

Professional Liability Insurance Task Force Recommendations

Fall 2013

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Executive Summary

This report has been prepared by the Professional Liability Insurance Task Force as part of a review by the Alberta Association of Architects of the *Architects Act* and *Governing Regulation*, the governing legislation in the province. The AAA's review is being undertaken in anticipation of the Government of Alberta amending the existing legislation.

This document is not a final draft; the draft recommendations are open to discussion and revision. It is being presented to the Legislation Committee, Council and AAA membership to determine: a) whether to endorse the recommendations in principle; and b) whether any fundamental changes to the recommendations need to be made. The recommendations will only be final once endorsed by AAA membership.

Current Legislation

Currently, the legislation does not require registered architects or licenced interior designers in Alberta to carry professional liability insurance. The Task Force was established to consider whether this should be changed in the new Act and, if so, in what way. The findings and recommendations in this report will be forwarded to the Alberta Association of Architects Council and membership for further consideration and action.

Issues

1. Is it in the public interest to require Alberta Registered Architects and Licenced Interior Designers to carry professional liability insurance (PLI)? Would this requirement also be in the best interests of AAA members and the profession as a whole?
2. If a professional liability insurance requirement is adopted, what are the options for implementation, and which model would be the best for AAA members, the profession as a whole and the public?
3. Who should be required to carry the insurance: the practice entity, the individual member or both?
4. If a PLI requirement is adopted by the AAA, what minimum amount of coverage should members be required to carry?

Recommendations

1. The Task Force believes, as a matter of basic principle, that AAA members who are actively practising architecture or licenced interior design in Alberta should be required to carry liability insurance coverage.
2. The Task Force recommends that the best option for implementation of this requirement, in the short to medium term, is a compulsory group purchase plan.
 - Under this option, the AAA would negotiate a contract with an established commercial insurance provider for a group plan under agreed terms.
 - All actively practising architectural and licenced interior design practices would be covered by this plan to the extent of the basic required minimum amount.
3. The Task Force recommends that the practice entity – i.e. the holder of a Certificate of Practice - should be required to carry PLI rather than the individual member.
4. The Task Force recommends that the minimum amount of coverage should be \$250,000.
5. The Task Force recommends that as part of the group purchase plan, the AAA should offer a Voluntary Excess program to provide any additional insurance that practice entities may desire above the basic minimum limit of \$250, 000. Members would also be free to obtain such excess insurance from commercial providers.

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Rationale – Protecting the Public Interest

The Task Force's recommendation that professional liability insurance be required is based on the primary responsibility of the AAA. Under the *Architects Act*, the profession is granted the privilege of self-governance on the understanding that the Association will regulate its members' professional activities so as to protect the safety and wellbeing of the public in the design of buildings. It follows that if an error or omission of a registered architect or LID in the course of practice causes harm or loss to a member of the public, whether a client or not, he or she should have access to compensation. The best way to provide this compensation is professional liability insurance.

What PLI Model Would Be Best for the AAA?

Having recommended that liability insurance be required as a matter of principle, the Task Force proceeded to investigate options for implementation. Building on the work of previous AAA committees, it looked for insurance models that would be effective and affordable for members and feasible for the AAA as an organization. The Task Force was supported in these investigations by Dion Strategic Consulting Group Inc., an independent insurance consultant with expertise in the provision of liability insurance for professional organizations.

The Task Force established five criteria to evaluate potential insurance program models:

- The selected model must be able to cover all practising members in good standing, so that no one could be prevented from practising because of an inability to obtain insurance;
- It must be feasible within the administrative capabilities of the AAA;
- Premium rates should be based on the actual risk profile of AAA members;
- The insurance program should be organized so as to provide practice support and educational opportunities for members in conjunction with liability coverage; and
- It should provide flexibility for the AAA to gain increased control of its insurance program and work toward other insurance options in the future, as Council wishes.

Several insurance models were considered by the Task Force. Upon thorough examination, and with the advice of the insurance consultant, three options were identified as having the best potential:

1. The **traditional open market** option: members would be required to obtain insurance through commercial providers and provide proof of coverage each year as part of membership renewal;
2. A **Compulsory Group Purchase Plan**: members would be required to obtain at least the minimum basic level of coverage from a group insurance plan negotiated between the AAA and a commercial provider; and
3. **Self-Insurance**: The AAA would assume primary responsibility for claims against members, and would operate an insurance program to administer claims and provide compensation.

The traditional open market model would clearly be the simplest option from the point of view of ease of administration. However, the Task Force did not favour this option because it would raise the possibility of members in good standing not being able to practice because they could not qualify for insurance. This would be unacceptable because it would place the ability to practice partly beyond the hands of the AAA.

The self-insurance option would offer the advantage of giving the AAA full control of its insurance program, free from the vicissitudes of the commercial market. Such a model has been developed very successfully by the OAA in Ontario. However, the Task Force recognized that the situation in Alberta is quite different, and this option was considered to be impractical for the AAA, at least in the short term. Presently, the association does not have the administrative capacity, the expertise or the financial capital to undertake such a program (a fund of at least \$5 million would be needed to cover claims).

Based on the current realities of the AAA membership and administration, a compulsory group purchase plan is the best option. In fact, this model has the potential to offer many of the advantages of self-insurance with few of the financial or administrative burdens. It would also allow the AAA to work toward a more independent insurance model in the future.

