



*Professional Liability Insurance for
Registered Investment Advisors*

**What Should Financial Planners &
Registered Investment Advisors Ask About Professional
Liability Insurance?**

WHAT SHOULD FINANCIAL PLANNERS AND REGISTERED INVESTMENT ADVISORS ASK ABOUT PROFESSIONAL LIABILITY INSURANCE?

We are committed to increasing awareness and understanding of professional liability insurance in the financial planning/investment advisory community. To this end, we provide the following questions most frequently asked us as underwriters. We recommend you ask these questions anytime you are purchasing professional liability coverage regardless of carrier.

What is the A.M. Best rating of the carrier?

Evanston & Essex Insurance Companies are part of Markel Corporation, a leading worldwide underwriter of property and casualty reinsurance and specialty insurance with over \$2 billion in policyholders' surplus. Evanston & Essex Insurance Companies are rated "A" by A. M. Best

Get References

Contact the **Financial Planning Association (FPA)** at www.fpanet.org and the **National Association of Personal Financial Advisors (NAPFA)** at www.napfa.org to obtain references for professional liability insurance. Ask your colleagues who they use and if they are satisfied with the quality of coverage and service.

Preserve Your Prior Acts Coverage

If you are replacing existing coverage, **make sure your retroactive date** on your expiring policy **is preserved** on the replacement policy or you purchase an **Extended Reporting Period (tail)** from the E&O program you are leaving. You **must** pursue one of these two options in order to preserve your prior acts coverage. **Never let a claims-made policy lapse** unless you are no longer practicing or you have replaced coverage.

What Are the Defense Provisions of the Policy?

Evanston/Essex's policy is a "right and duty to defend" contract which is the strongest defense provision available. Other defense clauses used in the industry are an "option but not duty to defend" which allows the insurance company to decide whether it will assume/manage your defense and may provide defense on an indemnity basis (you manage and pay for the defense and the insurance company reimburses you). Additionally, when defense is offered it may be portioned based upon whether parts of the claim are considered covered vs. non-covered acts. Evanston/Essex coverage is "right and duty to defend", includes defense on the whole claim, and "pays on behalf of" you in a claim. Our policy contains a **consent to settle** clause so be sure to ask about this to assure you have the right to consent to a settlement before it is finalized.

What Happens to Your Prior Acts Coverage If Your Policy is Cancelled?

If your policy is cancelled or non-renewed by your insurance company, does it contain language which gives you a **contractual right** (written into the policy language), which cannot be denied by the company, to purchase an **extended reporting period endorsement (tail) of at least one year's duration**? Some carriers will give you a contractual right to an extended reporting period endorsement, but this period is only for 90 or 180 days after coverage termination or it may apply only if you are retiring or are disabled. Evanston/Essex's policy provides a contractual right to an extended reporting

period endorsement of one year if we cancel (except for non-payment) or non-renewal of your policy.

Make Sure the Policy Has an "Incident Trigger" in its Definition of Claim.

It is critical to determine if awareness of potential loss (incident) constitutes a claim as defined in the policy. While all policies have the requirement to report incidents that might potentially give rise to a claim, the question is whether the policy language includes incident reports within the definition of claim, thus, triggering coverage under the policy. If there is no incident trigger, a carrier may take the incident report but advise you that there is no coverage under the policy until a written demand for damages is received from the client. This is a critical point since the earlier the carrier can intervene in a potential claim, the greater the likelihood of mitigating the severity of the claim.

Under the Evanston/Essex policy, if you make an incident report, the policy allows us to elect to spend our own funds investigating and defending such an incident. This investigation is at the Company's expense, is not subject to the deductible and does not reduce the applicable Limits of Liability. Further, once you report an incident, it is considered a claim made and reserves a slot for any future written demand for damages rising from the incident.

