

# SmartRisk A/E Economics & Professional Liability (PL) Insurance Survey Report

## Introduction

The situation in the financial markets is as tumultuous as we have ever seen. What started as a lack of liquidity in the U.S. sub-prime mortgage market has evolved into a global credit crisis touching an unprecedented number of companies and market sectors. Many professional firms, including architects, engineering, environmental consulting, and construction professionals and the carriers that insure them are faced with new and unique challenges. Industry surveys have shown that during a down economy, claims and litigation increase. This is a time when risk management efforts, including the selection of professional liability (PL) insurance are extremely important. Have economic conditions affected insurance decisions of A/E firms? What characteristics are important when making this decision? If firms are changing carriers, what are the reasons? This survey report provides answers to these questions and others posed to design and building professionals.

Many A/E firms are struggling in this slow economy just to stay in business. A majority of firms, 53% have seen annual revenue decrease by 10% to more than 50% in the last 12 months. The economic uncertainty posed by reduced revenues is compounded by delayed payments, reduced staffing levels, layoffs and retirements of senior management. Firms are responding by considering mergers, changes in business strategy, and pursuing alternative regions and market segments. All factors reflecting the realities of today's market conditions. They also heighten risk. Forty-eight percent (48%) of firms said they have had a claim in the last five years. The firms with reduced revenues accounted for the majority of claims in this survey at 76%. External economic forces are increasing risk and liability exposures as limited project financing increases pressures on budgets and schedules, and cost rather than quality begin to drive the selection of products, team members and contractors. When internal and external risk factors combine, it creates the "perfect storm" scenario for claims and litigation for A/E firms. In this challenging and changing environment, firms should be aware of their risks and identify methods to mitigate exposures.

## Make Risk Management a Priority

Forty-four percent (44%) of survey respondents said economic conditions have affected their PL insurance decisions. However, this is not the time to reduce risk management efforts as a cost-cutting measure. Firms should not be making insurance decisions based premium costs alone, reducing limits, or increasing insurance deductibles to levels that do not match a firm's risk profile. Such steps would only put the firm at higher risk during a period of increased litigation. This is the time when firms should be increasing risk management efforts and making them a priority within their practice. When firms focus

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on strategies to mitigate their risks, the natural fallout is maximized performance and profitability. Risk management strategies not only address contract and insurance issues, they also incorporate efficiencies into every aspect of the firm's practice. A "holistic" risk management approach protects the overall financial viability of the firm.

### **Professional Liability (PL) Insurance**

An important component of any risk management program is professional liability (PL) insurance. A majority of firms, 67% said PL insurance plays an important role in their overall risk management efforts. Insurance does provide a safety net when things go wrong, however a proactive approach in managing risk before a claim is filed is an effective strategy. Most carriers offer helpful services to mitigate risk prior to a claim, including pre-claims and claims management, contract review, and risk management services. Each PL insurance carrier varies in their underwriting expertise, products, and service offerings. Certain carriers offer limited-to-no value-added services. Others offer a wide variety of in-depth services and training options. It is important for firms to fully understand a carrier's capabilities, including insurance coverage provisions consistent with market exposures, segment expertise and depth of services. A majority of firms indicated they do inquire into a carrier's service offerings. Eight-one percent (81 %) of firms did not change insurance carriers in the past 12 months. However, 18.5% of firms did change. Why did firms change carriers? Firms said their decisions were driven mostly by economics. Premium costs cited as the number one reason followed by pre-claims and risk management services. These are difficult economic times; however, firms should be careful not to select a carrier based on premium cost alone. Appropriate due-diligence is recommended when selecting PL insurance providers. A specialized A/E insurance agent is an excellent resource that can guide a firm through the PL insurance selection process. Ninety-three percent (93%) of survey respondents agree indicating utilizing a specialized A/E agent.

## **Survey Methodology**

The survey was conducted by SmartRisk LLC, an independent, third-party, risk-performance management-consulting firm supporting the design, environmental, and building market segments. The survey comprised of randomly selected architectural, engineering, environmental consulting, construction management, surveyor and other design professionals from all regions of the U.S. Firms varied in revenue size and project segments. Sixty-eight firms participated in the survey providing anonymous responses focusing on economic conditions and PL insurance decisions.

### Survey Topics:

- Discipline
- Project Segments

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- Annual Revenue
- Revenue Changes in the Past Twelve Month
- Premium Limits and Changes
- Deductible and Changes
- Economic Influences on Insurance Decisions
- Risk Management Perspective
- PL Carrier Characteristics Ratings
- Carrier Satisfaction and Ratings
- Carrier Changes and Why Firms Changed
- Carrier Recommendations
- Additional Comments and Statements

## Key Findings

### Revenues and economics

- The majority, 53% of firms' revenues dropped between 10% to greater than 50% in the past 12 months.
- Forty-four percent (44%) indicated economic conditions played a part in their PL insurance decision.

