of other liability insurances, are claims made policies. This means it is the policy in force at the time a claim is made that will respond and not the policy in force when the work was undertaken or advice given. The policy is triggered when a claim, or circumstance which could give rise to a claim, is first made against the adviser and notified to the insurer during the period of insurance.

This differs from most other insurance policies where they operate on an occurrence basis, that is, the policy is triggered when the insured event occurs.



In the claim diagram example above, an adviser becomes aware in June 2018 that a client is seeking to hold them liable for an error that occurred in handling their business in 2011.

An occurrence wording would apportion the claim back to the policy that was in force at the time of the error, the 2011 policy.

However under a claims made policy, it is the policy in force at the time the claim is first made and notified to the insurer which will respond. In this example, this would be the 2018 policy, provided that there has been continuous cover in place or the current policy has a retroactive date, of prior to 2011.

THE FINANCIAL ADVICE NEW ZEALAND PROFESSIONAL INDEMNITY POLICY has an “Unlimited” retroactive date meaning the policy will cover a claim first made and reported during the policy period regardless of when the wrongful act occurred, providing cover has been held continuously (even with other insurers). This is the broadest cover available.

What is a claim?

The definition of a Claim, which can be further defined in a policy as a Valid Claim, differs from insurer to insurer and programme to programme.

This is also where some insurers differ in the way that their policies respond to the regulation around complaints and disputes.

The standard definition of a Claim under a Professional Indemnity policy would read something like;

Claim means;

- a. Legal proceedings instituted and served upon the Insured, or*
- b. Any threat or intimation that legal proceedings will be issued against the Insured.*

Inclusion of a Valid Claim definition would further define a Claim to be a claim which is first made against an insured, and notified to the insurer during the period of insurance, arising out of the Professional Business of the insured. The Financial Advice New Zealand Professional Indemnity policy contains a Valid Claim definition.

Some insurers have taken a pragmatic approach to the regulations and extended their definition of a Claim to include:

A complaint made to an approved dispute resolution scheme or to the reserve scheme under the Financial Service Providers (Registration and Dispute Resolution) Act 2008 or any replacement legislation.

This is the approach that NZI, the Financial Advice New Zealand’s Liability Programme insurer, has taken and in effect this extends the full Professional Indemnity policy to cover complaints and disputes as it would a traditional claim through the courts.

By contrast other policies and programmes in the market have taken the approach of treating complaints to a dispute resolution scheme as an extension to a Professional Indemnity policy, with a sub-limit of indemnity available for such claims.

IT IS IMPORTANT THAT AS AN ADVISER YOU UNDERSTAND THE EXTENT TO WHICH YOUR POLICY PROVIDES COVER.

Some programmes in the market also provide extensions or additional benefits that provide an agreed daily benefit to an adviser who is required to attend either a dispute hearing or court as part of a claim investigation or settlement proceeding. These are usually nominal benefits and are intended to go only part way to compensating an adviser for the time and effort needed to prepare and defend a proceeding against them.

THE PROFESSIONAL INDEMNITY POLICY included within the Financial Advice New Zealand Liability Programme provides cover for court and dispute resolution attendances, subject to a sub- limit of indemnity.

Section 2: The Policy Schedule

The policy schedule contains information that is specifically agreed with the insurer of your policy. Below is a description of the key aspects of a common policy schedule.

Professional business – What advice am i covered for?

A Professional Indemnity policy provides cover for a claim for compensation arising from an adviser's Professional Business, or Insured Business or Business Description. The term differs between underwriters; however this is one of the most important parts to any adviser's Professional Indemnity policy.

The policy will provide cover for the activities which are expressly contained in this phrase most commonly noted on the schedule of insurance. If a claim arises from an activity not included in the Professional Business description, then no cover will be afforded under the policy.

Therefore, this description should be fully inclusive of all activities undertaken by an adviser and include all areas where revenue or fee income is generated both previously and currently.

The Professional Business description should not only encompass an adviser's current activities, but also work undertaken in the past. This is important given the claims made nature of Professional Indemnity insurance discussed in the previous section. The Professional Business description should be reviewed regularly to ensure it is accurate, especially in light of any changes in legislation that may impact on an adviser's activities.

Commonly the Professional Business description will be quite explicit in naming the activities, and the extent to which an adviser can undertake certain activities.

For example, some policies in the market provide cover for advisers referring fire and general insurance only and not undertaking the work themselves.

The wording of the Professional Business description in the Professional Indemnity policy of the Financial Advice New Zealand Liability Programme contains the phrase;

“the sale of any financial product or provision of any financial advice.”

The wider the definition of Professional Business then the broader the cover provided by the policy.

An adviser considering a new aspect to their business should refer to their Professional Indemnity insurance policy and check whether the new activity would be deemed to be covered by the

N21, a business division of IAG New Zealand Limited

Professional Indemnity Insurance

Policy Schedule

Policy Number: 6000018963

Insured: Individual members of the Professional Advisers Association Inc.

Address: C/- P O Box 2221, Auckland

Policy Wording: PAA PI 2015

Period of Insurance: From: 1 October 2015 - 4pm local time
To: 1 October 2016 - 4pm local time

Insured Business: General Insurance Brokers, Life Agents, Investment Advisers, Financial Planning, and Mortgage Brokers, Consultants and Advisers in the sale of any financial product or provision of any financial advice.

Retrospective Date: Unlimited excluding known claims or circumstances

Territorial Limits: Worldwide

Jurisdictional: New Zealand & Australia

Limit of Indemnity: as per the limit option selected (in the aggregate during the Period of Insurance) by the individual member as paid and declared to N21

Investment Costs and Expenses: as per the limit option selected (in the aggregate during the Period of Insurance) by the individual member as paid and declared to N21

Aggregate Limit of Indemnity: \$30,000,000 in the aggregate during the Period of Insurance

Excess: \$1,000 each and every Claim exclusive of Costs and Expenses
\$5,000 each and every Claim inclusive of Costs and Expenses for Commercial Fire & General Claims

Premium: As agreed

Signed on behalf of N21, a business division of IAG New Zealand Limited:

Signed _____ Date 22 June 2016

Professional Business description or speak with their insurance adviser to identify if cover can be extended. In all cases it is prudent to get professional advice.

What is a retroactive date?

A retroactive date is the earliest date after which losses may occur and be covered under a claims made liability policy.

There are generally two types of retroactive dates which apply to all policies, a specified date, or an Unlimited date.

If the policy contains a specific retroactive date this means that any claims arising from an act, error or omission occurring before that specified date are not covered by the policy. The most common specified date is “policy inception”. This is common for professionals who have been operating in business for a period of time and purchase Professional Indemnity insurance for the first time.

