

XL Insurance @-Clips

Your Client's Impossible Insurance Requirements

It's only natural. Clients want to know that you have adequate and appropriate insurance. That's why most professional services agreements contain detailed specifications on the insurance clients expect you to carry.

But lately, many design professionals have found themselves in situations that would make seasoned insurance professionals weep. In addition to clients' usual unreasonable demands that they be named additional insureds on your policy or requiring you to defend them, they're also insisting on coverage terms that are impossible or impractical for most design professionals to meet.

MAXIMUM DEDUCTIBLES

Take, for example, deductibles. Our design professionals complain that clients are specifying maximum deductibles that policyholders should carry on their professional liability policies.

Your challenge is to explain to your client that choosing the right balance between the deductible, premium and coverage is a *business* decision negotiated between you and your insurance company. In fact, depending on price, market conditions, your annual billings and appetite for risk, this choice may change from year to year. You need the freedom to make the best choice for your firm.

EXTENDED COVERAGE

It's not unusual for clients to demand that you promise by contract to maintain specific levels of professional liability coverage for an extended time. But as we've all been reminded over the past few years, the professional liability insurance market can be volatile in both price and availability. Because of this, and the fact that the policies are generally annually renewable and written on a claims-made basis, it's unwise for you to agree to a contract requirement to maintain specific levels of coverage for a lengthy period. You might not be able (or want) to comply in the future. What if certain coverages were suddenly unavailable five years from now? If you had agreed by contract to carry these coverages for an extended period, you'd find yourself in a breach of contract—through no fault of your own.

The most you should promise by contract is to:

... attempt to maintain such coverage in effect for _____ years after substantial completion of the project *to the extent it is commercially available at reasonable rates.*

If you explain the issues, a wise client will likely agree.

HIGHER POLICY LIMITS

Clients are also asking for coverage at limits far above what you normally need for your practice.



Many clients don't understand that your policy limits need to bear some reasonable resemblance to the risk your design represents to the client. Instead, they tend to focus on the kinds of risks represented by contractors and the insurance coverages they have.

Let's think about this for a minute. What's the worst that can happen on a \$2 million constructed-value project if you're, say, the architect? Assuming that you don't undertake any jobsite safety responsibility (through your contract, actions or statements) and you do an adequate job of specifying materials and finishes, could your professional acts cause \$2 million in damages? Not likely. Your risk of causing a bodily injury claim—the really expensive type of claim is relatively small as well. In fact, statistics compiled by the XL Design Professional group of the XL Insurance companies show that such losses represent less than eight percent of claims against design professionals.

SPECIFIC JOB EXCESS

Market conditions can make it expensive to raise overall policy limits, which is one reason why client demands for higher limits on your professional liability policies are increasing. To get around the issue, some clients have been asking design professionals to get "specific job excess" coverage for their projects.

Specific job excess—SJX in insurance-speak—is a way of bumping up limits for a single project. As an additional layer of coverage for a particular project added by endorsement, SJX runs with and is subject to the terms and conditions of your practice policy. But unlike a project policy, SJX insures just your firm, not the entire design team, and is an annual, not multi-year, policy, with no guarantee that you can renew each year.

Still, SJX, together with underlying blanket policy limits, may offer the total limits the client seeks.

However, this approach poses two problems. First, clients are also asking for unreasonably high limits on SJX endorsements. We know of one individual who, on a project that involved a \$20,000 design fee, was told to get \$1 million SJX coverage. When he asked the client for an explanation, the client told him it was a million-dollar project and he wanted to be sure all the risks were covered.

Secondly, SJX isn't easy to get these days. The reasons are complicated. For one thing, the rates reinsurers are charging insurance companies are pushing premiums up. Also, the terms reinsurers require determine what insurance companies can underwrite. For example, most reinsurers prefer a limited number of SJX endorsements on a given practice policy.

Another reason SJX coverage is not readily available is that in today's insurance market, underwriters are really *underwriting*. That means they're taking a closer-than-ever look at projects, practices and risks in an attempt to limit their exposure and yours. Thus, specific job excess endorsements are generally available only for lower-risk projects. That almost certainly rules out condos and other over-the-top risks and may also rule out certain geographic areas. Your discipline and role in the project will also be factors.

When considering SJX endorsements, underwriters want to make sure the projects have squeaky-clean contracts, i.e. reasonable terms and conditions and no onerous indemnities. They want to know that the limits are in line with your fee, *not* the value of the project. Finally, they look at the limits you carry on your practice policy. If

you continually ask for SJX endorsements, perhaps it's time to raise your limits after all.

KNOW YOUR LIMITS

What should you do if your client asks for high limits?

Evaluate. Become more rigorous in your client selection. In this economy, insurance companies have to be responsible and realistic business people; so do you. Quality client selection is one criteria your insurance underwriter will look for. It should be one of your criteria too.

Communicate. Have a frank discussion with your client about why he or she is asking for blue-sky limits. Does the owner think your risk is somehow comparable to that of the contractor? If so, talk about the risk that you represent in the overall project. Explain that you (and every party on a project) should assume risk only in proportion to your contribution to the project as well as your ability to bear that risk. On the other hand, if the client's hoping for a convenient deep pocket to pay for any problems, it's time to reassess whether you want the project.

Negotiate. Surprisingly, you may be able to leverage such discussions to negotiate a better contract. Explain that insurance companies look very carefully at requests to raise limits. If your client persists, explain that your insurer will only agree to a reasonable limit and only if the client agrees to delete this warranty and that one-sided indemnity and water-down those other onerous clauses.

Limitation of Liability. Perhaps you can even get your client to agree to a Limitation of Liability clause. Limitation of Liability is not an avoidance of risk, rather, it's a way to properly allocate risk between you and your client. If you need help convincing your client, contact your insurance agent or professional liability insurance carrier.

READ THOSE CONTRACTS

Remember, clients often confuse professional liability with general liability and try to specify the same coverage they require of contractors. Therefore, it's important to review and negotiate client-drawn contracts and delete unattainable or unreasonable requirements.

Don't make the mistake of agreeing by contract to excessively high limits, specific job excess or any insurance provision before talking with your agent or broker. You might not be able to comply and will be forced to go back to your client, hat in hand, to renegotiate—surely not the best way to embark on a new project.

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