Dealey, Renton & Associates, *Insurance Brokers*

VOLUME 19 NUMBER 2

a/e RISK REVIEW

A PUBLICATION OF THE PROFESSIONAL LIABILITY AGENTS NETWORK

Project evaluation is now more important than ever

The following material is provided 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 own unique circumstances.

When work is scarce, struggling design and environmental firms can feel compelled to compete for virtually every opportunity. These firms feel they can't afford to be picky with the projects they pursue and aggressively go after work that they would ignore during better economic times. The survival of their firms or the jobs of their faithful employees may be at stake. They'll try to get anything and everything to keep the shop doors open and generate the revenues needed to survive.

In such an environment, project evaluation often takes a back seat. firms are less concerned about project risks. Their number one priority is getting the work. Yet it is in tough times such as these that project evaluation becomes more critical than ever. A firm that decides to take on a risky or unfamiliar project needs to know the potential perils and how to best mitigate them. When you say "yes" to a project you would typically say "no" to, you'd better proceed with your eyes wide open and your risk management toolkit fully stocked and ready for application.

Let's look at several factors that must be weighed when evaluating potentially risky projects.

Type of project

Some types of projects are so litigation-prone that only the most qualified—or most desperate—firm would accept them. Certain types of Phase I inspections, for example, have historically been high risk. Condominiums have been so high-risk that professional liability insurance companies are hesitant to insure firms that design them. Historic renovations are also higher risk due to the chance of hidden problems such as asbestos, lead paint and other hazardous materials and conditions.

According to insurance industry studies, other project types that can present higher than average risks include wastewater/sewage plants, residential custom homes, schools (k-12), high rises, hotels, residential subdivisions, airports and bridges/trestles. Lower-risk projects include malls/retail and commercial industrial buildings of nine or fewer stories.

This is not to say that design or environmental firms should never take on condos, historic restorations or

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other types of higher-risk projects. They should, however, approach these types of projects cautiously, making sure they have qualified individuals to work on them, set their fees to reflect the higher risk and are persistent in negotiating protective contract language.

Project delivery method

More and more projects vary from the traditional design-bid-build delivery method. In addition to the growth in design-build and fast-track projects, project delivery methods incorporating BIM, IPD and other hi-tech techniques are in increasing use. It is important to realize that each alternative project delivery method involves specific skills and risks and requires a different allocation of responsibilities for those risks.

Your risk on a design-build project varies depending on the role and contractual relationships you undertake. If you lead a design-build project, you become responsible for risks traditionally associated with contractors and not normally assumed by engineers, architects, or environmental consultants. On the other hand, with a contractor-led design-build project, your risk may be little different from that of the traditional design-bid-build delivery method.

The same holds true for firms that provide construction management services. Your risk as a construction manager depends on which role you play on a project and what contractual obligations and relationships you undertake.

The nature of fast-track projects often involves substantial modifications to plans and thus big change-order expenses. Unsophisticated clients won't expect change orders and, most likely, will not understand the need to have sufficient contingency reserves set aside in their project budgets.

BIM and IPD projects not only require a unique set of technology skills, they involve shared and often blurred roles and responsibilities. This is no time for on-the-job learning for consultants.

Other parties involved

Even the most plain-vanilla type of project can be high risk if the other parties involved in the project are litigious or prone to errors and omissions. A client with a history of litigation against its consultants, contractors and others should be a huge red flag when evaluating a project.

Indeed, when budgets are extremely tight and profit margins thin, the client may be the greatest risk factor associated with a project. An underfunded project is a high-risk project. Clients with insufficient capital will look to skimp on quality and will encourage their consultants and contractor to do the same. They may try to save money by eliminating a firm's construction-phase services. Should financing begin to dry up, they may delay payment for services or file trumped-up claims as a ploy to avoid payment altogether.

If a project appears to be underfunded, be sure to conduct a financial check of your client. Don't let the client reduce your scope of services to the point you can't adequately control your risks. Also, make sure you have a suspension of services clause in your contract that gives you a way to pull out of the project in the event funding problems result in project delays, slow payment or other breaches of your contract.

Likewise, the contractor assigned to a project is a significant risk factor. This is particularly the case when a contractor has been selected on a low-bid basis. It is always wise to investigate the history of the contractor as part of the project selection process. Are they experienced in this type of project? Do they have a history of litigation? Subcontractors and subconsultants (or the prime if you are a subconsultant) should be looked at as well.