Having an Unlimited retroactive date is the broader of the two, and means cover is provided for claims regardless of when the act, error or omission occurred.

The retroactive date applying to the Financial Advice New Zealand Professional Indemnity policy is Unlimited.

Territorial and jurisdictional limits

A liability policy contains two geographical limits;

Territorial Limits are the geographical area where the policy will cover the adviser undertaking work. If an act, error or omission occurs outside the policy's specified territorial limit then there is no cover.

Jurisdictional Limits are where and under which Court of Law a claim may be heard. Where a Jurisdictional Limit is New Zealand and Australia, the claim must be brought in either of those two countries' courts.

The Financial Advice New Zealand Professional Indemnity policy has Territorial Limits of Worldwide and Jurisdictional Limits of New Zealand and Australia.

Limits of indemnity

The Limit of Indemnity is effectively the sum insured under the policy: it is a nominated value of cover the client has elected to purchase.

While some carriers or product providers have a minimum level of cover which they require advisers to hold, there is no standard limit that an adviser must carry.

The selection of a policy limit must be an individual's decision. Some factors that an adviser must consider are:

- The product mix or types of advice undertaken;
- The demographics of your client base, for example a younger client base has potential for larger financial loss if a policy is not executed correctly;
- Peak risk versus Aggregate risk;

A Limit of Indemnity will contain two types of Limit, a Limit Any One Claim, and a Limit in the Aggregate.

The Limit Any One Claim is the maximum that the policy will cover for one claim or circumstance, and the Aggregate is the annual limit for all claims in any one policy period. It is important to note that claims arising from the same, causally connected or interrelated acts, errors or omissions are typically treated as one Claim under the policy.

Some financial adviser programmes in the market have a shared limit across all advisers in the programme – meaning the limit in the aggregate could be subject to many advisers claims and could jeopardise the cover available for advisers within these programmes as the cover would be available on a 'first in, first served' basis.

A PROFESSIONAL INDEMNITY POLICY MAY HAVE A LIMIT OF INDEMNITY OF:

\$2,000,000 any one claim and \$4,000,000 in the aggregate.

Therefore the adviser could have eight claims of \$500,000 during the policy period, or 1 claim of

\$2,000,000, as well as 2 claims of \$1,000,000, as long as any one claim does not exceed the \$2,000,000 limit. The maximum amount available for all claims brought during the policy period is \$4,000,000.

Other programmes such as the Financial Advice New Zealand Liability Programme have individual limits selected by each adviser applying to their Professional Indemnity policy, with an excess layer sitting above the individual adviser limits which is shared across all advisers in the programme.

THE FINANCIAL ADVICE NEW ZEALAND PROFESSIONAL INDEMNITY POLICY HAS A SHARED EXCESS LAYER OF:

\$10,000,000 Any One Claim and \$30,000,000 in the Aggregate.

Therefore the adviser could have all of the claims in the example above, and then have access to the programme's shared excess layer – which provides a further Limit of Indemnity of \$10,000,000 for any one claim, and \$30,000,000 in the aggregate.

Excess or deductible

There are two common types of excess structures for liability policies:

- Costs Inclusive, or
- Costs Exclusive

A Costs Inclusive excess structure means that at Day 1 of a claim or circumstance being notified to the insurer the adviser would have to contribute to the costs and expenses incurred in defending a claim regardless of whether the claim ever reaches a settlement.

In comparison, a Costs Exclusive excess structure means that an adviser would not contribute the excess towards a claim until there was a settlement made (or judgment awarded). The insurer would settle all of the costs and expenses associated with defending the claim from Day 1 of the notification of the claim or circumstance.

The benefit of a Costs Exclusive excess structure is that if a claim or circumstance is notified and the insurer elects to appoint legal counsel to investigate and over a period of time the claim is dropped or is not taken further, then the adviser would not have to pay their excess as there has been no settlement.

THE FINANCIAL ADVICE NEW ZEALAND PROFESSIONAL INDEMNITY POLICY HAS A COSTS EXCLUSIVE STANDARD EXCESS OF \$1,000.

Note: For Commercial Fire & General activities, and Share Broking activities this excess becomes \$5,000 Costs Inclusive.

It should be evident that the Costs Exclusive excess structure is more beneficial to an adviser and any Costs Inclusive excess structure should be reflected in the policy's premium.

Section 3: Common Extensions to a Professional Indemnity policy

Below is a brief description of the common extensions found in a Professional Indemnity policy:

- **Fair Trading Act** – consumer protection legislation is becoming increasingly evident in litigation against financial advisers. Cover is extended under the Professional Indemnity policy for sections 9 – 14 of the Act, which refers to misleading and deceptive conduct and false representations.
- **Defamation** – the cover is extended to include unintentional defamation either written or spoken. However, these unintentional acts must relate back to the Professional Business undertaken by the adviser.
- **Intellectual Property** – cover is also extended to include the unintentional infringement of copyright, trademarks, designs or unintentional breach of confidentiality.
- **Joint Venture Liability** – cover can be extended to include advisers' joint venture activities, so long as these activities are declared and agreed by the insurer. Cover is usually limited to the adviser only, and does not extend to insure the other joint venture parties.
- **Dishonesty of Employees** – the policy extends to cover the dishonest, fraudulent, criminal or malicious acts of an employee, causing a loss to a third party triggering a claim against the insured.
- **Loss of Documents** – cover for any claim arising from legal liability in connection with the loss, damage to or destruction of documents that were in the care, custody and control of the insured.
- **Consultants and Sub-Contractors** – cover is provided for claims against the insured arising out of the actions of consultants. Note: cover does not extend to the consultant him/herself without specific agreement.
- **Outgoing Principals, Partners, Directors and employees** – covering the liabilities of those various people who have now left the business for work done by them whilst there.
- **Acquisitions and Creations** – cover is extended for a specific period of time giving temporary cover to disclose these new entities to the insurer for their agreement.

The specific period of cover can differ between insurers.

Section 4: Complete Liability Protection

Professional Indemnity insurance is an essential part of a professional's insurance programme; however it is not just an adviser's advice where a claim or error could arise.

Organisations in New Zealand are exposed to a number of liability risks. Examples of the types of liability your business could face are:

- Causing damage to another person's property
- Breaching a legal statute such as the Resource Management Act
- Dealing with a personal grievance from an employee
- Causing damage or injury through a failure of a service you are selling.

The Financial Advice New Zealand Liability Programme is much more than just Professional Indemnity protection, and the covers included in the programme are briefly described below.

