

Claims Study

A STUDY OF EXPOSURE TIMES AND MERITLESS CLAIMS AGAINST DESIGN PROFESSIONALS IN NEW YORK

An analysis of claims against New York-based construction-related professional firms insured by the CNA/Schinnerer program illustrates the cost and effort spent by firms in defending themselves against claims. These findings indicate that the inefficiencies of the judicial system diminish the ability of firms to effectively provide design services to protect public health, safety, and welfare.

METHODOLOGY OF THE STUDY

The CNA/Schinnerer program examined two major factors that affect the exposure of firms in New York. They are the following:

- ✓ **The length of time between the completion of services and the filing of a claim.** This indicates the period when the greatest exposure to claims occurs. It also provides information on possible limitations as to when claims could be filed against firms. Limiting the period of exposure reduces the costs of record keeping and insurance, such as insurance for retired partners. Limiting the exposure provides a balance between the rights of project owners and third parties and the costs to design firms and society of meritless claims.
- ✓ **The percentage of claims that resulted in a payment by the CNA/Schinnerer program on behalf of a New York policyholder.** This indicates whether claims brought against design firms had merit in that a payment was required to rectify economic losses, correct damages, or compensate for bodily injury.

THE LENGTH OF TIME BETWEEN THE COMPLETION OF SERVICES AND THE FILING OF A CLAIM

Most Claims Happen Before or Soon After Project Completion

We examined 664 claims for which the dates of the completion of design services and of claims brought against the insured firms were clear. This sample included claims of all sizes brought against policyholders of all sizes. The claims appear to be representative of all claims against CNA/Schinnerer policyholders in all parts of New York.

Only claims in which a payment was made by the CNA/Schinnerer program were included in the information below. They represent 22.4 percent of 664 claims examined. The remainder of the claims resulted in defense

Victor O. Schinnerer & Company, Inc.

In 1957, Schinnerer—in conjunction with The American Institute of Architects and the National Society of Professional Engineers—developed the nation's first professional liability insurance policy and risk management program addressing the coverage needs of design professionals. Since that time, Schinnerer and CNA Insurance Companies, the insurer for the program, have kept records of the nature and sources of claims against design professionals insured in the CNA/Schinnerer program.

costs to the firms against which the claims were made but did not result in any payment to correct damage. The claims indicated below are considered to be claims with merit; payment was made on behalf of the policyholder because either through legal action or by settlement it was determined that the policyholder had liability because the cost, loss, or damage for which the payment was made was the result of the policyholder's negligence in performing or furnishing professional services.

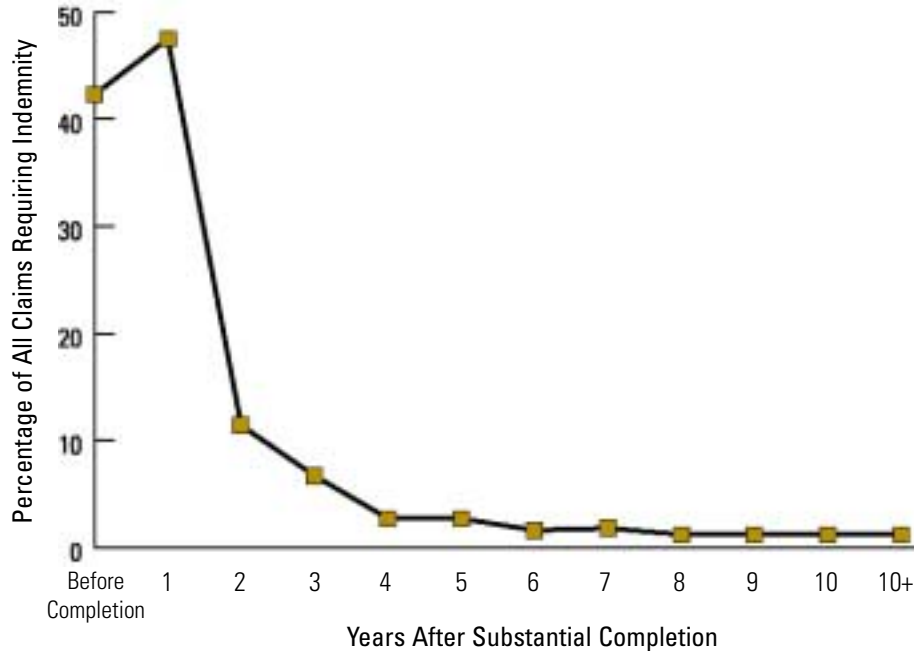
In this representative sample, over 42 percent of all claims brought against policyholders and over 33 percent of all payments made on behalf of policyholders occurred prior to the completion of projects for which the services were provided. Most of these claims were brought by project owners or contractors and were for the recovery of costs for project delays, extra construction expenses, or economic losses. During the study period, approximately 65 percent of all claims filed were brought by the clients of the design firm. About 24 percent were brought by others involved in the construction process. Only 11 percent of all claims were brought by those outside the construction process, and those claims were mainly for property damage and bodily injury.

