PLI Market 2024: A/E Firms See Steady Growth, Evolving Risks, and Inflation-Driven Costs

Ames & Gough Architects & Engineers Professional Liability Insurance Market Survey

I. Introduction & Overview

With the U.S. construction sector benefiting from moderate economic growth, insurers offering professional liability coverage for design firms witnessed consistent premium expansion for the third consecutive year. Looking ahead to 2024, insurers are confronted with the challenges of navigating the effects of economic and social inflation on claim expenses, alongside heightened risks associated with specific project types, professional design disciplines, and evolving alternative project delivery methods.

As we embark on the new year, Ames & Gough (A&G) remains dedicated to addressing these issues, along with ongoing developments in the professional liability insurance landscape. We are delighted to present the 14th edition of our annual survey, which delves into the following areas:

- Review of the 2023 market performance
- Insurer approaches to risk appetite, premium rates, and limit availability
- Analysis of claims activity
- Projections for the 2024 market outlook
- Trends in employee benefits liability for design firms
- Mitigation of emerging exposures linked to AI innovation

This year's survey includes responses from underwriting executives at 17 leading insurers providing A/E professional liability insurance. On a combined basis, they represent a significant percentage of the current overall marketplace for this line of coverage. Participants in the 2024 survey were: AIG/Lexington, Aspen, Beazley, Berkley Design Professional, Berkshire Hathaway Specialty Insurance, Euclid/Nationwide, Everest, Great American Insurance Company, Hanover Insurance, The Hartford/Navigator, Liberty Mutual, PUA, RLI, Riverton/Hudson Insurance, Sompo International, Travelers, and Victor Insurance.

We are thankful for each insurer's participation and are pleased to share the findings in our report.

II. Survey Findings
Another Year of Growth in Revenue and Risk

In 2023, insurers experienced substantial premium growth for the third consecutive year, with a majority seeing double-digit percentage increases. Among surveyed insurers, 82 percent reported growth in professional liability written premium, while 6 percent saw flat levels and 12 percent witnessed a decrease. Many insurers with premium growth reported significant gains, with over one-fourth achieving growth of 20 percent or more. This growth is attributed to increased billings from policyholders (87 percent), new policies written (93 percent), higher premium rates (73 percent), and clients purchasing higher limits (53 percent). Additionally, 40 percent of the insurers linked premium growth to their insureds' adverse loss experience. This growth reflects the increasing risk assumed by A/E firms, especially with larger and more complex projects.

AMES & GOUGH

Washington, D.C. (Headquarters)
8300 Greensboro Drive
Suite 980
McLean, Virginia
22102-3616
Phone: (703) 827-2277
Fax: (703) 827-2279

Boston
859 Willard Street
Suite 320
Quincy, Massachusetts
02169-7469
Phone: (617) 328-6555
Fax: (617) 328-6888

Charlotte
6825 Huntfield Drive
Charlotte, North Carolina 28270
Phone: (703) 827-2277
Fax: (703) 827-2279

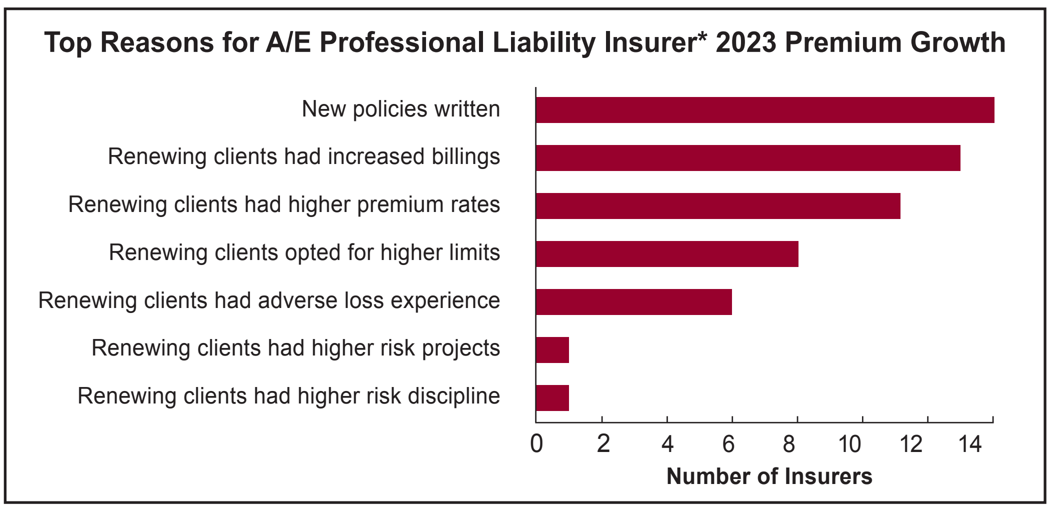
Orlando
111 North Orange Ave.
Suite 800
Orlando, Florida 32801
Phone (202) 680-4507
Fax: (703) 827-2279

