

ATRIUM

MEETING

Guide

TO THE
Schinnerer and CNA
Risk Mitigation Credit

This publication

has been prepared as a guide to the Risk Mitigation Credit described under Item E of Section V, Limits of Liability/Deductible in the 10/05 Edition of the *CNA Professional Liability and Pollution Incident Liability Insurance Policy*. The intended audience for this guide includes architects, engineers, environmental consultants, landscape architects, construction managers, and interior designers as well as their insurance brokers and legal advisors.

Introduction

CNA/Schinnerer's new Risk Mitigation Credit (RMC) is a unique feature of the program of professional liability insurance commended since 1957 by The American Institute of Architects (AIA) and the Professional Engineers in Private Practice Division of the National Society of Professional Engineers (NSPE/ PEPP). It offers eligible policyholders the option of receiving a deductible credit of up to \$25,000 if they implement certain "best practices" in the engagement and performance of professional services. The RMC is designed to reduce the frequency and severity of claims, make claims more defensible, and provide a mechanism to reward policyholders for their risk mitigation efforts.

The risk mitigation credit is most applicable to **risk-intensive** projects and services—those associated with project design and construction.

Eligibility to participate in the RMC is limited to firms whose annual gross billings do not exceed \$25 million. In addition, certain other restrictions apply to firms with annual gross billings between \$5 million and \$25 million. Finally, while otherwise eligible to participate, some firms will not be able to take advantage of the RMC because the nature of their projects or services may not afford them an opportunity to implement the minimum number of the best practices required. The RMC is most applicable to risk-intensive projects and services—those associated with project design and construction.

Background

The RMC was developed as part of a broad interdisciplinary review and update of the 7/99 edition of the CNA Professional Liability and Pollution Incident Liability Insurance Policy. From the inception of the Commended Program in 1957, the primary goal has been to provide professional liability insurance that meets the ever-changing needs of design professionals. Toward this end, the basic CNA policy has had 11 revisions since 1957. In addition, numerous policy endorsements have been developed to tailor the basic policy to specific circumstances, requirements, and underwriting considerations.

Generally, credits in insurance programs are designed to encourage or reward **desired** policyholder practices.

Generally, credits in insurance programs are designed to encourage or reward desired policyholder practices. Once the overall objective of the credit is fulfilled, the credit may be dropped and replaced by a new credit to encourage other practices or outcomes. For example, the 7/99 edition of CNA's basic policy form included a mediation credit of up to \$25,000 for eligible policyholders. While not appropriate for the resolution of all claims, mediation had proven itself to be generally more cost effective in resolving claims than either arbitration or litigation. Industry inertia and resistance to the unfamiliar, however, was hindering the use of mediation in circumstances where it would have been appropriate and beneficial. The mediation credit was designed to help overcome this industry inertia and resistance. By 2005, it had served its purpose—approximately 75 percent of all claims within the Commended Program were being resolved by mediation. As a consequence, the

mediation credit has been dropped in the 10/05 policy form and replaced by the new RMC.

As noted above, the RMC encourages the use of a set of best practices, long recommended throughout the design and construction industry. Receipt of the RMC is predicated on the policyholder's documented satisfaction of a baseline criterion—the timely execution of a written professional services agreement—plus any three of six best practices criteria. The policy language establishing these criteria, their rationale, and appropriate documentation demonstrating compliance are described in detail on the following pages.

The risk mitigation credit encourages the use of a set of **best practices**, long recommended throughout the design and construction industry.

“Baseline” Criterion: Written Agreement

Policy Language

We will reduce **your** Deductible obligation for a **claim** by 50%, up to \$25,000, if, within 60 days of the date of our request, **you** provide us with a copy of the written agreement that was executed by **you** and **your** client prior to **your** performance of the agreed-to **professional services** giving rise to the **claim** and **you** demonstrate, to our reasonable satisfaction, the existence of any three (3) of the following six (6) conditions:

Rationale

A written agreement is a fundamental risk management tool. Through a written agreement, the parties can state their goals and the expectations they have of each other and of third parties. They can allocate rights and responsibilities, risk and reward. Written agreements can also help parties deal with future changes. Even though it may not be possible to determine exactly what those changes might be, it is usually possible to establish a process and some procedures for dealing with change. Also, contracts can help prevent disputes and can establish a framework for the fair resolution of those that do occur.

Compliance Documentation

Appropriate compliance documentation consists of:

- a written agreement executed prior to the performance of the agreed-to services giving rise to the claim.

Contracts can help prevent disputes and can establish a framework for the fair resolution of those that do occur.

