

MAKING THE TRANSITION TO RUNNING YOUR OWN FIRM

**INSURANCE COVERAGE ISSUES
FOR PROFESSIONAL PRACTICES**



**Brought to you by The AIA Trust in conjunction with
Victor O. Schinnerer & Company, Inc. and CNA Insurance,
providers of the AIA Commended Program of professional
Liability insurance.**

For more information on insurance and benefits programs go to www.TheAIATrust.com

MAKING THE TRANSITION TO RUNNING YOUR OWN FIRM

INSURANCE COVERAGE ISSUES PROFESSIONAL PRACTICES

**Victor O.
Schinnerer &
Company, Inc.**

For more information on insurance and benefit programs for emerging firms, contact The AIA Trust at 1-202-626-7321. If the question involves the DesignOne package of insurance coverages, professional liability insurance, employment practices liability insurance or property and casualty coverages, contact Schinnerer at 1-888-867-9327. (DesignOne information is also available through 1-301-961-9889). Program information also can be obtained from The AIA Trust's web site, www.TheAIATrust.com, or from Schinnerer's sites: www.Schinnerer.com, or www.PlanetAEC.com.

In operating a professional practice as a private business, a licensed design professional faces many risks. A prudent design professional entering private practice should consider insurance to cover certain exposures, including professional liability, the risk of property loss, and the risk of personal loss. As firms grow and consider providing benefits to staff, they may participate in health insurance, life insurance, and pension plans. Sole proprietors consider acquiring insurance to protect themselves and their families from injury or financial harm.

As a participant in the highly complex design and construction process, a design professional encounters a variety of risks that can result in financial losses to numerous people. Insurance is a means of managing those risks by transferring them to an insurance company in return for a premium payment. While not all risks that challenge a construction-related professional service firm are insurable, a new firm must identify, assess, and plan for how its exposure to risk will be handled.

PROFESSIONAL LIABILITY

A key set of professional and business risks arises from the possibility of causing harm because of negligence in performing or furnishing professional services. Negligence, when referring to the services of design professionals, is a legal term stating that the design professional breached an obligation to a client or others to provide services in a reasonable manner as required by a contract for services or by operation of law.

Negligent acts, errors or omissions may cause damage to owners, contractors or other third parties. If such responsibility is established, the firm and its owner may be liable for correcting these damages. In buying a professional liability insurance policy, sometimes inappropriately called *errors and omissions* or E&O insurance, the firm is asking a broader financial entity—the insurance company—to absorb a portion of the costs of claims in exchange for a premium paid to the insurance company.

Not all firms elect to purchase professional liability insurance. This business decision is made as part of the firm ownership's overall approach to managing its practices and risks. Even

those firms that do buy professional liability insurance retain the risk for expenses that fall within their deductibles or exceed their policy's limits of liability—or that are excluded from the scope of coverage.

The Schinnerer Professional Liability Insurance policies with CNA are only available through independent brokers who represent the prospective policyholder by obtaining and assessing insurance information in an objective manner. Other policies may be offered by agents of insurance companies who may not be able to provide objective and rational opinions of coverage, suitability or value.

The Schinnerer policy with CNA was developed at the request of The American Institute of Architects and the National Society of Professional Engineers. These organizations still monitor the program's operations and evaluate the program's effectiveness and value. Since 1957, both the AIA and NSPE have awarded the Schinnerer program with CNA the unique status as their Commended Programs.

Sources of professional liability insurance. Most design professionals purchasing professional liability insurance coverage do so through independent brokers. These brokers represent the interests of their client and not those of the insurer. By contacting a broker experienced in design professionals' professional liability insurance, a firm can shop around for insurance, and usually obtain access to many insurance markets and, with the professional advice of the broker, decide which carrier best fits its needs. Some insurance companies are represented by agents who are authorized to place policies on behalf of that company in a predetermined territory. These insurance agents represent the interests of the particular insurance company and may not have access to the entire insurance marketplace.

Regardless of whether a firm chooses an independent broker or an insurance carrier's exclusive agent, the firm will want to select its broker or agent in much the same way it selects its lawyer and accountant — with care and scrutiny of qualifications, services available, cost, and, not least, chemistry and commitment.

In evaluating insurance options, design professionals will find that each professional liability insurance policy is different in some respects from all the others. The design professional must reconcile coverage and cost, but the variety of coverages available through endorsements, exclusions, and the core policies themselves makes reasonable cost comparisons very difficult. It is important to carefully evaluate endorsement options, coverage limits, and deductibles. The added costs for some of these add-ons, including increased limits, can be minimal.

In addition, the service and stability of the insurance carrier must be considered. Services provided by professional liability insurance companies range from extensive educational and management assistance programs such as those offered by the Schinnerer and CNA program to little or no information, advice or guidance. Some firms buy insurance policies while others prefer a total risk management program that includes professional liability insurance coverage.

The true value of a professional insurance policy probably is best defined by the claims handling process. The specialized expertise of a claims manager familiar with design and construction issues and the knowledge, interest and sensitivity of defense counsel may be the most critical characteristic for selecting an insurer.

While it is often difficult to rank competence and service above the cost of coverage, the “low cost” insurer may be quite like a “low bid” contractor. Certainly, the attraction of a lower initial premium cost should be weighed against the potential of future, significant rate increases and the risk that the carrier might not continue to offer professional liability insurance. In the insurance industry, carriers enter and leave the professional liability arena as business conditions change.

The Schinnerer program with CNA is the only professional liability insurance program that submits to regulation by every jurisdiction. While this admitted status makes operations more difficult, it provides protections to policyholders that do not exist in other programs that may operate on an “excess and surplus” basis to escape full regulation.

Admitted companies. States permit insurance companies to sell their products on either an admitted or non-admitted (what is usually called excess and surplus or E&S) basis. Companies that sell insurance on an admitted basis subject themselves fully to the oversight of the state and must have their rates, coverages, and policy forms reviewed (and, in many states, approved) by the state. In addition, admitted companies must contribute to a state guarantee fund to be drawn upon to pay claims should that company be declared insolvent and lack the financial wherewithal to pay the claim itself. This process protects the consumer.

Non-admitted carriers are not subjected to such scrutiny. Nor are they included in the state guarantee fund. Accordingly, they have an easier time moving in—and out—of the insurance market. For these reasons, many states require brokers to seek coverage from admitted carriers first, placing coverage in an E&S market only when admitted carrier coverage is not available for the specific firm. Some states even require brokers to warn the insured person or firm that they are placing their coverage with a non-admitted carrier by stamping the policy to that effect.

Claims-made basis. The possibility of encountering a limited number of admitted insurance carriers might leave the design professional in a difficult position due to the traditional *claims-made* nature of many professional liability insurance policies. “Claims-made” means the policy must be in effect at the time the claim is made against the architect—even

though this can be years after completion of construction—and the coverage had to be in effect when the negligence occurred. Claims-made policies are common to professional liability insurance and should not be confused with *occurrence* policies common to general liability insurance.

This distinction is important to understand. Under a *claims-made policy*, all coverage ceases when the policy is canceled or not renewed (by the firm or the insurer), even though the design professional may have been insured when the services were rendered. Under an *occurrence policy*, a claim filed after policy cancellation or renewal will be covered if the policy was in force when the incident that caused the claim occurred, regardless of whether the insured was covered when the claim was made.

The claims-made basis is used for professional liability insurance coverage because it makes costs to insurers more predictable. If coverage for professional liability risks were offered on an occurrence basis, the cost of such coverage would be prohibitive because the insurers would have to include contingencies for many more unknowns. This distinction, however, means that firms that buy insurance as a risk management tool have to keep it in force on a continuing basis for continuing protection. When a firm remains with one carrier, the claims-made nature of the policy is not an issue. If a firm switches carriers, *prior acts* coverage usually is available to cover the risks from the earlier period.

The claims-made feature raises the question of protection upon retirement or withdrawal from practice. Professional liability coverage is available in a few programs to continue the protection needed by design professionals who withdraw from active practice. Usually this “tail” coverage is arranged by endorsing the basic policy. Some states require admitted carriers to provide some level of tail coverage at an extra cost to the insured. For example, the CNA/Schinnerer program has coverage available to design professionals who have been insured for three consecutive years prior to retirement; the policy then covers the retired design professional for prior acts. Coverage is similarly available to protect the estates of deceased design professionals if this is warranted.

