

# A/E RISK REVIEW

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**FINANCE INSURANCE, LTD.**  
Quality Service For Your Insurance Needs

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## Getting the Right PL Coverage at the Right Price

*The following material is provided for informational purposes only. Before taking any action that could have legal or other important consequences, speak with a qualified professional who can provide guidance that considers your own unique circumstances.*

The professional liability insurance marketplace has continued to be soft. That is, there is significant capacity within the insurance industry and major carriers are in heated competition for your insurance dollars. Because of this intense competition, rates have remained relatively low.

True, the 2011 ACEC Professional Liability Insurance Survey of Member Firms forecasts higher rates in the coming year, but that forecast is based on the assumption that economic conditions will stabilize. Unfortunately, there is little on the immediate horizon to indicate that the economy will pick up significantly any time soon.

Regardless of whether rates remain low or begin inching up, design firms should not shop for insurance based solely on price. There can be significant differences in coverages among policies and, more important, differing quality in the claims, loss prevention and other services you receive from insurance carriers and agencies. Lately, some insurance companies have entered the A/E insurance market simply because they have excess capacity and are looking for an additional inflow of premiums. They seek income in this market even though they do not necessarily have expertise in the design industry or solid experience in defending A/E claims.

## Is Going Bare an Option?

In tough times, some design firms have decided to forego professional liability insurance altogether. They take the chance that they haven't made and won't make errors or omissions in their professional services and, if they do have a project dispute, they can resolve the problem without an expensive claim. Some architects and engineers reason that without professional liability insurance, they don't have "deep pockets" and therefore a claimant will look elsewhere to find remedy.

"Going bare" without insurance is obviously fraught with risk. Facing a claim without adequate coverage not only puts a firm's assets at risk, but the principals' personal assets can also be in peril. The corporate veil cannot always protect a design professional's personal savings, home and other valuables.

Most design professionals recognize professional liability insurance as a necessary cost of doing business. They realize they need the financial protection that PL insurance provides. Equally important, they realize that most clients require the designers they hire to carry adequate insurance limits.

Your best approach to managing professional liability risks is to work closely with a specialist insurance agent who knows the ins and outs of the A/E insurance market and who can help you manage your risks and your insurance premiums. An agency like ours can help select the appropriate insurance carrier and recommend the appropriate coverage limits and deductibles. These recommendations will be based on your exposure to claims, your appetite for risk, the types of design services you offer and the annual fees you earn. We can then quote you premiums from one or more insurance providers based on the current market conditions.

You should begin planning today for your next professional liability insurance renewal. Don't wait until 30-60 days before your current expiration date. Call us at any time to begin planning your strategy for keeping your insurance available and affordable.

How do you get the best bang for your insurance dollars? How do you minimize the cost while retaining the coverage you need? Here are some tried and true tips for getting the right insurance at the right price.

### **Take Advantage of Loss Prevention Education Programs**

Some insurance carriers offer substantial premium credits if you successfully complete their loss prevention education programs. These programs not only result in a sizable reduction in your premiums (typically 10%), they teach you valuable loss-prevention techniques that can avoid future losses and earn the professional continuing education credits you need to practice your profession.

### **Obtain Contractual Risk Management Credits**

Some insurers also provide premium reductions or credits when design firms agree to use specific clauses in their contracts with clients. Clients are often willing to negotiate such clauses when they are educated on the risk-reward inequities that most design firms face when such clauses are absent. These clauses can include:

- A Limitation of Liability (LoL) provision that contractually caps the amount of liability you have to your client, usually expressed as a set dollar limit or your available insurance limits.
- A waiver of your liability for consequential damages.
- A clause that specifies you will use mediation as your first method of dispute resolution.

### **Consider Alternatives to Higher Practice Policy Limits**

Suppose you currently carry \$2 million in professional liability coverage, but your new client on a large project is asking for \$5 million in limits. With claims severity on the rise, coupled with the ever-growing number of projects you have worked on over the years, higher insurance limits may indeed be in order.