The risk mitigation credit will not apply to any claim resulting from services rendered **prior** to the execution of a written agreement.

Discussion

For a variety of reasons, design and other professionals sometimes decide to provide services prior to execution of a formal written agreement. In those cases, firms should keep a record of the arrangements they have made with the client. This can take the form of a commitment letter, sometimes referred to as a letter of intent. It is also advisable to include a time limit for the authorization contained in the commitment letter. That provides an incentive to negotiate and execute the formal agreement promptly. As indicated by the policy language on the previous page, the RMC will not apply to any claim resulting from services rendered prior to the execution of a written agreement.

Practice Criterion 1: Payment Terms/Invoicing

Policy Language

Your written agreement with your client specified payment terms, including a schedule of when payments were to be paid to you, which you consistently followed and enforced, or documented your attempt to do so.

Rationale

Unclear or unspecified payment terms and untimely billing and collection of accounts commonly precipitate claims and counterclaims among contracting parties. By requiring clients to make timely payments for services rendered and by taking action to collect accounts when payments are overdue, policyholders may have an opportunity to identify and cure problems or unmet expectations. Left unaddressed, such problems often result in claims.

Compliance Documentation

Appropriate compliance documentation consists of:

- an agreement executed prior to the performance of the agreed-to services giving rise to the claim (per the “baseline” criterion) containing payment terms and a payment schedule; and
- dated invoices or a spreadsheet reflecting dated invoices; and
- dated unpaid balance reminders or other documents reflecting the policyholder’s attempt(s) to resolve payment problems, if any.

Unclear or unspecified **payment** terms and untimely billing and collection of accounts commonly precipitate claims and counterclaims among contracting parties.

Discussion

Generally, professional service firms extend credit to their clients from the time services are rendered until the time the service-related fees and expenses are collected. This aspect of any professional practice is fraught with risk. Firms that successfully manage this risk invariably do so by, first, checking the financial capability and payment practices of prospective clients before agreeing to perform services for the client. Second, they insist on written agreements with clear payment terms and conditions, including the right to suspend or terminate services for non-payment. Third, their billings are timely, accurate, and consistent with applicable contract terms. Fourth, they actively communicate with their clients so there are no surprises to either party. Finally, when clients unreasonably refuse to make timely payments, the firm follows the applicable provisions of the contract.

Generally, professional service firms extend **credit** to their clients from the time services are rendered until the time the service-related fees and expenses are collected.

Practice Criterion 2: Interprofessional Agreements/ Insurance Certificates

Policy Language

Prior to the performance of the agreed-to professional services giving rise to the claim, you executed a separate written agreement with and obtained certificates of insurance evidencing both Professional Liability and General Liability from each architect, engineer, landscape architect, land surveyor, contractor, or construction manager you engaged or who engaged you.

Rationale

Interprofessional agreements are often oral, not written. Putting pen to paper encourages the parties to address and memorialize the complete terms of their agreement. It also helps the parties avoid uncoordinated contracts and mismatched expectations. Insurance certificates help demonstrate and confirm financial responsibility and compliance with applicable contract terms.

Compliance Documentation

Appropriate compliance documentation consists of:

- interprofessional agreements executed prior to the performance of the agreed-to services giving rise to the claim; and
- certificate(s) of insurance evidencing professional liability (PL) and general liability (GL) coverages (or a spreadsheet reflecting all such certificate information) obtained prior to the performance of the agreed-to services giving rise to the claim.

Putting pen to paper encourages the parties to address and **memorialize** the complete terms of their agreement.

Inadequate or nonexistent
GL coverage can
erode the limits available
under the PL policy.

Discussion

Interprofessional or subcontract agreements should describe in detail the duties and responsibilities of the prime professional and the consultant. Virtually all design and construction projects involve multiple contracts—design and construction, prime, and sub—so they should be tailored to avoid conflict and ambiguity. The AIA and the Engineers Joint Contract Documents Committee (EJCDC) both publish families of coordinated documents. Generally, these agreements require the consultant to provide services to the prime professional in the same manner and to the same extent as the prime professional is bound by the prime agreement to provide such services to the client.

From a professional liability risk management perspective, in addition to a written agreement, it is important to obtain certificates of insurance evidencing both PL and GL coverage. But why, from a professional liability risk management perspective, should we concern ourselves with GL coverage? When PL or GL coverage is unavailable or inadequate, plaintiffs' attorneys typically assert legal theories that they hope will comport with the coverage available under the other policy. And, because the carriers' defense obligations are broader than their indemnity obligations, a considerable sum of money can be spent before the issues are sorted out. On the PL side, this is particularly problematic for policyholders because the defense of a claim may not only trigger deductible obligations, but the cost of defense is within the limits of the policy. As a consequence, inadequate or nonexistent GL coverage can erode the limits available under the PL policy.