Prior acts. Firms can buy coverage for professional acts and services that took place before they first became insured or when they were insured by another carrier. The scope and availability of this “prior acts” coverage varies from insurer to insurer. As an example, the CNA/Schinnerer program provides prior acts coverage (to the day the firm started practice) that is available to eligible firms after they have been in the program for two years.

Coverage. Generally, a professional liability insurance policy covers the insured firm’s liability for negligent acts, errors, or omissions arising out of the performance of professional services as a design professional, provided these services are performed within the territory defined in the policy. All policies cover the United States and many offer worldwide coverage in the basic policy or by specific endorsement.

A basic policy provides legal defense of claims covered by the policy and pays defense costs subject to the policy limit and deductible. Most insurance companies retain attorneys who are experienced in the defense of professional liability claims. When a defense attorney is selected and appointed to defend the policyholder, it is that policyholder—not the insurance company—that is the defense attorney’s client. Some firms, however, may be able to select their own defense counsel.

Broad policies insure not only the firm as the “named insured” but also any partner, executive officer, director, stockholder, or employee of the insured firm when that individual is acting within the scope of professional duties. Some lower-cost policies may not automatically provide such broad coverage. Because professional liability is a “personal” exposure of the licensed design professional, policies that only insure firms leave the individuals responsible for the design or who sign and seal the documents in a precarious position.

Endorsements and exclusions. Policyholders and insurance companies can modify coverage through endorsements and exclusions. Exclusions are sometimes added to specifically preclude coverage for identifiable risks. This can be done to reduce the cost of the policy or to allow coverage in situations where risks cannot be determined. Sometimes endorsements that expand coverage have an

additional premium cost; sometimes they are included automatically at no extra cost. Firms should be assertive about having their broker or the insurance company's agent, check into those expansions of coverage that they need to practice or that fit into their practice management goals. Endorsements include, for example, first-dollar defense, special project additional limits, expanded equity interest, and design/build coverage.

Limits of liability. How much insurance a firm buys is a function of its financial needs (including those of its principals), its tolerance for risk, its confidence in its risk management abilities, and the demands of its clients. Minimum annual and aggregate limits of liability for errors and omissions insurance are usually set at \$100,000, with maximum limits running as high as \$15 million. And even higher limits can be arranged for special circumstances.

“Annual and aggregate” limits of liability are available to pay for claims and associated legal expenses in a policy year. The costs of claims and legal expenses that exceed the limits must be absorbed by the firm. With most policies, the firm receives a new limit each policy year. Some insurance programs, such as the CNA/Schinnerer program, permit their policyholders to buy excess limits for specific projects or to buy “split limits” with one limit per claim and another for the aggregate in a year. The insurance company can determine the cost of these variations for the insured to consider (without an obligation to purchase them).

Deductibles. To encourage risk management, insurance companies require a firm to have a deductible that the firm must pay to defend each claim or after each determination of negligence. Deductibles as low as \$1,000 are available, but many firms increase their deductibles to lower their premium costs. As with most insurance, the higher the level of risk retained by the insured — is, the higher the deductible — the lower the premium cost. Determining the balance between the deductible, the premium, and the coverage basically requires weighing probabilities and finances and is best carried out by the firm with the advice of its broker. In making this decision, the firm will want to remember there is a new deductible obligation with each claim.

Costs of insurance. Each firm's premium is calculated individually, based on such factors as the firm's practice, project mix, claims experience, coverage needs, and resulting risks to the insurer. Hence, comparing premiums of different, but seemingly like, firms is difficult at best. This is true because firms, just as insurance policies, differ from one another. Thus, a firm should pay attention to its application and work with a broker who can present the firm well to the insurance company. Because prudent insurers must increase the cost of insurance if risks cannot be clearly delineated, the more specific and unambiguous the information provided, the more likely the premium will be minimized. A prospective policyholder should also feel free to call the company (with its broker) to ask how the firm's premium is determined.

Contractual liability. Professional liability insurance companies provide coverage only for the insured firm's negligence in performing or furnishing professional services. The firm has a duty to meet the standard of care for the services it has undertaken. Coverage for express warranties and guarantees—separate contractual promises—is excluded under most policies. Certificates that have the effect of warranties — for example those that do not state a known fact or express a qualified professional opinion— are also excluded. Promises to absorb costs of errors and omissions, absent negligence, are excluded, too, because such promises have the effect of a warranty.

Insurability problems also arise when owners ask design professionals to contract to hold them harmless or otherwise indemnify them. An extension of coverage is needed when a design professional agrees by contract, in writing or orally, to indemnify and hold harmless some other person such as the owner or contractor — unless the design professional is indemnifying the other person for the design professional's own negligence, at which point under many policies coverage is automatic. In most contractual liability situations, such coverage may not be possible.

A hold-harmless (or indemnification) clause essentially is a contractual assumption of another's legal liability. Under many circumstances, the use of a hold-harmless clause is an acceptable and advisable practice as long as the contractual transfer of liabilities is not against public policy and can be covered by insurance or available assets.

The use of standard documents is supported by the Schinnerer Program because the contractual liability established by their use parallels the professional liability as determined by an assessment of, and comparison to, the applicable standard of care. The Schinnerer risk management program provides information on contractual risks including the publication Managing Risk Through Contract Language and a "Terms and Conditions Review Guide."

For instance, in *AIA Document A201: General Conditions of the Contract for Construction*, a clause is included to require the contractor to indemnify and hold harmless the owner and the design professional for bodily injury or property damage claims arising out of the contractor's negligent performance of the work. Many states have "anti-indemnity" statutes to regulate the use of indemnification clauses in construction contracts; some states prohibit these clauses completely if the provision requires one party to pay on behalf of the other party's negligence.

The design professional should take care to look for hold-harmless provisions before signing any contract for professional services. A clause that otherwise appears innocuous might contain such a provision. A design professional who finds or suspects such a clause should submit the provision to the design professional's attorney and insurance advisor. A promise to indemnify may fall within the scope of professional liability insurance coverage, but broad wording may mean that the promise is a contractual obligation that cannot be covered by insurance.

It is important for architects serving as prime professionals to use subconsulting firms that have appropriate levels of insurance coverage. This is especially true with professional liability insurance coverage; subconsultants should be required to prove they have adequate levels of coverage with reputable carriers.

Inter-professional relationships. Design professionals routinely retain consultants. This relationship means that the design professional also has vicarious liability for any damage caused by the consultant's negligence. Insured design professionals will want to review their consultant's insurance status as they, for all intents and purposes, will serve as their consultant's insurer if that status is inadequate. Similarly, if a design professional agrees by contract to limit the liability of a consultant, the design professional may find that the risk of the consultant's negligence has been shifted to the design professional and the design professionals' insurer. At times, design professionals are subconsultants to other professionals or subcontractors to construction contractors. Examining the prime design professional's coverage—or the professional liability coverage of a construction contractor through which you are providing services to a client—can alert the subconsultant design professional to gaps in coverage that could result in the subconsultant becoming the only target of a claim.

Project professional liability insurance. Project insurance covers the design team participants—even those who are uninsured. The policy covers the design professional and

named professional consultants for the term of the project plus a predetermined discovery period after completion of construction. Depending on the insurance carriers of those firms covered by a project policy, coverage may then revert to the individual firms' professional liability policies.

Project insurance is intended to cover only one project and is usually paid for by the owner who wants coverage beyond that normally carried by the firms. Such insurance is also useful when the project is of such increased scope that it drastically affects the cost of basic coverage and as a way to get coverage for underinsured or uninsured consultants. From the design professional's standpoint, the billings associated with a project-insured project (and the cost of any claims) do not affect the premium set for the firm's practice policy. A broker is necessary to compare coverage.

Expanded project delivery approaches. Insurance companies have begun to provide coverage for design professionals practicing in roles such as design/builder, construction manager, and land developer. While some companies offer endorsements for these services to the basic policy under some conditions, potential gaps should be investigated to prevent uninsured liability. For example, a construction manager (as advisor to the owner) is covered under most professional liability policies; the at-risk construction manager—one acting as a general contractor—is not.