Under this model, the AAA would issue an RFP to established providers of professional liability insurance, and enter into a contract with the selected proponent for a group policy to cover all members in active practice (i.e. those holding Certificates of Practice). Terms of the agreement would include the following:

- All practising members in good standing would be eligible to obtain insurance under the plan;
- All practising members would be required obtain the basic minimum of \$250,000 coverage from the group plan.
- For excess coverage, members would have the option of buying from the group plan provider, or from any other commercial provider.
- The AAA would have access to generic information on claims, so that it will be able to build a base of information on the profession's risk profile and identify emerging issues.
- There would be an option to set premium rates so as to expect an excess each year which would be set aside to build up a dedicated insurance fund.

The Task Force arrived at its recommendation of \$250,000 as a minimum coverage limit after a review of other provincial requirements across Canada. This amount would provide an adequate level of public protection, while allowing new practitioners to acquire insurance at a reasonable cost.¹ It was recognized that many firms, particularly those doing public sector or larger private sector projects, will need to obtain more coverage. For this excess insurance, they will have a choice of providers, so they will be able to maintain established relationships with their current insurers.

The group purchase plan option provides the AAA with bargaining power to negotiate favourable insurance rates for members. With all practising members included (at least for the basic amount), the insurer will have lower marketing and administrative costs, and the savings can be passed on to the purchasing group.

The sharing of claims information (on a strictly confidential basis) will also be mutually beneficial. The AAA will be able to identify emerging issues in the profession's risk profile, and tailor its continuing education offerings to address them. This in turn will help to minimize claims and reduce premiums. Together with the potential to build an insurance fund with retained premiums, this will provide the AAA with flexibility to move toward a more independent insurance program in the future.

The Task Force has used member feedback from the previous consultations to move forward with the current recommendation. A large proportion of members supported the proposed requirement to carry PLI. The Task Force would like to present the members with its recommendations at the fall 2013 consultations to determine what model will be used to implement Professional Liability Insurance.

¹ Dion Strategic Consulting Group Inc., "Supplementary Report On Recommended Profession Liability Insurance Program Options: June 18, 2013", June 2013.

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Recommendations

Issue 1 Should the AAA Require Its Members To Carry Professional Liability Insurance?

1.1. Current Legislation

There is no mention of liability insurance in the current version of the *Architects Act* and *General Regulation*, or Bylaws.

1.2 Issue

There is currently no legislative requirement for Registered Architects or Licensed Interior Designers in Alberta to carry professional liability insurance, and the Association has no policy recommending that members carry such insurance.

Is it in the public interest that AAA members be required to carry professional liability insurance? Is it also in the best interests of the members and the profession for such a requirement to exist?

1.3 What We Learned

Protecting the Public

An important objective of the Alberta Association of Architects is the protection of the public. The Association is a self-governing body that can set standards for member professionals. These standards can protect the public by establishing minimum levels of professional practice, and by sanctioning members who fail to meet them. Registered architects or LIDs found guilty of unskilled practice or unprofessional behaviour may face suspension or expulsion from the Association, fines or other penalties. They may be required to refund fees unjustly earned, but the Association has no authority to order members to pay compensation for physical or economic loss.

Registered architects and LIDs have a great deal of responsibility in ensuring that buildings are designed according to applicable codes and standards, and they must review the construction work to verify that it is done in general conformance with the design. Should the architect or LID be negligent in this work, considerable damage or loss could result, not only to the client, but to others who use the buildings. People suffering such losses always have recourse to the courts to recover damages, but collection of any award depends on the ability of the architect or LID to pay. In the absence of liability insurance, collection is uncertain at best.

Protecting AAA Members

The need for professional liability insurance applies to registered architects and LIDs as well as the public, and for similar reasons. A finding of professional negligence could bring ruin without the protection of insurance, because their personal assets would be exposed to a judgment for damages. As prime consultants, architects and LIDs are responsible – and liable – not only for their own work but also for the work of their sub-consultants on a building project. Their liability also extends into the future, as many defects in buildings do not surface until two years or more after a building has been completed. Without insurance, the professional is at the mercy of liability claims made by past clients. The professional would need to have deep personal pockets to ensure his or her ability to pay rightful claimants, or run the risk of being bankrupted by liability claims.

With Professional Liability Insurance (PLI), the professional is assured that potential claims can be resolved without great personal monetary loss. For a reasonable annual premium, the professional is protected against claims.² Even on the high end of the payment scale, the annual cost of a premium is far less than the cost of personally paying out a liability claim.

² Dion Strategic Consulting Group Inc., “Report On Professional Liability Insurance Program Options: April 5th, 2013”, April 2013.

Current Trends in Canada

Among architectural regulators in Canada, the trend is toward requiring professional liability insurance. Six provincial architectural associations now have this requirement. Ontario was the first and Saskatchewan is the most recent, implementing a requirement in April 2012.

Comparing architecture with other professions, in Alberta most self-regulating professions require members to carry professional liability insurance.

Member Consultations

In two separate consultations (October 2012 and February 2013) the Task Force has asked AAA members for their feedback regarding whether PLI should be required. The response received at the October sessions indicated that the members were largely in favor of having a professional liability insurance requirement. The online web-survey from February/March 2013 indicated that 73% of participants in the survey either strongly or somewhat agreed that there should be some requirement for professional liability insurance for AAA members. Only 17% strongly or somewhat disagreed with the statement. The in-person and web survey feedback received indicate to the Task Force that members would be in favour of a PLI requirement.