Philadelphia
1781 Hunters Circle
West Chester, Pennsylvania
19380-6643
Phone: (610) 547-0663
Fax: (703) 827-2279

Economic and social inflation fuel rise in claim costs. Nearly all the insurers surveyed pointed to economic, social inflation, or both as key issues driving increased claim severity. From an economic standpoint, many insurers surveyed specifically cited higher labor, material and legal defense costs as key cost drivers. Meanwhile, social inflation has emboldened plaintiff attorneys to be reluctant to settle or to seek higher settlements than in the past. In this environment, the insurers are seeing higher jury verdicts – particularly with bodily injury claims. Not surprisingly, these trends have also complicated mediation.

To mitigate the impact of inflation – both economic and social – some insurers are assisting clients to improve risk management, including contract hygiene, as well as to encourage timely claim and circumstance reporting. They are also focusing more attention on underwriting and rate adequacy, encouraging some clients to structure their programs with higher self-insured retentions, and exercising greater scrutiny in their selection of risks. When claims occur, they are pushing for early mediation and settlements when liability is clear. They are also mounting more aggressive defenses, including taking matters to jury verdicts, in cases involving limited liability where they deem claimant demands to be unreasonable.

A&G Insight: In cases where a firm has experienced a significant loss, especially those influenced by social inflation, we at Ames & Gough believe it is beneficial to facilitate direct communication between the underwriter and the client. This allows for a deeper understanding of how the claim impacts the renewal process and enables us to offer insights into any improvements the firm has made to its Quality Assurance/Quality Control practices. We advocate for transparent and constructive dialogue with the underwriter to foster a positive renewal experience.



**Note: Based on 15 insurers reporting 2023 premium growth*

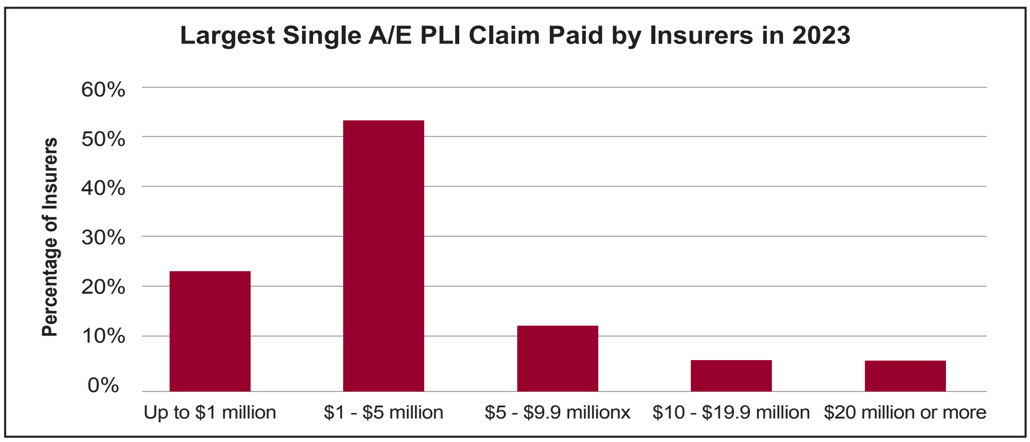
Insurers once again reported significant rate increases in response to ongoing challenges. Of the 17 insurers surveyed this year, 15 implemented rate hikes in 2023 due to persistently deteriorating claims experiences and heightened risks. Among these, a majority (53 percent) opted for modest increases of up to 5 percent, while the remaining 47 percent implemented hikes ranging from 6 to 10 percent.

