PROJECT RISK INSURANCE

Risk Management and Risk Transfer
Considerations from an Owner/Developer Perspective
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PRE-CONSTRUCTION / DESIGN PHASE

Site Liability
Professional Liability
Pre-Construction / Design Phase
Site Liability

- Undeveloped land and/or existing structure(s)
  - Separate general liability policy or include under existing operational insurance
- Demo and/or other pre-construction work
  - If contracted separately, need to review contract and address if/how work will be insured separately by contractor(s) performing the work or how best to include under main construction insurance program
- Environmental conditions (known & unknown)
  - No “new” coverage available for known contaminant(s)
  - “New” coverage may be available for unknown conditions prior to being found during pre-construction/construction (i.e. clean Phase I environmental site assessment)
Pre-Construction / Design Phase Professional Liability

- **A&E Practice Policies**
  - Provides coverage for errors & omissions across all projects
    - Subject to per claim and aggregate limit(s)
    - Potentially inadequate or eroded limits due to claims at other projects
  - Annual policy terms
    - Relying on firm’s stability/perpetuation and subsequent policy renewals for coverage out through project completion and then statute
  - Varying coverage terms & conditions across design team
  - Contractual considerations (consult proper legal counsel accordingly)
    - Sub-Consultants contracted through AOR or directly with Owner
    - Indemnification/Hold Harmless
    - Limitations of Liability/Liquidated Damages
    - Waivers
Pre-Construction / Design Phase Professional Liability

• **Project Specific Professional Liability (PSPL or “Design Wrap”)**
  - Single policy with limits dedicated solely to the project
  - Lead architect and all eligible design professionals (DP’s) are insureds
  - Owner is an indemnified party for vicarious liability of all insureds
  - Coverage term includes initial design phase through substantial completion + extended reporting period per applicable statute
  - Eliminates finger-pointing amongst DP’s in the event of a complex claim
  - Single retention per claim that is typically allocated between Owner/DP’s
  - Generally a more economical solution to each DP availing their practice policies and passing that insurance expense on to Owner
  - Limited insurers depending on size/scope of project
  - Insurers require/review current loss runs and contracts from lead architect, engineer and major DP’s as subjectivity to binding
Pre-Construction / Design Phase Professional Liability

- Owners Protective Professional Indemnity (OPPI)
  - Project specific policy/limit solely protecting the Owner
  - Supplements “primary” coverage and “sits” above DP’s practice policies or PSPL
  - OPPI trigger is exhaustion of applicable DP’s practice policy(ies) or PSPL limits
  - Policy warranties DP policies and/or PSPL are maintained and in-force with specified limits per scope of design services provided
  - Coverage term includes initial design phase through substantial completion + extended reporting period per applicable statute
  - Owner/third party must bring action against DP’s to potentially trigger OPPI
  - Insurers require/review evidence of practice policies in-force and contracts from lead architect, engineer and major DP’s as subjectivity to binding
  - Generally a more economical solution to each DP availing higher limits on their practice or project policies and passing that insurance expense on to Owner
COURSE OF CONSTRUCTION

Builder’s Risk
Cargo & Offsite Storage
Construction All Risks (CAR)
Site Liability
Course of Construction Builder’s Risk

Covers the Project Works (materials and labor) against:

- All risks of physical loss or damage unless otherwise excluded.
  - Perils included—Fire, lightning, earthquake, flood, impact from vehicles or falling objects, crane failure, explosion, theft, strike & riot, windstorm, landslide, transit, subsidence, rock fall, malicious damage, terrorism, resultant damage from faulty erection, upset or collision, and more
  - Testing & Commissioning risks like electrical failure, insulation failure, short circuit, breakdown of equipment
- Delay in Start-Up—loss of income due to a delay in start-up caused by a covered peril
- Transit—damage to project materials in transit to the project
- Offsite storage—damage to materials stored away from the covered premises
Builder’s Risk Insurance

- Traditionally for large projects—Owner procures the coverage, Why?
  - Control—Owner is primarily at risk and should control/own the program, not be a side party to the contractor’s program
  - Cost—Owner procured programs generally cost less than a contractor procured program. Eliminates contractor overrides/markups
  - Coverage—Design coverage that addresses the Owner’s risk first.
  - Lender preference—Lenders prefer project specific coverage versus a contractors in-house program. Lender specific coverages are easier to incorporate in Owner procured coverage
Builder’s Risk Insurance