In December of 2012, the PLI Task Force presented a recommendation to the Legislation Committee that there should be a PLI requirement. The Legislation Committee approved the recommendation, and it was reviewed by Council in January 2013. Council has endorsed the recommendation to require PLI.

1.4 Options

1.4.1 Status Quo Professional Liability Insurance is recommended but not required

Overview

Regarding the basic question of whether PLI should be required under the amended *Architects Act*, the first and easiest option would be to leave the legislation as it is currently, with no requirement for professional liability insurance. Council could recommend that members carry insurance, but compliance would remain voluntary.

Pros

- This option would save on administrative costs for the AAA, as there would be no additional documents to be filed upon membership registration or renewal.

Cons

- The public and clients would be left without access to reliable compensation for injuries they sustain from negligent practice of architecture and interior design.
- Uninsured members would continue to have their personal assets (house, car, and savings) vulnerable to loss through a liability claim.

1.4.2 Require AAA members to carry Professional Liability Insurance

Overview

The *Architects Act* would be revised to include a requirement that all members, either individually or through a practice entity, carry a minimum amount of professional liability insurance, with the details of the program to be determined by the Association through regulations or bylaws (the options for a PLI program are discussed later in this document).

Pros

- The public and clients would have access to reasonable compensation for injuries sustained from the negligent practice of architecture and interior design.

- Members' personal assets would be protected from loss through liability claims, and their livelihoods would be more secure.
- The stature and reputation of the professions of architecture and licenced interior design in Alberta would be enhanced by offering a better assurance of protection of the public interest. Members would gain more credibility and integrity as design professionals
- There would be more of a common standard among regulated professionals.

Cons

- A PLI requirement would bring additional cost and administrative burdens to AAA members, particularly those who are currently uninsured.
- There would be an additional administrative burden on the AAA to regulate the PLI requirement.

1.5 Recommendation

The Task Force believes, as a matter of basic principle, that AAA members who are actively practising architecture or licenced interior design in Alberta should be required to carry professional liability insurance. This requirement should be incorporated into the *Architects Act* to reflect its importance to the public and the profession.

1.6 Rationale

This recommendation is based on the Task Force's understanding of the primary responsibility of the AAA to protect the public interest. Any member of the public, whether a client or not, who suffers injury or loss through the negligent practice of an AAA member should have access to compensation.

The *Architects Act of Alberta* grants to the profession the privilege of self-governance, on the understanding that it will be exercised to protect the public interest. Under this mandate the Association establishes standards of education and practice to protect the safety and welfare of the public. It follows that if an AAA member in the course of practice fails to meet these standards, and a client or other user is harmed as a result, that person should be able to obtain compensation. Given the potential extent of liability and amounts involved, such compensation is best provided by liability insurance.

Additionally, it is a benefit to the members to have a PLI requirement. Without insurance, a successful claim could bring financial ruin to a professional. Even if a client agreed to a limit of liability, third party individuals who are injured by the professional's negligence could still bring claims, and these would not be limited in amount. With PLI coverage, the personal assets of the professional, including houses, vehicles, or personal savings, are protected from liability claims.

Finally, the inclusion of a PLI requirement would raise the stature of the architecture and licenced interior design professions in Alberta by making manifest their commitment to protect the public interest.

1.7 Consultations

As noted above, a substantial majority of AAA members have already indicated support in principle for a requirement for professional liability insurance. The question should be put before the members again for a formal vote.

Issue 2 Who Should Be Required to Carry PLI?

2.1 Issue

If a professional liability insurance requirement is implemented, who should be responsible for carrying the insurance – the individual member, the firm through which the member practices or both?

2.2 What We Learned

The current wording of the *Architects Act* indicates that every registered architect is entitled to practice the full scope of architecture and every licenced interior designer is entitled to practice the full scope of licenced interior design, as defined in the legislation.

However, the Task Force recognizes that there are many different functions in the architectural and interior design fields, and different members play different roles. The traditional model, the one best known to members of the public, is the design professional, creating concepts for buildings or interior spaces, producing drawings and working with contractors to have them executed. Many AAA members fit this model. However, many others do not. In the modern building industry there are many different roles including project managers, planners, facility managers, owners' representatives, teachers, writers and others. These people certainly use their architectural or interior design knowledge, but they do not practice architecture or licenced interior design in the traditional way.

Should all of these people be required to carry liability insurance? Certainly under the definition in the legislation the scope of "practice" is very broad indeed, including not only design and documentation, but also giving advice on building projects. Project managers who ask for particular products or assemblies, and facility planners who sketch floor plan layouts could be construed to be practising licenced interior design. Even a seemingly insignificant backyard conversation between neighbours about a new garage construction could be said to be practising architecture, leading to liability if the advice is wrong.

The Task Force heard from lawyers familiar with the design and construction industry that in the event of a problem on a building project, a lawsuit would likely name every person involved on the professional design team. The architecture or LID firm of record would be named, of course, but so would individual employees within that firm, including the partner in charge, project architect/LID, the job captain and others. However, the lawyers went on to say that in such a case the firm's insurance policy would normally cover the work of all of these employees, so that they would not be in jeopardy for damages (assuming that the coverage was large enough to pay the full amount of an award).

