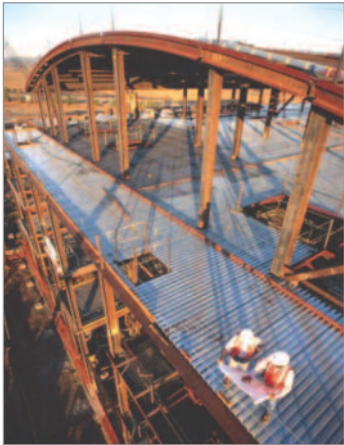




The Risks of Bending the Rules for Long-Time Clients

Anyone who's ever let a favorite niece or nephew sneak an extra slice of birthday cake knows what it's like to play favorites. But when design firms set aside principles of good management or relax their normally stringent contract requirements for the sake of a favorite client, such actions can backfire in a variety of unfortunate ways.



At the Design Professional group of the XL Insurance companies, we don't have to go far to find examples of the damage that can be done when design professionals let a client relationship overrule sound judgment. One of our insureds was retained by a long-time client to render an opinion on structural issues prior to acquisition of a large commercial office building.

After drafting a report that pointed out certain structural issues that might have interfered with the client obtaining the required financing, the design firm was urged by this client to downplay those issues in the final report. While the final report may have been to the client's liking, the firm later regretted making such a misstep. The client later claimed that had they known the true condition of the building, they would not have purchased the building and/or entered into the financial arrangements with the lending institution. The claim was settled for more than half a million dollars.

It's easy to understand why a firm would go to almost any lengths to satisfy a long-time client or reel in a big new one. A rich, prolific client that can provide a firm with a steady stream of revenue is a rare commodity. But every firm needs to recognize that its dependence on one or two clients for a majority of the firm's work can have a serious downside as well.

There are several ways in which a firm's dependence on a "cash cow" can come back to haunt it. The rush to please a single client can cloud a firm's judgment, particularly when negotiating a contract. Indemnity, payment terms, claims defense and resolution strategies are all areas in which the firm should treat a favorite client like everyone else. Don't equate having a big client with giving away control.

A firm's reliance on a dominant client can also put the firm's insurance carrier at a disadvantage during a claim defense. Our claims files bear out that, if a firm believes the result could drive the client away; the firm may be reluctant to fully cooperate. We've seen instances in which our insured wants to resolve a claim to the client's total satisfaction, even though the insured hasn't done anything wrong. While we try to help our insured's preserve their business relationships, their insurance policies are meant to cover errors in design.

The following are suggestions for preventing the types of problems that arise when you become too dependent on too few clients:

Diversify. While most A/Es would rather concentrate on design than marketing, depending on one or two big clients to carry your business is a poor strategy. Who knows what can happen to a client? They may bring design in house; new management may decide to go with a different design firm; or the company may suffer a financial calamity and go out of business. Your firm might be right behind them.



One way to maintain a strong relationship without surrendering control is to include language in your contract that requires the client to acknowledge that the firm's professional liability policy requires the firm to cooperate with the carrier, and gives the firm and the carrier the right to control the defense and dispute resolution process. It could also be pointed out that the firm's policy requires the insured to consent to a reasonable settlement, and that there are unfavorable consequences to the firm for unreasonably withholding consent.

And, as is so often the case, a rigorous client selection process is one of the best ways to prevent claims. After all, if you find yourself depending on one or two clients for a majority of your revenue, you'll want to know that you did your due diligence before choosing to work with them. Client selection, and especially managing client expectations, help the firm maintain a reasonable degree of control over its ability to manage its business and protect its own interests, without impacting its coverage and relationship with its insurance carrier. (To read more on client selection, click the following link: http://www.xldp.com/library/8179_Client_Selection.pdf)

The information in this article is the product of over 30 years of front-line claims experience and is part of the educational service provided to the design industry by the Design Professional group of the XL Insurance companies. For more information, other loss prevention resources and to find an agent in your area, visit xldp.com or phone 800-227-8533 ext.2102508.

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