Despite improvements in loss experience for some insurers, concerns persist regarding claims severity. Only 18 percent of insurers reported worse overall claim experience in 2023 compared to the previous year, with 41 percent stating it remained the same and another 41 percent indicating improvement. Nevertheless, the severity of claims continues to escalate, prompting serious concerns among the majority of surveyed insurers.

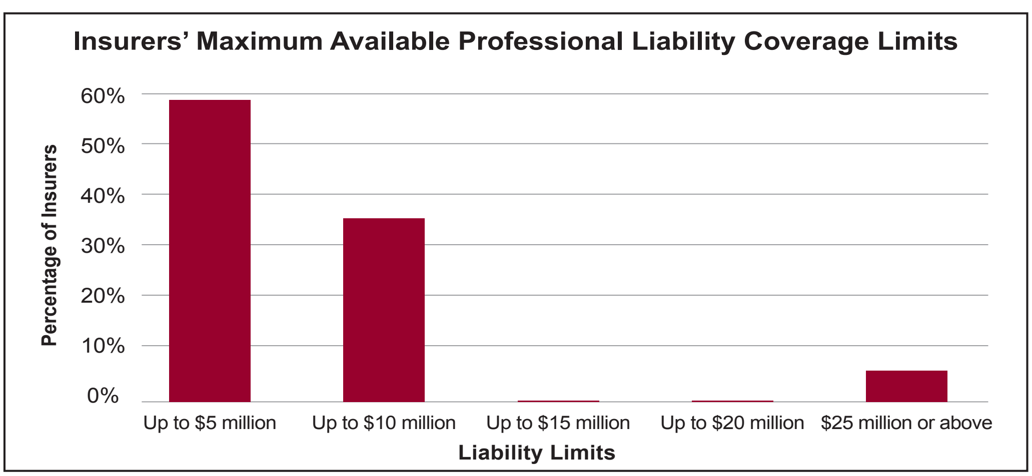
Rising claim expense costs, bodily injury claims, delays and cost overruns driving severity. Among the insurers surveyed, 41 percent saw an increase in claim severity in 2023, an improvement over 2022 when 75 percent saw increased claims severity. That stated, only 6 percent of the insurers surveyed reported lower severity in 2023. In terms of factors underlying claim severity last year, 71 percent of the insurers cited increased expense costs and 18 percent pointed to certain project types – including apartments/multi-family housing and custom residential construction – as contributing to their deteriorating loss experience.

Other insurers surveyed pointed to the impact on severity of bodily injury claims, plaintiff attorneys' demand for higher settlement amounts, project delays, and cost overruns. In addition, higher claim costs continue to be associated with backlogs in court cases leading to delays in litigation and resolution. Still, a few insurers have been able to weather the storm. In this year's survey, two insurers found no measurable difference in severity from the prior year and one insurer experienced a decrease in severity, which it attributes to its strategic decision to avoid large projects.

Insurers see more multimillion-dollar claims. When asked to reveal the amount of their largest single A/E PLI claim payout in 2023, 53 percent of the insurers reported paying a claim of between $1 million to $4.9 million. Twenty-three percent paid a claim of $5 million or more, including 12 percent that made staggering payouts of $10 million and higher. When asked to describe any lessons learned from large losses that might be shared with A/E firms, insurers continued to emphasize contract scrutiny, including clearly defined scope of service, meaningful limits of liability protection, and a careful review of indemnification provisions. They also



cited the need for effective quality assurance and quality control measures, including more rigorous project oversight and more frequent and effective communication with clients. The latter should include discussion and timely documentation of any issues or changes with owners and contractors. Insurers also encourage design firms to check that subconsultants have and maintain adequate limits. To protect themselves, some insurers indicated they have stopped writing certain high-risk projects.



