MANAGEMENT
FOR
DESIGN

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MANAGING RISK FOR ARCHITECTS, ENGINEERS, AND DESIGNERS

While Risk Management might not be the most engaging subject for leaders of Architecture, Engineering, and Design businesses, it's an essential concern that you can't avoid—and something you need to manage effectively. But, what does Risk Management actually mean?

- Surrounding yourself with the right expertise
- Adopting strategies and systems to minimise your risk and exposure.
- Effective quality control to keep yourself free of unwanted claims

Although this can be an extensive subject, we've simplified this by identifying the key issues most businesses encounter and categorised these into four main areas.

1. Business Structure and Legals
2. Clients, Fees and Fee Negotiation
3. Insurances

Business structures and agreements

Business Structure

Establishing a company, unit trust, or partnership is a decision you will need to make early on—and you probably won't fully understand the implications of your decision until you are directly faced with them. Each structure has its pro's, con's, and implications for the owners and directors. What works for you may not work for others.

A Unit Trust is different to a company in that the trust is not directly taxable on income it earns; however, all taxable income is distributed to the unit holders pre-tax, who then pay tax at their own rate. The workings of the unit trust are governed by the trust deed which is like the constitution of a company.

Some of the disadvantages of a trust structure compared to a company include:

- It can be more expensive to establish and administer
- It can be difficult to dissolve, dismantle, or make changes once established
- It can't distribute losses, only profits

And some of the advantages include:

- Reduced liability, especially for corporate trustees
- Assets are protected
- Flexibility of asset and income distribution

Shareholder | Trust Agreement

Why do you need this?

A formal agreement prevents disputes. Having an agreement prevents disputes and allows for the smooth functioning of companies, trusts and partnerships. Disputes often arise when owners wish to sell or exit. It doesn't matter how well you know the person you're doing business with – conflict is extremely common when you're doing business with someone.

Having a shareholder agreement provides you with the opportunity to tailor a contract to your needs. Without one you will just have to work within broad legal principles which may or may not work to your advantage.

An agreement is a private agreement. Unlike the constitution of a company, a shareholder agreement does not have to be made public. Also, only people or companies who are parties to the shareholder agreement can change it.

An agreement can result in the smoother functioning of the company. Because the shareholder agreement can divide management functions and spell out rights/obligations it can have a useful secondary use as a kind of collaborative management tool.

An agreement can save costs. The initial fees in setting-up an agreement is nothing compared to the costs of disputes or from bad deals which you might fall victim of in the future.

When third parties know you have a shareholder agreement is a strong indicator that this is a stable business—this applies particularly when applying for credit and dealing with financiers.

What should your agreement encompass:

- Ownership obligations and transfer of ownership
- Insurances
- Restraint (and upon exit)
- Decision making
- Other business interests
- Exiting the business
- % of profits linked to performance
- Employee share plans
- Buy / Sell Agreement

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Comprehensive employment agreements with your people

Employment agreements are an essential document for both employees and employers, legally establishing the working relationship and setting out important frameworks and policies. These contracts provide both the employee and employer with a clear agreement of what is to be expected from each party while outlining all rights, responsibilities, and obligations. This works to protect the rights of the employee, and also protect the employer from certain risks such as breaches of confidentiality.

Here are five reasons why employment contracts are a must-have in any business:

Understanding of Employee Role and Responsibilities. One of the first things an employment agreement will do is clearly spell out the position and responsibilities of the employee, salary, and benefits. There's nothing worse than stepping into a new role and not being quite clear on the tasks and duties involved. This should be established by the employer before the on-boarding process. Both parties should be clear around what is expected in terms of employee performance and this should include measurable criteria.

Understanding of Termination. The employment contract should specify exactly what actions can result in termination and the terms associated with this. Including this information ensures that each employee knows which activities are mandatory to their role and which actions or behaviours are outside policy and may result in dismissal.

Defined Pay Rates and Income. Regardless of whether an employee is full time, part time or casual, an employment contract defines pay rates and income and handling overtime. Having this information contained in one document shows an agreement between both parties on salary, leaving no room for miscommunication. Within the employment contract, you can establish the income your employees will be receiving and how often they work. You can also set what their annual income will be and any relevant bonuses, or basis for bonuses.

Clear Protocols for Annual, Personal, and Long Service Leave. Throughout their employment, team members will need to take all different forms of leave, such as annual leave, personal leave, maternity/paternity leave or compassionate leave. Having this information set out in a contract means that the procedure for taking leave is always consistent and legal, for all people.

Confidentiality for Employers. Many positions give employees access to confidential company information and data. A confidentiality clause in each person's employment contract acts to protect the business. With this clause in place, employees are prevented from divulging sensitive or confidential information to others. This can include being released to the media or public, shared on social media, or being used for any other purposes.

Employment contracts also often include a 'non compete clause' – a clause that prevents the employee from working for any competitors for a certain period (perhaps two or three years) after the employment ends.

Clients, Fee Agreements and Fee Negotiation

Risk often arises out of miscommunication and unrealistic expectations—both verbal and written. This is mitigated by having a comprehensive contract in place that describes the scope and terms of services.

