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# Marsh Specialty

CONSTRUCTION PRACTICE

# Increased Costs, Tougher Terms for Construction Industry

April 2021

# A challenging insurance market requires insureds to set clear objectives and be laser-focused during underwriting discussions.

Increased underwriting discipline together with poor claims experience over the past several years have led the construction insurance market in the US to become increasingly difficult, with base pricing applied to risk increasing by around 25% since the second quarter of 2018.

With the future trajectory of the market still in flux, companies in the construction industry face a period of uncertainty, both in relation to ongoing projects that may require renewals or extensions and even more acutely when it comes to planning for future developments. Projects in the New York metropolitan area or with wildfire exposures are facing the most difficulties.

## INCREASED UNDERWRITER SCRUTINY

Underwriters are carefully scrutinizing all applications, including extensions. Some carriers have reduced the amount of capacity they provide for extensions, while others are declining to extend capacity for certain risks.

Higher insurance prices have been accompanied by stricter terms and conditions, while attachment points are typically higher. These trends are expected to persist in the coming months.

Despite many ongoing challenges, there is still capacity for good risk, with insurers signaling they want to partner with contractors that have a strong focus on contract risk allocation, worker safety, and financial strength.

## BUILDERS' RISK UNDER INCREASED SCRUTINY

Available capacity in the builders' risk market continues to shrink and market response time to both existing and new business continues to slow. Some markets are withdrawing or reducing line sizes on extension periods. Some insurers are also imposing strict qualification measures to LEG 3 coverage, which most carriers are only offering during the construction phase.

Multiyear master builder's risk programs have become more difficult to secure. Insurers are rarely willing to guarantee pricing for more than 12 months without a client's firm commitment to a set of projects to be insured during the program's duration.

## AMPLE CAPACITY BUT INCREASED SCRUTINY FOR ENVIRONMENTAL COVERAGE

Ample capacity is still available for most risks and the environmental liability market remains competitive overall. However, the market for longer-term projects — typically exceeding 10 years — is tightening.

Pricing for practice-specific contractors pollution liability programs have across the board, with certain classes of business and those that have experienced losses the highest increases.

Project delays due to the pandemic and ensuing lockdowns are straining policies approaching or exceeding their maximum term. Meanwhile, the tight labor market is raising concern about a potential increase in construction defects.

Closed or abandoned projects that may have indoor air quality issues due to potential water intrusion or mold growth are also of concern to insurers. Some insurers are adding COVID-19 or communicable disease exclusions to contractor pollution policies, with most adding these exclusions to site liability policies.

Underwriters are applying greater scrutiny and discipline, asking more questions to better understand companies' operations and risk management strategies, especially in the middle market space. The increased focus is primarily targeting scope of work, claims, and merger and acquisition activity. Broad coverage for site liability coverage for development projects is tightening.

We expect carriers to pay close attention to potential changes and enhancement to environmental laws and enforcement as well as emerging risks — such as per- and polyfluoroalkyl substances (PFAS) and other "forever chemicals" — and their overall effect on the environmental market and coverage lines.

To avoid delays in securing coverage, insureds should ensure they have the necessary information ready before underwriting meetings. Insureds should work with their brokers to prepare solid underwriting submissions, both for new placements and renewals, and engage in virtual meetings with both incumbent and new markets, depending upon the program size/scope and need.

Accounts with favorable loss histories may benefit from marketing their programs. Marketing tougher risks may benefit from multi-carrier structures, rather than a monoline design.

# CASUALTY, EXCESS CASUALTY CHALLENGES EXACERBATED BY COVID-19

The casualty marketplace is experiencing rapid change and uncertainty, in part due to the COVID-19 pandemic. Insurers are requiring communicable disease exclusions on new business, with some insurers also inserting these clauses in extensions, although physical damage that may result from a communicable disease is typically still covered. Many insurers are also modifying renewal pricing, limits, retentions, and terms.

There is increased scrutiny on exposure to credit defaults on deductible liabilities. Insurers are often requesting mid-term credit discussions and have also indicated a more conservative approach for lower credit new business risks.

In addition, contractors are facing higher operating costs to keep their sites safe, while supply chain challenges have led to higher prices for basic materials, including lumber. Further, a shrinking project pipeline has fueled increased competition among contractors.

The excess casualty market has become significantly challenging for companies in the construction industry, with many carriers pushing for pricing increases, deploying lower limits, and increasing attachment points.

