

RISK REVIEW

2005 Second
Edition

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Just Who Are Your Business Partners?

You have probably heard numerous times that one of the non-technical causes of loss, that is a cause not specifically related to technical aspects of the design practice, is client selection. You are frequently reminded to investigate your client to determine whether or not that entity is a good business partner. However, what isn't discussed is what processes do you use to determine if the sub-consultants you retain are good business partners.

First off, you should be doing with your sub consultants what you should be doing with your clients – that is investigating them. Check on their financial stability. Get a list of their projects and try to contact their clients to get their view of the sub consultant. Try to find out all you can about the sub consultants you are considering including how are they to work with, what is their communication style when problems arise and so on. It is also very important to obtain a signed contract for the services that you expect from the sub consultant. Just as we want to confirm scope and other terms and conditions of the arrangement with the owner, you want that same clarity and discussion of how things are to be handled with the sub consultant. The contract with the sub consultant is as important as the contract with the client and should be treated as such.

When a design professional agrees to provide services for a client, that design professional takes the same level of responsibility for the service whether the service is performed directly or is delegated for performance by a sub-consultant. This is under the concept of vicarious liability which is the imposition of liability on one party, in this case the prime design professional, for the conduct of another party, the sub consultant, based solely on the contractual relationship between the two parties. What this means is that you are responsible for their actions. As one might expect, the owner wants one

Just Who Are Your Business Partners? (Cont'd.)

point of contact and one entity to pursue if things go wrong. Usually, the client cannot pursue the sub-consultant directly under the law, but rather pursue you since you have the contractual obligation. It then becomes your obligation to get that entity involved. The key is how to do it.

Recently I was made aware of a situation where a client retained an architect for the design of a commercial facility. The contract included civil engineering requirements and thus, the architect retained a civil sub consultant. The contract between the client and the architect required arbitration. The contract between the architect and its sub consultant did not contain a similar provision. Sure enough, issues arose related to the project and the client filed for arbitration against the architect. The architect then went to its sub-consultant for assistance in the defense of the matter. The sub-consultant was not responsive and in general ignored the requests of the architect. The architect then filed suit against the sub-consultant. However, due to state law, the action was dismissed. Why you might ask? Because the law required that the architect suffer its damage in order to pursue the sub consultant. The judge ruled that the “damage” would not be suffered until there was a finding against the architect for which the sub might be responsible. Thus, the architect was left to defend the arbitration filed by the owner without assistance from the sub-consultant. The architect settled its matter with the owner for about \$600,000 after spending about \$75,000 in fees and

costs and is now beginning its lawsuit against the sub consultant. The fees the architect will incur in that pursuit are not recoverable from the sub consultant.

How do we avoid this scenario? Watch your contracting. Whatever dispute resolution procedure you are required to participate in with your client is what you should be requiring of the sub consultant. And, you should be requiring that the sub consultant submit to joinder in the same proceeding if necessary. The C141 offers some good language:

An action to resolve a dispute arising out of or related to this agreement between the Prime Design Professional and the Sub consultant may be consolidated with a similar action between the Prime Design Professional and any other person or entity in such action to resolve a dispute involves common issues of fact relating to the performance by the Sub consultant of the Sub consultant's obligations under this Agreement.

Now that we have the sub consultant with an obligation to get involved if there is a claim, the next issue is to make sure they can respond if there is a claim. To see the importance of this, less review another war story. An architect retained a structural engineer to help in the design of a manufacturing facility. The project moved along alright and was completed. About three months after substantial completion the facility's roof collapsed. Luckily, this happened in the eve-

ning and thus, no one was injured. However, the owner had completed the installation of its manufacturing equipment, the most of which was destroyed in the roof collapse. The owner made a claim against the architect for about \$1.5 million dollars. A forensic investigation took place and it was determined that the roof trusses were significantly undersized. Faced with these issues, the structural engineer admitted its error and offered up its \$250,000 professional liability policy asserting that the insurance was all there was. Shortly thereafter, the structural sub consultant began to become very difficult to contact and was only providing limited assistance in the defense of the matter. Due to the contracting, the architect had vicarious responsibility for the errors of the structural engineer and with only limited assistance coming from the structural engineer to explain the reasons for the design, the architect was left with little choice than to try and settle the matter – utilizing its full deductible and about \$1M in coverage from its professional liability carrier.