There has been strong support from the members at the February 2013 legislation consultation sessions for the practice entity carrying the insurance (over 70%).

2.3 Options

2.3.1 The individual member should carry the PLI

Overview

Under this option, every member would be required to carry a professional liability insurance policy, and would submit proof of that coverage as a part of the declaration that accompanies the annual membership renewal.

Pros

- This option would recognize that, under the current legislation, every member has the right to practice the full scope of architecture or licenced interior design. It would provide insurance protection for all of the member's professional activities, including the work of those in non-traditional roles and even seemingly trivial examples of casual advice.
- It would be relatively simple for the AAA to administer.

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Cons

- This would be a burden to members who do not currently carry liability insurance.
- Further, it would likely result in redundant, overlapping insurance – employees with personal policies even though they are covered by their employer’ policies.
- It does not recognize the realistic potential of liability incurred by different roles within the profession. Some architects, teachers or writers, for example, have little or no chance of being sued.

2.3.2 Only practice entities should be required to carry the PLI

Overview

Under this model, only the practice entity - the holder of a Certificate of Practice - would be required to carry professional liability insurance.

Pros

- This option would recognize legal reality, and match the requirement for insurance with the practitioners who have the potential to incur liability.
- It would minimize the burden on members.
- It would clarify for the public the different roles within the profession.
- It would be clean and simple for administration.

Cons

- If the definition of the “practice of architecture” and the “practice of licenced interior design” are left very broad, it may raise the possibility that some uninsured members could be sued.
- It introduces a new distinction to the profession: those who offer services to the public and those who do not.

2.4 Recommendation

The Task Force recommends that only the practice entity – i.e. the holder of a Certificate of Practice - should be required to carry PLI, not individual members.

2.5 Rationale

The public interest requires that clients and other interested parties – mainly building users – should have access to compensation if they suffer damage or loss resulting from an AAA member’s error. It follows that:

- Only those activities of registered architects or LIDs that have the potential to cause such harm need to be insured,
- Only those AAA members who engage in such activities need to be covered.

The regulatory provisions of the *Architects Act* are aimed primarily at the traditional practice of architecture and licenced interior design – the design of buildings and interiors, and the specification and coordination work required to have them built. The responsibility of registered architects and LIDs toward public safety is reflected in the requirement to stamp contract documents for these projects, and sign the Professional of Record schedules. This is the work that gives rise to liability, and this is the point where the requirement for insurance must arise. This is the basis of the Task Force’s recommendation: it is registered architects and LIDs who actively offer design services to the public who must be covered by professional liability insurance.

As noted above, many architects and LIDs are involved in the design and building industry in non-traditional roles, such as project managers and facility planners. However, these people typically have discrete supporting roles. For the primary design and documentation of the project, registered architects or LIDs are engaged. These professionals take primary responsibility for the project. As long as they carry liability insurance as prime consultants for their work, the clients and building users will have access to compensation in case of a problem. It is not necessary for the other players to be insured.

The same reasoning applies to employees of architectural or LID firms. A firm's liability insurance normally covers the work of all employees in the course of their employment. Even if individual employees were to be named in a lawsuit, they typically would be covered and would not need their own personal policies.

If government agencies or private companies were to step out of their traditional role as clients and undertake building projects on their own, the situation would be different. In this case these agencies or companies would be practising architecture or licenced interior design, and they would have to follow the AAA rules. They would need to apply for registration and Certificates of Practice, and they would need to prove that they carried liability insurance coverage for their work.

Member consultations indicated that members (over 70%) support the requirement for practice entities to carry the liability insurance. Individual coverage can be optimum.

Issue 3 What Should the Minimum Coverage Amount Be?

3.1 Issue

If a PLI requirement is adopted by the AAA, the association will need to set a minimum amount of coverage that members will be required to carry. The issue is: what should that minimum coverage amount be?

3.2 What We Learned

The minimum amount of PLI required to be carried by professionals differs from profession to profession and from province to province. The lowest minimum requirements are often for Interior Designers, and are often \$250,000.00. The highest minimum requirements are held by doctors, who are required to carry a minimum of \$10,000,000 in insurance.

For architects in Canada, Saskatchewan requires \$250,000 inclusive of any one occurrence, and does not specify an aggregate amount. New Brunswick, Newfoundland, and Nova Scotia require \$250,000.00 for one claim and \$500,000.00 aggregate coverage. Ontario requires \$250,000.00 per claim, \$500,000.00 per project, and \$1,000,000.00 aggregate coverage.

At the high end of the scale, Quebec requires \$1,000,000 per claim coverage for its members. Additionally, it requires for partnerships or joint stock companies a minimum of \$1,125,000.00 per claim and \$2,500,000 aggregate for all fungi/mold claims. For other claims of partnerships or joint stock companies, it requires a minimum of \$100,000 per claim and \$2,500,000.00 aggregate. Quebec has most recently changed its legislation, which says the increase in minimum coverage jump to 1 million.

The average minimum requirement for PLI in Canada for architects is \$250,000 for one claim, and \$500,000 aggregate coverage for a year. These figures apply to both architect and interior designer associations.

3.3 Options

3.3.1 \$250,000 per claim

Overview

This option would require members to carry a minimum coverage of \$250,000 per claim, with \$250,000 to \$1 million aggregate coverage.