Control

- Owner dictates coverage parameters
  - Limits, perils covered, retentions/deductibles, sublimits to reflect requirements of lenders/equity partners, can include inland marine and ocean transit
  - Indirect Coverages—Delay in Start-Up, Soft Costs, Contingent Time Element, Cargo DSU are easier obtained through Owner’s Builder’s Risk
  - Owner is the loss payee (unless otherwise specified), not contractor
  - Additional Insured control
  - Waiver of Subrogation control
Builder’s Risk Insurance

Cost

- Owner procured Builder’s Risk costs less than coverage provided by contractor
- Program is project specific, self-contained and written for the duration of the project
- Eliminates contractor’s service fees and profit margins (can be 15-50% of the actual insurance cost, sometimes more)
- Lenders and equity partners preference
- Successful project can lead to operational insurance discounts
Builder’s Risk Insurance

Coverage

• State-of-the-art manuscript coverage forms, preferable to contractors “off the shelf” programs
• Program is written for the duration of the project and can potentially include 1-3 years of operational coverage following start-up
• Appropriate deductibles can be set to coincide with contractual requirements in the construction/lending agreements
• Limits and sublimits are included to comply with lenders / stakeholders
• Lending and equity partners preference
• Successful project can lead to operational insurance discounts
Builder’s Risk Insurance

Lender’s Preference

• Prefer project specific (Owner’s control), coverage more direct
• Bank risk consultant’s familiar with Owner placed programs
• Certificates of Insurance issuance and administration is directly under Owner’s (and their broker’s) control
Builder’s Risk Insurance
Cargo (Transit) & Offsite Storage

- Cargo/Transit - coverage for shipments of materials and equipment to the project site.
  - Types of shipments:
    - Ocean marine shipments—Marine Cargo
    - Air shipments—Marine Cargo
    - Inland waterways—Inland Marine
    - Overland—Rail, truck—Inland Marine

- Cargo/Transit Delay in Start-up

- Offsite Storage
  - Material receiving yard, lay up and staging site, warehousing, etc
Site Liability

- Traditional pass-through approach to GC & subs:

Each party maintains their own insurance program per contract requirements
Site Liability

• Potential risks to Owner with traditional pass-through approach
  • Exposes Owner to CGL Claims under its insurance due to:
    » Partial or contributory negligence
    » Inadequate contractor insurance
      » Coverage exclusions or omissions
      » Inadequate or eroded limits
      » Uninsured sub-tiers
  • Improper or non-renewed additional insured endorsements
  • Contractor/Insurer insolvency
  • Lack of control in claims situation & settlement negotiations
Site Liability

- **Owner & Contractor Protective (OCP)**
  - Separate CGL policy to protect Owner for **premised liability only** at project site (no products & completed operations coverage)
  - Supplemental coverage for Owner in addition to coverage availed through additional insured status on GC & subs insurance
  - Policy warrants minimum coverage maintained and in-force by GC and possibly critical subs
  - Policy term can be annual (and thus must be renewed annually) or project term
  - Fairly common lender or equity partner requirement since they have no direct contractual relation with GC
Site Liability

- **Owner Controlled Insurance Program (OCIP)**
  - Project-specific insurance program designed to cover all contractors on site
  - Consolidated insurance program provided by a sponsor (either the owner or the highest tier contractor)
  - Used in lieu of traditional insurance
  - Insures Owner, GC/CM, and all enrolled Subcontractors of any tier
  - Purchased by Sponsor
    - **Owner** = Owner Controlled Insurance Program (OCIP)
    - **Contractor** = Contractor Controlled Insurance Program (CCIP)
  - Funded by removing insurance costs from contractors’ bids
Types of Insurance in a Wrap-Up

- Core lines of coverage
  - General Liability and Completed Operations Liability
  - Excess Liability
- May include
  - Workers’ Compensation (often)
  - Owner’s Protective
  - Professional Liability
  - Environmental Liability
  - Railroad Protective Liability
  - Site Auto Liability
Coverage Secured by Contractors Under a Wrap-Up

- Automobile Liability (usually)
- Aviation Liability (as required)
- Watercraft Liability (as required)
- Contractor’s Equipment
- Off-Site Workers’ Compensation / General Liability
- Workers’ Compensation for Liability-Only Wrap-Ups
- Surety Bonds
- Deductible Buyback (not required)
Wrap-Ups Considerations for Sponsor