Joint ventures. From a legal standpoint, a joint venture is quite similar to a partnership; the main difference is that a joint venture normally has a more limited scope or purpose. If a professional liability claim is filed against a joint venture, one or all of the members can be held liable for any judgment rendered against it. Broad policies—such as the Schinnerer program with CNA—provide automatic joint venture coverage. Some insurers exclude joint ventures from the basic policy; coverage for joint ventures with other design professionals may be available by special endorsement for specific situations. The endorsement extends the coverage under the basic policy to provide for the insured's legal liability arising out of professional services performed on behalf of the named joint venture. However, coverage for other participating firms in the joint venture is not provided by this endorsement.

Each member of a joint venture should obtain evidence from the other joint venture partner(s) that their policies have been properly endorsed, if necessary, to cover participation in the joint venture. This usually can be accomplished by obtaining a certificate of insurance and a copy of the joint venture endorsement.

Strategic Alliances. Strategic alliances are business ventures. No matter how they are legally structured, attention must be given to how they are protected by insurance. Professional liability insurance should be of special concern. Clients, or other parties, claiming harm from the actions of a strategic alliance may be able to recover from any member of the alliance; from the injured party's perspective, the alliance may be viewed as one, integrated responsible entity. Therefore, the insurance concerns of a strategic alliance should be the equivalent of any joint venture or partnership.

Alliances Among Design Firms. With regard to responsibility, all strategic alliance partners may be held liable for the actions of all, but each looks to the others to be responsible for their own areas of expertise and obligations. From a professional liability perspective care must be taken to match final liability with eventual responsibility.

Relying on Separate Coverage. Firms often rely on their practice policies of professional liability insurance to protect and defend them in loosely structured business combinations. This may not always be effective; firms should talk with their insurance brokers to determine if their individual policies will provide adequate coverage. In any joint venture situation where firms rely on their separate policies, it is less stressful if the policies are all with the same carrier with the limits and deductibles in similar amounts for all firms. Otherwise firms may find one serving as the "deep pocket" for the others—a situation neither the firm nor the firm's insurer appreciates.

Securing a Policy for the Joint Venture. It is far more practical, and more protective, for the interests of the strategic alliance to be covered by a separate

professional liability insurance policy. As a result, coverage disputes and internal indemnification or contribution obligations can be minimized.

Obtaining a Project Policy. It is both possible and pragmatic for a strategic alliance to secure one policy for the joint venture's participation in a specific project. A project policy covers a prime professional and all other professional participants for a specific period of time. Contractual provisions can be used to allocate the deductible obligation among the parties so that if a claim does occur, the potential for conflict among design team members—and the eventual cost of resolution—is reduced.

Alliances With Non-Professionals. Design practice affects the life, health, and safety of the public. Design professionals must satisfy the licensing procedures that determine if they meet the standards of professional competence demanded by the scope of their practice. Where design professionals join with other professionals in a strategic alliance, it is fairly clear which portion of the responsibility each professional will assume and how that responsibility will be covered by separate professional liability policies, a policy for the joint venture, or a project policy. The same is not always true when a licensed design professional joins with a nonprofessional to produce a project. While it may be possible to secure a project policy covering both the design firm's professional liability exposure and the contractor's design exposure, thought must be given to how responsibility and liability are to be divided.

The evolution of the design and construction process has blurred the "bright line" typically dividing design services from construction work. With the increase of design/build—usually with a contractor as the design/build leader—design professionals should be aware of how the contractor on a project will cover its share of design liability exposures.

In many contractor–design professional joint ventures, little advance planning is given to a reasonable

allocation of risk. The design professional, through licensure, demonstrates responsibility for the adequacy of the project design, thereby providing the required public protection. The builder, however, is not required to be licensed by the state in the same manner. There is a general responsibility to avoid acting in a negligent manner in the pursuit of the work so as to prevent injury to the public. But when harm occurs, the responsibility may shift. And this shifting often is in the direction of the party with the appropriate insurance coverage.

A strategic alliance may be a “temporary partnership,” but for the purpose of rectifying harm to another party it is characterized as a joint venture in which all partners are liable for the actions of all other partners in the context of the jointly assumed project. The design professional, therefore, may be jointly and severally liable for exposures it can neither manage nor insure. Likewise, a contractor’s risk may extend to the design aspects of a project and be excluded from the contractor’s normal coverage as a professional liability exposure. Certainly a design professional does not want the other joint venture member to be “going bare” when design liability is such a great exposure. Whenever a contractor’s responsibility and liability goes beyond construction to project design or construction management, the need for contractors to carry professional liability insurance—design liability coverage—intensifies.

Claims. In professional liability insurance there are two common ways to define claims. The first is objectively defined: a demand for money or services with an allegation of a wrongful act. This definition produces a clear reference point indicating when the insured and the insurance company should intervene. It also is broad enough to cover not only a lawsuit but also that angry call from the client demanding that the design professional “fix it.” The second definition is subjective and requires alerting the insurance company to a potential problem. Such a problem may not necessarily become a formal claim, but rather a threat of an action—or just a very troubling circumstance. A careful review of these policy terms is important, as failure to report a claim in a timely manner may jeopardize coverage.

Most policies require the insurance companies to have the consent of the insured before settling claims. In cases involving a disagreement between the insured and the insurance carrier on settlement, the insured may be liable for the cost of any judgment above the amount for which the insurance company could have settled the claim. Similarly, the insurance company may be liable for the cost of any judgment above the amount that the insured asked the company to settle. This check-and-balance approach encourages both the insurer and the insured to work together to manage claims.

GENERAL LIABILITY

Liability exposures can arise from a design professional's office operations and nonprofessional activities at the job site. To cover such exposures, design professionals should carry a general liability policy. The following are elements of protection provided by a general liability policy.

Coverage. A general liability policy provides coverage for claims arising against the named insured involving third-party legal liability, but it doesn't cover professional, automobile, and workers' compensation exposures. The basic general liability policy covers only the named insured; it does not protect employees unless specifically endorsed to provide for such an extension of coverage.

Liability limits. General liability policies usually set definite dollar limitations on the amounts an insurance company is obligated to pay. These limitations relate to the type of claim (that is, bodily injury, property damage, or personal injury) and to the total dollar cost of all claims, sometimes called the aggregate limits. For bodily injury and property damage, there are two limits: on the dollar amount of the claim for each occurrence or accident and on the aggregate dollar amount for all claims. For personal injury — claims involving libel, slander, defamation of character, false arrest, and the like — the limit of liability is a single aggregate amount for all claims.

Contractual liability. In addition to professional service contracts, the design professional can encounter a variety of business contracts including office leases, purchase orders, service agreements, and the like, any of which may contain a hold-harmless provision that will contractually transfer

another's legal liability to the design professional. The design professional must be vigilant in checking all contracts, agreements, leases, and purchase orders for hold-harmless agreements. When these are found, the design professional should obtain a coverage extension, if the general liability policy does not already have one.

Other extensions of the general liability policy may be necessary to reflect the individual needs of the firm. A careful review of the liability situation should be made with insurance counsel to be certain the required coverage is being provided.

Automobile (aircraft, watercraft) liability. Comprehensive automobile liability protection is an essential part of the design professional's insurance program. The insurance should be written with adequate limits of liability to cover the use of automobiles by the policyholder, by employees, or by others. The policy should name, as insureds, the individual design professional, all partners in a partnership, and all officers and directors of a corporation. Coverage should include owned, non-owned, hired, and newly acquired automobiles. Personal automobiles of the individual design professionals also should be insured with adequate limits of liability to provide protection for possible business use. Similar liability coverage is needed for aircraft and watercraft if their use is part of the design professional's practice.

Employers' liability. As an employer, the design professional can be subjected to claims by employees for job-related injuries. In most instances, these claims are covered by workers' compensation rather than being treated as common-law actions. Situations may exist in which an employee's injury isn't covered under workers' compensation. In these instances, the employee may attempt to sue the employer. Employee suits are excluded both under general liability and workers' compensation policies, and a potential coverage gap exists. To avoid this gap, the workers' compensation policy is generally extended to cover what is called employer's liability.