Pros

- This is a low minimum amount, which will cost less in premiums to obtain than a larger coverage amount.
- Affordable for small practitioners and new practices.
- Allows larger practice entities to keep any excess insurance that they wish to carry with their existing provider, if they desire.

Cons

- Most professionals will require more insurance, due to the nature of the work that they perform.

3.3.2 \$500,000 per claim

Overview

This option would require members to carry a minimum coverage of \$500,000 per claim, with \$500,000 or \$1 million aggregate coverage.

Pros

- A more realistic amount of coverage that most professionals would require.
- Reduces the need for some individuals to purchase excess insurance from a separate source.

Cons

- May be more coverage than some professionals require, if they are only doing a couple houses each year, for example.
- Still an unrealistically low amount of coverage for larger firms.

3.3.3 Based on the volume of work/number of projects

Overview

This option would require members to carry a minimum coverage of \$1 million per claim, with \$1 million aggregate coverage.

Pros

- Provides more realistic coverage for members.
- Addresses the fact that some members only do a couple houses per year, while others are involved in multi-million dollar structures.

Cons

- More complicated to administer.

3.4 Recommendation

The Task Force recommends that the minimum amount of coverage should be \$250,000 per claim and in the aggregate, with a single deductible option of either \$2,500 or \$5,000 per claim.

3.5 Rationale

This coverage limit would provide an adequate base level of protection for the public while allowing new practitioners to acquire insurance at a reasonable cost.³ This option would provide the most benefits to the AAA and AAA members, with no risk being taken on by the Association. Larger companies that have existing relationships with insurance companies would be required to purchase the first \$250,000 of coverage from the required provider, but would be able to top-up their insurance with their previous insurer if they choose to do so. This offers some flexibility to members, while providing the advantage of group purchasing power.

Many provinces have reciprocal arrangements allowing Registered Architects from other provinces to show proof of insurance from another source to meet their \$250,000 minimum insurance requirement⁴. This would allow architects from Alberta greater mobility; they would be able to work in other provinces without incurring extra costs for insurance.

Issue 4 What are the options for implementation of a professional liability insurance program, and which one would be best for the AAA?

4.1 Issue

Having recommended that professional liability insurance become a requirement for actively practising architects and licenced interior designers, the Task Force wanted to investigate how this requirement could be met. What options are available to provide liability insurance, what are their respective advantages and disadvantages, and which would be best for the AAA and its members? The Task Force wanted some reasonable assurance that a liability insurance program could be established that would be accessible to members, realistically feasible for the Association and, equally importantly, beneficial to the profession as a whole.

4.2 What We Learned

In its investigations, the Task Force was assisted greatly by the expertise and advice of its insurance industry consultant, the Dion Strategic Consulting Group. This consultant provided analysis of the insurance industry for design professionals, the options that would be available to the AAA and the implications for each.

Dion Consulting presented its preliminary findings and analysis to the members at an AAA information session in the fall of 2012. Its reports are available on the AAA website under the legislative review section.

This subjects covered by the Dion Consulting report, and some of the relevant findings, are as follows.

Background and objectives of the report

Terminology

In considering the insurance options available to the AAA, one important distinction to be understood is between:

- **Mandatory coverage:** Members are required to carry liability insurance, but they are free to obtain it from the commercial provider of their choosing; and
- **Compulsory coverage:** Members must purchase coverage, at least to a basic minimum level, from an insurer designated by, and usually sponsored by, the Association.

³ Dion Strategic Consulting Group Inc., "Supplementary Report On Recommended Profession Liability Insurance Program Options: June 18, 2013", June 2013.

⁴ Dion Strategic Consulting Group Inc., "Supplementary Report On Recommended Profession Liability Insurance Program Options: June 18, 2013", June 2013.

Rationale for Professional Liability Insurance

Dion Consulting sets out compelling reasons why design professionals should carry liability insurance:

- Enhancement of the profession as a whole,
- Protection of individual members, and
- Fulfillment of the Association's obligation to protect the public interest.

Review of 2006 Report

A previous report by insurance broker Peter Kelly on the potential for an AAA insurance program as reviewed by Dion Consulting. It addressed some of the same issues as the present report, but was not as comprehensive and did not consider as wide a range of options.

Provincial Comparison

The report sets out a comparison of insurance requirements among the provinces:

- The two largest provinces, with the two largest architectural associations (Ontario and Quebec), both have compulsory liability insurance programs – i.e. plans operated by the associations themselves.
- Four other provinces (Saskatchewan, Nova Scotia, New Brunswick and Newfoundland) have mandatory insurance.
- The remaining four provinces (Alberta, B.C., Manitoba and P.E.I.) have no insurance requirement.

Among interior design associations, six provincial associations (B.C., Ontario, Quebec, Saskatchewan, Nova Scotia and New Brunswick) have mandatory programs and the others have no requirements.

The Insurance Market for Design Professionals

Dion Strategic Consulting interviewed 12 registered architects and 3 licenced interior designers about their insurance arrangements, and they inquired into the existing sources of professional liability insurance. They found that there is a healthy market with many well-established, knowledgeable and reliable commercial providers to the design community.

LIDs have access to insurance provided through the Interior Designers of Canada.