### Policy details

- Forty-one percent (41%) of firms carry a \$2 million limit.
- Seventy-nine percent (79%) of firms' PL limits remained the same at renewal.
- Seventy-six percent (76%) of firms' deductibles remained the same at renewal.
- Twenty percent (20%) of firms increased their deductibles.
- Twenty-three (23%) of firms carry a \$50,000 deductible.

### Claims, pre-claims and risk management

- Forty-eight percent (48%) of firms have had a claim in the past five years
- Architects accounted for 46% of claims, engineers, 30.8%.
- Firms with reduced revenues of 10% - >50% accounted for 76.2% of claims.
- Sixty-three percent (63%) of firms stated claim expertise and pre-claim assistance services as very important.
- Eighteen percent (18%) of firms changed carriers. Lower premium cited as the number one reason followed by pre-claims assistance and risk management services.

### Carrier information and services

- Sixty-seven percent (67%) indicated PL insurance and related services as important elements of their overall risk management program.
- Fifty-two (52%) of firms ranked pre-claims assistance as a very important services.

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- Sixty-three percent (63%) of firms ranked claims management as a very important service.
- Forty-one percent (41%) of firms ranked risk management services as important
- Eight-one percent (81%) of firms did not change carriers in the past 12 months.
- Eighteen percent (18%) did change carriers; cited premiums, pre-claims services, and risk management as the top reasons.
- Ninety-three percent (93%) of firms utilize a specialized A/E insurance agent.

Even though the survey was random and anonymous, more firms responding reported were very satisfied with their carrier offering than firms that were not. Firms that gave the carrier the highest ratings commented on the importance of their depth of knowledge, experience, responsiveness, financial stability, pre-claims, claim management and risk management services.

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# Survey Results

## 1. Firm Information

**Highest Percentages**

<b>Field of practice:</b>	
<b>Answer Options</b>	<b>Response Frequency</b>
Architect	29.4%
Engineering	29.4%
Environmental	11.8%
Geotechnical	5.9%
Surveying	2.9%
Other*	20.6%

\*Construction management, design-build

<b>Project segments:</b>	
	<b>Response Frequency</b>
Infrastructure	29.4%
Commercial/Industrial	55.9%
Residential	38.2%
Institutional	35.3%
Mixed	38.2%
Environmental	26.5%
Other	8.8%

<b>Annual gross revenue:</b>	
	<b>Response Frequency</b>
< \$500,000	11.8%
\$500,000 - \$1,000,000	2.9%
\$1,000,001 - \$3,000,000	11.8%
\$3,000,001 - \$5,000,000	14.7%
\$5,000,001 - \$8,000,000	23.5%
\$8,000,001 - \$10,000,000	5.9%
\$10,000,001 - \$15,000,000	8.8%
\$15,000,001 - \$20,000,000	5.9%
\$20,000,001 - \$40,000,000	5.9%
\$40,000,001 - \$75,000,000	2.9%
> \$75,000,001	5.9%

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<b>Annual revenue changes in the past 12 months:</b>	
<b>Answer Options</b>	<b>Response Frequency</b>
Down > 50%	17.6%
Down 25%	20.6%
Down 10%	14.7%
Even	29.4%*
Up 10%	5.9%*
Up 25%	11.8%*
Up 50%	0.0%
Up > 50%	0.0%

\*Environmental, energy, healthcare, renovation, remodeling and infrastructure.

<b>Per claim PL insurance limit:</b>	
<b>Answer Options</b>	<b>Response Frequency</b>
\$500,000	2.9%
\$1,000,000	35.3%
\$2,000,000	41.2%
\$3,000,000	11.8%
\$5,000,000	8.8%
\$7,500,000	0.0%
>\$7,500,000	0.0%

<b>Insurance limits changed this past year?</b>	
<b>Answer Options</b>	<b>Response Frequency</b>
Yes, decreased	8.8%
Yes, increased	11.8%
No, stayed the same	79.4%

<b>If yes to changing your PL limits, indicate the reasons why:</b>	
<b>Answer Options</b>	<b>Response Frequency</b>
Annual revenue increased	5.3%
Annual revenue decreased	5.3%
Except more risk	0.0%
Reduce insurance costs	10.5%

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<b>Deductibles:</b>	
<b>Answer Options</b>	<b>Response Frequency</b>
\$2,500 or less	2.9%
\$5,000	8.8%
\$7,500	0.0%
<b>\$10,000</b>	<b>11.8%</b>
\$15,000	2.9%
\$20,000	2.9%
\$25,000	5.9%
\$35,000	2.9%
<b>\$50,000</b>	<b>23.5%</b>
<b>\$75,000</b>	<b>11.8%</b>
<b>\$100,000</b>	<b>14.7%</b>
\$150,000	5.9%
\$200,000	0.0%
> \$200,000	5.9%

