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# **SMALL BUSINESS OWNER'S**

➡ GUIDE TO ◀

## **PROFESSIONAL LIABILITY**

*Insurance Claims*

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# The Small-Business Owner's Guide to Professional Liability Insurance Claims

As a small-business owner, you're no stranger to responsibilities. But responsibilities that can land you in court? That might be new terrain.

So let's get the hard truth out of the way: once your business opens, you can be held liable for the mistakes it makes and the financial losses it causes. This is your "professional liability." And here's a little more bad news: professional liability lawsuits can cost you thousands of dollars, both in money spent and hours wasted.

Data from the [Court Statistics Project](#) shows that the median cost of liability litigation is **\$122,000**. Additionally, the authors claim that professional liability cases take the most time across every stage of litigation, from a case's beginning to the post-trial disposition.

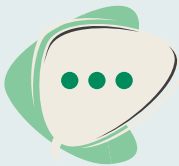
Don't freak out just yet. [Professional Liability Insurance](#) is designed to help your business weather this storm. And after you read this guide, you'll know what your policy covers and how to navigate the claims process like a stone-cold pro.



# Your Formal Introduction to Professional Liability Insurance

It's easy to see why Professional Liability Insurance confuses some small-business owners. For starters, the policy has a couple different names, including **Errors & Omissions Insurance** and Malpractice Insurance. No matter what you call it, Professional Liability is the policy you need to handle client disputes.

To illustrate that point, think about the risks you take on when you work with clients. You can be held liable for damages when...



A client thinks your professional advice cost them money.



You miss a crucial project deadline.



A client is disappointed with the results of your work.



Your services cost more than the client expected.

Miscues and miscommunication – real or imagined – can cause even the most amicable professional relationship to turn icy. Once that happens, a disgruntled client may sue if they think it's the only way to recoup their losses.

# Which Claims Does My Professional Liability Insurance Cover?

Professional Liability Insurance can address professional negligence claims. For example, it can step in when a client alleges your business...

- Failed to complete a project.
- Made mistakes in its work.
- Gave poor advice.
- Breached a contract.
- Fell short of professional standards.

If it's a claim over financial losses your work caused, it's usually a job for this policy. That's easy enough. But to receive your Professional Liability coverage benefits, the timing of the claim matters.

## Claims-Made Policies and the Professional Liability Sweet Spot

Nearly every Professional Liability policy is a **claims-made policy**. That means the policy must be active when the alleged incident occurs AND when the claim is filed in order for a claim to be covered.

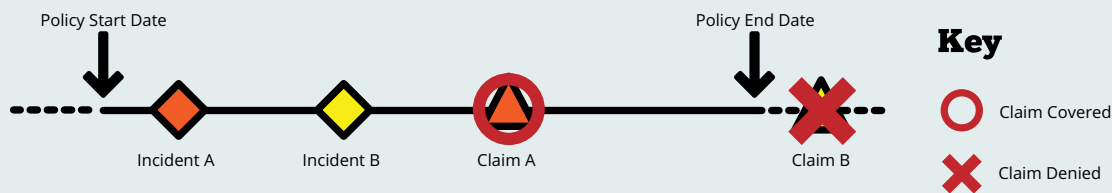
Let's say you're a freelancer with Professional Liability coverage. You contract with a client, complete the project, and go on your merry way. Later, you decide that you don't want your insurance, so you cancel the policy.



But what happens when that same client claims you made a mistake that cost them money? Even though you were covered when the alleged mistake happened, your insurance provider won't pay because your Professional Liability policy is no longer active.

If that's not clear, check out this chart:

### Claims Made Policies: Covered vs. Denied Claims



The solid line represents the policy term – let's call that the "sweet spot." The dotted lines show when the policy is not active. Take a look at Incident A and the corresponding Claim A. Both occur on the solid line (i.e., during the policy term) so Claim A is covered.

Now look at Incident B and its claim. Incident B happens during the policy term, but Claim B is not in the sweet spot. It's outside of the policy term, on the dotted line, so Claim B is not covered.

