



The What and Why of Builders Risk Insurance

Builders Risk insurance is a property coverage for buildings under construction. Builders Risk provides many of the same coverages that the Fund provides to the district's or authority's owned buildings. The coverage is usually provided on an "all risk except what's excluded" basis so most of the perils that cause damage to property already constructed are also covered under Builders Risk. Of course, with all insurance, there are exclusions that we will discuss later.

Builders Risk is an important coverage to require of the contractor that is building your new administrative building, clinic, or other facility. The contractor is the named insured on the policy because the contractor is at risk for the work until it is completed and turned over to the district or authority. The district or authority should be named as an additional insured on the policy to protect your interest in the incomplete building. The amount of coverage provided by the insurance company is based on the percentage of completion at the time of a claim, not the ultimate final cost of the completed building. For instance, if a \$10,000,000 value building burns to the ground when it is 50% complete the insurance company would only pay \$5,000,000 (subject to deductibles and possible sub-limits). This protects the district or authority and the contractor because the insurance proceeds will pay to re-build up to the percent of completion at the time of the loss. Then the project can continue to completion with the balance of the unused financing to finish.

Examples of insuring agreements from two insurance companies illustrate the breadth of coverage provided by Builders Risk insurance. The first is from Zurich Insurance and the second is from a Lloyds of London form:

"Subject to the terms, exclusions, limitations and conditions, the Company will pay for direct physical loss of or damage to "builders risk property" caused by a "covered cause of loss" while such "builders risk property" is (1) at the "project site"; (2) In transit; or (3) at a "temporary offsite location". (Zurich Insurance Co. insuring agreement)

"The Insurers will indemnify the Insured in respect of physical loss, destruction or damage to the Property Insured occurring during the Insured Project Period of Insurance arising from any cause whatsoever except as excluded as defined in the attached wording that forms part of this contract." (Lloyds of London insuring agreement)

The district or authority should specify in the RFP or contract that the contractor's insurance coverage include Builders Risk. The limit of liability is the final construction price with the possibility of increase if changes are made during construction. The time

period for coverage may also change as long as the insurance company is advised. They may charge additional premiums for the higher coverage amount or time extension.

The limits of liability often include sub-limits for flood, earthquake, and earth movement (landslide). Sub-limits typically apply to perils such as:

- Flood
- Earth Movement
- Property in Transit
- Property in Storage
- Expediting Expense
- Debris Removal
- Increased cost of construction due to operation of ordinance or law
- Preventive measures prior to loss

Any specifications for insurance for the contractor should spell out the important sub-limits, especially if the project is near a flood plain, includes expensive furnishings or fixtures, or equipment will be transported and stored before installation. Of particular importance to many building projects, is coverage for property being transported from a manufacturer or supplier to the job site and its subsequent storage nearby, before installation. Debris removal after a loss is also important as that cost can be quite high depending on the extent of damage or the complexity of the job site. The sub-limits are included in the total limit of liability and are not in addition to the total limit of liability.

As mentioned in both of the insuring agreements quoted above, exclusions are always a part of the insurance provided. Typical exclusions include:

- Penalties for non-compliance with the contract
- Defects in material or workmanship
- Wear and tear
- War and terrorism
- Money
- Aircraft or watercraft
- Radiological or biological contamination
- Pollution (except as covered in sub-limits)
- Fraud or dishonesty of the insured
- Asbestos

Builders Risk is a great coverage for districts or authorities to require of their contractors primarily for the assurance that vital facilities will be completed once construction starts. As with any insurance coverage there can be situations where policy provisions can cause problems for both the contractor and the owner. Severe and long-lasting flooding in Texas as the result of Hurricane Harvey revealed problems with time limits on recovery from flood damage. The flood stage in a Texas river did not recede for months and delays in recovery caused material prices to increase substantially. Another issue arose when there was a communications breakdown between the contractor and the owner. The

contractor allowed the builders risk coverage to lapse and the owner did not add their new building to the Fund's coverage over a weekend. A strong tropical storm moved through the area and did substantial damage to the new building that was ready for occupancy. A third issue can arise when a building is almost completed, and the owner wants to move in. Builders Risk policies may have provisions related to this frequent occurrence that may limit coverage. Generally, coverage ends when there is "final acceptance by the owner." Another common circumstance that can cause issues is the addition to an existing building or extensive remodeling. An extension of coverage in the Builders Risk policy can provide coverage to the existing structure.

In all cases involving insurance, read the policy. In the world of Builders Risk, no two policies are completely alike. Consult with the Fund's risk management consultant or senior underwriter if you have questions or want us to review a Builders Risk policy.