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CONSTRUCTION PRACTICE

Canadian Construction Industry Facing More Difficult Placements, Renewals

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Higher prices, narrowing terms and conditions, and greater underwriter scrutiny underscore the need for a more thorough and data-driven placement process.

Insurance pricing in Canada has been on a significant upward swing for the past two years, following more than a decade of soft market conditions. The swift change took many insureds by surprise, especially since new insurance costs were markedly higher than the amounts accounted for in existing budgets.

Due to the nature of the industry, pricing models are typically finalized well before construction is due to begin as different companies bid for projects. But insurance prices have often continued to inch upward well after contracts have been signed, with companies often having to dig into their contingency funds or pay the extra costs out of pocket. It is not uncommon for prices to be 20% more than insureds would have accounted for — a substantial difficulty for an industry known to operate on already thin margins.

PANDEMIC AGGRAVATES CHALLENGES

The COVID-19 pandemic has exacerbated an already difficult situation. Several job sites shut down in line with stop-work orders and reopened with new social distancing rules that contributed to longer timelines. Supply chain issues early in the pandemic led to scarcity and skyrocketing prices for basic raw materials, a situation that further affected companies' finances.

At the same time, prices for different lines of insurance continued increasing, including for coverage extensions. Underwriters, already diligently reviewing each application, are now adding another layer of scrutiny, including exploring contractor companies' ability to get workers to the jobsite amid pandemicrelated restrictions.

GREATER SCRUTINY OF PROFESSIONAL INDEMNITY RISKS

After experiencing a number of major claims, both in Canada and around the world, professional indemnity (PI) underwriters have restricted capacity, with some insurers exiting the line altogether. Engineers are typically seeing higher price increases than contractors, and greater difficulty securing coverage.

Underwriters are carefully scrutinizing each project and are being highly selective where they are willing to provide coverage. While there have not yet been widespread changes in terms and conditions, program enhancements are becoming difficult, if not impossible, to secure.

Underwriters are requesting highly detailed submissions and spending more time reviewing each application. Most insurers are now requesting additional information, especially on a company's pandemic response, fire safety standards, and risk management processes. Greater internal scrutiny, with many risks requiring head office review, is extending the underwriting timeframe.

Renewal meetings involving carriers and clients, previously reserved for the biggest risks, are becoming more common. With some players exiting the market, insureds may need to change carriers when applying for renewals or extensions.

The current reality underscores the need for insureds to start the renewal process early, allowing enough time for the longer underwriting process and the potential need to market their programs. They should work with their broker to better understand what pricing, terms, and conditions are likely to be offered in upcoming renewals, and budget accordingly.

Insureds should also include all requested information in their submissions and steer clear of seeking too many changes to the insurance program, which can lead to credibility issues.

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DIFFICULTIES EXPECTED TO PERSIST

There are no indications that market conditions are likely to materially change in the near future, which means insureds should be prepared for difficult conditions to continue across all lines.

The level of uncertainty about pricing structures has been a stressor for businesses as they complete budgets for projects that won't be placed for several months or even years. When seeking coverage in the current insurance market, insureds are sometimes faced with a need to fulfill contractual terms that are no longer commercially available, requiring additional negotiations with project owners.

While capacity remains, coverage for some projects – including residential construction and hot tar roofing – is becoming more difficult to secure, with insurers taking very firm stances.

HIGH-QUALITY DATA FUNDAMENTAL TO PLACEMENT SUCCESS

During the prolonged favorable market, insureds were typically able to obtain the coverage they needed at reasonable prices even if they provided limited information to underwriters and started renewal and new placement processes relatively late. Current market conditions, however, require revisiting previous practices.

Underwriters are carefully scrutinizing each project and have shown a willingness to walk away from certain risks. To secure coverage and obtain the best possible pricing, insureds should collect and present in-depth data that demonstrates their awareness of project-specific risks. They should also present information about the risk mitigation strategies they — and, where possible, their subcontractors — employ, including site safety rules. Quality information that clearly explains a company's risk mitigation strategy can help insureds, and their brokers, explain to underwriters why a specific project is a preferred risk.