Packaged Programs Including CGL Coverage. CNA and Victor O. Schinnerer & Company, Inc. have developed an innovative program to accommodate the broad spectrum of risks faced by firms in the design and construction industries.

The Schinnerer product with CNA is called DesignOne because it can combine property, casualty, employment practices and professional liability coverages into one convenient, cost-effective program. It offers a single source of protection—one broker, one business insurance program and one application process. The goal is seamless coverage so that a professional firm can focus on serving clients rather than on whether an exposure is covered under a professional liability insurance policy or some other coverage.

DesignOne coverage is available to architect, engineers, landscape architects, surveyors and specialty design consultants. Also protected are virtually all project delivery methods, include design-build, joint venture, construction management services and traditional design-bid-build.

With property, casualty and professional liability coverages under one roof, design firms get the most comprehensive and flexible insurance programs available.

Coordination of liability insurance. Programs such as DesignOne simplify practice because professional, general, automobile, and other liability policies are interrelated. The design professional should seek insurance counsel to avoid gaps in protection or duplication of coverage and to correlate limits. Umbrella or excess liability policies may sometimes be needed to provide higher limits than those provided by the basic liability coverage.

Excess (umbrella) liability policies. When higher limits of liability are required, certain underlying policy limits can be increased through the purchase of one additional policy—an excess or umbrella liability policy. This policy will provide higher limits in conjunction with underlying general liability, automobile, and employer's liability policies. Because it is an excess policy that is only tapped when the underlying policies cannot pay enough to satisfy a claim, the cost of an umbrella liability policy is not significant. Usually, additional limits, in increments of \$1 million, are provided over the limits of the underlying policy. Professional liability is not commonly included. Coverage generally will be the same as the underlying policies when coverage is broader. Claims are subject to a self-insured retention level (for example, \$10,000), similar to a deductible.

EMPLOYMENT PRACTICES LIABILITY INSURANCE

No one likes to think that their employees may sue them one day but, unfortunately, employment practices claims are becoming an increasingly common basis of civil litigation. Recent changes in the laws related to the employment process have dramatically magnified both the complexity and the potential legal dangers inherent in any professional service firm's personnel management function. The number of employee harassment, discrimination, and wrongful termination charges filed has increased correspondingly.

There are many federal and state laws that protect employees against harassment, discrimination and wrongful termination. Others require specific benefits for employees. While not all federal and state laws require compliance by very small firms, the exposure of employment practices liability is real for even the smallest firm that has an employee.

Sound management practices will help deter claims and lawsuits—and will help provide a strong defense when allegations are made against a firm. But management practices are only one way to respond to employee claims. Employment Practices Liability Insurance is another. While most design firms try to provide a workplace free of discrimination and harassment, mistakes can be made.

One of the fastest growing sources of claims against professional service firms is based on the failure to meet the statutory and tort law requirements on employment practices. While age discrimination leads the list of allegations, sexual discrimination and sexual harassment claims are becoming more common. Even the smallest professional services firm may find itself in a position of defending against an employment practices claim.

While some Commercial General Liability policies can be endorsed to add Employment Practices Liability coverage, most firms purchase a more comprehensive coverage through a stand-alone policy such as that offered in conjunction with the CNA/Schinnerer professional liability insurance policy or through a true package policy such as DesignOne. Smaller firms can endorse their CNA/Schinnerer policy to cover many of the specific EPL risks of design firms.

Commonly covered claims under an employment practices liability policy include wrongful termination, harassment, discrimination, and employer retaliation. Employment-related misrepresentation, libel, slander, humiliation, defamation, invasion of privacy are included as are wrongful failure to hire or promote, wrongful deprivation of career opportunity or negligent employee evaluation, wrongful discipline, failure to provide or enforce adequate or consistent policies and procedures, and violation of an individual's civil rights relating to any of the above.

OTHER BUSINESS INSURANCE

In addition to liability insurance, a professional service firm may choose to purchase insurance for other business risks.

Architects working out of their residences should not rely on homeowner's insurance for protection of their businesses. Most homeowner policies cannot adequately cover a home-based professional practice.

Design professional's property insurance. The design professional's office building or the leasehold improvements where the design professional is a tenant should be insured by a standard policy covering named perils or by a broader all-physical-loss form, which is generally available. Careful attention should be given to establishing an accurate insurable value for the building or improvements. The amount of insurance always should be adequate to meet the requirements of any coinsurance clause (that is, any required fractional payment by the insured in case of a loss). Otherwise, the design professional could end up paying for a substantially larger part of any loss. Consideration should be given to the purchase of insurance for the building improvements on a replacement cost basis rather than on a depreciated cash value basis. All leases and mortgages should be reviewed, as the frequently stipulate coverage requirements.

Package policies are generally available. These policies may combine several separate coverages, such as insurance on the building or improvements, on office contents, and for public liability—possibly at a lower premium cost than if these policies were purchased separately. The package policy should be scrutinized to determine if it fits the design professional's needs.

Office contents. The design professional's office contents can be insured by a standard policy covering fire, windstorm, and other extended coverage perils. Separate burglary and theft insurance also can be written to cover office contents. However, broader coverage of office contents is generally available to insure them against all risks of direct physical loss except as excluded in the policy.

Such insurance covers drawings that are damaged, but only to the extent of the cost of labor and materials to produce them. It does not cover the cost of the research that went into their preparation, although such coverage may be obtained by purchasing valuable-documents insurance.

Portable equipment that may be used outside the office can be insured under an all-risk floater policy. Money, securities, checks, travel tickets, and other negotiable instruments can be insured under a blanket crime or similar policy.

Business interruption. Business interruption insurance reimburses the design professional for continuing fixed expenses and for loss of profits in the event fire or other casualty interrupts normal business operations. This insurance can be written to cover fire, windstorm, extended coverage perils, computer crashes, and other hazards.

Coverage is available for an agreed sum or for actual gross earnings based on the firm's history. Options are available to reimburse the design professional for the extra expenses of continuing business at another location while the damaged premises are being repaired.

Valuable documents. This insurance is one of the most important property coverages sought by design professionals. It covers the total value of documents lost or destroyed by any of the means described in the policy and is generally an "all-risk" coverage. It is available on a scheduled form, a blanket coverage form, or a reporting form indicating periodic changes in value. Documents in storage as well as work in progress can be insured. Coverage also is available for clients' documents in the custody of the design professional.

Fidelity bonds and criminal loss insurance. Usually all persons involved with the custody or disbursement of funds, management of firm finances (receivables and disbursements), authorization of payments to contractors or others, purchasing, and other activities requiring the use of funds or liability for the misuse of funds of others should be bonded. A blanket form of bond covering all employees is typically recommended.

Money, securities, checks, and other negotiable paper may be insured both inside and outside the insured's premises under a broad-form money and securities policy to include loss by robbery, burglary, theft, and disappearance and destruction by fire or other causes.

Comprehensive bonds or blanket crime policies are available. These combine coverage for loss of money, securities, and other property under a blanket fidelity bond and a check

forgery bond. The design professional's professional liability policy does not cover claims and losses from the dishonest acts of associates or employees.

Directors and Officers Liability Insurance provides protection for leaders of a firm established as a corporation against claims alleging breach of duty, negligence, error or misrepresentation.

If a firm is set up as a business corporation or in just about any other corporate form, D&O coverage becomes essential.

In handling the affairs of a corporation, directors and officers must exercise such judgment and care as a reasonably prudent person would exercise in similar circumstances. Directors and officers are responsible for knowing how the firm is operating and making policy and managerial decisions that are intended to benefit the shareholders. All directors and officers must carry out their duties with the best interest of the organization in mind. This means avoiding conflicts of interest and keeping the trust of the company. While these duties of care and loyalty are owed primarily to the organization, there is a duty of obedience to other parties to follow the company's by-laws.

Fiduciary Liability Insurance provides protection of fiduciaries against liabilities that arise from their administration and oversight of any employee benefit or pension plan.

Even in a small firm where a partner or support staff member may be responsible for some pension plan decisions, coverage for ERISA exposure should be considered.