Practice Criterion 3: Pre-Project Planning

Policy Language

You engaged with your client in a structured, contemporaneously documented, pre-project planning process that produced a project definition document or package that substantially addressed the following project parameters (only “a” through “c” are required to satisfy this condition for study-and-report-only contracts):

- a. project objectives (e.g., business, economic, aesthetic, other);
- b. project constraints (e.g., budget, schedule, regulatory, other);
- c. the bases for the design/investigation (e.g., site data/requirements, utilities data/requirements, facility programming/requirements, equipment/technology requirements, alternatives to be considered);
- d. project execution approach (e.g., staging, procurement strategy, delivery method, other); and
- e. project monitoring and control procedures (e.g., quality, cost, schedule, other).

You engaged with your client in a structured, contemporaneously documented, **pre-project planning** process...

Rationale

Research by the Construction Industry Institute (www.construction-institute.org) and others has clearly demonstrated the benefits of pre-project planning. These include better definitions of risks, increased predictability of cost and schedule, better achievement of business goals, improved operational performance, and fewer changes and disputes.

Compliance Documentation

Appropriate compliance documentation consists of:

- project definition document(s) addressing the applicable parameters (“a” through “c” or “a” through “e”); or
- agreements annotated to address the applicable project definition parameters; or
- reports prepared as deliverables addressing the applicable project definition parameters.

Both the AIA and EJCDC have long attempted to address the need to **define** the project and its environment...

Discussion

Both the AIA and EJCDC have long attempted to address the need to define the project and its environment by including provisions in their standard client-design professional contract forms that require the client to provide “full information” (i.e., a program, schedule, budget, survey, geotechnical report, or other necessary information) before proceeding. In addition, under the AIA and EJCDC documents, the design professional should respond to the initial information provided and advise the client of apparent conflicts, or the need for additional information or consultant services. Practice Criterion 3 supports the fulfillment of these requirements.

Practice Criterion 4: Internal/ External Peer Review

Policy Language

Prior to delivery to your client of the instruments or deliverables of your professional services, a documented, independent peer review was completed, internally or externally, by a qualified professional to assess the likelihood that such instruments or deliverables would satisfy your client's objectives and would be in conformance with good professional practice.

Rationale

One of the best ways to minimize client dissatisfaction, anticipate problems, and control the quality of design documentation is through investing in a documented internal or external peer review. By definition, an "independent" review cannot be conducted by the person technically responsible for the services or documents being reviewed.

Compliance Documentation

Appropriate compliance documentation consists of:

- documents reflecting peer review activities, such as meeting minutes, memoranda, reports, completed checklists, and notations on design documents (at the conceptual/schematic and final design phases); and
- for external peer reviews, a peer review agreement or engagement letter and documents evidencing the completion of any such external peer review.

By definition, an **"independent"** review cannot be conducted by the person technically responsible for the services or documents being reviewed.

Discussion

While external peer reviews initiated by project owners have become more common in recent years, internal peer or “QA” reviews have long been a mainstay in firms committed to the delivery of services that satisfy client requirements and protect the public health, safety, and welfare. Whether internal or external, the factors that are critical to the success of a peer review include the following:

- First, the reviewer’s qualifications in terms of education, training, and experience should be appropriate to the design or other deliverable being reviewed and the reviewer should have some degree of independence from the person who initially prepared the deliverable.
- Second, the scope of the review should be clearly defined, and review activities addressing that scope should be carried out in a systematic, logical process. Ideally, the review should occur throughout the design process.

At a minimum, **reviews** should be carried out at the conceptual/schematic phase and final design phase of a project.

At a minimum, reviews should be carried out at the conceptual/schematic phase and final design phase of a project. Also, while checklists are not a substitute for experience, they can assist in minimizing oversights. Finally, review comments, responses, and the agreed-to resolution of identified issues should be clearly documented.

Practice Criterion 5: Constructability Review

Policy Language

You engaged with representatives of the project owner, entities responsible for construction and any other project stakeholders you deemed appropriate in a structured, contemporaneously documented constructability review process that provided for the timely integration of construction input into project planning, design, and field operations.

Rationale

Research by the Construction Industry Institute and others demonstrates that incorporating construction knowledge and experience into the planning and design of a project can reduce costs and schedule time and improve the safety of field operations.

Compliance Documentation

Appropriate compliance documentation consists of:

- documents reflecting participation in constructability review activities by representatives of the client and the design and construction teams, such as meeting minutes, memoranda, reports, and notations on design documents, during the pre-construction phase of the project or applicable portion of the project.

