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CONTRACTORS' EXCESS/UMBRELLA RATES IN THE INSURANCE HARD MARKET

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The insurance market, like any other type of supply and demand industry, is cyclical. The cycles are commonly referred to as "soft" and "hard" markets. A hard market is characterized by a decrease in limit and underwriting capacity and an increase in rate and premium; this type of market can also prompt carriers to review and amend their underwriting appetite and/or guidelines, causing a decrease in capacity and limited coverage overall. The soft market's character traits are the opposite; capacity is abundant, rates are lower, and coverage is more flexible. Unfortunately, for the first time in almost 20 years, we are experiencing a move towards a hard market. This article will provide insight as to how this specifically affects contractors in the excess/umbrella liability space.

Various factors push the insurance industry into a hard market: catastrophic losses, including, but not limited to, floods, earthquakes, hurricanes, wildfires, and similarly devastating disasters; a combined ratio of written premiums to losses paid out over 100%; dwindling investment returns, most commonly related to bonds, stocks, and real estate investments; the economy, which is currently being affected by COVID-19; and the cost of reinsurance. These are general factors applicable to commercial insurance as a whole, but can often have a greater effect on construction due to the various exposures not necessarily present with other industries.

HARD MARKET IMPACT ON THE CONSTRUCTION INDUSTRY'S EXCESS/UMBRELLA RATES

Construction companies' general liability policies are based on revenue, payroll, and/or subcontractor costs, automobile coverage is rated on the number of power units and their gross vehicle weight, and excess/umbrella policies are rated based on the underlying exposures and premiums over which the policy sits. These premiums include general liability, automobile liability, employer's liability, and/or employee benefits liability. On rare occasions, an excess/umbrella policy will also provide limits above pollution or professional liability coverages. In addition to the underlying premiums, the excess/umbrella underwriter considers the type of exposure you have, any claims history, catastrophic losses specific to the construction industry (e.g. tower crane collapses), court cases and resulting verdicts; and the limits purchased.

Forecasting models indicate that the excess/umbrella market is taking the biggest increase across the board. While other lines of liability coverage are seeing increases of 0% to 15%, excess/umbrella increases are facing 15% (low to moderate risk) to over 25% (high risk). The construction industry specifically has seen increases as high as 50% or more for excess/umbrella policies. Some insurance carriers are cutting back on their capacity; for

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example, one carrier that previously wrote a $15 million excess/umbrella primary layer in the past for numerous construction companies is now only offering a $5 million limit on renewal business at the same premium as the previous $15 million and not writing new construction accounts at all. Other carriers are asking to be taken off of the primary layer altogether and only be considered to write higher up in an excess/umbrella tower.

FUTURE MARKET PROJECTIONS

There will be impacts, known and unknown, felt by construction companies when it comes to excess/umbrella premium increases and coverage limitations. Many insureds will contemplate lowering their limits to offset the increase in insurance premiums. The most important thing to think about when considering this strategy is what is your true exposure to risk and how are you positioned to either accept risk or transfer it. Another item to consider is what your construction contracts require, not only for limits but also for the statute of repose requirements. While your project may have been completed for three years, what does that contract require and for how long? You must take stock of this to ensure that you comply with your contractual requirements for the appropriate amount of time.

Additionally, brokers are now going to have less negotiating power in some instances. They will be at the mercy of carrier underwriters and their guidelines, which may be more restrictive than in years past. Carriers will be more focused on the profitability of an insured's placement instead of writing new business than they have historically. Underwriters will be inundated with new submissions, in addition to their renewals, so they will be very selective about the accounts they choose to quote and write. We have also seen many lead carriers require underlying limits be increased from $1 million per occurrence / $2 million aggregate to $2 million per occurrence / $4 million aggregate on the commercial general liability, and auto limits increased from $1 million combined single limit per accident to $2 million. This will prove challenging for brokers as they are now approaching more markets, negotiating with more underwriters, and possibly having to build an excess liability program with several layers and more carriers. More carriers who have their own minimum premiums equals increased premium costs for the total limits purchased.

In closing, there will be many things to look out for in the coming months, and possibly years, with the excess/umbrella market. As the court awards for claims continue to climb and pierce the excess/umbrella layer and the construction industry continues to face high risk exposures, the excess/umbrella markets are going to be overly cognizant of what limits offered, what limitations they won't budge on during negotiations, and the state of the reinsurance market. To help minimize the effects of the hard market, we recommend strategizing with your insurance team earlier than ever before. Make sure you get the renewal exposure information back to your broker as soon as possible to give them ample time to market your program.

References and Resources

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