The Employee Retirement Income Security Act of 1974 (ERISA) is a federal law that sets minimum standards for pension plans in private industry. ERISA does not require any employer to establish a pension plan. It only requires that those who establish plans must meet certain minimum standards. The law requires accountability of plan fiduciaries. ERISA generally defines a fiduciary as anyone who exercises discretionary authority or control over a plan's management or assets, including anyone who provides investment advice to the plan. Fiduciaries who do not follow the principles of conduct may be held responsible for restoring losses to the plan.

As firms become more complex and sophisticated in their business operations, they become more aware of the firm's potential operational risks. There are many separate and package policies designed to provide protection against losses for negligent or inappropriate business conduct.

EMPLOYEE INSURANCE COVERAGES

Design professionals with employees must face the prospect of additional insurance coverage for their employees. Some of this coverage is mandated by statute; some is at the firm's choice.

Workers' compensation. By statute, an employer is required to carry workers' compensation insurance. Sold by commercial insurance companies (or, in some states, available through state-run facilities), workers' compensation policies provide protection for work-related injuries. Benefits are prescribed by statute and include medical expenses, lost wages, and death benefits. These benefits are provided regardless of employer or employee negligence. Employees are precluded from suing their employers for injuries covered by workers' compensation.

A workers' compensation policy is rated, based on the firm's payroll, to cover various classes of employees. A full-time field design professional performing construction contract administration services will have a higher rate than a design professional who does not perform these services. Care should be exercised in the classification of employees to ensure proper coverage and rates applicable to the hazards involved. Improper classifications can result in much higher premiums.

Disability benefits. State disability benefit laws provide benefits for employees who are disabled due to non-work-related injury or illness. Not all states require this coverage, but for those that do, minimum benefits are fixed and prescribed by statute. For those states where disability benefits are not mandated, or in situations where the architect wishes to increase mandated coverage, voluntary disability coverage is available through a number of commercial insurance companies as well as through the AIA Trust.

Health insurance. Health is a major but costly consideration, for both employees (the beneficiaries of the coverage) and employers (whose professional livelihood, to a great extent, depends on a productive and healthy staff).

The cost of health insurance has been increasing at a rate far higher than that of inflation and wages for the past four decades. As a result of spiraling health care costs, health

The AIA Trust recently began testing an endorsed medical plan for employers available in approximately 30 states. In addition, the Trust offers a service for AIA members to access reputable, cost-effective coverage with highly rated health insurance carriers.

insurance plans and health care delivery systems have undergone significant changes in recent years, and employers have had to develop strategies to control the increases in their benefits costs.

Medical insurance. There are many variations of health insurance plans, including both indemnity and managed care options. The AIA Trust recently began testing an endorsed medical plan for employers available in approximately 30 states. In addition, the Trust offers a service for AIA members to access reputable, cost-effective coverage with highly rated health insurance carriers. Members have easy access to free online quotes as well as live agent support to help evaluate their needs and provide expert advice on selecting an individual or a small group medical plan. Information on these alternatives and other health-related plans including hospital indemnity insurance, cancer insurance, and others are listed on the Trust website located at www.TheAIATrust.com.

Dental insurance. Benefits for dental care required as a result of illness or injury were generally provided under one's medical insurance plan; however, that is frequently no longer the case. Insurance to cover regular dental care can be obtained through either an indemnity plan or a dental HMO or PPO. Traditional dental plans typically provide benefits on the basis of a fee schedule, for example, paying a specific dollar amount for each scheduled treatment.

Vision care. Vision care plans typically provide benefits on the basis of a schedule, paying a flat dollar amount toward the cost of one routine eye examination and a set of appropriate lenses, frames, and contact lenses every twelve to twenty-four months.

Flexible health care spending accounts. These plans, authorized under federal tax laws, allow participants to make pretax contributions to a special employer-managed account and then to be reimbursed from this account for out-of-pocket health care costs. Contributions are exempt from FICA (social security), federal, and, in most states, state income taxes. Commonly such plans are combined with a *dependent care spending account*, which permits an employee to pay for work-related child care expenses with pretax dollars. Regulation of such accounts is an especially fast-moving field; advice from the firm's accountants is essential.

The AIA Trust offers a voluntary dental plan whereby each member of the firm has the opportunity to enroll in the program.

Income protection and replacement benefits. In addition to health benefits, a firm may offer life insurance and long-term disability protection.

Life insurance. These plans, which provide benefits in the event of the death of the insured, should be thought of as income protection for the spouse and other dependents and also as a potential source of protection for the firm in the event of the death of the owner or a principal. Group term life insurance (such as the product marketed by the AIA Trust) is commonly provided to all employees as a fixed-dollar amount per employee or as a multiple of salary. In addition, life insurance may be considered as a form of “key man” or “key person” protection for the firm in the event of the firm owner or partner. This principal can also be applied to long-term disability insurance for the key person(s) in a firm. In addition, life insurance is commonly offered as an employee benefit.

Disability benefits. These are provided in several forms:

- *Short-term disability* benefits protect against absence from work of short duration, typically three to six months. Small employers as well as large employers often self-insure against the risk of short-term disabilities through a sick leave program, although it is possible to buy insurance for this purpose.
- *Long-term disability* benefits protect against extended disabilities, often until the employee recovers or reaches age 65. The cost of this insurance is quite modest, and long-term disability (LTD) insurance provides greater assurance that the financial resources to pay the claim will be available indefinitely. A third party is often needed to determine the continuance of disability; for architects, it is important that the test of disability be their ability to practice their chosen profession. This is the test used in the AIA Trust’s policy. The Trust offers several forms of long term disability coverage, including individual and firm or employee insurance.

Business overhead expense. BOE disability benefits are similar to long-term disability benefits except BOE protects business-related expenses in the event of total disability of a business owner. Benefit periods range from 12 months to 24 months, and this low-cost insurance helps a business owner cover on-going business expenses such as rent, mortgage interest, utilities, and employee salaries. This valuable insurance coverage allows a disabled owner to maintain the business viability or avoid a “forced-sale” of the business should the disability condition be long-term or permanent.

The AIA Trust offers this program at very competitive rates and every business owner or partner in a firm should consider this type of coverage.

Retirement benefits. In times of increased life expectancy, retirement plans take on added significance. These plans can take different forms and offer many variations and options. They are important to consider for yourself, and for your employees as an employee recruitment and retention tool.

Defined contribution plans start with an annual contribution based on earnings. The amount received at retirement is based on total contributions made and the investment strategies employed. Firms have a choice of several types of defined contribution arrangements:

Profit Sharing plans allow a variable contribution annually. On an overall plan basis, they can generally range from zero to 25% of the total plan compensation.. Each year, the amount of contribution is totally flexible, and it may be as low as zero. The individual contribution limit for 2011 is the lesser of \$49,000 or 100% of compensation. Employers with demographics that include generally older highly compensated employees may want to consider using the cross-testing plan option to potentially provide for a higher percentage of the overall plan contribution.

Pension plans, which mandate annual contributions, are now all but obsolete since you can now reach the maximum 25 percent in a Profit Sharing plan and still have a flexible 0 to 25 percent contribution each year.

Traditional 401(k) plans allow individuals to defer a part of their salary over and above contributions the firm may make. Contributions made by employees are on a before-tax basis, and this plan is a good way to have employees share in the cost of saving for retirement. Of course, the IRS sets limits as to how much employees may contribute to a 401(k) plan. The firm must satisfy IRS 401(k) non-discrimination testing and minimum contribution requirements. The percentage of salary that can be deferred by highly compensated employees is dependent on the average deferral rate of the non-highly compensated employees.

SIMPLE 401(k) plans allow individuals to defer a part of their salary. The firm can adopt a SIMPLE 401(k) without being subject to "discrimination testing" or minimum contribution

requirements. The firm must offer eligible employees who participate a dollar-for-dollar matching contribution up to 3 percent of compensation or give a 2 percent contribution for all eligible employees regardless of participation. The firm must also provide an annual notice to all eligible employees at least 60 days before the beginning of each year. The notice provides the employees with information on the SIMPLE plan including whether the firm will make the matching or non-elective contribution in the coming year. SIMPLE plans do not allow for any other types of contributions. Although the maximum salary deferral limit is lower in a SIMPLE 401(k), the lower contribution cost is attractive to many firms.