## Mind the Gaps with Retroactive Dates and Tail Coverage

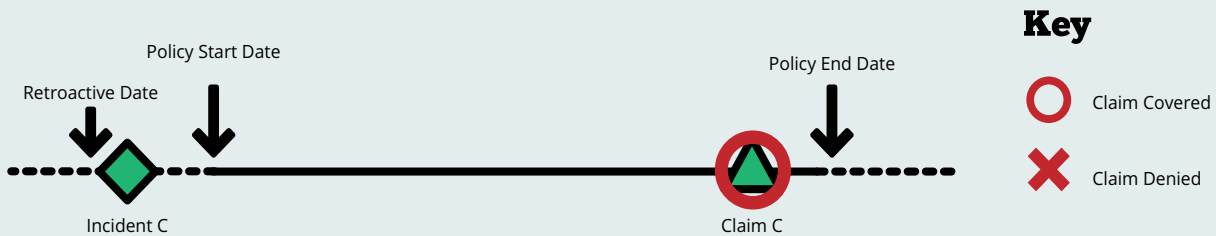
At first glance, that claims-made business doesn't seem too tricky. Just keep your Professional Liability policy active and you're set. Right?

Not so fast. If you did work before your policy started, you could have a potential coverage gap. That's why you also need to be aware of your policy's **retroactive date**. The retroactive date is the earliest point that an incident may occur and still be covered.

So let's say your policy goes into effect on January 1, 2017, but has a retroactive date of January 1, 2016. An incident in 2016 is covered as long as the claim is made during the policy term.

Again, this chart illustrates that point:

### Claims-Made Policy, Retroactive Date

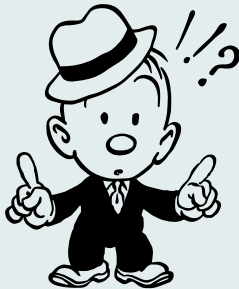


Incident C occurred before the policy began, but because it falls after the retroactive date and the claim was made during the policy term, Claim C is covered. Not every E&O policy has a retroactive date, so ask your agent if your policy has one.

Now let's talk about life after your policy. Unfortunately, small-business owners sometimes drop their insurance because they...

- Think it's too expensive.
- Decide to change carriers.
- Close their business.
- Retire.
- Forget their renewal date.

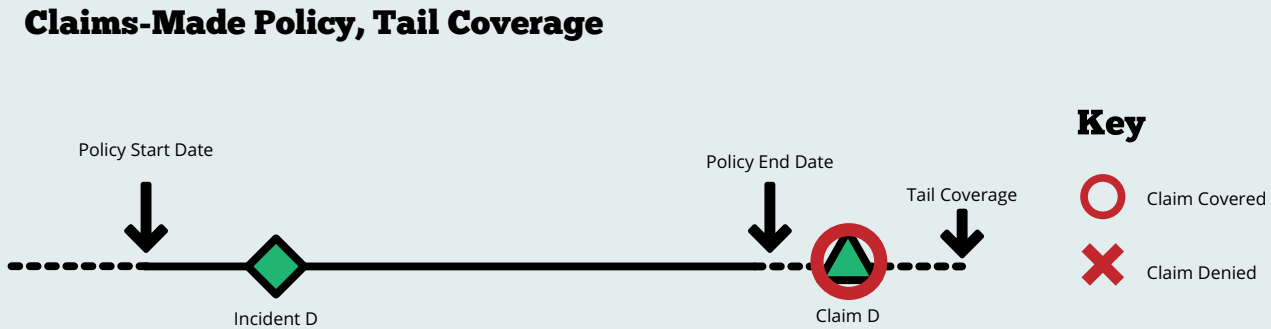
That's when the trouble starts. Remember, your policy needs to be active to cover claims (including those brought by clients you might have served years ago).



**Incidents that happen during your tail coverage period usually aren't covered by your policy.**

To stay covered after your policy is no longer active, you may want to consider tail coverage (also called “extended reporting period provisions”). Basically, a Professional Liability policy with tail coverage can cover claims made after the policy expires or is cancelled.

To illustrate that point, let’s look again at our trusty chart:



Incident D occurs during the policy term, but its corresponding claim occurs after the term. With **tail coverage**, Claim D can be covered.

Now that you have an idea of how your coverage works, let’s make sure you know how to use it. Next up: how to file professional liability claims.



Prevent gaps in coverage by maintaining your retroactive date when you renew or change carriers.



## 3 Steps to Making a Professional Liability Claim

Few things can make your fight-or-flight response kick in quite like a demand letter from your client. They haven't even filed a lawsuit yet, but seeing their complaints in writing can send all clear thinking out the window.

Before you say, "That would never happen to me," check out this [press release](#) from Hiscox about its 2014 survey of small-business owners. It reveals that...