<b>Changed deductible this past year?</b>	
<b>Answer Options</b>	<b>Response Frequency</b>
Yes, increased	20.6%
Yes, decreased	2.9%
<b>No, stayed the same</b>	<b>76.5%</b>

<b>If you changed your deductible, indicate reasons why:</b>	
<b>Answer Options</b>	<b>Response Frequency</b>
Annual revenue increased	4.2%
Annual revenue decreased	8.3%
Except more risk	4.2%
<b>Lower insurance costs</b>	<b>41.7%</b>

<b>Has the economic environment influenced your decisions when selecting your professional liability (PL) insurance?</b>	
<b>Answer Options</b>	<b>Response Frequency</b>
Yes	44.0%
<b>No</b>	<b>56.0%</b>

## Claims

<b>Has your firm had a claim in the past five (5) years?</b>	
<b>Answer Options</b>	<b>Response Frequency</b>
Yes	48.1%
<b>No</b>	<b>51.9%</b>

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<b>Claims:</b>	
<b>Answer Options</b>	<b>Response Frequency</b>
Architects	46.2%
Engineers	30.8%
Firm annual revenue: \$5 - 8 million	23.1%
Firms with annual revenue down 10% to >50%	76.2%
Firms with annual revenue even or up	23.1%

## 2. Insurance Evaluation

<b>When viewing Professional Liability (PL) Insurance, please select the statement closest to your perspective.</b>	
<b>Answer Options</b>	<b>Response Frequency</b>
Purchased based on contractual requirements.	14.8%
A line-item business expense.	3.7%
A safety-net when things go wrong.	14.8%
Services supporting the firms overall risk management program.	66.7%

<b>Importance when selecting professional liability (PL) insurance:</b>				
	<b>Not important</b>	<b>Somewhat important</b>	<b>Important</b>	<b>Very important</b>
Premium Rate	0%	0%	70.4%	29.6%
Limits	0%	7.4%	66.7%	25.9%
Deductible	3.7%	25.9%	63.0%	7.4%
Policy Coverage	0%	0%	48.1%	51.9%

<b>Pre-claims assistance:</b>				
<b>Answer Options</b>	<b>Not important</b>	<b>Somewhat important</b>	<b>Important</b>	<b>Very important</b>
How important is a pre-claims assistance program?	3.7%	3.7%	40.7%	51.9%

<b>Claims Handling:</b>				
<b>Answer Options</b>	<b>Not important</b>	<b>Somewhat important</b>	<b>Important</b>	<b>Very Important</b>
How important is the carriers claims handling expertise?	0%	0%	37%	63%

<b>Risk Management Program</b>				
<b>Answer Options</b>	<b>Not important</b>	<b>Somewhat important</b>	<b>Important</b>	<b>Very important</b>
How important is a carrier offering risk management training and services?	0%	22.2%	40.7%	37.0%

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### 3. Carrier Assessment

<b>Satisfaction with current Carrier:</b>				
	<b>Not satisfied</b>	<b>Somewhat satisfied</b>	<b>Satisfied</b>	<b>Very Satisfied</b>
Underwriting/Coverage Features	0%	3.7%	48.1%	48.1%
Premium Rate	16.7%	12.5%	37.5%	33.3%
Pre-claims assistance	0%	15.4%	42.3%	42.3%
Claims Management	0%	15.4%	42.3%	42.3%
Risk Management Program & Services	0%	14.8%	25.9%	59.3%

<b>Changed PL carrier?</b>	
	<b>Response Frequency</b>
Yes	18.5%
No	81.5%

<b>If yes, reasons for changing:</b>	
	<b>Response Frequency</b>
Premium	25.0%
Limit options	0.0%
Deductible options	0.0%
Pre-claims service	16.7%
Claims handling	8.3%
Lack of Risk Management Services	16.7%

<b>A/E Firms recommendations for carriers:</b>	
	<b>Response Frequency</b>
Improve insurance coverage features	16.0%
Improve pre-claims assistance	8.0%
Improve Claims handling	4.0%
Offer/improve contract review services	8.0%
Improve Risk Management Training & Services	12.0%
None to mention, happy with services	64.0%

### 4. Firm Feedback & Comments

#### Reasons for Staying with Carrier

- “Our firm change carriers based on depth of experience in the A/E market and financial stability.”
- “We changed carriers one year ago. We are happy with the services and responsiveness of our carrier.”
- “We are very happy with our carrier, status quo, very good job.”