Safe Harbor 401(k) plans allow individuals to defer a larger part of their salary than a SIMPLE 401(k). The firm chooses one of two contribution requirements — either a 3 percent non-elective contribution or a matching contribution based on the following formula, dollar for dollar up to 3 percent of compensation and 50 cents on the next 2 percent of compensation. The firm must also provide an annual notice to all eligible employees at least 30 days, but not more 90 days before the beginning of each year. The notice provides the employees with information on the plan including whether the firm will make the matching or non-elective contribution in the coming year. There is no nondiscrimination testing as long as the contribution and notice requirements are met. With a Safe Harbor plan the firm can also contribute to a Profit Sharing plan.

Owner's 401(k) plans are for a sole owner with no employees or owners who employ only family members. The impact of increased contribution limits and deduction rule changes allow the owner to employ a 401(k) plan, typically used by larger firms, to drastically increase his or her contribution.

Roth 401(k) option is available to employers in any of the 401(k) plan options above. This option allows participants to make contributions from their salary on an after-tax basis and if certain requirements are met be able to withdraw them tax-free.

Catch-up contributions, for participants age 50 or older, can be made in any of the 401(k) plans up to the IRS limit. These contributions are over and above the regular 401(k) contributions and are not counted against a participant's total contribution limit.

annual benefit at retirement for each participant. Actuaries calculate the annual contribution required to reach this goal. These plans can be expensive to maintain but usually allow for larger contributions for older employees than defined contribution plans. They are not well suited for sole owners with younger employees, but they can accumulate retirement savings faster for partners and employees nearing retirement age.

Simplified employee pension plans or SEP plans are retirement plans in which firms establish individual retirement accounts (IRAs) for employees. The contributions to the SEP have limits similar to a profit sharing plan. Firms must cover more employees than in a defined contribution or defined benefit plan, and therefore the SEP may be more costly. However, administration of a SEP may be simpler than some defined contribution or defined benefit plans.

SIMPLE IRA plans work the same way as the SIMPLE 401(k) plans described above except the contributions are made to employee IRAs. It offers many of the same advantages as a SIMPLE 401(k) with generally lower costs and no annual government filing requirement.

Individual Retirement Accounts (IRAs) are set up by individuals on their own behalf. Individuals are able to make relatively low annual contributions to an IRA. These contributions may not be tax-deductible, depending on income and whether the individual participates in a retirement plan. Earnings on the IRA accumulate on a tax-deferred basis until withdrawal at age 59 1/2 or later. Withdrawals at an earlier age carry a penalty.

Plan details. Regarding IRS and federal pension plan requirements, the IRS has rules relating to "qualified plans," SEPs, Simple IRAs, Roth IRAs and IRAs which direct firms with retirement plans to establish eligibility criteria, vesting schedules contribution levels, and integration with Social Security benefits.

However the program is designed, the key for firms as well as for individuals is to start early. Demographics (increases in the retirement age) and political necessity (taxing benefits for a growing number of people) have already caused major reductions in Social Security benefits.

Defined benefit plans
specify, at the outset, the

For more information on insurance and benefits programs go to www.TheAIATrust.com

The practice of architecture, like other businesses, requires firm managers take the time to identify, assess and manage risk. Insurance is only a part of that risk management approach – yet an important vehicle for transferring risk so that a firm can focus on delivering responsive and valuable professional services. For more information about professional liability and other insurance vital to managing a firm successfully, see the entire booklet on *Making The Transition To Running Your Own Firm.*

SUMMARY

For more information on insurance and benefits programs go to www.TheAIATrust.com 26

GLOSSARY OF LEGAL AND INSURANCE TERMS

Accord and Satisfaction - The execution of an agreement to cancel a legal obligation in return for something less than or different from the legal duty owed.

Act of God - An accident or event that is the result of natural causes, without human intervention, that could not have been prevented by reasonable foresight or care.

Action - A lawsuit brought in court for enforcement of a legal right.

Actuary - One who is trained in the mathematics and statistics of insurance and calculates premiums, reserves, and other values.

Additional Named Insured - A party added to the coverage of an insurance policy with the right of recovery but without the obligation to pay the premium or meet the other terms of the policy.

Adjuster - One who settles insurance claims; may be a salaried employee or an independent operator.

Admitted Carrier - An insurance company licensed and authorized to do business in a specific state and subject to regulation by the state insurance commission.

Affidavit - A voluntary written statement of facts, confirmed by oath of the maker before an authorized officer.

Agency - The relationship whereby one person, called an agent, has authority to represent or act for another person, called a principal.

Agent - A representative of one or more insurance companies who, operating under the authority of an agency contract, solicits, negotiates, and effectuates contracts of insurance.

Aggregate Limit - The total amount payable under a policy, regardless of the number of claims. This is usually based on an annual total.

Allegation - A statement in a claim or pleading asserting something expected to be substantiated or to be proved in court.

Alternative Dispute Resolution (ADR) - Settling disputes without resorting to litigation. Forms of ADR include arbitration, mediation and many other out-of-court methods.

Anti-Indemnification Statutes - State laws which invalidate contract clauses related to a party being indemnified or held harmless for damages or which limit the ways such contract clauses can be utilized.

Arbitration - A method of alternative dispute resolution in which parties contractually agree to have an arbitrator rule on the merits of their claims. In the construction industry the arbitrator's decision, called an award, is binding upon the parties.

Arbitrator - An impartial person chosen by parties to solve a dispute and who normally is vested with the authority to make a final and binding decision concerning the issues in controversy. An arbitrator's authority is defined by the arbitration agreement between the parties.

Assumption of Risk - An agreement, whether expressed or implied, where a party becomes responsible for the risk involved. A claimant who has assumed the risk cannot collect damages when the law presumes that the claimant was aware that a hazard existed and yet proceeded with action.

Assured - One who has been insured by an insurance company or underwriter against loss.

Award - An arbitrator's decision, as distinguished from a decision, order or verdict in a court action.

Binder - A temporary insurance agreement that obligates the several parties of the contract if the loss insured against occurs before the policy is written. Normally is binding upon the parties.

Breach of Insurance Contract - Failure to comply with the terms or conditions incorporated in an insurance policy, frequently resulting in a restriction of coverage or a voiding of a policy itself.

Breach of Contract - The failure, without legal justification, to fulfill a promise which forms the whole or part of an agreement, written or verbal. The breach of a contract can be intentional, inadvertent or caused by the negligence of the party breaching the contract.

Breach of Duty - A failure to perform an obligation created by law or by contract. See "negligence".

Brief - A written argument, usually prepared by a lawyer, setting forth the facts and legal points and authorities, to persuade a court about the merits or defenses to a claim.

Broker - The representative of the buyer of liability and other insurance who deals with agents or companies in arranging for the coverage required by the customer.

Burden of Proof - The duty of a party to substantiate an allegation or issue in order to convince a "trier of fact" as to the merits of the party's claim, which is necessary in order to prevail in a claim.

Capacity - The maximum amount of insurance that a company can write or the maximum net premiums that a company can book.

Captive - An insurance company formed by one or more entities to insure specific risks of the entities. A captive is a separately capitalized corporation existing only to provide insurance to the owners of the captive.

Case Reserves - The company claims adjuster's estimate of the potential liability of a claim subject to coverage by the policy.

Cause of Action - Facts sufficient to justify a court in rendering a judgment.

Civil Action - A lawsuit in court seeking enforcement or protection of private rights.

Claim - A demand for money, services or property based upon a right usually found in contract or by operation of law.

Claim Expense - The costs associated with the handling of a claim, such as defense-attorney fees, investigation costs, and expert witnesses. Not included are the salaries of insurance-company employees and direct expenses that they may incur in performing their job.

Claims-Made Policy - A policy that covers only those claims that are made against the insured during the policy period arising from acts or omissions occurring during the policy period; when a policy is continuously renewed, the policy period includes the entire time since the original claims-made policy was placed in the insurer.

Closed Without Payment (CWPs) - Claims closed without indemnity payment(s) and for which expense payments may or may not have been made.

Coinsurance - A concept where the insured shares with the insurer a percentage of the loss. Coinsurance allows the insured to benefit from reduced insurance costs while increasing the exposure to loss.