For A/E firms and their brokers, obtaining adequate capacity may require creativity. Among insurers surveyed, more than three-fourths reported consistent availability of professional liability limits year-over-year. However, only 40 percent can now provide limits exceeding $5 million, a significant drop from the previous year when two-thirds of the insurers were willing to offer such limits. While market capacity remains stable overall, some insurers are scaling back limits for single accounts. Consequently, insureds aiming for higher limits may encounter increased underwriting scrutiny and may have to seek coverage from multiple sources.

A&G Insight. Project owners are increasingly seeking higher limits to address the escalating costs of construction, the complexity of projects, and to protect themselves more effectively against increasing cost of claims. As insureds look to meet these requirements, insurers are scrutinizing requests for higher limits carefully. In response, A/E firms might try negotiating with project owners to determine whether the higher limits are warranted. If they still need to increase their limits, they might explore alternative structures, such as Specific Additional Limits Endorsements/project excess or revisit their existing program structures to include building towers with policy layers from multiple participating carriers to achieve the limits an owner requires.

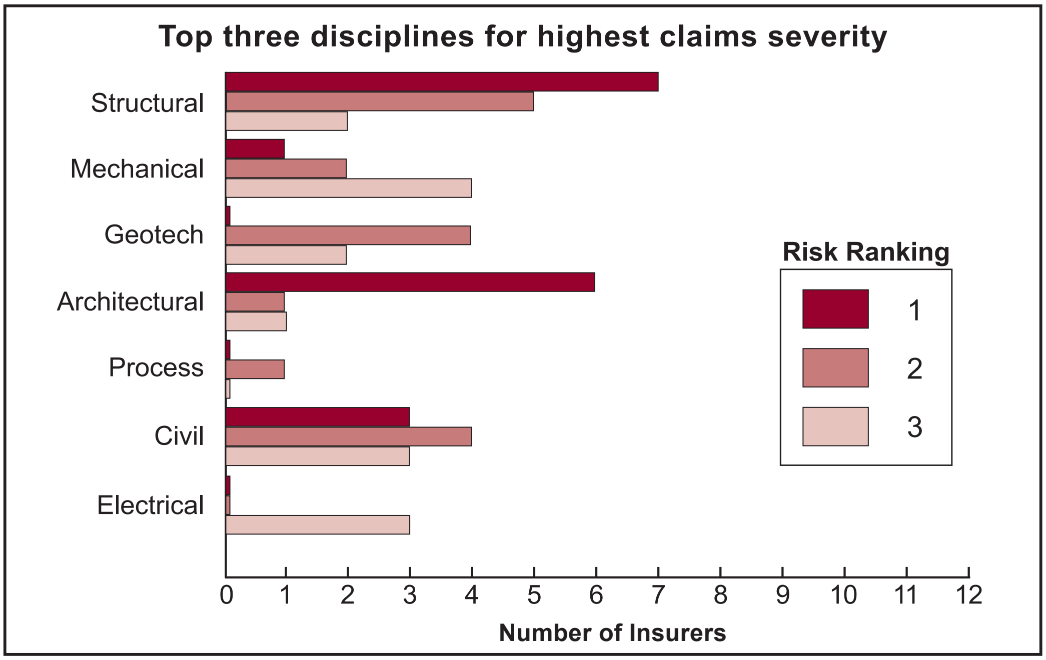
Planned 2024 PLI Rate Actions: Insurers Seek Additional Rate Hikes. Despite the steady premium growth, the drive by insurers to seek increases in their professional liability insurance rates that was revealed in survey findings of the past three years is continuing in 2024. Accordingly, 94 percent of insurers in the 2024 survey are seeking rate increases this year with only one survey participant planning to keep rates flat.

Insurers remain concerned over impact of inflation. Even as economic inflation appears to be cooling, 81 percent of the insurers surveyed cited inflation as having an impact on their decision to implement a rate increase. Some asserted that construction inflation has been higher than headline inflation, given persistently rising costs of materials, supplies and labor. Insurers also cited the continuing impact of social inflation in driving up claims severity and related legal defense costs.

As has historically been the case, this year 75 percent of insurers will continue to target rate increases for accounts with adverse loss experience. At the same time, there remains a sharp focus on accounts with what underwriters consider to be high-risk projects or disciplines. Accordingly, 56 percent of survey participants plan increases related to high-risk projects; the same percentage will target high-risk disciplines.

