

Builder's Risk

Introduction and Coverages

March 9, 2018



Why Builder's Risk?



- Purpose: First Party Coverage to protect Insureds against damage & resulting loss to work in Course of Construction, before delivered & accepted to the owner











Box Girder-Segmental Bridge



Floating Pontoon Bridge



Builder's Risk Insurance

What does it Cover?

- Property in the Course of Construction, Installation and/or Renovation
- Property for Project at Off-Site Storage Locations
- Property for Project in Transit
- Permanent and Temporary Property Involved in the Project
- Existing Property in some Cases (if Values Reported)
- Soft Costs
- Loss of Rents
- Advanced Loss of Profits

Builder's Risk- General Information

- Specifically for Property in the Course of Construction, Installation and/or Renovation
- Policy period and coverage terms for the life of the Project including Extensions.
- The coverage can be placed to cover All Parties by either the Owner or Contractor
- Coverage for Projects is placed on the basis of estimated completed values comprising **Hard Costs** and **Soft Costs**.
- Coverage can be included in the All Risk Property Policy, placed as a Separate Project Policy or a Master Builder's Risk Program
- Each Project is different – need to understand the Project and Contract requirements.

Builder's Risk- Policy Coverage Options

- **Coverage Under Annual All Risk Property Policy**
 - The intent is for small incidental construction projects
 - Availability sometimes unpredictable in changing markets
 - Usually provided as a throw-in by Insurers
 - Normally, limited Policy conditions for construction
- **Stand-Alone Builder's All Risk Policy**
 - Policy Period for the life of project
 - Known Terms and Conditions specific to Construction Risks
 - Preferred by Lenders
 - 60-90 days NOC but can be non-cancellable except for non-Payment of premium

Master Builder's Risk Program

- Used for multiple projects performed by Owner or Contractor
- Consistent Policy conditions (Rating Structure) for all projects
- Premium rating benefits by funneling more dollars to Insurer

Builder's Risk

Stand-Alone B/R vs All Risk Property Program

- **Coverage Under the Annual All Risk Property Policy**
 - Coverage subject to Annual Review
 - Availability of coverage is unpredictable year to year, potential for change in coverage mid project
 - May have limited specific policy conditions- (Annual Agg. Limits)
 - B/R losses could affect All Risk Program
 - Changing Insurers could affect coverage- annual versus term
- **Builder's Risk Stand-Alone Policy**
 - Wording specifically designed for Property Under Construction
 - Policy period for life of project – important for larger projects
 - Broader extensions of coverage
 - Known terms and conditions, deductibles and limits for projects
 - Preferred by lenders and designed for contractual obligations.
 - Premium rated for estimated Construction period.

Builder's Risk

Stand-Alone B/R vs MBR Program

- **Coverage Under Stand Alone B/R Policy**

- Wording specifically designed for the project including coverage extensions
- Pricing may be more competitive depending on market conditions
- Known terms, conditions, deductibles and limit for term of project

- **Coverage Under MBR Program**

- Economy of scale so pricing may be more competitive
- Locked in rates for all projects- consistency
- Pre- agreed rates can be used for future projects/budgeting
- Automatic coverage for projects (up to 90 days) after inception
- Annual MBR but projects attaching are for term of project

Builder's Risk – Hard Cost and Soft Costs

What are Hard Costs?

The cost of all the materials and labor, including the Contractor's reasonable profit, that go into the construction of the Project. These include the foundations, walls, floors, doors, windows, equipment, temporary structures. Essentially, what it would cost to physically repair or replace damaged or destroyed covered property

What are Soft Costs?

This is the general term for Time Element coverage resulting from physical damage to the Project that causes a delay and can include additional costs incurred during the Delay Period that would not have been incurred if there were no loss. Includes the following categories

- Can be incurred by Owner or GC; usually sublimited by line item for the following costs:

Builder's Risk – Types of Soft Costs

Soft Costs Can include the Following:

- Interest on money borrowed to finance the Project
- Realty Taxes and ground rent, if any
- Additional advertising and promotional expenses necessarily incurred
- Cost of additional commissions incurred upon renegotiating leases
- Additional architects, engineers and consultant fees
- Continuing project administration expense
- Continuing legal and accounting fees
- Insurance costs
- Other, as accepted by Insurer(s) and scheduled in extension of coverage

