

Damages Recoverable in Delay of Construction Coverage in Builders Risk Insurance

Wednesday, March 20, 2019

Presented By the IADC Construction Law and Litigation Committee and Insurance and Reinsurance Committee

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What Is Builder's Risk Insurance?

- Most construction contracts require either the building owner, developer, or contractor to purchase and/or maintain builder's risk insurance for the expected life of a construction contract
- The coverage provided under a BR policy generally will cover the loss or damage to an unfinished building or other structure and/or building materials as a result of a covered event
- Provides protection in the event of an unforeseen event delaying completion of the project
- If properly procured, the BR policy will provide coverage to all project participants at every tier, so all subcontractors, no matter how small their role in the project, should be listed as additional insureds when the policy is procured

2017 AIA Forms and Their Insurance Requirements

- 2017 AIA Form A101 and A102 and Their Insurance Requirements
- Pursuant to A.2.4.7, soft costs insurance may be required by the property owner and/or general contractor/construction company

Are BR Policies All Standard?

- ISO forms CP 10 10, 10 20 and 10 30 were developed by the Insurance Services Office to provide the industry with standard language and forms to use in writing BR policies
 - Many insurers have their own form policies, however, which may differ substantially from the ISO forms
 - BR is an area particularly fertile for the participation of syndicates of multiple insurers, so the resulting BR policy may be an amalgamation of many different individual insurers' forms
- Most BR policies are project-specific, although some larger general contractors or construction companies have “rolling” BR policies that cover all their construction projects going on at any one time

What Are The Different Types of BR Coverage Typically Offered: All Risks Policies

- All risks: ISO form 10 30
- Most common due to the comprehensive nature of the coverage provided
- Courts generally have agreed that the insured has the initial burden to demonstrate coverage under an all risks BR policy (this has been construed as a relatively light burden as compared with the showings required in the context of other types of insurance policies)
- Once coverage has been established by the insured, the burden then shifts to the insurer to show that an exclusion in the policy unambiguously applies (*Zurich Am. Ins. Co. v. Keating Bldg. Corp.*, 513 F. Supp. 2d 55 (D.N.J. 2007))

What Are The Different Types of BR Coverage Typically Offered: Named Perils Coverage

- Named perils: ISO forms 10 10 and 10 20
 - ISO basic or short form (ISO form 10 10) covers losses caused by any of the following:
 - Fire
 - Lightning
 - Explosion
 - Windstorm or hail
 - Smoke
 - Aircraft or vehicles
 - Riots or civil commotion
 - Vandalism
 - Sprinkler leakage
 - Sinkhole collapse
 - Volcanic action

What Are The Different Types of BR Coverage Typically Offered: Named Perils

- Named perils: ISO form 10 20
 - ISO broad form (ISO form 10 20)
 - All named perils under ISO form 10 10 **plus the following:**
 - Falling objects
 - Weight of snow, ice or sleet
 - Water damage

What Types of Properties Does BR Cover?

- Commercial/office buildings
- Luxury condominium buildings and other high-rise multi-unit residential buildings
- Parking garages, warehouses, and other large buildings

How Is Builder's Risk Insurance Different Than Other Types of Insurance?

- It may be required by the specific construction contract
- Temporary in time-only extends for the life of the construction project
- Given the sheer number of manuscript BR forms available, each of which is different from one another, there is relatively little case law construing particular exclusionary provisions, which can make coverage counsel's job doubly difficult
 - Counsel is then forced to rely upon treatises and/or expert commentary or cases construing similar but not identical policy language
 - This difficulty is made even worse by the fact that, given these are contract disputes, state law controls the interpretation of insurance policy dispute

When Does BR Insurance Typically Come Into Play?

- When some sort of delay has occurred in the progress of construction which makes the scheduled completion date untenable
- Industry professionals will tell you anecdotally that virtually every construction contract comes in late due to a variety of factors beyond the GC's control
- BR was developed as a risk mitigation tool in the event certain enumerated events occur that naturally delay the project's completion which occur that are outside the general contractor's control

What Does BR Cover?