Collateral Source Rule - A rule which prevents a defendant from introducing into evidence the fact that a plaintiff has received benefits for his or her injury/damages from other sources such as disability insurance and/or worker's compensation payments.

Collateral Estoppel - A legal doctrine which bars further litigation of issues in a case previously decided by other courts.

Combined Ratio - The sum of the incurred loss and company expense divided by the earned premium.

Common Law - The body of principles and rules of action that derive their authority solely from usages and customs or from the judgments and decrees of the courts, distinct from legislative enactments or governmental regulations.

Comparative Negligence - The proportional sharing of liability between a plaintiff and defendant for damages based upon the percentage of negligence of each. Not all states allow a sharing of liability based on comparative negligence.

Compensatory Damages - Damages awarded to compensate a plaintiff for his or her injuries; includes direct out of pocket losses as well as compensation for pain and suffering.

Commercial General Liability (CGL) Policy - A broad form of liability insurance usually covering business organizations to protect them against liability claims for bodily injury and property damage arising out of operations. CGL policies exclude liabilities arising out of professional services and some other risks such as the use of automobiles.

Consequential Loss - Loss occurring after, and as a result of, some other loss.

Contract - An agreement, written or oral, between two or more parties creating legal rights and duties that something shall, or shall not, be done. A contract requires "consideration" (a bargained-for benefit) to be legally binding.

Contractual Liability - Liability assumed under any contract or agreement over and above that which may be imposed by law.

Contributory Negligence - The plaintiff or claimant, by not exercising ordinary care, contributed to the injury; in a few states, a plaintiff's contributory negligence precludes the plaintiff from recovering alleged damages.

Copyright - Exclusive right to control the making of copies of a work of authorship, such as design plans, granted by federal statute to the author for a limited period of time.

Counterclaim - An independent cause of action or demand made by a defendant against a plaintiff. This occurs during a case when a defendant files a claim against the plaintiff.

Covenant - A written, signed agreement by two or more parties pledging that something is done, shall be done, or shall not be done as, for example, a covenant not to sue.

Coverage - The insurance afforded by the policy.

Damages - The amount claimed or allowed as compensation for injuries sustained or property damaged through the wrongful acts, negligence or breach of contract of another.

Declaratory Judgment - The order of a court that establishes the rights of parties on a question of law or on a contract.

Deductible - A provision requiring the insured to pay a specified portion of the loss on each claim.

Defendant - The person or party against whom a claim is brought.

Deposition - Pre-trial testimony in the form of oral questions and answers, by a party or witness, which is taken under oath and may be used during a trial or arbitration proceeding.

Direct Loss - Any loss resulting directly and immediately from the hazard insured against.

Discovery Period - The period of time allowed an insured to identify and report to the insurance carrier losses or claims occurring during the period of an insurance policy.

Discovery - The process by which parties to a lawsuit are required before trial to disclose to the other side all evidence they expect to use as a part of their presentations in court or which they possess in relation to the other party's claims or defenses.

Due Care - The degree of care that a person of ordinary prudence and diligence would exercise under the same or similar circumstances; negligence is the failure to use due care. (See Standard of Care.)

Duty - An obligation imposed by rule of law.

Easement - The right of one or more parties to make lawful and beneficial use of the land of another, created by an expressed or implied agreement.

Economic Loss - A legal doctrine by which a defendant is liable for purely economic losses only to the party with whom he/she has a contractual relationship.

Endorsement - A written amendment affecting the declarations, insuring agreements, exclusions, or conditions of an insurance policy; a rider. An endorsement records a change to the insurance contract.

Estoppel - A legal bar preventing a person from asserting a legal position because of his or her own conduct or because of some other reason created by operation of law.

Ethics - The rules of moral conduct governing the duties of a professional person in dealings affecting other people.

Evidence - The records, documents, exhibits and testimony which are submitted to a trier of fact in support of one's claim or defense.

Excess and Surplus Lines Carrier - An insurance company that is not admitted in a jurisdiction but is able to place coverage on an unregulated basis, in accordance with the excess or surplus lines provisions of state law, for those risks for which there is no market available through admitted carriers.

Excess of Loss Reinsurance - A form of reinsurance which would indemnify the insurance company for losses incurred above an agreed upon amount of underlying insurance coverage.

Excess Insurance - Insurance that provides a higher limit of coverage than that provided by primary insurance but that only covers the loss which exceeds the limit of the primary insurance.

Exclusion - Coverage that is specifically eliminated from an insurance policy.

Expense-Only Claim - A claim that results in only claim expenses being incurred, with no indemnity payment being made.

Expert Witness - A witness recognized as having special knowledge of the subject at issue and whose testimony assists the trier of fact in understanding the technical aspects of a claim.

Express Warranty - A representation, usually in writing, that a fact in relation to a transaction is as stated or promised. A guarantee.

Foreseeable - Reasonable to predict or anticipate.

Frequency - The measure of claim count per unit(s) of exposure over a given time period.

Frivolous Suit - A suit that is so totally without merit on its face as to show bad faith or other improper motive on the part of the plaintiff.

Going Bare - Undertaking a risk without insurance to cover it.

Guarantee - A contract that something shall be done exactly as it is agreed to be done. Synonymous with Warranty.

Hazard - A condition that creates or increases the probability of a loss.

Hold Harmless Agreement - A contract provision whereby one party assumes certain legal liabilities on behalf of another party. Such a contract provision could be of limited form, where a party reaffirms responsibility for its own negligent acts thus protecting another party from vicarious liability; an intermediate form, where a party reaffirms its responsibility and agrees to share responsibility for joint and concurrent negligence of both parties; or a broad form, where a party assumes responsibility for all liability including that arising out of the sole negligence of the other party. Synonymous with "Indemnification."

Implied Warranty - A representation, not in writing, that insurable conditions exist or that a fact in relation to a transaction is as stated or promised resulting from an inference by law based on the circumstances.

Imputed Negligence - Negligence that is not directly attributable to one person but that is the negligence of a second person who is in privity with the first and with whose fault the first is chargeable as in vicarious liability.

Incurred Loss - The total of paid losses (indemnity plus expenses) plus the loss reserves outstanding and expected to be paid in the future.

Indemnification - An agreement by one party to pay certain specified losses or damages incurred by another party. Synonymous with "Hold Harmless".

Indemnify - To protect against loss or damage or to promise compensation for loss or damage. The duty to indemnify may be created by rule of common law, by statute, or by contract.

Indemnitee - The party who is to be indemnified from loss or damage.

Indemnitor - The party who is providing the indemnification.

Indemnity - The restoration to a victim of a loss up to the amount of the loss. In the insurance contract, it is the payment by an insurer to a claimant that covers the entire loss for which an insured is legally liable.

Insurance - A contractual relationship which exists when one party (the insurer) for a payment (the premium) agrees to reimburse another party (the insured) for a loss caused by designated contingencies. A contract of indemnity.

Insured - Under a liability insurance policy, the party to whom or on whose behalf benefits are payable.

Interrogatories - A series of written questions exchanged between parties to a lawsuit, which must be answered under oath.

Joinder - Uniting two or more elements into one such as the joinder of parties as coplaintiffs or codefendants in a suit or as parties to an arbitration.

Joint and Several Liability - A legal concept where defendants can be held both collectively and individually liable for all damages, regardless of their degree of fault.

Judgment - The final decision of a court with respect to the rights of the parties in a suit. A summary judgment is a decision of a court without hearing evidence, usually because the pleadings show no issue of fact.

Lapse - Termination of a policy due to failure by the insured to pay the premium as required.

Latent - Hidden or concealed such as a latent defect which a reasonably careful inspection will not reveal.

Legal Liability - A legal obligation that arises out of contract or by operation of law.

Lien - A legal mechanism that allows a person or party to attach the property of another as security for payment of labor, materials or other goods and services provided to enhance the value of the property.

Limit of Liability - The maximum amount which an insurance company agrees to pay in the case of loss.

Liquidated Damages - Amounts stipulated in advance for damages to be recovered for breach of contract.

Litigation - The contesting of a matter in court.

Loss Frequency - The number of claims made against a policy during a premium period.

Loss Ratio - The relationship between net earned premiums and net losses incurred.