Builder's Risk – Delay in Start Up Coverage

- Delay in Start up is designed to protect the anticipated future profits/revenues, debt servicing and future operating costs of Project.
 - Loss of Rental Income
 - Loss of Gross Earnings(Advanced Loss of Profits-ALOP)
- Trigger is similar to a Business Interruption claim – must result from insured physical damage to insured property.
- Loss is paid from the date of anticipated completion, not the date of loss.
- Three key considerations in determining the appropriate coverage
 - If there is physical loss or damage, how long will this delay the start up of the Project?
 - What are the financial consequences of the delay?
 - What sum is produced by applying the indemnifiable interest to the Indemnity period?
- There is normally a Day Deductible

Builder's Risk – Testing Coverage

What is Cold Testing?

Any functional testing, exclusive of Hot Testing including but not limited to electrical, mechanical, hydraulic, hydrostatic and pneumatic, but excludes simple cycle operation for commercial purposes. Startup and testing of Building Systems is considered Cold Testing.

What is Hot Testing?

Any startup, commissioning or other forms of testing making use of any feedstock or similar media including operation and performance tests.

The testing of insured property under load or operational conditions, including the use of feedstock or other materials for processing or to simulate working conditions, and in case of electrical motors, electrical generating, transforming, converting or rectifying plant or machinery, connection to a grid or other load circuit.

Builder's Risk – Who Should Purchase the Insurance?

- Which Party contractually bears the “Risk of Loss”?
- Will the Project require Delay In Start Up Coverage?
- Are there any phased handovers contemplated prior to the final completion.
- Could this risk be covered under the Owner's All Risk Property Program?
- Could this risk be covered under a Master Builder's Risk program in place with either the Owner or Contractor?
- Who is responsible for the Deductibles?

Builder's Risk – Owner vs Contractor Placed

Owner Placed Builder's Risk

- The Owner Pays for the Insurance either Directly or Indirectly
- Soft Costs/Delay In Start Up coverage are for the Owner's benefit and involve the Owner's financial information.
- Owner would have control of claims settlement which is a key issue and the Insurer(s) would be the Owner's Insurers.
- The Owner would be familiar with the placement including the coverage terms, premium payments, certificate requests etc.
- Coverage protects the Investment and Lender requirements.
- Tailor- made wording designed for Owner's specific needs

Contractor Placed Builder's Risk

- Deductible levels and coverage scope are key issues for the Contractor
- Contractor would have control of claims settlement and Owner would have to deal with Contractor's Insurers
- Contractor could purchase Soft Costs/Delay coverage for Owner; however would need Owner's financial information.

Builder's Risk Key Coverage Issues

- Insured Parties
 - Named Insured
 - Additional Insureds
- Scope of Coverage/Coverages
- Period of Insurance
 - Inception
 - Completion
- Extension of Period of Insurance
- Premium Determination, including Deposit Premium
- Reporting Provisions and Premium Adjustment
- Exclusions

Builder's Risk Key Coverage Issues

Insured Parties

Named Insured (Owner or Contractor- Purchaser)

ABC Company Inc. and all associated and/or all other subsidiaries, companies, corporations, trusts, partnerships, associated companies which are now or may hereafter be owned by, controlled by, operated by or subsidiary to all at present or as may hereafter be constituted or acquired as the respective interest of each may appear with respect to the Insured Project.

Additional Named Insured(s)

To the extent required by contract for the Insured Project and then only as their respective interests may appear, owners, contractors, subcontractors and other individuals or entities specified in such contract shall be recognized as Additional Insured's hereunder, but limited only to their activities at the Project Location

All of above herein referred to as the Insured.

The Named Insured shall be deemed the sole and irrevocable agent of each and every Insured for sending or receiving notices, giving instructions and making and receiving payments etc.