So how do you avoid this scenario? The first key is to require in your contract that the sub consultant maintain appropriate insurance coverage. Just as the owner requires certain coverage for you, you should be requiring certain coverage by your sub consultants. Generally, one would want a sub consultant to have limits which meet or are very close to the requirements that have been made of you in the owner contract. Obviously, the key is to what extent is the sub consultant involved in the project and to what extent does the work performed by the sub consultant influence the other as-

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pects of the project. The existence of insurance can be confirmed by a certificate of insurance. The certificate should list the general liability coverage, workers compensation coverage, business auto coverage and professional liability coverage. Further you should be reviewing the certificates to confirm that the coverage is current and establishing a tickler system to requesting new certificates if your project goes beyond the policy term of your sub consultant. It is important not only to make sure there is insurance at the start, but it is just as important to make sure it is maintained.

Another requirement that can be made is to request the sub consultant's loss run related to their professional liability. Remember, the professional liability policy is a policy that erodes with the payment of expenses. Thus, even if the policy coverage is \$1,000,000 to start, those coverage limits beginning decreasing upon the retention of a defense attorney.

As discussed above, the key to retaining sub consultants is to have their contract terms follow what you are obligating yourself to in the contract with your client. Another issue is that of limitation of liability. More and more these are being discussed in the design community. Consider the following: A prime designer is retained to perform design services related to a jail facility. The prime designer retains a mechanical engineering sub consultant. In the contract between the prime designer and the sub consultant, there was a provision for a limitation of the mechanical sub consultant's liability to

\$50,000. Upon completion of the facility, a mechanical issue arises for which the owner is claiming \$850,000. There is no limitation of liability in the prime design professional-owner contract. The mechanical sub consultant tendered its \$50,000 and the prime designer was left defending the claim and facing the exposure.

As you can see, granting a limitation of liability has some concern for exposure attached to it. As we such, when considering granting a sub consultant's request for a limitation of liability, you need to consider to what extent is the sub consultant involved in the project and to what extent does the work performed by the sub consultant influence the other aspects of the project.

A final suggestion is to have the owner retain the various professionals necessary for the project. This is obviously something that owners generally do not want – they seek a single point of contact for the project, but I would recommend that you push back particularly when geotechnical services or cost estimating services are involved. These are areas where it is reasonable to have the owner deal directly with the discipline. Further, depending upon the extent of the involvement of the structural, you might also consider it as well.

The use of sub consultants on a project is something to consider very carefully. We recommend that you pay attention to what entities you work with, investigating them as you would investigate a new client. Further, your contract with them

should reflect what your obligations are to your client and, in general, follow in form. Lastly, it is key to review their insurance coverage to make sure they can address an issue should it arise.

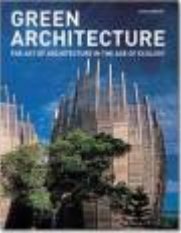
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This article is written for informational purposes only. Before taking any action that could have legal or other important consequences, speak with a qualified professional who can provide guidance that considers your unique circumstances.

Green Design

DJP/Dr. Ujjval Vyas of FGPP



A very important, though unrecognized, synergy exists between LEED certification and the design-build construction delivery mechanism.

LEED certification requires one thing above all else to succeed: an integrated and comprehensive approach to building design and construction to create a high performance product. All the parties involved in the construction process—owners, contractors, design professionals and sub-contractors far down the chain—are encouraged and often required to participate from the outset in the planning and coordination of the project to achieve the requisite goal.

This means that the process must be non-adversarial at the least and actively synergistic at best. Studies have found that attempting to attain LEED certification after the project has already been designed or undergoing construction will create large cost premiums. Buildings which choose at the outset to seek certification and attain buy-in from the various parties can attain certification, even at the highest levels, with little or no cost premium. In light of this, it should be little wonder that a single point responsibility

project delivery mechanism such as design-build would work most efficiently to deliver the high performance product desired. Such a delivery system eliminates the adversarial aspects of a traditional delivery system—especially between the contractor and the designer. To achieve a LEED certified building, it is exactly the contractor's) and the designer's) that must be willing to participate and help each other in coordinating and solving problems to achieve the certification. Whether it is the waste-hauling sub-contractor, the HVAC engineers and installers or the need for the prime contractor to help with ensuring a curtain-wall design can be efficiently incorporated into the building, coordination towards a common goal is vital.