Dion expressed a belief that he AAA would have no trouble in finding a commercial partner with the expertise and resources needed to establish a program in Alberta.

Review of Coverage

The report reviewed the provisions of policies carried by architects and LIDs in Alberta, based on their interviews. Typical terms include:

- Coverage is on a claims-made basis;
- Defence costs are deducted from the policy limits;
- Coverage is for wrongful acts or claims arising out of professional services;
- Some limited additional coverage is available, such as reimbursement of lost earnings due to hearings, legal costs for disciplinary hearings and loss of documents.
- The option for extended reporting periods is available at somewhat discounted rates, and
- There is a range of exclusions from coverage, such as claims arising from mold, dishonest acts, bankruptcy, etc.

Review of Underwriting and Risk Factors

The five main criteria used by insurers to underwrite the risks of design professionals are:

- size of the operation,
- revenue,
- type of projects undertaken,
- where the work is performed, and
- claims experience.

Dion reviewed the typical premiums paid and coverage received for architects and LIDs, based on the interviews and some contact with insurers (although most are reluctant to provide this information). The consultants believed that if the AAA were to set up a group-purchase agreement with a commercial provider, savings in the order of 10% to 20% could be realized in premium rates.

Review of Insurance Options

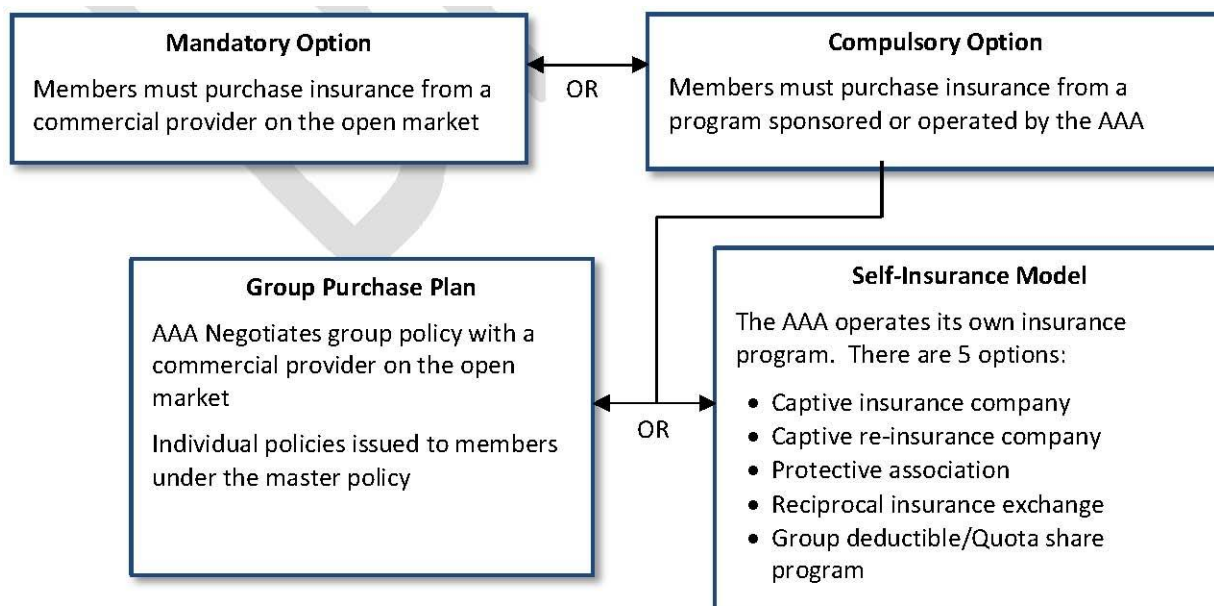
The Dion Report includes a comprehensive overview of the options that are available to the AAA if it decides to implement a PLI requirement. There are two steps to this decision:

1. Should the program be mandatory or compulsory, and
2. What form should the program take?

These questions are difficult for people who are unfamiliar with the intricacies of the insurance industry. As a guide, the consultants set out a list of criteria that can be used to analyze the issue and work toward a decision.

- **Protection of the Public and AAA Members:** Both the mandatory and compulsory options would provide insurance protection for both the public and AAA members, but the compulsory option may be preferable because consistent levels of coverage could be provided, likely at a lower cost.
- **Affordability and Availability:** A compulsory system would provide insurance to all members, almost certainly at a lower cost; whereas under a mandatory plan some members may not be able to get insurance.
- **Selection:** A compulsory plan could be designed to include a voluntary excess option to provide coverage above the required minimum.
- **Stability and Sustainability:** With all practising members included, a compulsory program would provide the AAA with bargaining power to negotiate favourable rates over a longer term, insulating it somewhat from the vicissitudes of the insurance market. Further, it could accumulate knowledge and potentially capital that would allow it to work toward a self-insurance model in the future.
- **Administration:** Either option would impose new administrative burdens on the AAA, a compulsory system more so. This will need to be addressed in the implementation of the option chosen.

With these criteria in mind to help with the selection, the “decision tree” looks like this:



4.3 Options

The Task Force, with information and advice provided by Dion Strategic Consulting, carefully considered all options that were identified as being available to the AAA for a liability insurance program. Based on an analysis of the current circumstances of the profession and the capabilities of the Association, and using the criteria set out above, three options were selected as having the best potential for the AAA:

1. a mandatory model using individual policies issued by the traditional open insurance market;
2. a compulsory group-purchase model, and
3. a compulsory model using self-insurance by the AAA.