The study also looked at claims from projects completed more than ten years ago. Some were completed decades ago. The following chart shows that after seven years following the substantial completion of a construction project, few claims are brought against design professionals. ***From the eighth year on, only 1.2 percent of claims for which an indemnity payment is made occurs. Payments made on these claims represent only 2.7 percent of all the payments made on behalf of insured firms.***

Years after Substantial Completion	Percentage of All Claims Requiring Indemnity	Cumulative Percentage of Claims Requiring Indemnity	Percentage of All Indemnity Payments	Cumulative Percentage of All Indemnity Payments
Before Completion	42.3	42.3	33.2	33.2
1	47.5	71.8	29.6	62.8
2	11.4	83.2	12.8	75.6
3	6.7	89.9	11.2	86.8
4	2.7	92.6	3.1	89.9
5	2.7	95.3	2.7	92.6
6	1.6	96.9	2.4	95.0
7	1.8	98.7	2.3	97.3
8	1.2	98.9	2.7	97.9
9	1.2	99.1	2.7	98.3
10	1.2	99.3	2.7	98.7
All Remaining Years	1.2	100.0	2.7	100.0

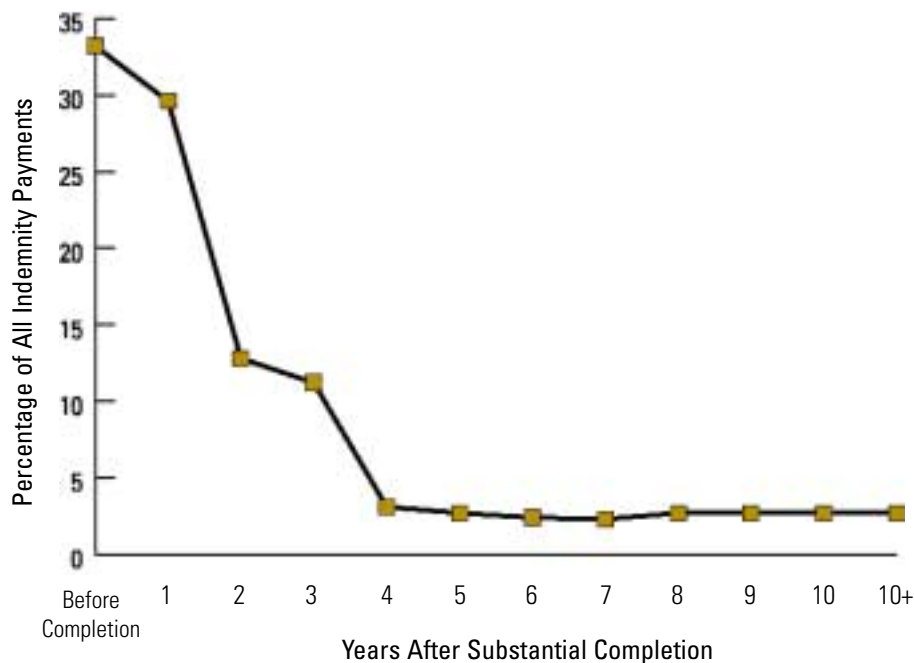
Percentage of Claims Requiring Indemnity

Graphically, the above information is even more dramatic. The line chart below, which shows the percentage of claims filed, clearly indicates how quickly claims taper off in the number filed each year that require a payment after the first few years following completion of construction.



Percentage of Indemnity Payments

The following chart shows the distribution of indemnity payments. These are the payments made by the insurer on behalf of a policyholder to correct a problem or compensate for a loss resulting from the negligence of the policyholder.



In looking at the specifics of the claims brought after the seventh year, it is clear that the claims rarely result in a payment on behalf of the insured design professional because there is no causal link between negligence on the part of the insured and the harm being alleged. The claims that occur many years after substantial completion usually involve personal injury claims that do not result in any payment by the design professional because there is no justification for a finding of fault on the part of the design professional. Those claims that are filed by project owners many years after the completion of a project also rarely result in a payment by the design professional. During the intervening years between services and the claim, conditions often have changed and many other factors, such as maintenance or external forces, are found to have created problems alleged as being caused by the negligence of the design professional.

Time Limit for Claims Would *Not* Significantly Reduce Rights of Plaintiffs

In most states, statutes of repose exist to recognize that it becomes increasingly difficult as time goes by to determine fault for a defect in constructed facilities. Our claims analysis has shown that most claims alleging damage caused by the negligence of the design professional, and that ask for remedial services or compensation, happen within only a few years following substantial completion.