Public liability

This policy insures an adviser for the compensation they become legally liable to pay for personal injury or property damage suffered by a third party. Additionally, it will pay the costs and expenses of investigating, negotiating and defending the claim.

Liability can arise under common law or statute from many sources including:

- Premises occupied
- Work in other parties' premises
- Loss or damage to goods in care, custody or control.

UNDER THE FINANCIAL ADVICE NEW ZEALAND LIABILITY PROGRAMME, THE LIMIT OF INDEMNITY IS \$5,000,000 IN THE AGGREGATE PER ADVISER.

Employers liability

This policy provides financial compensation to help employers against common law claims (capable of being brought in a New Zealand court) which they may be liable to pay for personal injury sustained by an employee that is not covered by ACC legislation.

The policy indemnifies the insured for compensation or damages they become legally liable to pay, and also covers the costs of investigating, defending or settling such claims.

Defence costs are payable in addition to the policy's limit of indemnity. The separate defence costs limit is equal to the policy limit.

UNDER THE FINANCIAL ADVICE NEW ZEALAND LIABILITY PROGRAMME, THE LIMIT OF INDEMNITY IS \$1,000,000 IN THE AGGREGATE PER ADVISER BUT ONLY APPLICABLE TO THOSE ENTITIES WITH EMPLOYEES.

The types of claims for personal injury that are covered;

- Mental injury or mental anguish without physical injury (e.g. stress)
- Gradually occurring diseases (e.g. chemicals or workplace environment)
- Disease or infection (e.g. legionnaires' disease)
- Non-physical stress or fright (e.g. heart attack or stroke)
- Punitive or exemplary damages.

Statutory liability

This policy protects advisers, and their employees, from prosecution under almost all New Zealand Acts of Parliament where they have unintentionally broken the law and face prosecution, in the ordinary course of their business.

The policy responds to most Acts of Parliament including breaches of the Health and Safety at Work Act, the Resource Management Act, Fair Trading Act and other commercial Acts.

Cover is provided for the fines awarded against an adviser for breaching an Act, together with the associated defence costs.

Defence costs are payable in addition to the policy's limit of indemnity, up to an amount equal to that limit.

With respect to the Health and Safety at Work Act, fines are prohibited from being insured by law, however the Statutory Liability Policy will cover the reparation awards ordered by the courts.

UNDER THE FINANCIAL ADVICE NEW ZEALAND PROGRAMME, THE LIMIT OF INDEMNITY IS \$1,000,000 IN THE AGGREGATE PER ADVISER.

Health and safety changes

The new Health and Safety at Work Act came into effect on 4th April 2016, including new requirements for directors of businesses to ensure health and safety is actively and properly managed. With the government's renewed focus in this area and greater budget for compliance and prosecution, commentators predict there will be increased activity and early prosecutions by Worksafe for unfortunate individuals and businesses that fall under its increasingly fierce spotlight. Defence of regulatory actions can be complex, involve multiple defendants with different interests and take time to resolve, incurring expensive legal costs even where a prosecution is successfully defended. Companies may be legally precluded from paying for the defence of such action on behalf of their directors and officers (unless or until they are acquitted) leaving them personally financially vulnerable in the absence of insurance cover.

Whilst it remains illegal for insurers to cover fines issued under the new Act, Statutory Liability insurance provides cover to businesses, their directors and other specified individuals, for the legal costs in defending an investigation and/ or prosecution and reparations to be paid by the victim (if ordered by the Courts). With the stakes increasing, and the overall regulatory environment for businesses in New Zealand continuing to evolve (health and safety fines being one of the few areas that insurers are legally prohibited from covering in New Zealand), Marsh recommends all businesses – no matter what industry – carry Statutory Liability cover.

CHANGES TO THE ANTI-MONEY LAUNDERING AND COUNTER FINANCING OF TERRORISM ACT 2009 (AML/CFT) – OPTIONAL EXTENSION:

Your insurer NZI has provided optional cover:

The AML/CFT extension provides cover to reporting entities under the Statutory Liability policy for the legal costs incurred in defending any civil actions brought under this Act.

Cover under this extension if taken is limited to \$500,000 for Civil Pecuniary Penalties (which is currently excluded) and \$500,000 for Defence Costs for any one insured Adviser.

Trustees liability

This policy provides cover to individual trustees and office bearers for committing a wrongful act that leads to interested parties such as creditors or beneficiaries suffering a financial loss.

If the trust provides indemnification to the individual in such an event, the policy will pay the loss on behalf of the trust, or if the trust does not provide indemnification, the policy will pay the loss on behalf of the individual.

In response to the 2013 Supreme Court decision in the “Steigrad/Bridgecorp” case [BFSL 2007 Ltd v Steigrad [2007] NZSC 156], a separate, ring-fenced defence costs limit applies in addition to the policy’s Limit of Indemnity. This separate limit is available in the event a section 9 charge under the Law Reform Act 1936 is laid against the policy, thus preserving the full policy limit for compensation. The separate defence costs limit is 100% of the total policy limit, which is shared across the Directors & Officers Liability policy.

UNDER THE FINANCIAL ADVICE NEW ZEALAND LIABILITY PROGRAMME, THE LIMIT OF INDEMNITY IS \$1,000,000 IN THE AGGREGATE PER ADVISER, AND \$12,500,000 IN THE AGGREGATE FOR ALL INSURED. THIS LIMIT IS SHARED WITH THE DIRECTORS & OFFICERS LIABILITY LIMIT.

Directors and officers liability

This policy provides directors and officers of companies with the resources to defend allegations of mis- management while they carry out their day-to-day management duties.

Directors and officers can come under fire from any number of claimants including employees, creditors, shareholders, competitors, regulators and customers.

Directors and officers have duties and obligations, for which they are personally responsible, some of which may carry unlimited personal liability. Such liability can be incurred, not only as a result of their own activities, but also from the activities of fellow directors.

Many companies indemnify their directors and officers through their constitution. When indemnifying a director, a company may incur liabilities that have a severe impact on its bottom line. A Directors & Officers Liability policy will address the concerns and liabilities of both the director, and the company when indemnifying the director.

In response to the 2013 Supreme Court decision in the “Steigrad/Bridgecorp” case [BFSL 2007 Ltd v Steigrad [2007] NZSC 156], a separate, ring-fenced defence costs limit applies in addition to the policy’s Limit of Indemnity. This separate limit is available in the event a section 9 charge under the Law Reform Act 1936 is laid against the policy, thus preserving the full policy limit for compensation. The separate defence costs limit is sub-limited to 25% of the total policy limit, which is shared across the Trustees Liability policy.