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- “Our carrier has shown interest in our business, has been very responsive and risk-management oriented.”
- “Our carrier is responsive, fair, and knowledgeable regarding our service needs.”
- “We obtain top-rated service from our carrier on all fronts, very satisfied.”
- “I would rate our carrier very good on service and knowledge regarding our firm and services.”
- “Our current carrier took the time to find out more about our firm, requested an outside risk management consultant to evaluate risk management efforts and identify methods for mitigating our risk. It put us on the right track, we found it very helpful.”

### Comments and Reasons for Change

- “This is a very challenging time. I made a change of carriers based on lower premium and deductible options.”
- “Our premium rate is very high related to our annual revenue.”
- “Our firm has never had a claim in 12 years and our premium continues to escalate.”
- “Our carrier could be more responsive and proactive to the needs of our firm and offer more risk management services.”
- “Premium is brutally expensive, expected to reach 10% of our gross revenue this year.”
- “No problems with past carrier (no claims) and service seems about the same with our new carrier. We changed based on premium to reduce our overhead costs.”
- “We just changed to a new carrier in March 09. Too soon to tell if they live up to their references. We made the change based on premium saving.”

Do you use an agent that specializes in A/E Professional Liability (PL) insurance?	
Answer Options	Response Frequency
Yes	92.6%
No	7.4%

## 5. Final Thoughts & Comments

**Good agent identified the right carrier:** “We have been fortunate to have a good PL Agent that has assisted us in finding the appropriate carrier that meets our needs and goals of meeting any potential claim head-on and aggressively. Our firm has had claims within the last five years, but very little in actual settlement paid out due to the aggressive pre-claim approach of our carrier and appointed defense counsel.”

**Risk assessment provided significant benefits:** “Our carrier utilized an independent risk management firm to perform a risk assessment of our practices. Our firm obtained significant benefits from the process, making us more aware of risk management

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strategies that we have incorporated into daily business practices. The process was very helpful and insightful. Our previous carrier identified no such option.”

**More insurance options needed for smaller firms:** “Our firm is small, less than \$500,000 in annual revenue. This is a very challenging time for firms, especially the small to mid-size firm. However, premium rates are too high for most small and medium companies. We are being forced to take more risk, consider going bare, not buying insurance. We need more insurance options for smaller firms.”

**Pre-claims and claims management services essential:** “Our firm pays a great deal each year for professional liability insurance. When we need assistance and guidance, it is very important that we have a very knowledgeable claims manager working on our behalf as well as a local attorney that can help us if things go wrong. We view claims service as a highly important service. We changed carriers based on poor pre-claims and claims management service”

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### Conclusion

It is obviously a challenging time for many A/E firms with more than half reporting a substantial decline in revenues. Firms are tightening their financial belts to reduce overhead costs and try to survive this turbulent economic period. Some firms are changing business strategies, offering additional services in new regions at the same time reducing staffing levels. Any one of these items increases risk. Some firms have moved to higher deductibles—a logical strategy if a firm has the financial capability to handle a higher deductible. However, firms must recognize the risk of increasing deductibles in a litigious period. A few claims at a higher deductible that is outside the firm's financial reach can put a firm out of business. Risk management efforts are extremely important at this critical period. It helps in mitigating risk and liability exposures. It also helps to improve performance and profitability. A critical element of any risk management program is the selection of a professional liability (PL) insurance carrier. Competitive premium rates are important. However it is also important to evaluate a carrier's knowledge and expertise in the A/E market as well as the services offered to help firms in managing and mitigating risk.

*The survey report is intended to provide information for discussion of the subject matter. Readers are recommended to consult with appropriate advisors for advice applicable to their individual circumstances.*

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**Minimize Risk- Maximize Performance**

SmartRisk LLC is a consultancy providing risk and performance management services supporting the design, environmental and building market segments.

Survey report author Timothy J. Corbett is Founder and President of SmartRisk LLC. Tim has over 25 years of experience developing and implementing insurance and risk management programs for architects, engineers, environmental consultants, and building professionals. He has implemented model programs for numerous firms, including international engineering/construction firms Bechtel and EG&G, where he obtained a Department of Energy (DOE) Top Secret Security "Q" Clearance. Tim held VP and Director Positions with insurance carriers DPIC and Zurich with responsibilities for Underwriting, Risk Management and Industry Relations. Mr. Corbett is a member of American Council of Engineering Companies (ACEC), American Institute of Architects (AIA), and the United States Green Building Counsel (USGBC). Tim sits on ACEC's Risk Management, Business Practices and Environmental Practices Committees and serves as the liaison to AIA's Risk Management Committee. He is regularly called upon as a speaker at regional and national forums, has been published and quoted in international and national publications, and owns copyrights to risk management practices and strategies. Mr. Corbett holds a BS in Security and Risk Management and an MS in Management and degrees focused on Environmental Studies and Architectural Design Technology.

For more information on how SmartRisk can help improve your performance and profitability through specialized assessments, risk and performance management solutions, please contact us.

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