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## **Builders risk insurance protects from the time the shovel hits the ground to certificate of occupancy - by Spencer Macalaster**

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In recent months we have seen an uptick in construction related activity throughout the real estate marketplace. Residential, retail and commercial developments are all either under construction or being considered by owners and developers. The insurance marketplace is responding well to this increase in demand and ample carriers are vying to underwrite the required coverage.

Builders risk insurance is purchased by owners of construction projects to insure their construction costs and related expenses during the period of construction. The policy protects the developers and builders from the time the shovel hits the ground to the time when the certificate of occupancy is issued or construction ceases. Owners use builders risk insurance to “carve out” construction risks from their property policy to protect and preserve this policy’s integrity from an adverse loss during the construction phase. It is during construction that the likelihood of loss from the perils fire, collapse and water damage are high when full loss prevention and control features, like sprinkler and alarm systems, may not have been installed. While a typical property policy may cover incidental builder risk, it is not meant to be a “working” policy for a portfolio of renovations and new construction projects.

There are two approaches to insure builder risk projects; a project specific policy or a master builders risk policy. Both cover multiple parties, such as the project owner, general contractor, and sub contractors of all tiers for their respective interests. Both offer broad coverage, streamlined administration, and competitive pricing. The master builders risk policy, which insures multiple renovations and new construction projects under one form, is the more efficient of the two approaches. One policy covers multiple projects for any duration when they are bound during the term of the master policy.

Either approach gives you the opportunity to insure a project for the entire length of the construction term; whether two years, three years, or five years. They are very flexible and are often extended

when project completion dates are delayed. Contrast this to a property policy which is typically issued for a one year term. And, if you change property insurers at renewal, the new underwriter may be reluctant to pick up coverage for a partially completed project at expiring terms, conditions and price.

Builders risk insurance is written primarily on inland marine coverage forms. Inland marine forms are not filed nor regulated by states insurance commissioners. This means that inland marine insurers are able to provide broader coverage at more competitive terms and price. With an inland marine form, wording can be scripted to fit a specific project or client need.

Builders risk policies cover hard costs (construction costs, contractors profit and overhead, general conditions and general requirements and construction contingencies) and soft costs (A&E fees, interest expense, legal and accounting expenses, insurance premiums, and bonds) associated with a project. We typically manuscript policy forms to include transit, off site storage, boiler and machinery including testing, permission to occupy, terrorism, upgrade to green, and site preparation among other extensions.

In addition, builders risk policies insure exposures that are found at construction projects such as foundations, underground property, piping, flues, drains, wiring, and certain types of landscaping including trees, plants and shrubs. These exposures are generally excluded in common property forms.

Builders risk policies included boiler and machinery coverage including testing. Property policies generally limit boiler and machinery coverage to equipment that is connected and ready for use. This means that there is no coverage for testing activity which is an integral part of any construction project.

Builders risk policies can also insure delay in start up or loss of revenue coverage for those projects that are expected to produce income and revenue once they are completed.

We build in a profit sharing or no claims bonus provisions in our builders risk forms to incentivize and reward owners who establish effective loss prevention and control procedures that eliminate or reduce losses. The amounts can be substantial depending upon the builders risk premium. It is not uncommon for premium credits of \$50,000 or more when a project is loss free. It is rare to find profit sharing in a property insurance policy.

During the early stages of project planning and design, we analyze project budgets and talk with project owners and managers to determine the appropriate level of hard and soft costs limits. We review the project timeline to establish the proper policy term. We hold quarterly stewardship meetings to review actual costs against budget and progress in meeting the construction timeline.

It is extremely important to review the insurance provisions of the construction contracts between the building owner and the general contractor to confirm that the coverage is arranged to fit contractual obligations, including waivers of subrogation. Construction contracts often require

deductibles that are considerably less than deductibles in an owner's property insurance policy. We tailor deductibles around the size of the project, contractual obligations and client's needs.

The marketplace for builder risk has become somewhat restrictive due to adverse loss experience as relates to water damage. Water leakage occurring on upper floors of a project can penetrate the lower floors a cause significant damage, resulting in project delays and increase exposure to mold and fungus. Underwriters are imposing higher deductibles for water damage due to these increased exposures.

As Risk Strategies we work with the insurance companies and third parties to provide plan review during the design phase and routine inspection service during the life of the project. Our construction practice and real estate practice work hand in hand to assure every aspect of the construction exposure is covered. Making sure the intricate details of the builders risk policy are intact and the contracts are well written will protect the owners and developers from unnecessary exposure to loss.

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