Consult
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Unit Pricing Errors - are they insurable or not?

Unit Pricing Errors (UPE) are a contentious type of loss in insurance.

A typical UPE scenario involves underpayment to one type of exited member and/or current member; and overpayment to another type of exited member and/or current member. Whilst current members are 'made good' – probably by way of a journal entry; and exited members (who have been underpaid) are made good by a 'top up' payment/cheque; the main source of loss is the inability to recover the overpayment made to exited members. Hence the fund ends up in shortfall.

There are also a range of other costs incurred related to a UPE: costs of indentifying and quantifying the problem; costs of rectification; costs of correspondence and postage; possibly the costs of members tax returns (if the member has to re-do the tax return) etc.

Professional Indemnity polices trigger on a liability to a third party resulting from a claim made against the insured (e.g. a demand for compensation). However in the case of a UPE, there is often no demand for compensation. Instead, the Insured recognises that they have committed a UPE; self reports to the regulator (as required by law) and then undertakes to rectify.

The insurance company can argue that the policy has not been triggered. An exited member who has been overpaid won't bring a claim. Underpaid members don't bring claims because usually they are completely unaware of the issue until they have been fixed. In other words – what triggers the policy? In many ways it's just a case of timing – the insured acts too quickly.

The Insured would rightly argue that 'it would be crazy to become aware of a UPE issue and do nothing until such time as ASIC issues an enforceable undertaking and/or the underpaid members realise their loss and bring a claim (with due reputational damage ensuing)'. This is true, but by acting so quickly the Insured runs into issues with their insurance policy e.g. there is no claim trigger; even if there was a claim costs are incurred and amounts are settled without Insurer consent etc.

In many ways the solution is obvious: dialogue – early and transparent. Speak to the Insurer immediately you become aware of a UPE. I have been involved in UPE claims (as an Insurer) where we paid the loss on the basis that we understood that whilst technically no claim had been made, we understood what would have happened if the Insured had delayed (ultimately a claim would have

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been made). This is commonsense. However, you do not want to be testing an Insurer's commonsense after you have already paid out millions to rectify a UPE.

Lastly, be very careful on the costs you incur and how you record it. The policy definition of loss probably won't extend to all types of financial cost you incur during a UPE. However, good records, clear rationale and early discussion will see you best placed to get some of the 'grey' costs covered (especially if your policy has mitigation cover).

Are all policy restrictions/limitations contained in the Exclusions?

It would be understandable to assume that all restrictions/limitations to your policy coverage are outlined and defined by the policy exclusions. However this is not the case. In fact, many restrictions to your policy coverage are contained in policy definitions (i.e. where key words are defined) and in general conditions (clauses that define items that you and the Insurer need to abide by).

Here are some common examples taken from leading policy coverage's, but I could have selected many more:

1. Your policy covers professional services in relation to Funds. However, if you look at the definition of fund, it may well say something like this:

   Fund means each managed investment scheme, unit trust, partnership or investment company anywhere in the world managed, operated or administered by an Organisation but does not include a Hedge Fund, Mortgage Fund or Property Construction Fund unless such fund is specified in a scheduled endorsement to this Coverage Section.

2. Your policy covers Loss. The definition of Loss is often long and comprehensive, but almost all definitions then say *"Loss does not include..."* and then outline an equally long list of items not covered.

3. Tucked away under 'General Conditions' you may find that many policies have a very specific restrictions in relation to 'Changes in Risk; Other Insurance; Valuation of Losses'. All these items are relatively standard, but each in their own way imposes a restriction on the cover that you have purchased.

Key message: if you ever take the time to read your policy exclusions to see what you are not covered for, you may as well continue through the rest of the document. If this doesn't appeal to you (and I don't blame you!) then at least ensure your Broker takes the time to go through the whole document.

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