The design-build delivery mechanism provides the requisite amount of coordination and mutual problem solving needed to become the preferred project delivery system for all buildings seeking LEED certification. Further, this system allows the architect to once again reassert his role as a master-builder if an architect-led design-build delivery system

is used. This option has great potential to reward architects, but it also requires a clearer understanding of the risks. An architect taking on the task of leading a design-build project delivery will shed the protection afforded to architects under professional liability standards and will be held to the standards of the contractor. This is both a boon and a risk. It is a boon in the sense that the architect can now promise to the owner a guaranteed price and a guaranteed performance. The architect will be able to complete what he begins and have the control to obtain the results by contracting directly with the prime contractor. The owner, on the other hand, is pleased to have only one party to deal with and the often fast-track advantages such a delivery mechanism allows. The risks are the same risks a contractor faces. Although this set of risks is not new, it is new to architects. For the last hundred years, architects have sought to decrease to an absolute minimum the liability that can arise from the provision of their services. Whether this is the proper direction is a matter of some debate.

(Continued on Page 6)



Benefit Briefs

For the past 25 years, clients have entrusted their business with AVA not just because of the name on the door, but because of the staff and the dedication to service that the name represents. In order to ensure that we continue to meet or exceed these high standards in all facets of our business, we have allocated additional resources to our benefits department.

We have expanded the benefits staff to five members, with a combined total of over fifty years' experience in employee benefits; this includes two dedicated Customer Service Representatives in order to provide a prompt and efficient response to client inquiries and issues. We now have staff members with experience as broker/consultants and insurance carrier representatives, providing a unique perspective into how best to work with insurance carriers on your behalf.

As part of Hilb, Rogal & Hobbs (HRH), your AVA benefits team is now part of a national practice consisting of over 400 employee benefits professionals in 49 states, with access to a wealth of resources and expertise in all facets of employee benefits. In addition to managing your Health & Welfare plans, we can assist in many other areas, such as Voluntary Benefits, 401(k) and Retirement Planning, Executive Benefits Planning and many other consulting services in order to maximize the value of your employee benefits investment.



HRH's national resources include technologies that optimize financial efficiencies, help to identify the most appropriate and reasonable solutions, and reduce your administrative burden. MyWave is a web-based tool available to AVA clients that provides a central source of information and materials (legislative information, benefits benchmarking studies, informative employee newsletters, etc.) to assist you and your Human Resources staff. HRConnection is another web-based system available to clients to provide similar information to employees, as well as any company-specific information. It is completely customizable and can dovetail with an existing intranet, or act as your company intranet in the event one does not currently exist.

It is our goal to maximize the resources available to AVA as part of the HRH family while remaining an organization dedicated to providing the highest level of personal service and ensuring the highest return on your employee benefits investment.

Green Design (Cont'd. from page 4)

What is not debatable is the growing importance of LEED certification and the rapidly increasing percentage of buildings using design-build. What remains to be seen is the response of the architectural profession to these looming changes on the horizon. If architects do not step up and creatively manage the risks attendant on this burgeoning situation, contractors will come to dominate this field and further marginalize the role of architects.

The insurance and liability protection systems an architect should have in place are quite different under the architect-led design-build scenario and require careful guidance from both attorneys and insurance providers. As is commonly known, any warranty provided by an architect will abrogate the professional liability coverage normally obtained by design professionals.

Often, there will be questions related to standard of care issues in regard to LEED certified buildings and the design professionals involved. After all, a LEED certified building means that it adheres to higher standards of design and performance than non-LEED certified buildings. Alternative insurance vehicles beyond the conventional professional liability policies may have to be obtained to take advantage of the growing opportunity that the new synergies will create, as will new business structures for architects and architecture firms. The appropriate business, contractual, insurance and bonding requirements to service architects seeking to lead a design-build team providing a LEED certified building are only now beginning to be addressed by innovative legal and risk management entities.