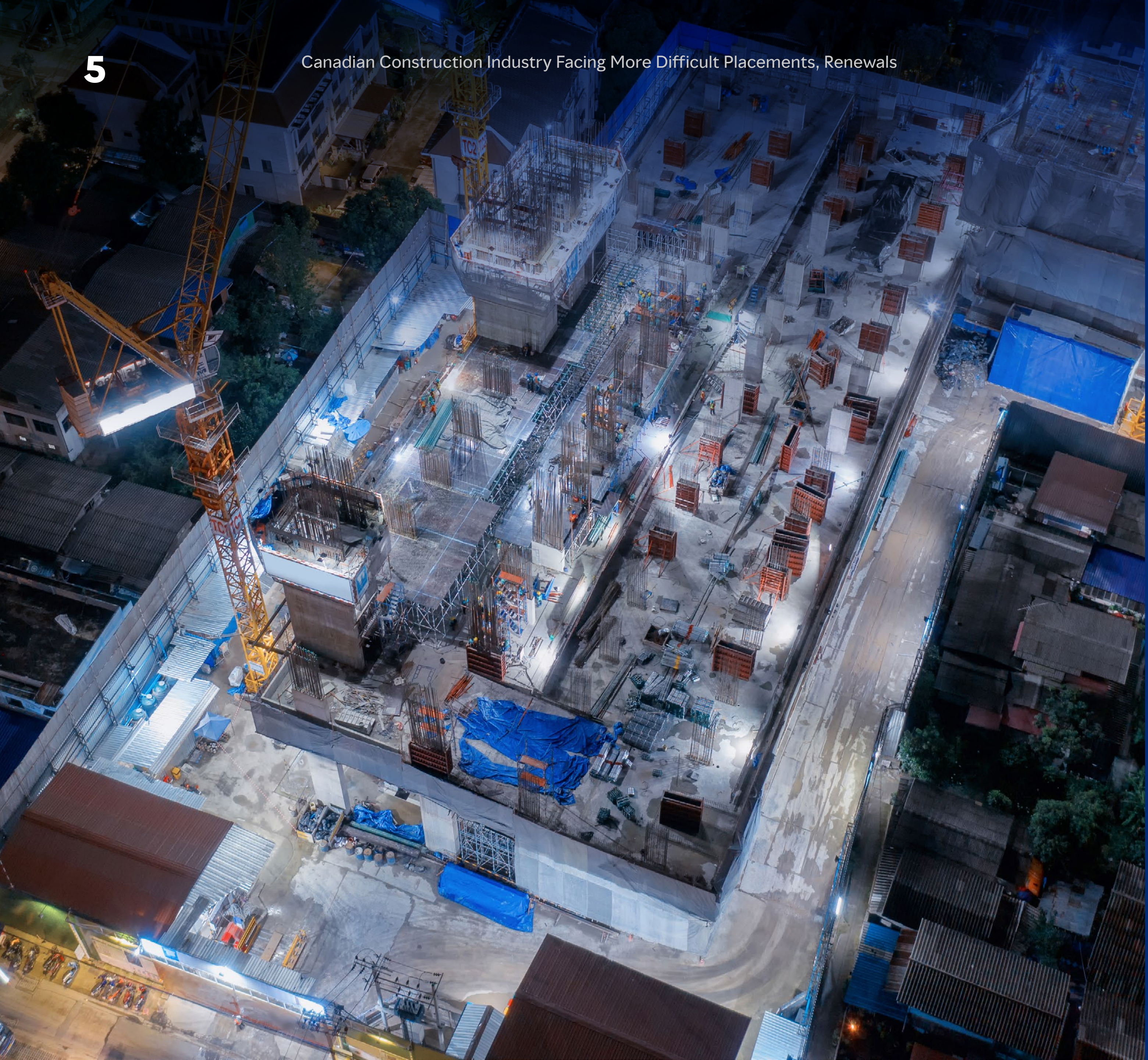
Further, insureds should work with their brokers to:

- Explore whether they can obtain more favorable pricing and terms through foreign markets.
- Consider different ways to structure their risk transferportfolio, including trying to secure premium credits from insurers by consolidating programs.
- Revisit their retention levels and determine whether it would be financially effective to assume more risk.

The underwriting process in general is taking more time tocomplete. For insureds to be able to explore all their options, they need to start conversations with insurers early, allowing enough time for negotiations.

Timing will be crucial when they need to pivot to other strategies – including marketing their program to other insurers – if they are unable to secure acceptable pricing and terms.

Despite the challenges faced in 2020, low interest rates aswell as the potential for greater public infrastructure investments this year could lead to more new projects, which could give a much-needed boost to the construction industry. But with current insurance market difficulties expected to persist, insureds need to be meticulous during negotiations and use data to help underwriters understand why they should consider a particular project.



SURETY

While the surety market remains strong, insurers are being increasingly cautious, especially amid continued uncertainty caused by the COVID-19 pandemic.

Underwriters are carefully scrutinizing each application and taking more time to understand contracts that insureds have already signed and analyzing the effect that potential supply chain challenges may have on a client’s ability to deliver projects on time.

Surety pricing generally remains stable for contract risks, although certain commercial risks are seeing moderate price increases. There have, to date, not been any outright exclusions, but increased due diligence from underwriters requires clients to be more transparent. Underwriters are typically requesting copies of contracts, current financial information and work-on-hand reports, and real-time updates of any disputes and claims. Although underwriters are generally interested in historical results, they are keen to understand how contractors are dealing with present-day challenges, especially ones caused by the pandemic.

Large general contractors are generally under increased scrutiny since they tend to have more subtrades and greater exposure to potential supply chain challenges. Public-private partnerships, which are expected to be numerous in 2021, are under the microscope. As underwriting discipline increases, marginal credit risks are being squeezed tighter.

Despite the increased scrutiny, ample capacity remains for both contract and commercial risks. However, with more internal approvals required to sign off on a risk, the underwriting process is taking longer. Insureds should prepare for more regular contact with their surety providers.

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