UNDER THE FINANCIAL ADVICE NEW ZEALAND LIABILITY PROGRAMME, THE LIMIT OF INDEMNITY IS \$1,000,000 PER ADVISER AND \$12,500,000 FOR ALL INSURED ENTITIES. THIS LIMIT IS SHARED WITH THE TRUSTEES LIABILITY LIMIT.

Legal prosecution defence insurance

This policy covers legal expenses associated with defending any Legal Action alleging an offence under any statute of the offence arising out of their employment with the Insured. The need for protection may arise from:

- Serious Traffic Offences
- Criminal Nuisance
- Assault
- Trespass
- and other breaches of the Crimes Act.

UNDER THE FINANCIAL ADVICE NEW ZEALAND LIABILITY PROGRAMME, THE SUM INSURED IS \$100,000 PER ADVISER.

Employment disputes (Optional)

This policy provides cover for claims brought against an adviser's business by an employee alleging an employment- related wrongful act. Such wrongful acts can include:

- Unjustifiable disadvantage, unlawful discrimination, wrongful unjustifiable demotion, or unjustifiable failure or refusal to promote;
- Actual or constructive termination of an employment agreement, in breach of the law;
- Harassment (sexual or racial or otherwise);
- Invasion or breach of the right of privacy as provided in the Privacy Act 1993.

The excess applying to this policy is \$3,000 per claim (Costs Inclusive), increasing to \$5,000 per claim (Costs Inclusive) where no employment contract exists.

In response to the 2013 Supreme Court decision in the "Steigrad/Bridgecorp" matter [BFSL 2007 Ltd v Steigrad [2007] NZSC 156], a separate, ring-fenced defence costs limit is available in addition to the policy's Limit of Indemnity. This separate limit is available in the event a section 9 charge under the Law Reform Act 1936 is laid against the policy, thus preserving the full policy limit for compensation. The separate defence costs limit is sub- limited to 100% of the total policy limit.

The inclusion of this policy is optional and is not part of the standard Financial Advice New Zealand Liability Insurance programme.

Cyber liability (Optional)

Technology is now an integral part of conducting business. All organisations, regardless of size or industry, face increasingly complex information and computer security risks.

Any company, or individual, who collects data or confidential information (be it personal or commercial information), and relies upon computer networks for day-to-day operations, faces potential risks arising from the cyber world. The nature of the work conducted by advisers, particularly with respect to the personal information obtained from clients, creates a significant exposure to such risks. Cyber Liability insurance has been developed to address the potential gaps in cover which exists within traditional insurance policies.

A Cyber Liability policy, responds not only to third party losses, but also to an adviser's own losses arising from a business interruption caused by a cyber event. It therefore provides advisers with a broader and more comprehensive cover.

Cyber events can include:

- Hacking attacks or viruses
- Malicious damage to your computer records by an employee
- Accidental damage to your computer records caused by an operational/involuntary error by an employee
- Cyber extortion.



CYBER CLAIM SCENARIO

An insured discovered that over the weekend a hacker had gained access to their network via a scanner. As a result, the hacker had encrypted all their data and made it inaccessible. The threat was that if the insured wanted access to their data back, they needed to click the link provided and follow the instructions noted, including paying the required amount to have the data unlocked.

The insured did not wish to be a party to this crime and was unwilling to pay the ransom. Instead they contacted Marsh and we helped them to obtain access to a forensic expert who could analyse what had happened, what if anything could be done to retrieve/recover the data and also what could be done in the future to prevent recurrence. If the data cannot be restored the insured would need assistance to recreate all their data, which would be a mammoth task and could take some time.

In the meantime, the insured has limited access to their systems and data, which is hugely affecting the management of their business.

Financial Advice New Zealand, together with Marsh, has developed a preferred Cyber Liability policy for advisers. This policy provides protection for:

- Business Interruption – Loss of profits due to a cyber event;
- Privacy – includes loss of personal or corporate information by an insured or by a service provider;
- Harassment (sexual or racial or otherwise);
- Invasion or breach of the right of privacy as provided in the Privacy Act 1993;
- Social Engineering Fraud Cover – sub limit \$100,000

The inclusion of this policy is optional and is not part of the standard Financial Advice New Zealand Liability Insurance programme.

Section 5: Significant extensions included under Financial Advice New Zealand Professional Indemnity policy

In consultation with its members, Marsh and NZI, the Financial Advice New Zealand Professional Indemnity policy offers advisers a number of coverage enhancements to several of the extensions available with other offerings in the market. These enhancements are:

Run off cover

This cover is purchased by firms who cease trading, professionals who retire, or split partnerships that move back to individual businesses or practices.

Due to the claims made nature of Professional Indemnity policies, Run-off cover is designed to protect the business for their past liabilities by having an active policy in place even though the business or person has ceased trading. The Run-off cover will only respond to claims brought during the policy period, that arise from acts, errors or omissions committed prior to the date the business ceased trading, was sold or wound up, or a professional retired.

For financial advisers this is a significant aspect to your Professional Indemnity policy. Insurers and other programmes available in the market treat Run-off cover in many different ways.

Typically Run-off policies are maintained for a period of 6 – 7 years after the firm has ceased trading, been sold or the adviser retired. A new premium is usually charged each year the Run-off policy remains in force, however some programmes in the market have automatic Run-off provisions and it is essential that when you are considering merging, or winding up a business that these past liabilities are considered and Run-off cover discussed with your insurance adviser.

UNDER THE FINANCIAL ADVICE NEW ZEALAND PROGRAMME, RUN-OFF COVER IS PROVIDED AT NO ADDITIONAL COST, PROVIDED THE ADVISER HAS BEEN IN THE FINANCIAL ADVICE NEW ZEALAND LIABILITY PROGRAMME FOR MORE THAN A YEAR AND THEY ARE RETIRING, EXITING THE INDUSTRY OR CEASING TO TRADE. IF THEY REMAIN WITHIN THE INDUSTRY, AND PURCHASE NEW COVER WITH AN ALTERNATIVE PROVIDER, RUN-OFF COVER IS STILL AVAILABLE BUT WILL NO LONGER BE COMPLIMENTARY AND WILL INCUR A CHARGE.

Past liabilities of a business are equally as important to consider when acquiring or purchasing a business or advisers book of business. It should be clear to each party in the sale and purchase as to who is responsible for any claim which may arise in the future for the work that was carried out in the past.

It is always a good idea to discuss these past liability aspects with your insurance adviser to ensure that your Professional Indemnity cover will respond in the manner you believe.