Builder's Risk Key Coverage Issues

Coverages :

- Physical Damage to the Project Works
- CAT Perils – Earth Movement, Flood and Windstorm
- Debris Removal
- Demolition and Increased Cost of Construction (Ordinance or Law)
- Inland Transit and Off-Site Storage
- Expediting and Extra Expenses
- Contractor's Extra Expense
- Service Interruption
- Hot and Cold Testing
- Soft Costs and Delay in Start Up (Time Element)

Builder's Risk Key Coverage Issues

Period of Insurance/Term of Insurance

Inception/Effective Date: September 1, 2017

Expiration/Completion Date: September 1, 2019

This Policy shall be effective during the period commencing with the Inception Date and ending on the earliest of:

- Formal acceptance by the project owner
- When the interest of the Named Insured ceases
- When the Insured Project is occupied for its intended purpose
- When the Named Insured abandons the construction with no intention to complete it.
- When the Policy expires or is canceled

Builder's Risk Key Coverage Issues

Extension of Period of Insurance

- Most Insurers will extend (excluding Hot Testing) for 30 days, 60 days or 90 days at a pro-rata premium based on the inception rates with notice to the Insurer prior to the extension date.
- Additional extensions beyond those periods are subject to additional premium at rates and terms to be developed by the Company. They could increase the inception rates and change other terms. e.g.- Named Windstorm season, Hot Testing extension

Builder's Risk Key Coverage Issues

Premium Determination

- Physical Damage Premium
PD Annual Rate x PD Values/\$100 x Policy Term
- Delay/Soft Cost Premium
Delay Annual Rate x Delay/Soft Cost Values /\$100 x Policy Term
“ A rule of thumb is that the Delay/Soft Cost Rate is 1.25 to 1.5 times the PD rate”
- Hot Testing Premium
Testing Rate (Monthly) x Total PD & Delay Values/\$100 x Testing Term
- Deposit Premium
100% and/or or some Percentage of the Total Premiums for PD, Delay and Testing. There is usually a Minimum and Earned Premium listed.

All rates will be specifically listed in the Policy Form

Builder's Risk Key Coverage Issues

Reporting Provision and Premium Adjustment

Reporting Provisions

At expiration, cancellation or extension, the Named Insured has to report the final Estimated Total Contract Value including any change orders, wages, expenses, materials, supplies, equipment, machinery that are part of or were expended on the Project.

Premium Adjustment

The final earned premium is calculated by applying the Annual Inception Rates (unless changed) by the final Estimated Total Contract Value and the actual final term.

If the premium differs from the Deposit Premium then either an additional or return premium applies subject to any minimum premium. In some cases there is also a percentage change (such as 3% or 5%) that requires no adjustment

Builder's Risk – Key Exclusions

Key Property Excluded

- Land and land values to cut, fill, backfill etc.
- Existing Property
- Prototype Equipment
- Vehicles or Equipment licensed for highway use
- Contractors Tools and Equipment
- Liquidated Damages or Performance Guaranties

Key Perils Excluded

- Normal Property exclusions such as War, nuclear etc.
- Loss or damage from an implied or written warranty by any manufacturer or supplier
- Rain, sleet, ice or snow, all whether driven by wind or not, entering the interior of any insured property unless the exterior of insured property is complete.
- Cost of Making Good (Faulty material, defects, error in design, faulty workmanship) unless resulting damage from an insured peril ensues

Builder's Risk – Cost of Making Good Exclusion

There are several options for this Exclusion/Coverage

- **LEG (London Engineering Group) 1/96- outright Exclusion**
Excludes loss or damage due to defect or material workmanship, design plan or specification.
- **LEG 2/96- Consequences Defect Wording**
Excludes all costs necessary by defect of material, workmanship, design, plan specification and should damage occur to any portion of Insured Property containing any of the defects, the cost of replacement or rectification which is hereby excluded is that cost which would have been incurred if replacement or rectification of Insured Property had been put in hand immediately prior to the said damage. Excludes the defective part or material. Will cover resulting damage if an Insured peril ensues.

Builder's Risk – Cost of Making Good Exclusion

There are several options for this Exclusion/Coverage

- **LEG 3/96- Improvements Defect Wording**

Excludes all costs necessary by defect of material, workmanship, design, plan specification and should damage occur to any portion of Insured Property containing any of the defects, the cost of replacement or rectification which is hereby excluded is that cost incurred to improve the original material workmanship design plan or specification.

Protecting the Project

- Nightly/weekly/weekend patrols
- On- site watch service making hourly rounds
- Video surveillance
- Site/perimeter fencing/locked gates
- Waterflow/fire alarms
- Permitted access to jobsite
- Hot Work Permit system
- Water mitigation plan

Builder's Risk

Major Builder's Risk Markets

- ACE/CHUBB including Starr Tech
- AIG
- Allianz
- Liberty Mutual
- Liberty International (LIU)
- Munich Re America
- Travelers
- XL/Catlin
- Zurich
- Swiss Re
- Berkshire Specialty

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