

An Introduction to Indemnity Insurance

Business Information Factsheet
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Introduction

Whatever type of business you run, you may be liable to pay compensation to a third party who has suffered damages or has been injured as a result of negligence by you or your employees, or due to a faulty product or service. If this happens, and you are found to be responsible, a successful claim for damages could ruin your business financially unless you are covered by appropriate insurance policies.

This factsheet defines the different types of third-party indemnity insurance, including public and product liability, and professional and personal indemnity cover. It explains the benefits of indemnity insurance, which is provided to protect you and your business from the risks and consequences of claims against you. It also provides suggestions about what you need to consider when choosing indemnity policies.

This factsheet is intended as a starting point only and you should take advice from a professional insurance broker before you make any decisions.

Third-party indemnity insurance explained

Just as third-party motor insurance protects you from having to pay compensation should you cause loss, damage or injury to another road user, commercial third-party indemnity insurance will protect you from the consequences of claims for compensation made by anyone other than an employee who has suffered loss, damage or injury as a result of your business activities. This kind of insurance is not mandatory, but it is advisable to take out cover to protect you in the event of a claim.

There are several basic types of third-party indemnity insurance relevant to business:

- Public liability insurance.
- Product liability insurance.
- Professional indemnity insurance.
- Personal indemnity insurance.

Claims made by your employees for loss, damage or injury sustained while at work are covered by a separate, mandatory insurance policy called employers' liability insurance. See BIF 375, *Employers' Liability Insurance*, for further details.

Public liability insurance

Public liability insurance protects your business in the event that someone, other than an employee, brings a civil action claiming compensation for loss or losses sustained as a result of negligent actions or omissions by you or your employees.

A basic public liability insurance policy should cover you against claims made for:

- Injury - for example, if a member of the public slips on a wet floor at your place of business.
- Contraction of a disease or illness - for example, if a diner at your restaurant gets food poisoning.
- Damage to another's property - for example, if earth-moving equipment cuts through a water main and floods a neighbouring house.

In addition, it may be advisable to choose a policy that offers specific cover to suit your type of business. For example, a policy that indemnifies a business against accidental discharge of pollution into a watercourse would be advisable if you are running a small tannery. Your insurance broker will be able to provide advice on any specialist policies that apply to your particular type of business.

Unlike employers' liability insurance, public liability cover is not generally mandatory, but it is worthwhile to have this cover in place before starting to trade.

In some cases, the licensing authority, regulatory body or specific laws governing your type of business may insist you have public liability insurance in place before you can begin to trade. This applies, for example, to adventure activity establishments. Some customers may also refuse to use your services if you don't hold public liability insurance.

Naturally, premiums for public liability insurance vary considerably according to the risks and consequences associated with the nature of your business. Annual premiums for public liability cover can be low for a sole trader involved in a low-risk business. On the other hand, premiums may amount to several thousands of pounds for high-risk activities such as demolition or scaffolding work.

Basic public liability cover is often included as standard with employers' liability insurance under business office and content policies at no extra premium. Cover is usually tailored to suit the needs of your business. The indemnity limit - the maximum amount the insurance company will pay out in the event of a claim - is usually fixed in increments of £500,000. The typical level of cover starts at £2 million.

Product liability insurance

Product liability insurance protects you from claims made following loss, damage or injury sustained as a result of a product manufactured or supplied by your business. Generally, product liability insurance will not cover you for recalling faulty items, unless this has been specifically requested as part of the policy.

It is common for insurance companies to offer product liability cover to manufacturers and supply businesses as part of a complete public liability package. Again, the typical level of cover starts at £2 million.

Professional indemnity insurance

Architects, lawyers, solicitors, doctors, accountants and other professionals involved in a service that provides a particular skill, or offers specialist advice, may be held liable for loss, damage or injury sustained as a result of a breach of professional conduct or negligence. This relates to situations where a professional skill is exercised negligently or where incorrect or substandard professional advice is given.

An example could be a property surveyor who fails to identify that a house for sale has structural defects. They could then be liable to pay for repairs, any other expenses incurred and damages for stress and inconvenience suffered by the house buyer.

In addition to protecting against claims for breaches of professional conduct, a good professional indemnity policy should cover negligence involving:

- Breach of duty.
- Breach of legal liability.
- Breach of contractual liability.
- Breaches of intellectual property rights.
- Breaches of confidentiality.
- Defamation (libel and slander).
- Loss of documents entrusted to you.