Malfeasance - The doing of an act that is contrary to law or contractual obligation.

Malpractice - Any failure in professional duty by one rendering professional services, resulting in injury.

Mediation - Effort by an independent party to assist others in reaching the settlement of a controversy or claim. The mediator participates impartially in the proceedings, advising and consulting the various parties involved. A mediator cannot impose a settlement, but can only seek to guide the parties to the achievement of their own settlement.

Meritless Claim - A claim which is so obviously insufficient that it should be rejected on its face without argument or proof.

Misfeasance - The doing of a lawful act in an improper manner.

Misrepresentation - A misstatement of a material representation that, if done with intent to mislead, may void the policy of insurance.

Motion - An application made to a court seeking some order or ruling in relief of the applicant such as a motion to dismiss.

Named Insured - The one named in the policy. It could be any person, firm, or corporation or any of its members specifically designed as insureds in the policy as distinguished from others who, although unnamed, are protected by the policy definition. A named insured under the policy has rights and responsibilities not attributed to additional insureds.

Negligence - Failure to exercise that degree of care that an ordinarily careful and prudent person would exercise under the same or similar circumstances which results in injury or damage.

Negligence *Per Se* - An act or omission regarded as negligence without argument or proof because it violates a standard of care defined by statute or is so obviously contrary to common prudence.

Nonadmitted Carrier - An insurance company not licensed to do business in the jurisdiction.

Occurrence Insurance - An insurance contract whereby coverage is provided for losses stemming from an event when the insurance policy was in force even if the claim is not made for several years. Professional liability insurance, because of the unpredictability of future loss is written on a claims-made rather than occurrence basis.

Occurrence - An accident or exposure to injurious conditions during the policy period that resulted in bodily injury or property damage that the insured neither expects nor intends.

Permissible Loss Ratio - The maximum percentage of premium income that can be expended by an insurance company to pay claims without the loss of profit.

Personal Injury - Physical or mental injury to a human being.

Plaintiff - A party to a lawsuit who brings charges against another party called the defendant.

Policy Term - The period for which the premium has been paid. With professional liability insurance practice policies it usually is a year. With project policies it usually is a period of years.

Policy - The insurance contract of agreement.

Policy Reserve - The amounts that an insurance company allocates specifically for the fulfillment of its policy obligations; reserves are so calculated that, together with future premiums and interest earnings, they will enable the company to pay all future losses.

Premium - The payment, based on the insurance rate, amount of coverage, and other factors that a policyholder agrees to make for an insurance policy.

Prior-Acts Coverage - Retroactive coverage for negligent acts or omissions occurring prior to a claims-made policy period so long as the claim is first made against the insured during the policy period and, upon the inception of the policy, no insured had knowledge of the act or omission precipitating such claim.

Privity - The direct relationship between two parties to a contract. Privity continues when certain subsequent parties succeed to the rights of a contract.

Producer - An agent for an insurance company.

Professional - A person who is deemed to have specialized knowledge and skills, acquired through education and experience, to be used in advising or providing services to others.

Program Year - The period of time subject to a set of underwriting or rate actions associated with a particular line of business.

Provisions - The terms and conditions of an insurance policy.

Proximate Cause - A cause leading directly, continuously, and naturally to a given result.

Punitive Damages - Damages that are separately awarded and are in addition to compensatory damages. Normally these would be awarded because of a finding of malicious or wanton misconduct on the part of the defendant, and they serve as a punishment and a deterrent to others.

Purchasing Group - Under the Liability Risk Retention Act of 1986, a buyers' collective formed to purchase liability insurance for the group members to cover their similar or related liability exposure.

Pure Premium - The cost of claims per unit of exposure. Pure Premium is the product of Frequency times Severity.

Rate - The cost of a unit of insurance.

Reinsurance Agreements - There are two principal forms for spreading risk through reinsurance: facultative reinsurance, under which each transaction is treated separately and both the insurer and reinsurer retain the privilege to accept or reject individual reinsurance agreements, and treaty reinsurance, under which the reinsurer agrees to accept specific types and amounts of risk.

Reinsurance - The transfer of insurance business from one insurer to another for financial reasons (so that reserves can be maintained on an increased amount of business) or technical reasons (so that the risk of loss can be distributed).

Reinsurer - A company that receives a certain amount or proportion of the risks or losses of insurance companies or other reinsurance companies.

Release - A document which memorializes the fact that the claimant has abandoned the claim, because of either satisfactory payment or recognition that the claim is invalid.

Right - That which a person is entitled to have or receive from other people, as secured by law; the correlative of a duty.

Risk - The possibility of loss.

Risk Retention Act - A 1981 federal law expanded by amendment in 1986 that preempts certain state laws and regulations enabling groups to purchase or provide liability insurance for individuals or organizations with similar liability exposures.

Risk Retention Group - A corporation or limited liability association, established under the Liability Risk Retention Act of 1986, whose primary activity involves assuming and spreading all or some of the liability exposure of its members; a licensed liability or casualty insurance company owned by its members who are engaged in similar or related businesses.

Settlement - Voluntary agreement to resolve a claim.

Severity - The measure of the average claim amount.

Sovereign Immunity - A long-standing doctrine to the effect that government entities cannot be sued without their consent. Federal and state laws allow suits against governmental agencies under certain circumstances.

Standard of Care - As applied to design professionals, the ordinary and reasonable care required and established by expert testimony of what a reasonable and prudent professional would have done under the same or similar circumstances. It is the measure by which behavior is judged in determining legal duties and rights.

Statute of Repose - The legal time limitation of the right to bring an action on a specific cause of action after which no suit can be maintained. The suit must be brought within a specified period that normally starts to run from an event specified in the statute (for example, the date of substantial completion); this is distinguished from the statute of limitation which runs from when the party bringing the claim knew or reasonably should have known of his or her injury/damages.

Statute of Limitations - The legal time limitation of the right to bring an action on a specific cause of action after which no suit can be brought; such time periods normally start to run from the date of injury or other event that gives the injured party a cause of action.

Strict Liability - Liability without fault or, in the case of professionals, without negligence.

Subpoena - A writ issued under the authority of a court or arbitrator to compel the appearance of a witness for deposition, trial or arbitration hearing.

Subrogation - An equitable doctrine entitling a party to be substituted for one of the original parties to a transaction; for example, an insurance company may be given the right to recover from a third party the amount it paid to its policyholder for a loss caused by that third party.

Summary Judgment - The decision of a court without hearing evidence, usually because the pleadings show no issue of fact.

Summons - A legal paper to be served on a person named as a defendant in a legal action notifying him or her to answer the complaint or be in default. Also used to require non-party witnesses to appear for depositions or at the trial or arbitration hearings.

Term - The length of time covered by a policy or a premium.

Testimony - Oral evidence given by a witness.

Third Party - Someone other than the original parties directly involved in the claim or action. A third-party beneficiary is one for whose benefit a contract is made.

Tort - A violation of a right created by operation of law; a private or civil wrong or injury.

Tortfeasor - One who commits a tort.

Underwriting - The process by which an insurance company determines whether or not and on what basis it will accept an application for insurance.

Underwriting Expense - The costs incurred by the insurance company to write a particular line of business. Included are commissions to agents, company claim-handling expenses, premium taxes, and general expenses.

Uniform Commercial Code (UCC) - A model statute dealing with commercial transactions that has been adopted by every state except Louisiana. UCC provisions do not normally apply to professional services.

Unjust Enrichment - A legal concept that prevents a party from a monetary benefit to which he or she is not entitled.

Verdict - The findings of a fact of a judge or jury. A directed verdict is one the court prescribes if there is no material issue of fact for the jury to decide.

Vicarious Liability - Indirect liability imposed on a party resulting from the acts or omissions of another person for whom the party is responsible.

Waiver of Subrogation - The relinquishment by an insured of the right of its insurance carrier to collect damages paid on behalf of the policyholder.

Warranty - An undertaking that a fact is as stated or promised. May be based on an explicit representation (an express warranty) or inferred by law based on the circumstances (an implied warranty.)

Workers Compensation - An insurance system in which liability is imposed by statute on an employer, who must provide benefits prescribed by law to employees or their dependents as a result of job-related injuries or death.