- **13 percent** have been sued by a vendor, employee, or client.
- **29 percent** said they lost customers because of the lawsuit.
- **47 percent** of those sued said the lawsuit negatively impacted their business.

Scary numbers, indeed. But this is not the time to panic. Remember, your [Professional Liability Insurance](#) is most likely a claims-made policy, so time is of the essence when you need to make a claim. Many providers want you to contact them as soon as you suspect a suit is imminent, including when you receive a...

- Demand letter.
- Complaint letter.
- Threatening phone call.
- Notice of investigation from a regulatory agency.
- Request for your Professional Liability policy information.
- Subpoena for documents, deposition, or testimony.

These actions put you on notice, but again, don't panic. Take a deep breath and follow these three simple steps when you need to make a professional liability claim.

## Step #1: Notify Your Provider ASAP

When faced with a potential claim, one of the biggest mistakes small-business owners make is ignoring it, according to Shavon J. Smith (@TheSJSLawFirm), a small business attorney at SJS Law Firm. “Ignoring the notice or waiting until the last possible minute to act gives your attorney less time to prepare an effective initial response,” says Smith.

Another problematic trend Smith has noticed? “Many small businesses forget about promptly notifying their insurance company,” she says.

Insurance providers typically require you to notify them about a professional liability claim as soon as possible. If you fail to do so, your provider may allege you breached your insurance contract and may not cover the lawsuit. In other words: don’t risk it.

You can usually find instructions for alerting your insurer in your policy documents or on the company’s website, but typically, providers want to see...

- A copy of the complaint.
- Your policy number.

Contact your insurance provider with this information as soon as you can, and be prepared to work with your carrier to resolve the claim.



**Your insurance policy may make coverage dependent on timely claim reporting.**

## Step #2: Gather Additional Documents

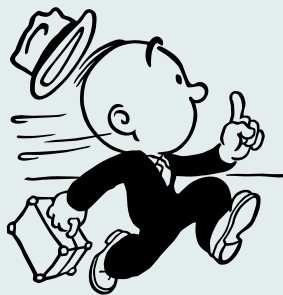
Your provider may request additional documentation to learn more about the claim against you. Be ready to pass along...

- The original client contract.
- Change orders.
- Agreements.
- Emails between you and the client.
- Documents outlining your service fees.
- Sample bills or invoices.
- Proposals.

It may seem pretty obvious that it's in your best interest to help your provider investigate your claim, but most Professional Liability policies make it a requirement. Perhaps that's because some small-business owners make the mistake of withholding information if it makes them look bad.

"I've had clients not produce emails," says David Lilenfeld (@DavidLilenfeld), founder of [Lilenfeld PC](#) in Atlanta. "I've had clients delete emails, but typically they'll say 'we don't have any' or only produce emails that are favorable. And then it's like we have half the story."

The people who are trying to help you need the full story to give you the best advice. And withholding information from your insurance provider may mean it doesn't have to cover the lawsuit.



**Why would a business owner withhold information from their lawyer? According to David Lilenfeld of Lilenfeld PC, "They worry it's going to hurt the case if it comes out, or they worry that their lawyer may think less of the validity of their claim. But if you withhold information, I can't give you the best advice"**

## Step #3: Work with Your Provider

We can't stress this enough: you must cooperate with your insurance provider throughout the claims process. That means you should be ready to:



Provide more documentation.



Answer lots of questions.



Attend depositions.



Negotiate a settlement with the plaintiff.

If you want the swiftest resolution (and to get back to work faster), it's usually best to follow the insurance company's lead and the advice from the lawyer it assigns to your case. However, just because you're working with the provider's lawyer doesn't mean you can't have one of your own.

"For clients we serve as outside counsel, we quarterback those insurance counsel relationships," says Gina Bongiovi

(@LawyerGina), founder of the [Bongiovi Law Firm](#) in Las Vegas, Nevada. "It provides the client with some level of comfort that someone's looking over their shoulder."

In Bongiovi's book, ideally a business owner would already have an attorney working to close the gaps that can lead to lawsuits. "If a lawsuit pops up, an attorney is already on the scene with a working knowledge of the business and the history leading to the dispute," she notes. In other words: the best time to hire a lawyer is before you need one.

Now that you know how to make a claim, let's look at some ways you can improve your chances of winning a professional liability lawsuit.