Costs of representation at disciplinary proceedings

Most Professional Indemnity policies available in the market extend cover to include statutory or regulatory body investigation defence costs if related to a claim that would fall under the policy.

If any professional or statutory body, such as the Financial Markets Authority, claims jurisdiction to enquire into or adjudicate any matter, this extension would provide cover for the costs and expenses associated with the investigation, so long as the insurer has given their consent and had the opportunity to appoint counsel to represent you if appropriate.

These extensions can be sub-limited, but under the Financial Advice New Zealand Professional Indemnity policy the full policy limit applies.

Insolvent insurer or fund manager legal costs and expenses

Some policies and programmes in the market specifically designed for financial advisers are extended to include cover for costs and expenses in connection with claims brought against advisers arising from the insolvency, bankruptcy, or liquidation of any Insurance Company, Assurance Company or Fund Manager.

These extensions are usually sub-limited in the cover they provide and are an additional benefit of being part of a larger programme rather than having an 'off-the-shelf' Professional Indemnity policy.

In response to the 2013 Supreme Court decision in the “Steigrad/Bridgecorp” case [BFSL 2007 Ltd v Steigrad [2007] NZSC 156], a separate, ring-fenced defence costs limit applies in addition to the extension’s Limit of Indemnity. This separate limit is available in the event a section 9 charge under the Law Reform Act 1936 is laid against the policy, thus preserving the full extension limit for compensation. The separate defence costs limit is sub-limited to 100% of the total extension limit.

THE FINANCIAL ADVICE NEW ZEALAND PROFESSIONAL INDEMNITY POLICY PROVIDES A LIMIT OF INDEMNITY OF \$125,000 FOR LOSS AND \$125,000 FOR COSTS AND EXPENSES PER ADVISER SUBJECT TO AN ANNUAL AGGREGATE OF \$2,500,000 FOR ALL INSURED.

Mentored advisers

Some programmes in the market extend cover to provide for mentored or trainee advisers as insureds under the policy for a period of time.

The Financial Advice New Zealand Professional Indemnity policy allows an adviser to bring a new person into the advisory business, who is learning “the ropes” for a period of up to 6 months as long as everything they do is supervised and signed off by the adviser.

THE FINANCIAL ADVICE NEW ZEALAND PROFESSIONAL INDEMNITY POLICY PROVIDES COVER FOR A PERIOD OF 6 MONTHS FROM THE TIME AN ADVISER IS ACCEPTED AS A MENTORED ADVISER.

Fire and general advice

Insurers appetite to include cover for Fire & General (F&G) insurance activities lessened following the Canterbury Quakes in 2010 and 2011, as the number of errors and omissions claims brought against advisers relating to advice and insurances placed for risks located in Christchurch increased.

Coverage for F&G insurance advice remains limited. Some programmes in the market include cover for advisers offering F&G advice on domestic risks only, with even fewer programmes providing restricted cover in respect of commercial F&G advice.

The Financial Advice New Zealand Professional Indemnity policy provides cover for domestic F&G advice undertaken by advisers, with automatic coverage available for commercial F&G advice provided that the annual income derived from such advice is less than \$125,000.

IT IS IMPORTANT THAT AS AN ADVISER YOU UNDERSTAND THE EXTENT TO WHICH YOUR POLICY PROVIDES COVER. TALK TO YOUR INSURANCE ADVISER IF YOU HAVE ANY CONCERNS.

THE FINANCIAL ADVICE NEW ZEALAND PROFESSIONAL INDEMNITY POLICY INCLUDES COVER FOR BOTH DOMESTIC AND COMMERCIAL F&G ACTIVITIES, SUBJECT TO CERTAIN CRITERIA BEING MET.

Investments extension

The finance company collapses in 2007 illustrated the potential risks associated with providing investment advice.

Cover for investment advice ranges in the market with some programmes specifically excluding all advice.

The Financial Advice New Zealand Professional Indemnity policy contains the following exclusion:

3.9 Investment Exclusion

The Insurer shall not be liable to indemnify the Insured in respect of any liability arising out of any Claim alleging, arising out of, based upon or attributable to, or in any way involving, directly or indirectly:

- a) any investment offered pursuant to a prospectus or product disclosure statement that is not compliant with all statutory requirements; or
- b) any contributory mortgage or contributory scheme as these terms are defined by the relevant financial markets legislation; or
- c) any diminution of, or any failure to appreciate, in value of any money, securities property, or any other item of value, unless such diminution or failure to appreciate is as a direct result of an Administrative Error.

DEFINITIONS

Administrative Error means an unintentional failure by the Insured to effect a specific investment transaction in accordance with the prior instructions of the Insured’s client.

It is important to understand that investment fluctuations are normal, and diminution in value of an investment is explicitly excluded from cover.

However, the Financial Advice New Zealand Professional Indemnity policy contains an extension to cover the legal costs and expenses incurred in defending any claims which fall within the parameters of the Investment exclusion. This extension is as follows;

Investments Endorsement

The Insurer will pay for Losses and Costs and Expenses in the defence of any Claim otherwise excluded by 3.9 (Investment Exclusion), provided that the Insurer's total liability to pay such Losses and Costs and Expenses shall be limited to the sub-limit specified in the Schedule.

If investment advice forms a significant part of your business it is prudent to talk to your insurance adviser around the extent of cover provided by your policy.

Losses and Costs and Expenses paid under this form part of, not in addition to, amounts payable pursuant to the limits of indemnity of the policy.

In response to the 2013 Supreme Court decision in the "Steigrad/Bridgecorp" case [BFSL 2007 Ltd v Steigrad [2007] NZSC 156], a separate, ring-fenced defence costs limit applies in addition to the extension's Limit of Indemnity. This separate limit is available in the event a section 9 charge under the Law Reform Act 1936 is laid against the policy, thus preserving the full extension limit for compensation. The separate defence costs limit is sub-limited to 100% of the total extension limit.

The maximum liability of the Insurer for all Costs and Expenses will not exceed \$3,000,000 in the aggregate during the Period of Insurance for all individual members of the Professional Advisers Association covered under this Policy.

The Excess applicable to this Extension shall be \$5,000 or the Excess specified in the Schedule whichever is the greater amount.

IT IS IMPORTANT THAT AS AN ADVISER YOU UNDERSTAND THE EXTENT TO WHICH YOUR POLICY PROVIDES COVER. TALK TO YOUR INSURANCE ADVISER IF YOU HAVE ANY CONCERNS.