Incorporating construction

knowledge and experience into the planning and design of a project can reduce costs and schedule time and improve the safety of field operations.

Discussion

For the purposes of this criterion, “entities responsible for construction” shall include contractors, construction managers, or construction consultants engaged by or on behalf of the client to advise on the constructability of the subject project. The key to maximizing the value of the constructability review process, however, is to understand and respond to the fact that the most important constructability input often comes from trade contractors and suppliers—the people who build the project. And because opportunities to influence cost, schedule, and quality diminish during the course of design, trade contractor and supplier input is most effective when it occurs early in the planning and design process. Regrettably, low bid procurement strategies work at cross-purposes to timely constructability input.

The most important
constructability
input often comes from
trade contractors and
suppliers—the people who
build the project.

Practice Criterion 6: Submittal Management

Policy Language

You maintained a contemporaneously documented construction phase submittal log indicating the as-planned and actual dates you received and responded to every submittal and the action taken.

Rationale

A submittal log that tracks as-planned and actual submittal dates is a powerful project management tool that can be used to mitigate the policyholder's exposure to contractor delay damage claims. It also reflects the AIA/EJCDC contractual mandate that the contractor submit a submittal schedule, coordinated with the contractor's construction schedule, for the design professional's approval.

Compliance Documentation

Appropriate compliance documentation consists of:

- a contemporaneously documented submittal log or spreadsheet reflecting as-planned and actual receipt and response dates and actions taken.

A **submittal log** that tracks as-planned and actual submittal dates is a powerful project management tool...

Experience demonstrates that a well-defined **submittal process** that allocates responsibilities to the appropriate parties is vital to a successful project.

Discussion

Experience demonstrates that a well-defined submittal process that allocates responsibilities to the appropriate parties is vital to a successful project. Claims resulting from project delays and faulty construction are the alternative. The AIA and EJCDC documents require the contractor to provide a schedule for submittals that incorporates the required time for review and resubmittal, if necessary. Since part of this schedule affects the services of the design professional, the contract requires the design professional to approve this schedule, in contrast to the construction schedule, which the design professional merely reviews. The AIA and EJCDC documents also require that the submittal schedule be prepared in conjunction with the construction schedule so that submittals are made in logical sequence and in a timely manner so they can be reviewed and approved when called for by the construction schedule.

Contractors often claim that they cannot provide the required submittal schedule because they have not yet “bought out” the job. That is a spurious argument. The contractor has contractually committed to provide coordination and superintendence of all of the work. If the contractor can contractually commit to a completion date for the project and furnish a construction schedule for the project reflecting that completion date, it is axiomatic that the contractor can and should provide allowances for submittal review and approval in that construction schedule—notwithstanding that the contractor may not have executed purchase orders or contracts for all labor, materials, and equipment necessary to complete the work.

Policyholder Eligibility and Participation

As was the case with the mediation credit, policyholder participation in the RMC is optional, with no underwriting penalties for not participating. Also, like the mediation credit, the eligibility of Large firm policyholders (defined as having annual gross billings of \$5 million or more) is subject to restrictions.

Large firm restrictions applicable to participation in the RMC are as follows:

Firms with annual gross billings in **excess** of \$25 million are not eligible to participate in the risk mitigation credit.

- As noted previously, firms with annual gross billings in excess of \$25 million are not eligible to participate in the RMC. In those cases, the credit will be deleted by endorsement.
- Firms with annual gross billings between \$5 million and \$25 million are not eligible to participate in the RMC if (1) they have retention or deductible obligations equal to less than one (1) percent of their annual gross billings or (2) they have aggregate deductible options. In those cases, the credit will be deleted by endorsement.
- For eligible firms with gross annual billings of \$5 million to \$25 million, the policy language quoted above, under the section titled, “‘Baseline’ Criterion: Written Agreement,” will be amended by endorsement to read as follows:

Your Deductible obligation as shown in Item 5. on the Declarations is reduced to \$_____ for a claim where, within 60 days of the date of our request, you provide us with a copy of the written agreement that was executed by you and your client prior to your performance of the agreed-to professional services giving rise to such claim and you demonstrate, to our reasonable satisfaction, your compliance with any three (3) of the following six (6) conditions:

The consequence of this endorsement for eligible firms with gross annual billings of \$5 million to \$25 million is that the credit applies to their deductible obligation on a “top down” basis, rather than on a “50-50, bottom up” basis as is the case for firms with annual gross billings below \$5 million. From an underwriting perspective, this change is necessary due to the difference in claims frequency and severity between smaller and larger firms.

