Known circumstances: better safe than sorry

Most general liability insurance policies are occurrence-based. When a claim is made, it reverts to the policy that was in effect at the time the relevant event took place. However, as Directors and Officers (D&O) policies are claims-made, cover is provided by the policy in place on the date of the claim rather than the event, which triggered it.

"Most directors understand that they have to notify the insurance company as soon as a claim is made against them," says John Kelly, senior partner at McDougall Kelly & Martinis. "However, a typical claims-made policy also requires you to tell your insurers about any circumstances that could give rise to a claim before you take out a policy."

These circumstances are hard to define. "This is a surprisingly complex area because it tends to be very subjective," says Kelly. "Whether a director believes that he or she has been negligent is irrelevant. The assessment is based on whether a reasonable person in the insured's professional position would have thought before taking out the policy that an event might result in someone making an allegation against them. Clearly this requires a judgement call that could vary from insurer to insurer."

The consequences of failing to mention an event, which is later defined as a known circumstance can be severe. "You could prejudice your rights to cover for any associated claim," says Kelly.

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However, as all notifications are lodged in the system, some directors are concerned that they might appear to be a poor risk and be penalised with higher premiums even if no claim eventuates.

"If there is no claim, it is likely that the notification will be removed from the records after a period of time," says Kelly. "And, in any case, the risks of notifying too much are far outweighed by the risk of forgetting to notify. On a practical level, it makes sense to be conservative when considering these matters. If you are in any doubt, talk to your insurer."