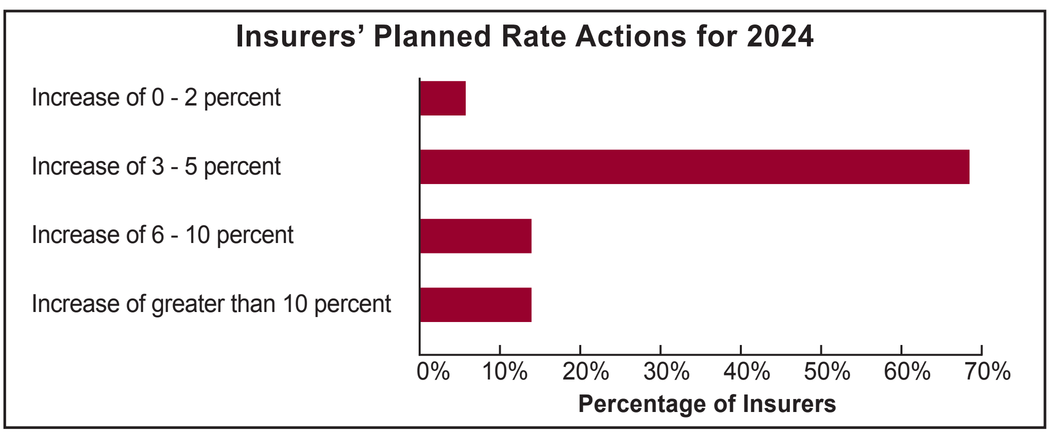
When asked to list the top three disciplines in terms of high claim severity, an overwhelming majority (82 percent) of the insurers cited structural engineering, followed by civil engineering (59 percent) and architecture (47 percent). Meanwhile, 82 percent of the insurers surveyed considered architecture as having the greatest claim frequency, followed by civil engineering (76 percent) and structural engineering (65 percent).

With respect to projects, insurers continue to single out condominiums for having elevated risks, along with other residential construction, including multifamily apartment dwellings. Many also classify street, road and highway/infrastructure as associated with higher risks.



States pose issues over high-risk project concentrations, legal developments. Some insurers have become increasingly wary of projects in Florida, Texas, New Jersey and New York. Notably, the insurers cited Florida and Texas as states with concentrations of higher risk projects, such as schools, condominiums and multifamily construction, while New Jersey and New York raised insurer concerns regarding legal environments that may lead to larger awards, higher defense costs and greater claim severity.

Thus, from the insurers' perspectives, project types, discipline, and individual state construction and legal trends are all factors for potential rate actions in 2024. In addition, 25 percent of the insurers surveyed plan to raise rates across their entire book of business, reflecting their concerns about rate adequacy given the impact of both economic and social inflation on loss experience.



In this environment, it's crucial for A/E firms to adhere to risk management protocols to bolster a favorable risk profile. Key practices include:

- Thoughtful selection of clients and projects
- Implementation of quality control measures
- Effective allocation of contractual risks
- Thorough documentation of project-related interactions with owners and contractors
- Prompt reporting of incidents and claims