However, if increasing your aggregate practice policy limits is overkill for your situation, or the increase in premiums is simply too big of a hit on your pocketbook, you might consider a few less-expensive options that provide added protection for your demanding clients:

1. **Specific-project excess.** With specific-project excess coverage, you can maintain your current limits on your practice policy while purchasing an endorsement that provides a higher limit to cover a specific project. For example, you can maintain a \$2 million practice policy and purchase a \$5 million limit on one project for substantially less than raising your entire policy limit to \$5 million.
2. **Specific-client excess.** Let's take the previous example one step further. Suppose you find a new client who wants you to work on multiple projects, but demands higher insurance limits. Specific client excess is similar to specific project excess, except the higher limits apply to all projects performed for a particular client. Again, this increased coverage is more affordable than raising your entire limit.
3. **Split limits.** Instead of purchasing a \$5 million practice policy you might purchase a \$2 million/\$5 million split-limits policy. Here, the policy limit on a single claim is capped at \$2 million, but the total coverage for any one year is \$5 million. This eliminates the chances that your policy would be wiped out by another claim and increases the chances that coverage will be there for all of your clients' projects.

### **Investigate Project Insurance**

There is one coverage option that can provide a project owner the higher limits it demands, virtually guarantees that coverage will be there when needed – and may actually *reduce* your insurance premiums. This unique coverage option is called project insurance.

With a project insurance policy, the owner realizes the following benefits:

**A single policy for a single project.** All members of the design team can be covered under one policy, and the limits are dedicated to that project only.

**Full control over policy terms.** The owner chooses the policy limits and the duration of coverage -- often available up to five years after substantial completion.

**Secure coverage.** Most project policies are noncancellable, as long as premiums are paid, policy conditions aren't breached and no material misrepresentations or concealment have been made on the application.

**No premium rate surprises.** The project policy premium is typically determined according to a guaranteed rate based on final construction cost.

**Single-point claims responsibility.** Insuring the entire design team with one policy makes it easier to solve problems with less finger pointing and more cooperation.

So what's the catch? Why would an owner turn down the project policy option? Typically, project owners pay for the project policies, since they benefit most from the coverage. However, costs can be offset and shared with design firms through premium reimbursements or negotiated lower fees. (Since fees on the project likely won't be counted to determine practice policy premiums, a design firm saves money on its annual insurance costs.)

Unfortunately, insurance companies have had severe losses on project policies and have become quite selective in writing them. Some insurers do not issue project policies and, among those that do, the cost and the required deductibles can be high. Because we specialize in professional liability insurance for design firms, we can help you determine whether such coverage is available. We can also help explain the benefits and costs of the project policy to your client, coordinate implementation, and provide loss prevention assistance throughout the life of the project.

Despite the advantages, owners may be unwilling to incur the cost of a project policy. A less expensive alternative may be owner protective insurance.

## Owner Protective Insurance

An owner protective (OP) policy provides protection for the project owner in the form of excess coverage over and beyond the architects' and engineers' practice policies. The design team's individual practice policies provide primary coverage and come into affect first. Then, if the responsible party's practice policy limits are depleted, the OP policy covers some or all of the additional damages, depending on the policy conditions and limits. This enables the project owner to secure the policy limits they desire without you having to increase your practice limits.

Because the OP policy comes into force only after the practice policy of the design firm has been exhausted or is otherwise unavailable, owner protective insurance is less expensive than a project policy. OP policies can be purchased annually or for the life of the project. Retroactive coverage can often be provided on projects already in the construction phase. Environmental engineering exposures can also be covered. "Blanket" OP policies may also be available for an owner's multiple projects.

In most cases, the design firms must maintain a minimum level of coverage (often \$1 million to \$2 million) on their practice policies. These limits may be higher for projects with substantial construction values. Also, any litigation costs incurred by the owner to bring the claim are not covered. Conversely, since the owner is the named insured on the project, OP limits will not be depleted by the legal defense fees incurred by the design firms.

As an example of an OP policy in action, suppose there is a \$1.5 million loss to an owner's project that is determined to be the result of the negligence of the prime architect. The architect has \$1 million in coverage through a practice policy. The architect's primary policy would cover the first \$1 million in damages and the OP policy would cover the balance of \$500,000. However, if \$50,000 of the losses were made up of the owner's litigation expense, the policy would cover only \$450,000.

## We Are Your Ally

As we've shown, there are a number of practice management techniques and coverage options that design firms can consider to provide adequate PL insurance coverage while controlling costs. We are

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willing and able to help you evaluate your needs, discuss your options and help educate your clients on the various options available. We can even help you bring a client with unreasonable or uninsurable demands back to realistic coverage expectations.

**Can We Be of Assistance?**

*We may be able to help you by providing referrals to consultants, and by providing guidance relative to insurance issues, and even to certain preventives, from construction observation through the development and application of sound human resources management policies and procedures. Please call on us for assistance. We're a member of the Professional Liability Agents Network (PLAN). We're here to help.*