INVESTMENT ADVICE FORMS PART OF THE PROFESSIONAL BUSINESS DESCRIPTION APPLYING TO THE FINANCIAL ADVICE NEW ZEALAND PROFESSIONAL INDEMNITY POLICY, AND COVER IS PROVIDED SUBJECT TO THE TERMS AND CONDITIONS OF THE POLICY.

THE LEVEL OF COVER PROVIDED BY THE INVESTMENT EXTENSION IS \$100,000 FOR LOSS AND \$100,000 FOR COSTS AND EXPENSES PER ADVISER, SUBJECT TO AN ANNUAL AGGREGATE OF \$3,000,000 FOR ALL INSURED. A HIGHER "PER ADVISER" LIMIT OF \$250,000 FOR LOSS AND \$250,000 FOR COSTS AND EXPENSES IS AVAILABLE IF PURCHASING A \$5,000,000 PROFESSIONAL INDEMNITY LIMIT.

If investment advice forms a significant part of your business it is prudent to talk to your insurance adviser around the extent of cover provided by your policy.

Section 6: Why should you choose this liability programme?

Why place your risk with the Financial Advice New Zealand Liability programme?

- Financial Advice New Zealand has renewed its group Liability Programme with NZI, New Zealand’s largest insurer of financial advisers, through Marsh. The Financial Advice New Zealand wording is customised and exclusive to Financial Advice New Zealand. It has been developed by the Board for advisers, and is continually reviewed to ensure the risk exposures of advisers are addressed.
- Sustainability of insurance programmes are important in an environment of continual change and increased litigation. The Financial Advice New Zealand Liability Programme has stood the test of time, and based on the strength in numbers will continue to be one of the most sustainable programmes in the marketplace.
- The Financial Advice New Zealand cover has served members well and we have a strong relationship with our insurer NZI, and our advisers, Marsh. NZI have confirmed their ongoing support of the Financial Advice New Zealand liability scheme for the 12th consecutive year.
- The Financial Advice New Zealand Liability Programme continues to enjoy an excellent claims history. This is a key reason why it offers enhanced and comprehensive cover at expiring premiums.
- The Financial Advice New Zealand Liability Programme continues to enjoy one of the lowest PI excess amounts available at \$1,000 per claim (costs exclusive).
- A valid claim expressly includes a complaint made to a Dispute Resolution Scheme, and therefore the full Professional Indemnity policy and Limit of Indemnity applies to this.
- It offers extensions such as Court Attendance and Disputes Resolution Attendance cover which provides a daily attendance rate if you are required to attend court or mediation.
- The Financial Advice New Zealand Liability Programme and cover is designed for you, as a member, and also covers your business entities.
- The Financial Advice New Zealand Liability Programme is with a NZ-based insurer, with a NZ-based claims team consisting of specialist claims handlers including legally qualified claims counsel.
- The Financial Advice New Zealand Liability Programme is independent from other providers.

Members are encouraged to take advantage of the substantial benefits that the Financial Advice New Zealand Liability Programme provides.

If you are comparing your Financial Advice New Zealand Liability Programme with an alternative offering, make sure you review the following:

	YES	NO
• Is the cover independent of a product provider ?		
• Is the Professional Indemnity excess costs exclusive ?		
• Is there Automatic Run-Off Cover?		
• Does the cover include Disputes Resolution Attendance Cover?		
• Is there a Shared Excess Layer of Professional Indemnity Cover to comprehensively protect you?		
• Does cover include Mentored Advisers Cover?		
• Does the policy offer Directors and Officers Insurance Cover as an automatic inclusion?		
• Does the policy offer an on-line proposal process to ensure privacy and security of your declaration?		
• Is the policy administered by a professional party with a long history of providing highly valued service to its members ?		

Questions to ask when buying professional indemnity insurance

The following questions are a selection only, and seek to highlight some key aspects to consider:

OPERATIVE OR INSURING CLAUSE

- Does the insuring clause clearly describe what is insured?
- Does the cover you understand you have bought meet the cover you need?

DEFINITIONS

- Do any of the definitions change the meaning of the words or expressions in the insuring clauses or exclusions?

EXCLUSIONS

- Do any of the exclusions remove cover for any activities necessary to conduct your core business?
- Do any of the exclusions remove cover for any activities necessary to conduct your non-core business?

EXCESS AND RELATED CLAUSES

- Do you understand how the excess operates in practice?
- Does the insurer pay the costs and expenses incurred in defence of a claim (or does this fall within the excess)?

Appendices

Claims case studies

Case Study 1 (Life Agent)

Mr Smith was an accountant in practice for 26 years. He had a longstanding friendship with Mr Broker of Life Insurance Brokers Limited. Mr Smith had used Mr Broker's service from time to time over the years and through Mr Broker had arranged income protection, life insurance and business expenses policies with a number of insurers.

In late 2009, Mr Broker raised with Mr Smith the prospect of taking out a Terminal Illness policy. Mr Smith was fit and healthy and he had always advised Mr Broker that he did not think he needed such cover, especially given that no one in his family had ever suffered from a terminal illness.

However, in 2010 a mutual friend of Mr Smith and Mr Broker, Candy Camellia, suffered from serious health problems and as a result Mr Smith asked Mr Broker to tell him more about the Terminal Illness policy.

Mr Smith and Mr Broker met in October 2010. At the meeting, Mr Smith completed an application for cover which was forwarded to Insurance Company Ltd on 31 October 2010. Mr Broker asked Mr Smith to pay a premium at this time but Mr Smith, being an accountant, declined to pay anything until his cover was "all sorted out". The Terminal Illness cover sought by Mr Smith would pay him \$1,000,000 upon diagnosis of a terminal illness.

Insurance Company Ltd advised Mr Broker that it required some additional health information and this was eventually received from Mr Smith and forwarded to Insurance Company Ltd on 15 November 2010. On 1 December 2010 Insurance Company Ltd advised Mr Broker that cover had been accepted, but the premium for that cover had not yet been paid. On 21 December 2010, Mr Broker wrote to Mr Smith asking him to pay the premium and advising him that cover had been accepted. Mr Smith forgot to pay the premium in the Christmas rush but after being followed up by Mr Broker at the end of January 2011, he eventually paid the premium on 15 February 2011.

Insurance Company Ltd processed the application and issues a policy on 1 March 2011 with a start date of 1 March 2011.

On 1 April 2011, Mr Smith rang Mr Broker to advise he had been diagnosed with cancer and the outlook was not good. A claim subsequently made on the policy was declined by Insurance Company Ltd on the basis that the policy contained a 60 day exclusion period which ran from the date cover was effected after payment of the premium.