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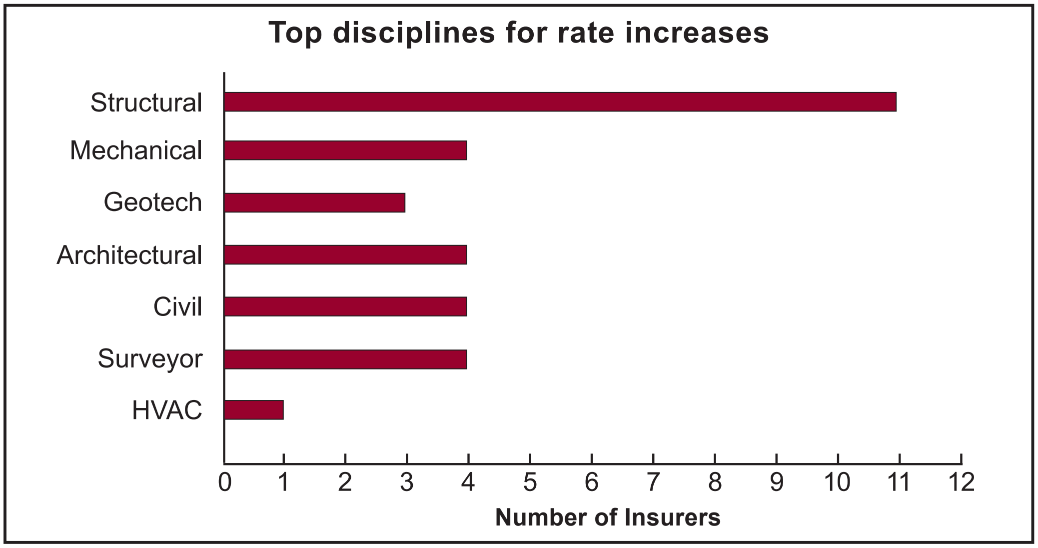
Underwriters again target high-risk disciplines for rate increases. The majority of insurers surveyed placed structural engineering in the top three disciplines they plan to target for rate increases in 2024, followed by mechanical engineering, civil engineering and architecture, each of which was cited by 24 percent of the insurers.



A&G Spotlight: Managing Employee Benefit Costs

Employers throughout the U.S. continue to face rising employee health care costs. A/E firms might consider four key drivers of 2024 health care costs and strategies to manage them:

- **Mental health challenges.** While employee mental health concerns and needs, such as depression, anxiety and substance use disorder, rose during the COVID-19 pandemic, they continue to linger. In response, employers are expected to continue to expand access to mental health support and services, and many plan to provide more options for support and to reduce cost barriers to care. They may also explore manager and employee training to recognize mental health issues, anti-stigma campaigns and flexible working arrangements so employees can discreetly seek mental health care during work hours.
- **Pharmacy costs.** Rising prices of new pharmaceuticals along with the high prices of drugs already on the market – including high-demand diabetes and obesity drugs and gene therapies – continue to drive up employer pharmacy costs. To address these costs, employers can implement pharmacy management strategies, such as requesting detailed reports, auditing PBM services, requiring compensation and pricing disclosures, negotiating contract terms, and making plan design changes to address costly medications and treatments. Specific changes may include requiring prior authorization, step therapy and sites of care management.
- **Cancer treatment.** In many cases, preventive screenings were disrupted during the pandemic. As a result, employers are anticipating more late-stage cancers among workers. In response to rising cancer care, employers can encourage advanced screening measures, maintain full coverage of recommended prevention and screening services, and monitor oncology clinical advancements, such as biomarker testing and immunotherapies. They can also help guide employees to high-quality care to improve health outcomes.
- **Health care delivery.** Health care innovations, specifically on-site or near-site clinics and virtual care, gained popularity during the pandemic. Even with demand leveling off as employers migrate to hybrid or remote work environments, convenient access continues to be critical for employees who are prioritizing primary or preventive health care. Moving forward, more employers are looking to expand health care offerings to better support primary care and mental health and prioritize employee health outcomes.

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Insurers anticipate rebound in industry M&A activity. Although M&A activity among A/E firms slowed in 2023 primarily due to higher interest rates, insurers surveyed believe a resurgence of transactions is likely should interest rates begin to stabilize. Meanwhile, they continue to adopt a variety of approaches with respect to firms involved in combinations.

While some offer automatic temporary (90-day) coverage for newly acquired firms, most apply more rigorous underwriting to assess how the combination affects the acquirer's risk profile. In anticipation of acquisition activity picking up, some insurers are considering adding questionnaires to their underwriting process to assess an applicant's plans to grow by acquisition. In terms of A/E firms managing their potential M&A risks, a critical concern for both insurers and A/E firms now centers around evaluating and addressing potential cyber threats.