Administration of the Risk Mitigation Credit

If there is a claim against a policyholder, the policyholder has an obligation to notify CNA or Victor O. Schinnerer & Company promptly and in accordance with the provisions described under Policy Item E of Section VI, titled, “Your Duties if there is a Claim.”

Following a policyholder’s written notice of a claim, CNA will confirm that a claim file has been opened and will ask whether the policyholder intends to apply for the RMC. If the policyholder advises CNA that it intends to do so, CNA will request that the policyholder

If there is a claim against a policyholder, the policyholder has an **obligation** to notify CNA or Victor O. Schinnerer & Company promptly

complete the “Application for Risk Mitigation Credit” and submit the application and the following documentation to CNA, within 60 days:

- a copy of the written agreement that was executed by the policyholder and client prior to the performance of the agreed-to professional services giving rise to the claim; and
- documentation demonstrating, to CNA’s reasonable satisfaction, that the policyholder had implemented three of the six best practices criteria described under Policy Item E of Section V, titled, “Limits of Liability/Deductible.”

The descriptions of “appropriate compliance documentation” are meant to assist policyholders in implementing best practices and in demonstrating their compliance with the RMC criteria. From an evaluation standpoint, the substantive content of the documentation, rather than its specific form, will determine compliance. However, the documentation should be well organized and clearly keyed to each applicable RMC criterion.

From an evaluation standpoint, the substantive content of the documentation, rather than its specific form, will determine **compliance**.

How to Obtain Additional Information

To obtain additional information concerning CNA/Schinnerer’s new risk mitigation credit or to obtain other information about the CNA/Schinnerer professional liability insurance program, call 301/961-9800 or visit our website at www.PlanetAEC.com.

Compliance Document Checklist

The following checklist includes the submittals in each category. Once the “Baseline” Criterion of a written agreement is met, three of the six Performance Criteria need to be included in the application for the RMC. The application is available from the CNA claims offices or from www.PlanetAEC.com.

“Baseline” Criterion (Written Agreement)

Documentation Submitted:

- A written agreement executed prior to the performance of the agreed-to services giving rise to the claim.

Practice Criterion I (Payment Terms/Invoicing)

Documentation Submitted:

- An agreement executed prior to the performance of the agreed-to services giving rise to the claim (per the “baseline” criterion) containing payment terms and a payment schedule;
- Dated invoices or a spreadsheet reflecting dated invoices; and
- Dated unpaid balance reminders or other documents reflecting the policyholder’s attempt(s) to resolve payment problems, if any.

Practice Criterion 2 (Interprofessional Agreements/Insurance Certificates)

Documentation Submitted:

- Interprofessional agreements executed prior to the performance of the agreed-to services giving rise to the claim; and
- Certificate(s) of insurance evidencing professional liability (PL) and general liability (GL) coverages (or a spreadsheet reflecting all such certificate information) obtained prior to the performance of the agreed-to services giving rise to the claim.

Practice Criterion 3 (Pre-Project Planning)

Documentation Submitted:

- Project definition document(s) addressing the applicable parameters (“a” through “c” or “a” through “e”);
- Agreements annotated to address the applicable project definition parameters; or
- Reports prepared as deliverables addressing the applicable project definition parameters.

Practice Criterion 4 (Internal/External Peer Review)

Documentation Submitted:

- Documents reflecting peer review activities, such as meeting minutes, memoranda, reports, completed checklists, and notations on design documents (at the conceptual/schematic and final design phases); and

- For external peer reviews, a peer review agreement or engagement letter and documents evidencing the completion of any such external peer review.

Practice Criterion 5 (Constructability Review)

Documentation Submitted:

- Documents reflecting participation in constructability review activities by representatives of the client and the design and construction teams, such as meeting minutes, memoranda, reports, and notations on design documents, during the pre-construction phase of the project or applicable portion of the project.

Practice Criterion 6 (Submittal Management)

Documentation Submitted:

- A contemporaneously documented submittal log or spreadsheet reflecting as-planned and actual receipt and response dates and actions taken.



Victor O. Schinnerer & Company, Inc.

Two Wisconsin Circle

Chevy Chase, MD 20815-7022

Phone: 301-961-9800

Fax: 301-951-5444

E-mail: vos.info@Schinnerer.com

www.Schinnerer.com

www.PlanetRiskManagement.com

© 2006 by Victor O. Schinnerer & Company, Inc. Statements concerning legal matters should be understood to be general observations based solely on our experience as risk consultants and may not be relied upon as legal advice, which we are not authorized to provide. All such matters should be reviewed with a qualified advisor.