- **Hard Costs Coverage: “Sticks and Bricks” or “Bricks and Mortar”**
 - Generally covers physical loss or damage to an unfinished building or project and/or the building materials as a result of a covered loss
 - Would cover such things as actual construction expenses associated with and/or necessitated by the covered loss
 - Examples: costs of material and labor
- **Soft Costs**
 - Available as a separate coverage under a Delay in Completion endorsement under most BR policies (for a separate premium) which extends for a certain period of time after the project’s anticipated completion date
 - Often contains a “time deductible” pursuant to which coverage does not kick in until the 30 days or whatever respective period has passed

What Does BR Cover As It Relates to Soft Costs?

- Soft costs (ISO form specifically lists a number of covered areas):
 - Interest upon money borrowed to finance the contract work;
 - Realty taxes and ground rent, if any;
 - Advertising and promotional expenses necessarily incurred;
 - Costs of additional commissions incurred upon renegotiating leases;
 - Architects, engineers and consultant fees;
 - Project administration expense;
 - Legal and accounting fees;
 - Insurance premiums;

Case Study

- Building explosion in the boiler room of a luxury beachfront high rise condominium building on the day the penthouse unit is scheduled to close prior to the post-2008 housing market collapse caused by the accumulation of gas in the boiler room when they were working on a gas line
- Overlapping commercial insurance policy had been procured by the Condominium Owners' Association which covered damage to the building's common elements
- Building suffers considerable damage to both the common elements and individual units, including some of the developer-owned units, thus triggering coverage under the overlapping commercial policy
- BR policy in question involved the participation of a syndicate of no less than five insurers (including a separate Lloyds syndicate) and the policy was an amalgamation of multiple insurers' forms

Case Study continued

- Policy language:
- The expense must be listed in the definition of “Softs Costs/Additional Expenses.”
 - Interest upon money borrowed to finance the contract work;
 - Realty taxes and ground rent, if any;
 - Advertising and promotional expenses necessarily incurred;
 - Costs of additional commissions incurred upon renegotiating leases;
 - Architects, engineers and consultant fees;
 - Project administration expense;
 - Legal and accounting fees;
 - Insurance premiums;
 - Other Expenditures, as accepted by the Company and scheduled in the Declaration of this Endorsement

Case Study continued

- Policy exclusions
 - “Other Expenditures” were further limited by an exclusionary provision that any such “expense[s] must be acceptable to the Insurers”
 - Exclusion applied to “claimed expenditures that ‘are any consequential loss including but not limited to loss of market’”

Case Study Continued

- Disputed items included:
 - Overlapping expenses
 - Unsold developer-owned units
 - No business or loss of rental income had been purchased, but yet was included in the Proof of Claim
 - Apportionment issues between the BR policy and the COA's commercial insurance policy

What Are Some of the Non-Covered And/or Specifically Excluded Items That May Generate Litigation?

- Overlapping items
 - Multiple sets of individuals and/or firms being claimed as necessary for a particular item
- How long the coverage is good for: was it extended to the point where construction actually had been completed
- Lost business or lost rental income
 - Unless this coverage was completed, a BR policy with a soft costs endorsement will not include such consequential damages

Other Issues to Consider in BR Coverage Disputes/Litigation

- Construction Contracts and Limitations on Indemnity Under State Law: Florida Statute Section 725.06
- Attorney's fees entitlement
 - State law specific
 - Coverage counsel vs. litigation counsel for the insured
- Other forms of overlapping insurance
 - Building owner/COA may have purchased a Commercial Property policy that may provide coverage for some of the same items as the BR policy
 - Can be an alternate source of recovery
 - Typically may only cover the damaged common elements of the particular structure, but not damages to any particular units
 - Need to ensure coverage was effective when the incident occurred, i.e. who held the insurable interest in the building at that time
 - BR policy may have "other insurance provisions" that may come into play in this scenario

Questions?



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