A&G Perspective: Addressing looming risks of AI innovation.
AI innovation presents both opportunities and risks for design firms. Regulatory gray areas and potential legal compliance issues arise due to the largely unregulated nature of AI in the workplace. Design firms must reevaluate existing policies to accommodate AI deployment, considering varying federal and state laws across jurisdictions. Additionally, they need to address employee concerns about job security amidst AI adoption. Key concerns include:

1. **Data privacy and surveillance.** AI-driven employee monitoring requires careful consideration of privacy rights and compliance with consent and notice requirements in different jurisdictions.
2. **Copyright and intellectual property.** AI-generated content may infringe copyright laws or third-party intellectual property rights, necessitating updates to confidentiality policies and employee training.
3. **Anti-discrimination.** AI tools can perpetuate bias in decision-making, leading to discrimination issues. Firms should conduct bias audits and review AI-based compensation systems for compliance with anti-discrimination laws.
4. **Ethical use.** Employers must establish ethical AI policies to guide responsible AI utilization, with regular reevaluation as technology evolves.

Be proactive. Given AI's evolving impact on employment, design firms must proactively establish AI-related policies to mitigate risks and prevent violations. This includes identifying emerging exposures and developing strategies to address them effectively.

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Other Key Findings:

- **Most insurers offer coverage for alternative project delivery, but A/E firms should double-check policy language.** Among insurers surveyed, a small number have specific exclusions for alternative project delivery, but nearly all asserted their professional liability coverages will respond to circumstances involving professional negligence (subject to the policy terms and conditions). That stated, some insurers expressed concern over potentially elevated exposures related to alternative project delivery and apply underwriting scrutiny to project-specific policies. They caution A/E firms to exercise care in reviewing contracts and encourage them to be aware of heightened risks associated with rising material costs, compressed schedules, and labor shortages, which can lead to greater claim frequency. Insurers also noted a higher potential for claims if design firms issue a GMP.

- **Few insurers plan enhancements to their A/E professional liability policies as most stay with status quo.** While 65 percent of the insurers surveyed aren't planning to make changes to their existing A/E PLI policies during 2024, a few will be making some adjustments. Most significantly, one insurer is planning to launch a new A/E professional liability policy form and rates. Another is introducing a per unit deductible in some states for housing projects with more than 250 units. A third is planning to expand its risk management services and a fourth will add optional bodily injury and physical damage exclusions for design firms unable to find standard professional liability cover. Beyond their A/E insurance programs, one insurer is planning to enhance its contractors professional liability policy this year while another is rolling out miscellaneous professional liability (MPL) coverages centered around property managers, project managers and certain real estate-related risks.

III. Closing Commentary

In 2024, most insurers remain particularly concerned about the impacts of economic and social inflation – the former driving up material and defense costs and the latter causing spiraling jury verdicts and spiking settlement demands. Some also fear the looming prospect of recession and its potential impact on the housing market, which could lead to lower A/E firm billings and premium flow in conjunction with an uptick in claims typically linked to economic slowdowns.

This year, insurers raised a new wrinkle on climate change with one survey participant concerned about whether A/E firms can adapt to designing to address more extreme and complex weather conditions not yet contemplated by existing construction codes. At the same time, with the prospect of a more stable interest rate environment, insurers anticipate a resurgence of M&A transactions involving A/E firms and plan to maintain careful underwriting discipline in assessing any related risks.

As A/E firms continue to pursue growth or maintain market share in 2024, they need to remain diligent about maintaining sound risk management practices, including mindful client and project selection, quality control measures, proper contractual risk allocation and careful documentation to support a positive risk profile. Given the increased potential for large losses, they should also have measures in place to report circumstances that could evolve into claims in a timely manner.

We hope this survey report provides insight into your insurance coverage and strategy for this year and beyond.

ABOUT AMES & GOUGH

With more than 1,700 architects, engineering firms, and other construction professionals of all sizes as clients, Ames & Gough is the leading specialty insurance brokerage and risk consulting firm serving the needs of these professionals. Ames & Gough also has established itself as a committed, superior resource for law firms and associations and nonprofit organizations in need of professional liability, management liability, property/casualty insurance, risk management, and employee benefits assistance. Established in 1992, the firm has offices in Boston, MA; Charlotte, NC; Philadelphia, PA; Orlando, FL; and Washington, DC.

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