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BUILDER'S RISK vs CGL POLICIES – WHICH POLICY RESPONDS FOR DAMAGES ON A PROJECT?

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From Seattle to Charleston, tower cranes are dominating the skylines. New construction projects seem to be on every street corner in most metropolitan cities these days. With all of this activity, the possibility that damage may occur on one of those projects; insurance may be needed to pay for the damage; and the owner, developer, and contractors may be confused as to which policy should respond is foremost on the minds of claims professionals.

A builder's risk policy (also known as a course of construction) insures against accidental loss or damage to contractors' work and property during the period of construction. Also, the policy usually insures equipment, materials, and supplies to be used and incorporated into the project.

The project contract identifies the party who must procure the builder's risk policy for the project: the owner, developer, or general contractor. The industry's standard contract, "General Conditions of the Contract for Construction (American Institute of Architects' AIA Document A-201 ([1997, 2007 or 2017]))", says the owner must procure the policy, but that condition is occasionally amended to require one of the other parties

to procure the policy. The AIA contract also states that the builder's risk policy is to cover the interests of the owner, general contractor, and subcontractors of all tiers, and there must be a waiver of subrogation in favor of all of those parties.

Still, when damage occurs, it is common for the party who purchased the builder's risk policy to expect the responsible contractor to use their own commercial general liability (CGL) policy to pay for the damage. The contractor may not want to jeopardize their business relationships with the other parties on the project, so they will agree to initiate a claim with their CGL insurer. That's when the confusion arises.

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Claims professionals understand the "business relationships" pressure on the responsible contractor, but there are several reasons why builder's risk, and not the CGL, should be the first line of insurance to respond to damage on a project involving new construction.

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First and foremost, builder's risk insurance pays without regard to who was responsible for the damage. Therefore, the initial and primary focus of the builder's risk insurer is to see that the damage is repaired in a timely manner, so there is as little disruption as possible to the original construction schedule. The initial focus of a CGL insurer is to determine who is responsible for the damage, which can lead to "finger pointing" between contractors and delays while everyone waits for the insurer's determination.

Secondly, the responsible contractor will likely encounter a coverage issue when they initiate a claim with their CGL insurer.

The CGL policy includes the standard "other insurance" condition, which states:

"This insurance is excess over: Any of the other insurance, whether primary, excess, contingent or on any other basis: That is ... Builder's Risk, ..."

This condition also includes the following statement:

"When this insurance is excess over other insurance, we will pay only our share of the amount of the loss, if any, that exceeds the sum of: The total amount that all such insurance would pay for the loss in the absence of this insurance; and the total of all deductible and self-insured amounts under all that other insurance."

Simply put, the CGL policy will not pay for damage when there is a builder's risk policy that may pay, and the CGL policy will not pay the deductible under the builder's risk policy.

Another reason that the builder's risk policy should be the first line of insurance is because the waiver of subrogation in the project contract precludes the builder's risk insurer from subrogating against, or seeking reimbursement from, the responsible contractor.

Additionally, the builder's risk policy is usually a project-specific policy, so payments under that policy should not have an adverse effect on an annual insurance program. In contrast, payments under a CGL policy do negatively influence a contractor's loss history, and could result in higher annual premiums.

Lastly, and possibly most importantly, the party who agreed to procure the builder's risk insurance did so willingly when the project contract was negotiated, so they have a contractual obligation to initiate a claim after damage occurs. A party refusing to initiate a claim is contrary to the intended purpose of builder's risk insurance, and can amount to a breach of contract.

It is difficult to predict how long the current construction boom will last, but if damage occurs on a project, initiating a builder's risk claim immediately will help get the repairs started, the project back on track as soon as possible, and maintain a cooperative spirit among all parties involved in the project.