Insurers' self-imposed capacity restrictions have led to approximately $500 million of excess capacity leaving the market; while some new insurers are entering the market, this is not happening quickly enough to replace exiting capital.

Traditional coverage grants in the excess space – including per-project general aggregate limits and contingent "excess of wrap" coverage – are becoming more difficult to secure. Certain projects, including those located in the New York metropolitan area, with wildfire exposures, and for-sale residential projects continue to be most challenging, with an ever-shrinking market and facing significant pricing increases. Large commercial projects and annual programs for commercial contractors tend to have less difficulty securing coverage.

More insureds are using the same carrier for primary casualty and lead excess due to reduced appetite for monoline lead excess. Many insurers are restricting limits for both lead policies and excess casualty. And some excess carriers are attaching additional exclusions that are not included in underlying layers.

# TIME AND DATA CRUCIAL FOR PLACEMENT SUCCESS

To date, there are no clear signs that the market will shift in the near future. Current conditions and difficulties are expected to persist for at least the rest of the year.

For insureds, this reality requires a change in the way they approach placements for new projects and extension requests. Most importantly, they need to establish clear objectives around their insurance program and remain laser-focused on their targets during underwriting discussions.

With underwriters carefully scrutinizing each submission and often requesting more information than before, the placement process is taking longer. Insureds should start discussions as early as possible and make sure they have enough time to provide underwriters with all the information they require. Although underwriters are unlikely to commit to pricing and terms early on, brokers are typically able to provide benchmarking information on similar projects to help clients budget for insurance expenses.

Quality data has become critical, with underwriters generally not willing to commit to any projects before they are presented with all the data they have requested. For insureds, this means it's critical to prepare and ensure all necessary data is available prior to underwriting meetings. Brokers can help construction companies identify the data that underwriters typically require, develop marketing plans, and create a clear timeline for deliverables.

Finally, insureds need to reset their expectations and understand that the current market conditions mean that pricing and terms secured for earlier projects may no longer be achievable.

# SURETY MARKET REMAINS STRONG

**While most construction lines are experiencing pricing increases, tougher terms, and reduced capacity, surety remains a competitive market with ample capacity. These trends have been ongoing for the past two decades, mainly due to limited loss activity and good profitability for insurers.**

The COVID-19 pandemic, however, has raised ample concerns about a shift in the favorable market. Steps taken to stem the spread of the virus forced many businesses in various parts of the US to shut down their job sites, causing the underwriting community to become worried about significant losses. This prompted several major insurers to review existing accounts and reduce underwriting activity while waiting for more clarity about a potential change in their principals' risk profiles.

Fortunately for construction companies, the slowdown quickly reversed. Since the industry was considered an essential business in the US, many construction companies were able to get return to job sites by mid-2020. Several small companies — which would typically struggle most during a downturn — were able to secure loans through the Paycheck Protection Program (PPP), helping them improve their liquidity. Further, the residential sector as well as several other key segments such as health care and public safety saw growth in 2020, helping counter the downturn in other sectors, such as lodging.

There is still ample capacity in the market, but pricing drops that had become relatively common prior to the pandemic have slowed. Major carriers have enjoyed several years of preferable loss ratios, making surety a profitable business and allowing insurers to continue offering competitive pricing and favorable terms. Current flat pricing is expected to continue in the coming months, with no indications of substantial changes in the surety market.

# PROFESSIONAL LIABILITY REMAINS STABLE

**Unlike some other lines, the professional liability market for contractors and architects and engineers in the US remains stable.**
**There is sufficient capacity in the marketplace for most contractors' practice programs as well as their project-specific needs.**

Certain carriers have cut back the capacity they will deploy on any individual risk or ceased writing the class of business entirely, but other insurers have entered the marketplace. As a result, we are not seeing a capacity shortage or extreme increases in pricing.

A US contractor with good loss experience can generally expect renewal pricing increases of between 5% and 10%. Contractors and architects and engineer firms with losses are typically seeing larger increases.

US underwriters are becoming more disciplined due to a tightening of the professional liability marketplace in other regions — particularly London — and a more challenging marketplace for other lines, such as builder's risk and excess casualty. As a result, more thorough underwriting submissions may be required.

Underwriters are scrutinizing public-private partnerships (P3) and fixed-price design/build projects; contractors have suffered financial losses due to these projects' delivery methods, which can translate to professional liability claims. They also have a limited appetite for process plants, as that class has sustained some very large professional liability losses.

We are not seeing COVID-19/communicable disease exclusions being attached to professional liability policies.

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