# 4 Strategies to Maximize Your Odds of Winning a Professional Liability Lawsuit

Once a liability lawsuit is filed, you and your lawyer become a team. They know the law and have experience defending small-business owners in **Professional Liability Insurance** claims. You know your business and your relationship with the plaintiff. These perspectives need to come together to create a successful defense.

You can make that happen and increase the chance of winning a professional liability lawsuit with these four steps:

1. Document everything.
2. Maintain clarity.
3. Listen to your lawyer.
4. Be honest with yourself.

## #1 Document Everything

Good recordkeeping is the cornerstone of a good defense, and it should start way before you have your day in court. Remember that without documentation, it's just your word against your client's. That means the fate of your case may hinge on which party is more likable, and that's a roll of the dice you want to avoid.

To make sure your documentation can properly support a legal defense, be sure to:

- **Get everything in writing.** "Whether one party fails to understand all the terms of an agreement or whether business partners are in a dispute, they boil down to he-said / she-said battles," says Bongiovi. "The best way to prevail in these situations is to document, document, and document some more."
- **Send confirmation emails.** A follow-up email after a client meeting or phone call might seem like overkill, but it's the ounce of prevention that may save you a pound of cure. One "agreement recap" email gets everyone on the same page and provides a date stamp that may prove valuable if you're sued.

- **Hire a lawyer.** Because of financial pressures, “owners often abstain from having a lawyer involved in the drafting process or agree to a deal even though the terms are unfavorable,” says Robert Stetson, an attorney with [Bernkopf Goodman LLP \(@BernkopfGoodman\)](#). Work with a lawyer when you first draft or sign contracts to prevent mistakes that can expose you to significant liabilities and litigation costs later.

Stetson also recommends training your next generation about proper documentation. “There’s no one-size-fits-all approach for ensuring the integrity of client conversations and agreements,” he says, “but once a small business identifies what works, it must ensure that its practices last.”

## #2 Maintain Clarity

The people who decide your case – either a mediator or jury – may not know the nitty-gritty specifics of your industry or business, so don’t assume they’re subject-matter experts. To help make your case crystal clear for them, give your defense team plenty of documentation that can be readily understood.

Keep in mind that documentation that is difficult to grasp may make the jury more sympathetic to a client who says they couldn’t understand the contract in the first place.

To keep your documentation clear from the outset, be sure to:

- Identify jargon and explain it.
- Write contracts, agreements, and proposals in plain English.
- Make contact obligations clear and precise with no room for subjectivity.
- Include date and time stamps.

Perhaps the best piece of advice is to think like a lawyer when you’re creating documents and communicating with clients. Ask yourself, “Could a lawyer – preferably mine – use this as evidence if I am sued?”

## #3 Listen to Your Lawyer

Following your lawyer's lead during a lawsuit is usually the quickest way to a resolution. Think about it this way: you don't go to the courthouse very often. But your lawyer? She knows the lay of the land, the people in it, and the expectations those people have. Listening to her makes sense.

While some small-business owners may question the loyalty of carrier-provided legal representation, remember that you're still the lawyer's client. That means your lawyer has a professional and ethical obligation to defend you, even if the carrier is footing the bill.

But there may be circumstances when hiring your own attorney makes sense. According to Michael S. Eisenbaum, a lawyer with [Gray-Duffy, LLP](#) in California, "If the carrier is raising significant coverage issues on the claim or the claim potentially exceeds the value of the insurance policy, then it is wise for a company to consult an independent attorney."

### HOW EMAIL DOCUMENTATION SAVED THE DAY

A computer company was revamping its client's computer system. To implement the changes the client wanted, the computer company recommended the client upgrade their entire system, noting that the client's software wouldn't run at maximum efficiency without the improvement. The client refused. When the software was operational, the client saw that their whole system needed to be upgraded and sued the computer company. Luckily, the company had email documentation of all the recommended upgrades. The emails helped the computer company because they demonstrated that the client failed to implement their recommendations.

## #4 Assess Your Situation Honestly

No one can blame a small-business owner for getting angry when they've been smacked with a liability lawsuit. However, strong emotions can be counterproductive, so Robert Stetson recommends business owners perform a cost-benefit analysis. "Take a step back and view the dispute as a business problem rather than a legal problem," he says.

You might start by asking yourself the following questions:

- Why am I going to court?
- How will the time spent on a lawsuit impact my business?
- Can I afford to see the suit to the end?
- Did I make a mistake?

