

BLOG

Time is Money And Other Consequential Losses

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There's an old adage in insurance. Limits come in two sizes, too big or too small. The problem is you don't know until it's too late.

Figuring out whether you're in the too big or too small category requires an accounting of many factors in the world of architects and engineers. Among the questions insureds should ask:



- What does the client require you to cover?
- What's the purpose of your limits? Are you trying protect your client, yourself or your firm?
- What are your peers doing and are you consistent with the limits of similar-sized firms? What types of design problems can come back to you?
- How complicated are they?
- What is the typical value of the projects you work on?
- Are you working on \$1.2 million homes or billion-dollar commercial properties?

One of the questions often asked once it's too late is: What kind of damage might arise beyond simple replacement costs?

For example, if you're designing the renovation on a factory that does processing work, let's say a plant that turns potatoes into french fries, and an engineering mistake causes delays that force you to miss your completion date, you might be on the hook for more than the costs to fix the mistake. Depending on the contract, as the A&E firm, you might be responsible for loss of income for the time frame beyond the completion date when the manufacturer couldn't make their french fries.

Instead of a potato-processing factory, let's say it was a toy manufacturer. A delay might mean the toys that were expected to ship in time for the Christmas rush won't be ready until January. Now you're looking at more than just income. You're looking at loss of profits and potential loss of retail business and reputation.

This type of exposure is known as **consequential loss**, and it's an important consideration for any A&E firm.

With revenue-producing businesses, lost profits for project delays can add up fast.

When a major league ball park experienced a structural design error that caused a late opening, and games had to be moved to another venue, it meant a major-league loss in ticket sales, refunds and vendor sales. Similarly, casinos incur such astronomical per-day losses, that most A&E firms won't sign a contract without a waiver of consequential loss.

If you're working on a school and the job isn't finished on time, then the school district might have to rent additional space to accommodate students. That's another consequential loss that can be passed on to you, the design professional and a factor to consider when determining the right amount of insurance.

Cost of money is another potential consequential loss when rates are high. Increased cost of funding can be the source of a delay damage claim.

Duty to defend a third party is another hidden consequential loss. At times design firms knowingly or unknowingly will assume the contractual duty to defend a third party whether or not the design professional was at fault. This includes legal fees and costs incurred by the third-party. Finding an insurance product that covers duty to defend is an important way to mitigate risk.

Negotiating your contract to eliminate your exposure to potential consequential loss is a good idea, but it's not always possible. Government contracts are notoriously difficult if not impossible to negotiate. While federal, state and municipal contracts are often sought after, they can also force you to take on higher limits of liability as well as all consequential loss exposure.

Higher limits cost more, but more insurance is a lot cheaper than inadequate insurance when a loss is involved. To learn more about setting appropriate limits of liability for your next project, contact mwelbel@risk-strategies.com or dcrow@risk-strategies.com.

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