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AVA Insurance Agency 2005 Upcoming Public Seminar Schedule

May 19, 2005

4:00pm to 5:00pm

Casino Queen Hotel in E. St. Louis

The Ten Commandments of Loss Prevention,” Presented by Laura Guagliardo from AVA Insurance Agency. This program will review the top risk management practices that every firm needs to be made aware of in order to enhance project management capabilities and prevent professional liability claims. Qualifies for 1 PDH.



July 20, 2005

9:00am to 11:00am

Merchandise Mart, AIA Conference Room

CYA with CA Services – Construction observation can be a strong risk management tool. Please join us as members of AVA Insurance agency discuss how to use this phase of services to assist you in lessening the likelihood of professional liability claims. This program is meant for anyone who visits the field during construction administration and will give you recommendations on how to deal with frequent scenarios on the construction site. This program is approved for 2 hours of HSW credits.

ALA “Insurance For Dummies” Risk Management Workshop Summary

On March 15, 2005 representatives from AVA Insurance Agency presented a program describing the fundamentals and finer points of commercial insurance to over 100 ALA members at the Carlisle in Lombard, Illinois. The following is a brief summary of the exposures discussed during this workshop facing design professionals.

General Liability exposures arise from the duty to reasonable care to refrain from harming others. Architects can mitigate their exposure to job site injury claims by being added as Additional Insureds on the Contractor's General Liability policy on a primary and non-contributory basis. The Architect must make the Owner do this by requiring it in the Owner/Architect agreement. Note that the AIA documents do not call for additional insured status, so the General Conditions for the Contract of Construction must be modified or supplemented.

Professional Liability insurance covers

Architects for a failure to meet the professional standard of care. Architects should be careful not to increase their standard of care by agreeing to warranties, guarantees, or over broad indemnity agreements because they may be taking on uninsured liability.

As Contractual Liability results from voluntary agreements rather than unexpected losses, insurance for Contractual Liability is limited. It can be found in the General Liability policy for that part of a written work agreement where the Insured agrees to assume the tort liability of another to pay damages resulting from bodily injury or property damage arising from activities of the Insured. All Professional Liability policies exclude coverage for liability assumed under contract above and beyond the professional standard of care.

Employment Liability claims are now more common than General Liability claims for most businesses outside of the

construction industry. Employment Practices Liability Insurance covers employers against claims by employees for discrimination and sexual harassment. Fiduciary Liability insurance covers employers for errors in administering employee benefits programs, or giving bad advice regarding employee benefits.

Workers Compensation statutes impose Statutory Liability on employers to pay benefits to employees who are injured on the job. While injured employees cannot sue their employer, they are free to sue third parties, who in turn can sue the employer.

AVA also described how employee benefits are becoming more of a focal point for employers, particularly in the small group market. Current industry trends were discussed in detail that described various programs that employers are utilizing in an effort to reduce premiums.



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If you would like
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AVA INSURANCE AGENCY BENEFITS

Specialized Personnel

We maintain a staff of professionals specifically trained in the unique insurance needs of the design professional.

Market Knowledge

Our continuous study and assessment of available markets enables us to assist our clients with selecting the best insurance company for their specific needs.

Complete Insurance Service

We can fulfill all of the property and casualty needs of our design professional clients including professional and general liability, property, workers compensation, health insurance, employee benefits and employment practices liability.

Contract Review Services

Design professionals are often asked to sign client contract forms. We will review these forms and identify any uninsurable provisions. We then work with the design professional to develop solutions and provide protection.

Seminars

We provide custom in-house training and loss prevention seminars, which are tailored to meet the unique needs of each firm. As an AIA registered provider, many of our programs qualify for AIA continuing education credits.

Loss Prevention Assistance

Formal loss prevention programs benefit firms because they minimize risk and can positively influence premium pricing. We can assist your firm in the development of such programs and provide up-to-date information which will keep your programs current.

Member of Professional Organizations

Among others, we are an active member of AIA and Association of Licensed Architects as well as ACEC, NCSEA, NSPE and others.

Exclusive Carrier Relationships

Because AVA Insurance Agency, a member of Hilb, Rogal & Hobbs (NYSE:HRH), is a recognized leader by the insurance community, we can negotiate the best coverage and pricing for our clients.

D I F F E R E N T B Y D E S I G N