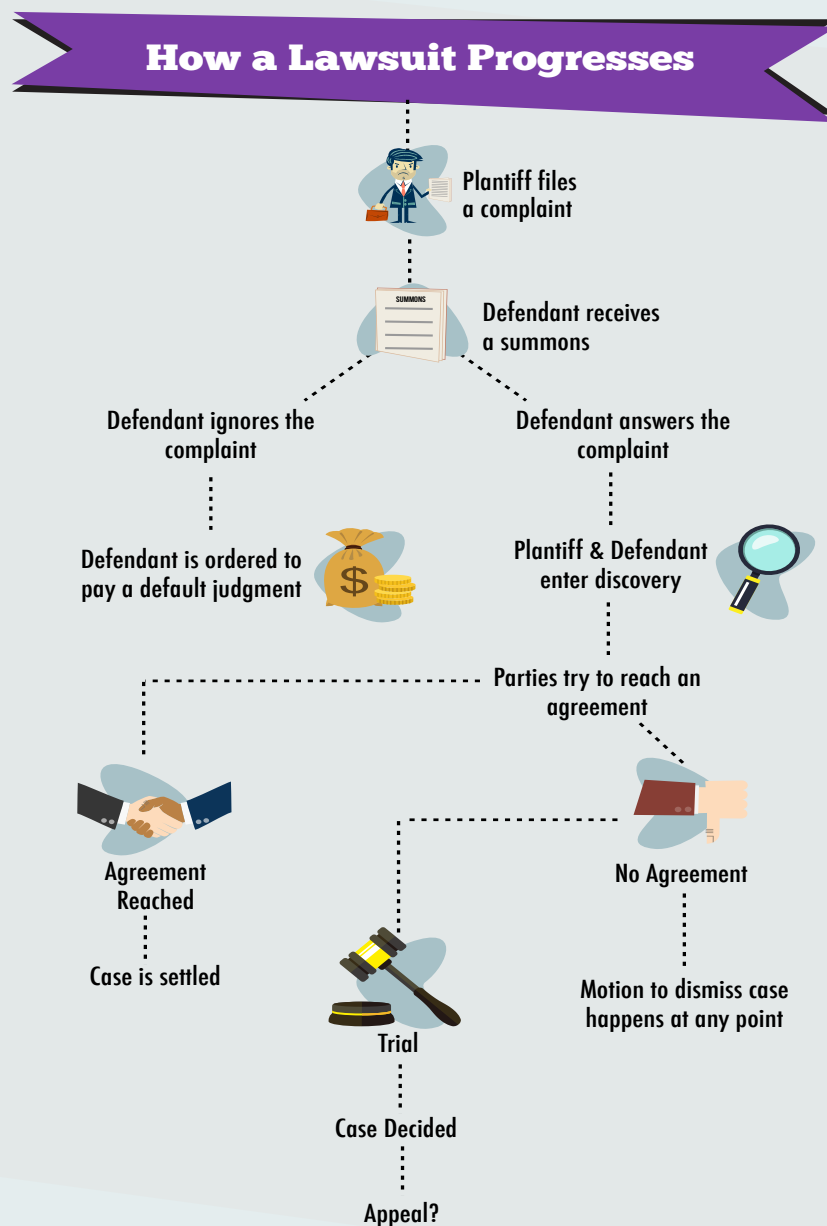
That last one is a tough question to answer, but it may be the most important one to think about, according to Lilenfeld. "You've got to be able to look yourself in the mirror and say, 'I made a mistake,'" he says. "And not only 'I made a mistake,' but, 'I'm going to do what I can to make it right.'"

Of course, you can settle even if you think you are in the right. In fact, settling is often the smartest and most cost-effective move you can make – unless you count avoiding court altogether. Read on for tips on preventing professional liability lawsuits.



# Preventing Professional Liability Claims

On a courtroom drama, a civil trial can go from initiation to settlement in a few weeks. But in real life, you can expect to spend at least six months, if not years, fighting the claim. Take a look at the image below to get an idea of how a lawsuit progresses.



Even if you negotiate a settlement with the help of your [Professional Liability Insurance](#) benefits, the claims process takes time and pulls you away from your business.

In short: you're better off avoiding court in the first place. Let's look at how documentation and communication can help prevent professional liability claims.

## How Documentation Helps Prevent Professional Liability Claims

"I'd say the biggest mistake small-business owners make is failing to have complete documentation related to the claim," says Shavon J. Smith. "Small businesses have a lot to juggle, and many tasks, such as thorough recordkeeping, go by the wayside."