Ask What the Policy Covers

Some insurers of investment advisors offer coverage only for fee activities. Subject to policy terms and conditions, the Evanston/Essex policy covers both fee activities and product sales coverage in the areas of securities, life, health, disability and accident products. Evanston/Essex's product sales coverage is designed to be an adjunct to the financial planning/asset management activities of the advisor. The securities/life product sales coverage is designed for mainstream products. **Read Exclusion 26 carefully** since alternative investments are generally not covered. Evanston/Essex "bundles" coverage for both fee and commission activities in one policy to allow for a wide range of variation in the nature of practices. It is not uncommon for practitioners to gradually move their practice from fees and commissions to fee-only or to ask for coverage tailoring.

Determine How the Policy is Rated. Are Claims-Made Step Factors Used on Renewal Rating?

Claims-made step factors are increases in premium that **are not based** on an individual risk characteristic (e.g. revenues, staff). These factors increase the premium in each of the insurance company's three renewals even if the insuring characteristics have not changed. This leads to a stable "fully mature" rate which is much higher than the Evanston/Essex year rate. The Evanston/Essex program does **not** utilize claims-made step factors. We have created a level rate structure to avoid the sharp increases on renewal caused by claims-made step factors. Renewal rating is no different than new business rating. The premium is driven by such factors as number of financial advisors, annual revenues, the limits and deductible chosen and the type of services rendered.

Ask What Discounts Are Available.

Evanston/Essex offer a multiple advisors discount if the aggregate limit is shared by more than one advisor. We also offer a fee-only discount to practices which do not engage in product sales. Ask if there are any affinity discounts for association members. We offer limits up to \$5 Million per Claim and higher deductible options for larger practices.

AREAS TO CONSIDER WHEN COMPARING TO A BROKER-DEALER POLICY

Are Outside Approved RIA Activities Covered?

If you are dually registered as a registered representative with a FINRA broker-dealer and as a Registered Investment Advisor at the federal/state level, and you conduct investment advisory activities "away from" your registered FINRA firm, obtain your broker-dealer's approval and confirm the broker dealer's position on **NASD 94-44**. NASD 94-44 requires broker-dealers to oversight these "outside RIA" activities. **In some cases, the broker-dealer E&O program will not cover these outside activities even if they are approved. Check with your compliance officer at your broker-dealer.**

Aggregate Depletion

Remember that the annual **aggregate limit** may be quite high for a broker-dealer policy, but all registered representatives under the broker-dealer policy share it. The Evanston/Essex aggregate also applies to all insureds under the policy but it covers only your practice. Take this into consideration when you are comparing limits, premium and coverage. The greater the number of insureds under the same policy, the greater the risk that the annual aggregate limit can be depleted thus leaving no coverage for any further claims reported during that annual policy period. This is also the reason that group broker-dealer coverage costs less than a limit dedicated to your practice.

Consider Whether Portability Is Important To You.

Your Evanston/Essex policy is portable regardless of changes in your broker-dealer or life company affiliations. Under a broker-dealer policy or a life company policy, you may lose all coverage once you change your affiliations. Your broker-dealer could also lose its insurance or change carriers. **If you have your own policy, you retain control of your insurance.** If you maintain your own insurance, in the event of a covered claim, you will have your own defense counsel separate and apart from the defense counsel for the broker-dealer. Under the claims-made policy form, you will maintain your original "retroactive date" (date on which you first obtained claims-made coverage) as long as continuous coverage is maintained in effect without lapse. This will preserve coverage for your prior acts back to the original retroactive date. Consider the importance of portability and the preservation of your prior acts coverage. When insurance is controlled by someone else acting on your behalf, or by the claims experience of other practitioners, the result may be the loss of your coverage.

Consider Whether Maintaining Dual Insurance Coverage Is Important to You.

Many practitioners maintain coverage with both Evanston or Essex Insurance Companies and a group broker-dealer policy. The advisor does this to assure that if anything happens to the broker-dealer coverage, they will still have independent coverage which they control and which maintains their retroactive date. Please read the **Other Insurance** clause in the CONDITIONS Section of your policy for the handling of claims covered by more than one insurance policy. The Evanston/Essex policy is excess over any other valid and collectible insurance. If the other insurance policy has similar wording, then, as a practical matter, the two carriers coordinate to work out each carrier's role in a covered claim.