Mr Smith is understandably upset and challenged the declination. He complained that Mr Broker was responsible for the problem since he did not tell Mr Smith of the importance of paying the premium and the impact which failing to do so, or doing so late, would have. He stated that this was the first time he had heard of the exclusion period. On further investigation of the policy, he found other clauses which he believed not to be in his interests and which Mr Broker had not pointed out to him. He stated that he would see his lawyer regarding Mr Broker's "negligence".

Mr Broker checked his client file and realised that he had not taken a note of what exactly he had told Mr Smith about the policy. He is sure he would have gone through it carefully with him.

QUESTIONS

1. What are the causes of the claim?
2. What should Mr Broker do now?
3. What risk management procedures could be adopted to avoid this type of claim occurring again?

ANSWERS — CASE STUDY 1 (LIFE AGENT)

CAUSES OF CLAIM

- Possibly a failure to go through the important aspects of the policy with the client and draw the exclusions etc to Mr Smith's attention and explain the effect.
- Failure to give advice about the procedure for paying premiums and the effect that this may have on a policy of this type.
- Failure to keep written notes / correspondence regarding content of advice given, probably exacerbated by the fact of friendship or a longstanding relationship.
- Arguably failure to act promptly once advice of cover received from Insurance Company Ltd.

WHAT SHOULD MR BROKER DO NOW?

- Notify the claim.
- Avoid admitting liability.
- Gather the file together.
- Prepare memorandum outlining events.

RISK MANAGEMENT STEPS

- Keep detailed file notes of advice given and received and confirm in writing.

- Make a practice of going through important clauses of policy with clients and recording in writing (file note at least) fact of doing so and basic tenor of advice given.
- Act promptly — here if prompt advice of fact of cover and need to pay premium had been given after 1 December, whether or not Mr Smith would still have ‘forgotten’ to pay in the Christmas rush, Mr Broker would be in a stronger position especially if that advice was given in writing or recorded in a file note.

Case Study 2 (Financial Planner)

Financial Planners Ltd (“FPL”) acted as financial planners for Anne and Paul Jones for a number of years. In early 2008, Anne turned 60 and Paul turned

61. They went to FPL to talk about their impending retirement and sought general investment advice. FPL advised the Joneses that it would keep an eye out for new opportunities for them.

In May 2008, FPL advised the Joneses of the opportunity to invest in a property owning company called Industrial Properties Ltd (“IL”) which owned industrial rental properties. FPL explained the expected rate of return and the Joneses jumped at the opportunity and gave FPL authority to buy as many shares as possible in IL, which FPL did, acquiring the shares between May 2008 and October 2008. FPL (on behalf of the Joneses) purchased 20,000 shares during that period at a cost of between \$1.24 and \$1.35.

In December 2008, Jim the director of FPL sold the business to New Planners Ltd (“NPL”), who took over the client base including Anne and Paul Jones.

In December 2009, the Joneses advised NPL that they were disappointed at the overall return since inception of 1.09%. The Joneses asked NPL to reduce their shareholding in IL by 75% as soon as possible.

NPL advised the Joneses that the portfolio had only completed 1 year of an 8 year plus strategy and therefore in order to get the expected rate of return, the investment would need to be viewed as “locked in” for a minimum period of 8 years. NPL also advised the Joneses that NPL’s ability to sell the shares would be dependent on the purchasers’ interest in the shares at that particular time. NPL advised that the closer the Joneses waited to the end of the minimum term (8 years), the more likely it would be that the Joneses would achieve the desired average rate of return. Nevertheless, NPL noted the Joneses directive to reduce their investment and advised that NPL would endeavour to action the request, but could give no guarantees as to the timeframe for reasons discussed at the time of making the investment.

In May 2010, the Joneses wrote to NPL expressing their continued disappointment with the investment and requesting NPL immediately reduce the Joneses shareholding by 75%.

NPL responded advising that they were aware of the Joneses instruction to sell and would advise them once an opportunity to sell the shares arose; however it could give no guarantees as to when it could action the Joneses request.

In September 2010, NPL advised the Joneses that it had been unable to find purchasers for their shares in IL, so if the Joneses wished to sell immediately they would need to indicate to NPL what level of discount they would be prepared to accept. NPL would continue with its endeavour to sell the Joneses shares at this level. NPL requested the Joneses indicate the level of discount they would be prepared to accept against the current \$1.00 net asset value of the shares. NPL advised that once it received responses from those wishing to sell their shares, NPL would pursue the realisation of the Joneses shares as appropriate. The Joneses responded that they wished their shares to be sold as soon as possible as they could not have their money “locked in” for 8 years.

In March 2011, the Joneses wrote to NPL advising that it had been 14 months since the Joneses asked NPL to exit the shares and advising NPL to do so at once. NPL asked the Joneses to first indicate the level of discount against the then current \$1.05 net asset value of the shares that they would be prepared to accept for their shares.

In November 2011, the Joneses wrote to NPL advising that they wished their shares to be sold by the end of the month and they were not prepared to accept a level of discount on their shares. The Joneses say that they were never advised that the investment was locked in for a period of 8 years and had they known this they would never have invested in IL. They say they want their money back or they will issue proceedings against NPL.

QUESTIONS:

1. What are the causes of the claim?
2. What should FPL do now?
3. What risk management procedures could be adopted to avoid this type of claim occurring again?

ANSWERS — CASE STUDY 2 (FINANCIAL PLANNER) CAUSES OF THE CLAIM

- Failure to consider/ recommend an investment suitable for the specific clients and their requirements / needs.
- Failure to go through the important aspects of the investment, i.e. that it was a long term investment and that funds were locked in for a defined period.
- Failure to explain the process of selling shares / rate of return.

- Failure to keep written notes / correspondence regarding content of advice given.
- Failure to clearly identify the risks associated with the investment and recording these in writing.

WHAT SHOULD NPL DO NOW?

- Notify insurers.
- Make no admissions of liability.
- Prepare memorandum of events and gather files together.

RISK MANAGEMENT STEPS

- Keep detailed file notes of advice given and received and confirm in writing.
- Make a practice of going through each investors requirements, explaining the risks associated with the investment and recording in writing (file note at least) fact of doing so and basic tenor of advice given.

Case Study 3 (Fire & General Insurance)

Playground Equipment Ltd (“PEL”) manufactured and sold a range of children’s outdoor adventure play equipment made out of recycled wooden packing boxes. PEL was the brainchild of Mr Wood, an ex yacht builder, who was its sole director.

PEL had been operating on a relatively small scale for several years. The products were well received by the public and were beginning to develop a good reputation. Demand was increasing.