This type of insurance will cover you for the damages you may have to pay out to the claimant and any legal costs involved.

The law does not require you to have this type of cover but, if a claim is made against you and you are taken to court, a successful claimant could force you into personal bankruptcy unless your business has such a policy. You may also find that the professional body, licensing authority or specific laws regulating your business activity require you to have a professional indemnity policy in place before you can set up in business. Solicitors and accountants, for example, must have professional indemnity insurance cover. If you are in doubt, consult a specialist insurance broker for advice.

Personal indemnity insurance

Even if you operate your business as a limited company, you are not immune from being sued personally in the civil courts. This is because the law treats the directors (and other responsible personnel) of a limited company and the company itself as two distinct and separate legal entities. Both the company and its staff can be held accountable, either separately or jointly, in any legal action or prosecution.

Personal indemnity insurance, often referred to as directors' and officers' cover, is a relatively new type of insurance cover created to offer protection to company directors (and others in positions of corporate responsibility) for actual or alleged breach of fiduciary duty, neglect, misstatements, errors or omissions.

Some policies also provide cover for corporate liability, employment practices liability and pension trustee liability. A good policy should offer the same type of protection as that offered

by professional indemnity cover. Areas a policy may cover could include health and safety, data protection, maintaining accounts, fraud and negligence. It should also cover any legal costs involved if a claim arises.

As with the other types of indemnity insurance, it is not a legal requirement to hold personal indemnity cover. However, a growing awareness among the general public of their rights as consumers and the introduction of new legislation in the UK and Europe means anyone in a position of corporate responsibility should give serious consideration to taking out this type of insurance cover.

What should you look for in a third-party indemnity insurance policy?

In addition to the basic standards of cover described earlier in this factsheet, a good third-party indemnity insurance policy should cover your business activities when:

- Visiting a customer or client at their home.
- Visiting a customer or client at their place of work.
- Customers or clients are visiting you at your home or place of work.

You should also check that your policy has the following:

- Cover for any compensation awarded against you, including settlements of such claims out of court.
- Cover for any reasonable legal costs and expenses incurred in the defence of civil or criminal actions.
- Cover for both you and your employees, including temporary staff, subcontractors and freelancers.
- Cover for punitive damages, such as the extra compensation awarded as a punishment over and above recompense for any loss.
- An adequate limit of indemnity so that the maximum amount your insurers will pay out is sufficient to meet any claim.

You should also check that it meets any requirements made by your professional association or licensing body in your industry or sector.

Hints and tips

- Always use a specialist insurance broker who has expertise in and experience of your type of business. The British Insurance Brokers' Association publishes a directory of specialist brokers which can be viewed at www.biba.org.uk/CustomHome.aspx.
- Be specific about exactly what cover you need, so that you do not pay premiums for cover you are unlikely to use. However, do not underestimate the value of the cover you will need. Average compensation awards are increasing year by year.
- If you or your employees work away from your regular place of business, you should ensure that your insurance cover remains valid in those situations.

- Make sure you update your insurance policies if any of your business circumstances change.
- If you change insurers, you may need to arrange 'run-off' cover so that your new insurer will cover you for events that happened prior to you buying the policy from them.
- Read the small print and pay particular attention to any exclusions of liability stipulated by the insurers.
- Shop around and get at least three quotes before making a decision.
- Pay your premiums on time, as failure to do so will almost always invalidate cover.
- Don't forget that, as with most insurance policies, you may have to pay an excess.
- Ask your professional or trade body, local chamber of commerce, enterprise agency or similar organisation to recommend an insurance broker who specialises in policies for your type of business or industry.

Further information

BIF 6 Insurance Cover for Business

BIF 32 Choosing the Right Business Legal Structure

BIF 341 An Introduction to Business Regulations when Starting Up

BIF 375 Employers' Liability Insurance

Useful contacts

The Association of British Insurers is a trade association representing UK insurance firms. It has a useful guide to business insurance on its website.

Tel: (020) 7600 3333

Website: www.abi.org.uk

The British Insurance Brokers' Association represents insurance brokers and intermediaries. The website includes a jargon buster, insurance guides and a 'find a broker' facility.

Tel: 0870 950 1790

Website: www.biba.org.uk

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