These three were analyzed in more detail, as follows.

4.3.1 Traditional Open Market Model

Overview

Under this model, the legislation would state that members must carry PLI of a minimum amount of coverage, but would leave it entirely up to them to negotiate policies individually with commercial insurance providers. Each member would be required to present proof of adequate insurance upon registration, and each year thereafter for annual renewal.

Pros

- This would be the simplest system for the AAA to administer.
- It would avoid reliance on any one insurance provider.
- It would offer members flexibility in choosing a provider.
- Members who currently have insurance would be able to retain their current relationships with their insurers/brokers.

- It would minimize risk to the AAA.

Cons

- Some practices – particularly new start-ups - may be unable to obtain coverage, because of cost or lack of experience, which may prohibit fully qualified members from practising their profession.
- Inconsistency of coverage – different members’ policies could have different limits and exclusions (e.g. some could have mold and fungus coverage and others not).
- Cost – policies would likely be more expensive than under a group purchase plan, considering premiums, brokerage fees and commissions.
- Lack of stability – all policies would remain subject to the volatility of insurance markets.
- Lack of information and control - the AAA would gain no knowledge of claims trends, and would not be in a position to assume more control over its insurance options in the future.

4.3.2 Compulsory Group Purchase Plan Option

Overview

Under this model, members would be required to carry at least the basic minimum level of coverage from a group insurance plan sponsored by the AAA. As in Option 1, the insurance would be provided by a commercial insurer operating in the open market. The Association would issue an RFP to established providers, and enter into a contract with the selected proponent for a group policy to cover all members in active practice (i.e. those holding Certificates of Practice). Terms of the agreement would include the following.

- All practising members in good standing would be eligible to obtain insurance under the plan;
- All practising members would be required obtain the basic minimum of \$250,000 coverage from the group plan.
- For excess coverage, members would have the option of buying from the group plan provider, or from any other commercial provider.
- The AAA would have access to generic information on claims, so that it will be able to build a base of information on the profession’s risk profile and identify emerging issues.
- There would be an option to agree to accumulate a portion of unused premiums each year in a dedicated AAA insurance fund.

Pros

- No members excluded – coverage would be guaranteed to members in good standing.
- Consistency of coverage - common standards of coverage would be built into the policy wording.
- Cost savings (the “law of large numbers”) – the inclusion of all members would reduce marketing and administration costs, and the savings could be used to reduce premiums. It would also give the Association considerable bargaining power in negotiating rates.
- Members would be able to continue their existing insurance relationships for excess insurance.
- Risk to the AAA would be minimized because the insurer would be liable for claims.
- There would be only a moderate additional administrative burden on the AAA.
- Access to non-specific claims data would allow the AAA to address liability issues through continuing education opportunities.
- Future opportunities – knowledge gains and potential insurance fund accumulation would provide the AAA with the opportunity to move toward self-insurance in the future.

Cons

- Reliance on a single provider for a period of time.

- Members with existing coverage may need to deal with an additional insurer (i.e. the AAA for base coverage and their existing insurer for excess insurance).

4.3.3 Compulsory Self-Insurance Model

Overview

Under this model, the AAA would operate its own insurance program, either on its own or through a “captive” insurance company. All members would be required to obtain their liability insurance from this program, at least to the extent of the basic minimum coverage.

There are five different models for self-insurance.

1. A *captive insurance company* is an incorporated insurer owned by the association and operating to some extent at arms’ length. The Pro-Demnity company, owned by the OAA in Ontario, is a very successful example.
2. A *captive re-insurance company* is owned by the association but domiciled offshore. A Canadian company is the insurer of record, but assigns the risk to the re-insurer to pay the claims.
3. A *protective association* is not an insurance company, but is rather a “mutual defence” organization. Members essentially agree to spread the cost of claims among them.
4. A *reciprocal insurance exchange* is similar. Members sign a subscriber agreement to “insure” each other’s risks. The reciprocal can purchase re-insurance to limit its exposure.
5. *Group deductible* and *quota share* arrangements allow groups to take responsibility for a portion of claims against their members – a fixed amount or a percentage of the overall claims. This reduces the risk borne by the insurer, and thus reduces their annual premiums.

Although the details of these options vary, all self-insurance models have one common feature. The Association would take on the liability for claims against all of its members. This risk could be limited by obtaining re-insurance, but the primary responsibility would lie with the AAA. This would represent a significant step for the AAA, with serious implications for Council and the administration.

Pros

- A self-insurance program would largely insulate AAA members from the vicissitudes of the insurance market. Premium rates could be set according to the actual risk profile of the profession, although some exposure would remain because of the need to obtain re-insurance.
- All members in good standing would be able to get insurance, so that the PLI requirement would not be a bar to entering or practicing the profession.
- The AAA would have access to non-specific claims data, which would allow it to identify and address emerging liability issues through continuing education.
- Members would have broader coverage from a single carrier.
- Minimum standards of coverage would be built into the standard policy wording.
- Members would be able to continue their existing insurance relationships for excess insurance (insurance in excess of the minimum coverage required by the AAA).