In 2001, realising that business would need to expand to meet demand; Mr Wood began looking for opportunities to take on an equity partner. As a result, Cooper Investments Limited (“CIL”) was given the opportunity to purchase a 40% shareholding in PEL.

CIL is a company owned by a client of Bob’s Business Insurance Ltd — Mr Cooper. Bob has previously acted for Mr Cooper and provided him with a range of financial planning and life insurance advice. Mr Cooper asked Bob to provide him with advice and recommendations on the insurances for PEL.

Bob arranged a meeting with Mr Wood and Mr Cooper to discuss exactly what PEL is doing. Mr Cooper advised that the investment made by CIL will enable PEL to;

- Continue to expand on its overseas activities with further product exports to the USA.
- Employ one person in the USA to seek out sales opportunities and take orders.
- Develop the warehouse space they have leased previously to store stock in the US for distribution.

PEL will continue to manufacture the products in New Zealand and export them to the US for distribution. Mr Cooper has suggested that he would move to the US to run the business on behalf of PEL for the next 6-12 months.

Mr Cooper then asked Bob for advice in respect of the insurance needs for the organisation. Bob responded with the following:

- Key Man Insurance was required
- A business pack needed to be put in place
- Public Liability and Motor Vehicle insurance were also required.

The quotations were duly delivered and, after some delay, Mr Wood and Mr Cooper accepted Bob’s recommendations and purchased cover.

The Business Back provided Asset and Business Interruption coverage & the Public Liability insurance was issued for their activities in New Zealand.

Upon receiving the policy document, Mr Cooper enquired of Bob how the policy was to respond to their activities in the United States. Bob’s insurer extended the policy to include an Expona clause which he understood to provide USA coverage.

Some months after the meeting, Mr Cooper contacted Bob from the US in a state of concern. Two unrelated events had occurred in the same week to cause potential harm to the business. Mr Cooper advised Bob that he had sold a playground to a play centre in Texas and a small child had injured themselves when falling off the equipment. The parents of the child had threatened to sue PEL, suggesting that the playground equipment was unsafe, poorly constructed and lacked appropriate warnings on how it should be used.

They threatened to sue PEL for US \$10 million and the public liability insurer had declined the claim arguing coverage was for exports only.

In addition, Mr Cooper broke his arm in the US. When he was admitted to hospital and asked for insurance, he realised that the travel insurance he had in place would not provide cover as he was no longer “travelling”.

Two weeks later Mr Cooper, on failing to receive any adequate advice from Bob following declination of the claims by the public liability and the travel insurers, instructed his lawyers to further investigate why there was inadequate cover in the US, both for the product liability exposure and the accident medical costs which he had to meet personally.

Upon being questioned by the lawyers, Bob commented that he had arranged appropriate cover for US activities but acknowledged that he had not addressed the needs for cover

“on the ground”, had not given any thought to the expatriate status of Mr Cooper and had provided no recommendation to the client in respect of appropriate limits of indemnity under the product liability coverage.

Even though Mr Cooper had offered contracts and sale and agreement clauses for review by the financial adviser, these had not been reviewed.

Mr Cooper states that he holds Bob liable for any damages of settlement brought by the claim in Texas, given that the insurance put in place did not adequately cater to their needs.

Mr Cooper is also going to sue Bob for the uninsured medical costs not covered by the insurance.

QUESTIONS:

1. What are the causes of the claim against Bob?
2. What should the financial adviser do now?
3. What risk management procedures could have been adopted to avoid this claim?

ANSWERS — CASE STUDY 3 (FIRE & GENERAL INSURANCE) CAUSES OF THE CLAIM

- Lack of investigation by the financial adviser to truly understand the risk issues of the company.
- Inappropriate products put in place to provide risks for the company.
- Public Liability poorly structured
- No mentioned of Directors & Officers insurance
- No disclosure about expatriate medical
- Lack of understanding of how the product solution would apply to the issues and risks raised by the company.
- Expona clause covers travelling/ exporting exposure only with no cover for “on the ground activities”.
- Failure to provide any advice in respect of the risks faced by the business.

WHAT SHOULD BOB DO NOW?

- Notify their professional indemnity insurers.
- Do not admit liability.
- Gather the files together.
- Prepare a detailed summary of event.
- Follow the steps detailed by the insurer.

RISK MANAGEMENT STEPS

- Keep detailed file notes of client meetings.
- Seek appropriate advice from specialists when risk issues are presented that you are not familiar with.
- Do not rely on insurers to provide appropriate policy responses without understanding the implications of their extensions.
- Be very careful when providing advice to clients with exposures in overseas jurisdictions.

About Marsh

Marsh is a global leader in insurance broking and risk management. In more than 130 countries, our experts help clients to anticipate, quantify and more fully understand the range of risks they face. In today's increasingly uncertain global business environment, Marsh helps clients to thrive and survive.

We work with clients of all sizes to define, design, and deliver innovative solutions to better quantify and manage risk. To every client interaction we bring a powerful combination of deep intellectual capital, industry-specific expertise, global experience, and collaboration. We offer risk management, risk consulting, insurance broking, alternative risk financing and insurance programme management services.

Since 1871 clients have relied on Marsh for trusted advice, to represent their interests in the marketplace, make sense of an increasingly complex world and help turn risks into new opportunities for growth. Our more than 27,000 colleagues work on behalf of our clients, who are enterprises of all sizes in every industry and include businesses, government entities, multinational organisations, and individuals around the world.

Marsh has been operating since 1958 and have over 400 experienced staff in offices throughout New Zealand.

About NZI

NZI is one of New Zealand's largest and most well-known insurance brands, offering an extensive selection of flexible, comprehensive insurance services for people and businesses throughout the country.

For 157 years, we've been helping Kiwis in all lines of work, in all parts of the country, through good times and bad. We know, better than any other insurer, what it takes to plan and prepare for the unexpected.

With our nationwide network of branches, working closely with brokers, we're close to the challenges and the opportunities that Kiwi businesses are working with every day, so you can receive a tailored solution for you and your business.

NZI is proudly backed by IAG – the largest general insurer in Australia and New Zealand, with a growing presence in Asia.

In 2011, 2012 and again in 2013 we were voted intermediated Insurance Company of the Year. We're proud of our reputation for delivering innovative solutions, supported by a solid record of focused, responsive performance. This is reflected in our Standard & Poor's financial strength rating of AA- ("Very Strong") and our solvency margin.

FINANCIAL STRENGTH RATING

NZI is a business division of IAG New Zealand Limited, which has received a financial strength rating of AA- from Standard & Poor's (Australia) Pty Ltd, and approved rating agency. This means IAG have a "very strong" rating.

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