Have you noticed how often the word "documentation" pops up when discussing professional liability lawsuits? That's not surprising, considering documentation helps your lawyer prepare your defense. However, written records can also nip professional liability claims in the bud because they...

- Make sure you and your client have the same expectations.
- Detail changes to a project's scope, deadlines, and pricing.
- Substantiate client requests.
- Provide an easy way to settle disagreements.

So when a client thinks you were responsible for data security, you can show them the obligations listed in your contract. If a client claims they never authorized a change, you can simply forward them the confirmation email you sent after you both agreed on that decision.

You may have a lot on your plate, but given how many problems good recordkeeping can prevent, documentation is one of the tasks you shouldn't let slide.

# What Kinds of Documents Can Prevent Professional Liability Claims?

Let's be clear: no document can actually stop a professional liability claim from happening. However, documentation can discourage certain claims. Here are some of the written documents you may want to have on hand:

- **Contracts.** Doing business on a handshake might seem like a good idea until there's a disagreement. According to Bongiovi, "All parties entering into an agreement need to be clear about both their expectations and what they intend to contribute – what are you getting and what are you giving?" A written contract not only makes that more clear, but may settle future disputes before they turn ugly.
- **Confirmation emails.** Did something come up in a phone call that changes the scope of your project? Did you get permission to go over budget in a meeting? What may be a universal agreement one day may be remembered differently another. Send a quick email recapping verbal communication so you have a date-stamped record.
- **Client complaint resolution.** Clients are going to complain. Your goal? Fix things before they get out of hand. Develop a written procedure for handling complaints. It should outline how to document the complaint, the steps you take to resolve the complaint, and your communications with the client.

You can create most of the documentation you may need on your own. However, consider teaming up with a lawyer for contracts and legal agreements, suggests Stetson.

"Most small business disputes center around a legal document, such as a contract, lease, or insurance policy," says Stetson. "Often, they turn on a phrase which could have been crafted in a manner more conducive to the small-business owner's needs and the realities of their business."

# Is Written Documentation the Only Way to Prevent a Professional Liability Claim?

When it comes to thwarting professional negligence claims, documentation rules the day. However, that doesn't eliminate the need for good old-fashioned customer service. Usually, it's the surprises that tend to upset clients, so try to notify them when you expect...

- Timeline changes.
- Budget overruns.
- Shipment delays.

Nobody wants to tell their client that a project is going to take longer and cost more, but clear communication may stave off disputes and salvage relationships. Alert your client to the problem and tell them the steps you're taking to fix it.

Just be sure to do it in writing.

## WHY CLIENT COMPLAINT RESOLUTION PROCEDURES ARE IMPORTANT FOR SMALL BUSINESSES

Gina Bongiovi, founder of the Bongiovi Law Firm, had a client who ordered thousands of dollars of merchandise from a promotional products company. When their order came, Bongiovi says, "The merchandise was all wrong - the logo was the wrong color, the shirts weren't the color listed in the catalog, the quantities were off." After many attempts to remedy the situation, the promotional products company sued Bongiovi's client for nonpayment. But instead of letting her client duke it out in court, Bongiovi made a call to the company's CEO, who was mortified. He had no idea a suit had been filed and agreed to rectify the situation.

Three years later, the two companies still work together.

Bongiovi's initiative ultimately saved both businesses from a major headache. However, if the promotional products company had enforced a complaint resolution process, she wouldn't have been involved at all.

# Takeaways on Surviving a Professional Liability Claim

Let's take one last look at the numbers. According to [RocketLawyer](#), an online legal services provider, a small-business owner's chances of being sued are high, considering that...

- Approximately **100 million** business lawsuits are filed in the United States every year.
- **20 million** of those are civil cases.
- **60 percent** of those civil cases are over contract disputes.

You don't have to do anything wrong to get dragged into court. Many lawsuits are the result of simple human errors like miscommunication.

Long story short? Professional liability claims happen. If you're prepared for them, they don't have to wipe out your business.

Just remember to:

1. Carry Professional Liability Insurance (here's the skinny on average [Professional Liability policy costs](#)).
2. Keep good client records.
3. Use contracts liberally and update them often.
4. Communicate with your clients.
5. Alert your Professional Liability Insurance provider if you get a whiff of a potential claim.
6. Follow your lawyer's lead throughout the claims process.

Even if the worst-case scenario becomes a reality, remember what you learned here so you can get back to business quicker.