Cons

- Start-up costs would be very high – an initial capitalization of at least \$5 million would be required. This would have to be financed by a levy on the membership.
- The AAA currently does not have the expertise to start or operate such a program. It has little information on the risk profile of the profession in Alberta, and no experience in the insurance industry.
- It would also be beyond the administrative capacity of the AAA.

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- Any program would be subject to Insurance Regulator's rules and regulations, as well as income tax and regulatory reporting.

4.4 Recommendation

The Task Force recommends that the Alberta Association of Architects implement professional liability insurance through a compulsory group purchase plan (Option 2.3.2).

4.5 Rationale

Why not a traditional mandatory model – individual members obtaining policies from insurers in the market?

The primary reason why the mandatory option is not preferred is that insurers may use different criteria for acceptance than the AAA. Members who are in good standing with the Association may still not be able to obtain insurance, perhaps because of inexperience, claims history or areas of practice. If these people were barred from practice because of an inability to get insurance, the AAA would effectively have out-sourced a part of its basic mandate – the decision on who can practice in Alberta. In the opinion of the Task Force, this is not acceptable.

Beyond this, a mandatory model would pass up on some real opportunities to benefit the profession. The move to a new liability insurance model offers the opportunity to advance member support, continuing education and professional awareness. It also allows the design profession to gain greater independence and control over its own destiny. These opportunities would be lost with the mandatory insurance model.

Why Not Self-Insurance

The success of the Pro-Demnity program in Ontario makes self-insurance a highly attractive option. Their achievements in protecting and supporting members while also reducing premiums are very impressive indeed.

However, we must consider this option in the light of a realistic assessment of the situation in Alberta. The AAA does not have the resources – financial or administrative – to make self-insurance a viable option here at present. Beyond this, the Association does not have the expertise in the insurance industry needed to venture into this field with any confidence.

At the same time, the success of programs such as Pro-Demnity can provide a valuable example of features to be included today and a model we can work toward in the future.

Why Compulsory Group Purchase Plan

A compulsory group purchase plan offers many of the advantages of self-insurance, but keeps the AAA's risk at a minimum.

The inclusion of all practising members in a compulsory plan, together with competitive bidding through a RFP process, should put the AAA in a good position to negotiate a group insurance policy on terms that will meet the Association's short and long-term goals (as listed on page 17 above).

Dion Consulting advises that reductions in marketing and administrative costs under a group plan would almost certainly lead to lower premiums than members are currently paying.

The access to claims data is of fundamental importance. This will give the association an overview of emerging trends in claims. Knowledge of "risky" areas of practice will enable the association to provide continuing education in these areas to build up the competence of members and reduce the likelihood of liability. In the long term, a

reduction in the number of claims and an increase in the knowledge of members provides an opportunity for further reduced premiums and greater coverage being offered by the insured.

Additionally, fewer claims lead to an improved stature of the professions in the community, as members are seen as more skilled, professional, and competent.

Licensed Interior Design Insurance

As noted above, licensed interior designers are in different circumstances regarding insurance. LIDs in Alberta are able to get coverage at very favourable rates through the group plan sponsored by the Interior Designers of Canada, only if they are members of IDA. Those that are members may be, understandably, concerned if this relationship were interrupted by a move to compulsory insurance by the AAA. The Task Force addressed this issue directly with Dion Strategic Consulting.

For the purpose of bargaining from a position of strength, it would be best to include LIDs in a compulsory group insurance plan. The “law of large numbers” works better with larger numbers. However, the unique circumstances of LIDs could and should certainly be taken into account in negotiating the plan.

Dion Strategic Consulting has advised that there is no reason to believe that LIDs would pay higher premiums under an AAA-sponsored group plan. The premiums that LIDs pay under their current plan are based on a realistic assessment of the risks of their professional practice, refined by many years of industry experience. This risk would not change under an AAA plan, so there would be no reason for the premium rates to change. The agreement between the AAA and the insurer could deal with the LIDs as a separate group under the plan, with its own premium rates based on its own risk profile.

Further, as with all other AAA members, LIDs would only need to purchase the first \$250,000 of coverage from the group plan. Any excess insurance could be obtained from the IDA-sponsored plan.

Pooling of Risk

A compulsory group plan would include all practising AAA members, including those who are insured and those who are uninsured. Initial rates would be based on the best available information about practice profiles and claims history, and the rates would be adjusted in later years as more information is accumulated. As with all insurance plans, members with more claims could expect to pay higher premiums. This is where continuing education and practice support come in. With better information, the AAA would be in a much better position to identify potential problems early and address them before they turn into claims.

Conclusion

The compulsory group plan option is recommended by the Task Force because it offers the best way to meet the AAA's goals. In the short-to-medium term it would serve the public interest by providing insurance protection for clients and other building users. It would benefit AAA members by providing the protection at a reasonable cost and on favourable terms. It would also improve the Association's initiatives in continuing education and practice support. Finally, it would enhance the public reputation and stature of the profession as a whole.

In the longer term, this plan would also give the AAA options to take more control of its insurance program. By collecting information and by accumulating capital (from retained premium income), the Association would be in a position to move toward self-insurance if it wishes.

4.6 Consultations

The Task Force has used member feedback from the previous consultations to move forward with the current recommendation. A large proportion of members supported the proposed requirement to carry PLI. The Task Force

would like to present the members with its recommendations at the fall 2013 consultations to determine what model will be used to implement Professional Liability Insurance.