- Administrative costs
- Contractor concerns and objections
- Bidding process must be clear and detailed
- Collateral requirements (Sponsor)
- Potential of unrealized savings
Sponsor Responsibilities

• **Control**
  - Program Design
  - Program Administration
  - Legal counsel selection
  - Claims settlements within retentions

• **Financial**
  - Program profitability (savings vs. loss)
  - Maintenance of collateral
  - Financial integrity of insurers
Suitable Projects for Wrap-Ups

- **Eligible Projects**
  - AS 21.36.065 - "major construction project" means the process of constructing a structure, building, facility, . . . . having a contract cost of more than $50,000,000 of a definite term at a geographically defined project site

- **Sponsor must have or arrange for:**
  - Management commitment
  - High quality safety program
  - Effective and open communication
  - Deliverables are distributed in a timely manner
  - Professional administrative services
  - Customized claims management processes
## Comparison of Approaches

### Wrap-Up
- Single Policy
- Same Coverage Limits
- Contractors “enrolled” in program
- Coverage throughout Statute of Repose / Limitation
- Single primary GL policy
- Unified defense
- No “fault”
- Cross-suits eliminated

### Traditional
- Numerous Policies
- Varying limits of coverage
- Upstream protection by additional insured status
- Contractors must continue to provide completed operations
- Fragmented defense
- Each contractor pays for defense
- Who is at “fault”?
- Cross-suits are common
Common Obstacles to Success

- Sponsor or their Insurance Partners Lack
  - Experience
  - Strong safety / claims management programs
  - Commitment, preparedness and focus
  - A supportive culture
  - Vision past insurance credit amounts
  - Poor program design
  - Poor communication between participants
  - Conflicting agendas of participants
  - Faulty expectations of participants – bid credits
Common Contractor Concerns

- Administrative complaints
- Perceived loss of profit
- Unfair or abusive credit calculations
- May impact cost of traditional programs
- Resistance by insurance brokers/advisors
- Failure of sponsor to provide timely information
- Documentation / Deliverables
- Mandatory adoption of stringent safety requirements
Potential Contractor Concerns

- Discrepancies between contract, manual and policies
- Failure to specify responsibility for retentions
- Named insured and additional insured errors
- Failure to complete enrollment process
- Inadequate limits of liability
- Inadequate “project” or “site” descriptions
- Self-insured retentions vs. deductibles
- Failure to extend coverage for delayed projects
- Failure to include primary/non-contributory endorsements
Contractor Coverage Concerns

- Missing extended products/completed operations endorsements
- Subrogation actions by Wrap-Up insurers against participants
- Failure of excess insurance to “follow form”
- Damage to the project
Why a Sponsor Wants a Wrap-Up

- Isolates construction risk to a project-specific program
- Known dedicated limits, coverages and insurers
- Known completed operations coverage and term
- All contractors comply with on-site insurance requirements
- Reduced exposure to litigation
- Centralized safety and claims management
- Project term pricing protection
- Provides broader scope of coverage and higher limits
- Eliminates concerns over improperly insured contractors
- Potential reduction in the cost-of-risk
COURSE OF CONSTRUCTION
Owner-Placed
Builder’s Risk Insurance
Owner-Placed Builder’s Risk - Control

- Owner’s own project specifications and values are utilized
- The contract is formed by the owner – more certainty of promise/obligation
- Owner is first named insured
  - Has greatest rights of recovery under the policy
  - All payments made to Owner under policy
- Controls deductible allocation
- Can specify and orchestrate coverage nuances
Owner-Placed Builder’s Risk - Control

- Controls limits of coverage and coverage types
  - DIC; Earth movement and Flood
  - Time element coverages – Important for:
    » DSU
    » Soft Costs
    » Testing & Commissioning
    » Loss of Income
- AOP Limits
  » Owner-furnished equipment
  » Change orders can be positively incorporated to assure adequate limits
- Risk Control can be managed to Owner’s best interest
- Waivers of subrogation control
Owner-Placed Builder’s Risk - Leverage

- Opportunity to incorporate CAR-type placement
  - Includes liability arising out of the course of construction for third parties
  - Eliminates issues with property damage and rework exposures
  - Consolidates claims to single point
- Pricing
  - Can provide a cost savings through a larger potential “footprint” in the market through transition to a permanent placement for the completed project through the same underwriters.
QUESTIONS?

Thank You