Level of experience and knowledge

Take a hard look at the capabilities of your firm when evaluating projects. How much experience do you have with this type of project? Who on your staff has the necessary expertise? Have you worked with the owner or contractor before?

Consider your projected workload and the mix of other projects you will be working on concurrently. If you have reduced your staff down to the bare bones, will you need additional personnel to take on this new project? Chances are there is a substantial pool of available consultants that you can hire or subcontract to. Taking on a project that severely stretches your staff and skill set can be a recipe for disaster.

Scope of services and fees

Even when overall project funding seems adequate, be wary of projects for which you are offered a severely limited scope of services and/or inadequate fees. Projects that omit construction observation services, for example, are more prone to errors since you are not available to provide guidance in the execution of your plans.

Contractual provisions

Beware of the "contractually hazardous" projects that "take-it-or-leave-it" owners may present during hard economic times. This could be any type of project—even a simple, single-story commercial building—for which the client issues a contract containing such unfair or onerous provisions that you could wind up accepting most or all of the client's liability.

Sometimes, an unsophisticated client with a small project may attempt to issue a purchase order or similar short contract form, which is thoroughly inappropriate for engaging a professional's services. Some might argue that such a project is among the riskiest of all because you have none of the standard contractual provisions professionals need for protection.

Alternately, strong contractual language can make an otherwise risky project palatable. Contractual limitations on your liabilities can offset a lot of project sins. You can often negotiate additional contract protection in exchange for a smaller design fee.

A project evaluation checklist

Project selection is rarely a cut-and-dried, yes-or-no decision. Projects usually contain a number of risk factors that, considered separately, might be acceptable. But together, these risks could add up to a big liability headache.

Your best course during project evaluation is to strive to identify all of the potential risks of a prospective project and then make a calculated decision based on a combination of factors, including the current economic climate.

Some architects, engineers and environmental consultants use a Project Evaluation Checklist to evaluate projects before submitting a proposal or negotiating an agreement. This checklist should cover issues such as:

- ❒ Is the project type one that is inherently risky, such as condominiums, amusement rides or historic renovations?
- ❒ Does the project team, including the owner, the prime consultant, subconsultants and the contractor, have experience with this type of project?
- ❒ Does your firm have the necessary skills and staffing for the project? If not, can you acquire it?
- ❒ Is the project adequately financed?
- ❒ Does the project owner or contractor have a litigious history?
- ❒ Does the project include an adequate scope of services?
- ❒ Are you receiving an adequate fee?
- ❒ Is the project schedule realistic?
- ❒ Are there any unusual features, such as unfamiliar code requirements, new technologies or unstable geological conditions?
- ❒ Can mitigating factors be offset with contractual protection, such as a limitation of liability clause or indemnity provisions?

Add your own checklist items based on the unique characteristics of your firm.

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Once you've analyzed the risks of a potential project, determine how the risks you've identified might be managed. You can minimize some risk by educating your clients, providing more comprehensive services and assisting the owner with a qualification-based selection of a competent contractor. You can also reduce your risk by developing a contract that is fair and precise—and that includes reasonable mutual indemnities and a limitation of liability clause. And, of course, you can limit your financial risks by purchasing adequate professional liability insurance.

It is in everyone's best interest for you and your client to take a good, hard look at the risks you cannot prevent or control. Understand that on a high-risk project, the risk should be borne by the party best able to control it. If no one can control the risk, then it rightly remains with the project owner, who has the most to gain from the project.

The risks that remain on your plate —those that rightly belong to you and cannot be otherwise transferred or managed—will require a hard-nosed business decision. Is the fee or other incentive so attractive or necessary that you can accept the risk?

In the end, project evaluation and selection requires a business decision that only you can make. In tough economic times you may feel compelled to accept any and all project offers. Before accepting risky business, however, make sure you are well armed and educated to proceed in the safest way possible.

Can we be of assistance?

We may be able to help you by providing referrals to consultants, and by providing guidance relative to insurance issues, and even to certain preventives, from construction observation through the development and application of sound human resources management policies and procedures. Please call on us for assistance. We're a member of the Professional Liability Agents Network (PLAN). We're here to help.

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