It goes without saying that you must have a signed agreement/contract with the client. This should incorporate:

- The scope of the project
- The time-frames for deliverables and the project
- Preparation and delivery of documents
- Engagement and coordination of consultants
- Budgets

Not only that, but typically architects, engineers, and designers are great at articulating what will be provided, but not so good at communicating what is additional to the agreed services. You need to include an itemised list of exclusions and where additional fees are applicable, e.g:

- Delays in gaining approval
- Changes in documents due to changes in scope
- Additional drawings – as builts etc.
- Negotiation related to novation
- What happens when things aren't working out
- Additional inspections

Your contract needs to incorporate your typical terms and conditions that will include:

- Payment terms
- Dispute resolution
- Intellectual property and moral rights
- Disbursements
- Clause for increasing rates and hourly rates

The fee you negotiate and agree to forms the foundation for your project, the on-going relationship with the client and project success. Considerations include:

- Do you have the required project expertise?
- What is your current workload?
- What capacity do you have?
- Who is the client? Have you worked with them before?
- Can you reasonably achieve the time-frames?
- Can you achieve an expected project profit?
- Can you negotiate and determine an appropriate fixed | lumped fee?
- Can you capture more of the fee earlier in the project?

Insurances

There are 3 key insurances your business must have:

- Professional Indemnity
- Public Liability
- Business Insurance

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Professional Indemnity

Professional Indemnity insurance protects professionals against claims of negligence or breach of duty made by a client as a result of receiving professional advice or services from your business. If someone alleges that you've made a mistake, overlooked a critical piece of information, misstated a fact, or they have misinterpreted you in the course of your work, and this results in a financial loss for your client, then they may take legal action against you to recover these losses. You need an **effective relationship** with your PI Insurer

Whether or not the allegation is true, Professional Indemnity Insurance seeks to protect your assets, your reputation—and our bank balance. This means you can continue in your business without the stress of financial or reputational ruin should a claim arise. Regardless of the merit of a claim, your Professional Indemnity Insurance will pay for your legal defence as well as any judgments or settlements that you or your business may have to pay to compensate the suing party, up to stated policy limits.

A professional liability policy will cushion the possibility of financial struggles as a result of a claim. Additionally, many insurance companies offer risk management services to all of their insureds and they are usually complimentary. One such service is **contract review**. The insurance carrier will typically use in-house risk management consultants have a third-party risk management firm to handle these services.

In either case, the risk management consultant will review and suggest changes to the contract or how to improve on the wording to further detail what the architect or engineering firm will or will not be responsible for. The risk management consultant will also be reviewing contract language to be sure the firm is not agreeing to something not typically covered by insurance and are not agreeing to a higher standard of care than typically expected.

You are obligated as a business leader to be clear about **indemnity clauses** and their implications

Public Liability

Business owners and Directors have a responsibility to the safety of their clients, employees, suppliers and the community; as well as third party property. Public Liability insurance protects you and your business against the financial risk of being found liable to a third party for death or injury, loss or damage to property. Business owners and Directors have a responsibility to the safety of their clients, employees, suppliers and the community; as well as third party property. If you are found to be negligent the financial repercussions can be devastating.

With the right **Public Liability cover,** the insurance company will provide the funds to cover your legal costs and any compensation claims, leaving your business free of financial risk.

If the risk to your businesses is such that you would go out of businesses should you experience a public liability claim, then you need the insurance. It's as simple as that. And if you are doing business with another business, make sure they have public liability insurance too, should an accident or injury occur from their negligence.

Business Insurance

Business Insurance can provide cover for your business' premises and contents, against loss, damage or theft, also offering protection against financial loss experienced from an insured interruption to your business. It is usually broken down by the following types of protection:

- Material damage loss for your physical assets
- Financial loss due to business Interruption

There are many different types of Business Insurance cover options, each designed to protect different areas of a business' operation. The **options**, depending on your business circumstances include:

- Building Insurance which covers any physical buildings which you may own against fire and perils.
- General Property Insurance which covers against theft and accidental damage of equipment, such as tools, laptops, and mobile phones whilst you are away from your office
- Office Contents Insurance which covers against burglary, theft and accidental damage of office equipment, such as chairs, desks and computers.
- Tax Audit Insurance which covers fees of any accountants engaged in connection with an audit by the Australian Taxation Office.
- Business Interruption which covers you for loss of income due to material damage within your business.
- Protection of copyright, moral rights which covers you for the cost of retribution and legal costs associated with infringement of copyright and moral rights

Additional Considerations

Upon the establishment of your practice, one of the biggest, if not the biggest risks a business can face is **financial under-performance**, *and that means*:

- Not making a profit/business in loss mode
- Underpaying yourself, your leaders and your people
- Not investing in your systems and people
- Poor collections and bad debts
- Liabilities outstripping assets

It goes without saying that issues relating to financial under-performance will overwhelm any practice. What's required? Great systems, strong financial control, constant monitoring.

Finally, you don't need to do it all on your own. **Surround yourself with experts** in their professions.

You need great legal, insurance, financial and management support. These people and businesses are out there. Look for:

- A demonstrated track record of success
- Extensive expertise in the industry
- Great client testimonials
- Pro-active attitude to addressing problems

Conclusion

The Opal Tower and Grenfell tower "disasters" have once again highlighted the requirements for understanding the risks associated with working in the industry. Ask yourself, does our business have the appropriate expertise, the strategies, systems, and effective quality control to minimise and manage our exposure. While some risk is out of the control of the business, most of the risks that a firm might encounter can be managed, reduced or eliminated. ■

"Upon the establishment of your practice, one of the biggest, if not the biggest risks a business can face is financial underperformance"

Management For Design provides can provide you with a framework to turn your ideas into actions. Refocussing your way of working means you'll spend less time micro-managing, while the key decisions will always remain firmly in your hands.
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