If a statute of repose setting an absolute cut-off of claims related to a project is set, a design professional has the ability to better assess the exposure to claims. In turn, the design professional can better protect assets from claims that may have little true relationship to the design professional's negligence. Setting this cut-off date at seven years after the substantial completion of a project, for example, is a reasonable method of giving some certainty to risk. Based on the information in this study, a seven-year limit in New York would preclude only about **1.3 percent** of claims that require some payment by the design professional.

THE PERCENTAGE OF CLAIMS THAT RESULTED IN A PAYMENT

Most Claims are Meritless

Few claims after the first few years following the completion of a project result in an indemnity payment by the design professional's insurer. It is clear from both national statistics and statistics specific to New York that professional service firms are infrequently found responsible for causing property damage or personal injury through their negligence in providing design services. ***These meritless claims, however, drive up operating costs for design firms and insurance costs for insurers, which in turn drives up costs for design firms.***

It also becomes apparent that because of the nature of the United States civil justice system and a misunderstanding of the services provided by design professionals, they are often subjected to defending their professional practices against unfounded allegations of negligence. These claims appear to result in:

- ✓ Unnecessary judicial administrative costs;
- ✓ Defense costs to those design professionals alleged to be negligent—costs that must be covered by increasing fees to all public and private clients;
- ✓ Loss of productivity because of the time that such claims consume; and
- ✓ Groundless damage to the reputation of the firm and its profession.

Few Claims Result in Indemnity Payments

Our study of claims on a national basis indicates that from 1998 through 2002, a small percentage of claims (less than one in five claims had sufficient merit to require a financial remedy) resulted in a payment and that this percentage was significantly less than the national average. **Only 17.8 percent of all claims brought against New York design professionals insured by CNA/Schinnerer resulted in a payment by the program on behalf of the policyholder to correct property damage or provide compensation for a personal injury.** The national average is 23.9 percent.

This indicates that in 82.2 percent of the claims, design professionals were determined to have had no responsibility for damage or injury as measured by having no indemnity payment by the insurer on behalf of the design professional. In each situation, however, these firms were forced to diminish their productivity by expending their time and money to defend themselves. With property damage claims, the time and defense costs can be significant even if no liability is established. Bodily injury claims, whether brought by injured workers or other parties, account for very few of the paid claims. Usually, the involvement of the design professional in such a claim is inappropriate or is an effort by the injured party to coerce a settlement even though fault is not determined. **Clearly, claims that resulted in no payment to correct damage or harm drained the design professions and the economy of productive time and forced an increase in the cost of providing professional services.**

Claims Rarely Require Fault-Based Indemnity

The table below separates claims into those for which the insurer either made no payment whatsoever or paid only expenses, such as defense costs, and those claims that required an indemnity payment by the insurance company on behalf of the insured firm.

Status of 2,170 Closed Claims Brought in New York Against CNA/Schinnerer Insured Firms							
Resolution of Claim	Percentage of Closed Claims						
	1998	1999	2000	2001	2002	New York Average	National Average
Closed Without Any Payment by Insurer	48.7%	43.3%	43.8%	37.5%	37.3%	41.8%	44.3%
Closed With Expense Payments Only	35.4%	36.1%	37.8%	46.3%	44.3%	40.4%	31.8%
Closed With Indemnity Payment Made by Insurer	15.9%	20.6%	18.4%	16.2%	18.4%	17.8%	23.9%
Meritless Claims (Without Any Indemnity Payment)	84.1%	79.4%	81.6%	83.8%	81.6%	82.2%	76.1%

Those claims that had sufficient merit—a finding of fault or an agreement to pay—to require the insurance company to pay on behalf of the insured for damage or harm account for less than 20 percent of claims filed. In more than 80 percent of the situations, there was no payment to rectify damage or compensate the party bringing the claims for an injury or loss. In New York,

it appears that a greater percentage of claims brought against design professionals are without merit and produce no recovery for the plaintiff.

Every insured firm carries a deductible obligation as part of its professional liability insurance coverage. That deductible is usually consumed by the expense of the firm's defense. Firms must charge clients to recover these defense costs as well as to pay for insurance coverage and lost productivity. It is clear that design firms that pay to defend themselves, and erode their productivity by responding to claims without merit, are victimized by a civil justice system that allows specious allegations or unfounded complaints to drive up the operating costs of professional service firms. Firms must pass on to public and private clients a very significant cost of claims that result in no payment to remedy damage or injury caused by their negligence.

Minimizing Meritless Claims and Limiting Long-term Exposure

The citizens of New York would be well-served by legislative action that would preserve the rights of parties harmed by the negligence of construction-related professional service firms while limiting the exposure of design professionals to claims without merit and claims that occur years after professional services are rendered.