

Picking the Right Limit for Professional Liability Insurance

Picking the right limit for your professional liability insurance—or for any liability insurance—is as much an art as a science. On the one hand, you don't want the insurance limits to be so large as to make your firm a target; on the other, you don't want to go so low that the policy limits are exhausted by even a modest claim, putting the viability of your firm at risk. How little is too little? How much is too much? The epoxy anchor-bolt system designed for the "Big Dig" resulted in a \$21 million settlement. Allegations of construction defects in a homeowners association in Palm Desert, California, led to a settlement of almost \$13 million. And these were just the settlement amounts; defense costs—which erode professional liability limits—can also mount to substantial sums.

Most firms will never face a professional liability claim that hits eight figures, but six- or seven-figure settlements are not so uncommon. So how do you find that happy medium? In this article, we offer you some guidelines for picking a limit that allows you to sleep at night without breaking the bank.

The Range of Limits

Professional liability limits range from \$100,000 per claim up to the millions. Smaller firms tend to purchase lower limits because they're involved in smaller projects and because higher limits may be out of their price range.

Most small firms will buy at least \$500,000 per claim. The most typical limit is \$1 million per claim. One rule of thumb, and one we recommend, is to purchase an aggregate limit twice the per-claim limit; for example, \$1 million per claim/\$2 million aggregate. As firms grow larger, they tend to buy higher limits because they tend to be involved in bigger projects, their contracts sometimes require higher limits, and they have more to lose.

Benchmarks

One way to gauge the most appropriate limit for your firm is by looking at what your peers are buying. Look at the limits carried by other firms that do the same types of work and are roughly the same size as your firm.

To determine what limits your peer group buys, you need to talk to a firm that has access to that type of information. One excellent source is an insurer that provides coverage to a lot of architects or a lot of engineers. CNA, for example, provides professional liability insurance to a large number of architects and engineers. The company keeps track of what firms buy what limits and can provide those benchmarks.

Another potential source of data is insurance brokers that serve a large number of firms in your field. They have access to information across a range of insurers, not just one.

Trade associations may also keep track of limits purchased by members. For example, the American Council of Engineering Companies (ACEC) publishes a matrix of limits by revenue brackets. The downside of such information is that the information is usually self-reported by the member to the association. One caution on this type of information: Self-reporting tends to be less reliable than third-party (such as insurer and insurance broker) reporting.

Claims Correlations

There are several factors that correlate with the frequency and severity of claims—and, thus, the limits you may need.

The type of project is a key predictor. Designing and building a single three-story office building is likely to result in fewer and smaller claims than designing a 500-unit, stick-built, coastal condominium complex. A structural engineer is more susceptible to a large loss than an interior designer.

And some areas of the country—and of the world—are more litigation-prone than others. The frequency with which your firm and its peers get sued in your area of the country should also have a bearing on how much coverage you buy.

Of course, you should not rely entirely on such generalities. A landscape architect working on a tight budget for a difficult client may end up cutting corners and facing a claim; a geotechnical engineer may never cut a corner and never face a claim. Still, the type, size, and complexity of your firm's typical projects should be major factors in determining the appropriate limits for your firm.

Clients' Requirements

Frequently, the project owner will specify required limits in the prime project contract. If you find that your firm's limits are consistently lower than the limits required by your projects, you should likely be purchasing higher limits across the board. If this is more of an occasional issue, you have two primary options:

1. You can increase your practice policy limits to meet the contract requirements.
2. You can purchase a "SALE" (a specific additional limits endorsement) or an "SPX" (a specific-project excess endorsement) that applies to the specific project.

The second option places project-specific limits under (in the case of the SALE) or over (in the case of the SPX) your practice policy. These two limits are added together to meet the project limits requirement. (A variation on this theme is the "CALE"—a client additional limits endorsement—that applies only to projects for a particular client.)

There is a third option that really only makes economic sense when your firm is involved in a particularly large and/or complex project:

3. A project-specific professional liability policy that covers the entire team may be the best solution.

Approaching the coverage requirements from this group perspective has the additional benefit of minimizing—almost eliminating—any "he-said-she-said" finger pointing if there is a claim because all are covered by the same policy.

If You're in Charge...

If your firm is the prime consultant, dealing directly with the project owner and doing the subcontracting, that may put you in position to dictate the limits to others. In these cases, the prime contract frequently dictates not only the limits required of you, but also of all of your subconsultants. But if the prime agreement is silent on limits for subconsultants, the prime consultant should set its own requirements. You should do so since, in many instances, you will be responsible to the owner for the consequences of the actions of those below you in the contractual chain. Requiring adequate insurance of them protects your interests.

Take care to assess the project and the services your subconsultants will provide. Requiring the same limits from a landscape architect and a civil engineer likely means you're asking too much from one, too little from the other, or both. Instead, tailor your limits to each task within the project.

In the Final Analysis...

Unfortunately, no one can tell you with certainty you how high is high enough. As we said earlier, picking a limit is as much art as science. What do your peer firms buy? How often do you get sued? Where in the country—or the world—do you work? What do your contracts require? And how much can you afford?

There is no magic formula because there is no limit that will be high enough in all cases, but a serious discussion of your risks with a trusted advisor, such as an insurance broker that specializes in insuring your type of operation, should help you determine the right amount that will let you sleep at night without breaking the bank.

If you would like to discuss your limits with us, please contact a Greyling office, or send an e-mail to info@greyling.com. Please put "Limits" in the subject line.