THE CAPITOL FORUM

AIA California Council

Insurance for Residential Multi-family/Condo Projects

AN EXECUTIVE SUMMARY PREPARED FOR THE AMERICAN INSTITUTE OF ARCHITECTS CALIFORNIA COUNCIL and THE CAPITOL FORUM

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Executive Summary

The prime objectives of this project are: identify insurance companies writing project specific policies for condos/residential projects; identify underwriting criteria for residential policies; and, OCIP/CCIP /OPPI availability.

Project policies were originally designed to be purchased by design teams for their own protection, but owners and contractors began buying them and using them as contingency funds. In addition, when claims were filed, it became impossible to effectively defend against them due to “finger pointing” among the insured’s. Losses became “horrific” to quote Jack Doran, co-president of Arrowhead Insurance (he headed the project policy program for DPIC, now defunct). Since 2002 most of the larger, well known insurance companies have stopped writing them except for very large projects with existing clients, and rarely if ever for residential. The policies are heavy with exclusions (condos being one), have high deductibles and hefty premiums that often keep them from being commercially viable.

Five traditional (admitted) insurance companies will write project specific policies: Avreco, Zurich, Lexington, Schinnerer, and Liberty. Lexington is the most aggressive of the carriers and has the most comprehensive project and OCIP policies. No one has written a project specific policy for condos/multi-family or strictly residential in California. The main reason seems to be that in addition to the high risk inherent in this kind of project, the 10 year statute of repose is unacceptable. In addition to Lexington, Zurich and Liberty also write OCIP policies. Details, by company, are included later in this report.

The good news is that there are surplus lines (non-admitted) insurers currently writing both project specific and OCIP/CCIP/OPPI policies for condos and other residential projects in California. These carriers specialize in providing innovative insurance solutions for design professionals. Products include design professional liability, project primary professional liability, errors and omissions coverage, project insurance, and owner controlled coverage.

Jason White, a surplus lines broker in Southern California, wrote half a dozen project policies last year and just completed writing one for a large condo project in Los Angeles. Policies typically provide active coverage for the entire design team from the date design begins through construction completion. They offer up to a 10 year tail, limits up to $25 million (although most fall in the $5-$10 million range) with a minimum premium of $250,000 on a $1 million limit. The value gets better at higher limits on a percentage basis. Most successful policies are driven by owners who team up with their architects, although they can be bought by architects alone. An overview from Jason is attached.

Surplus lines carriers employ underwriting criteria that relies heavily on risk assessments of the lead designer and team. To that end, many provide risk management services such as contract review, design professional briefings and workshops, risk management presentations and pre-claims assistance. In addition, many track by building type, with Types I and II being most desirable, although they will write them for Type III. They will not write them for frame or stick construction. Other areas of concern include roof size (water exposure), acoustics, and smell; also whether it is new construction, a tear down or rehab. Capacity is generally up to $25 million with the desired minimum annual written premium for a professional liability program at $10 million. Most will consider smaller programs depending on the profitability and ease of implementation, and consider writing larger accounts on an open brokerage basis.

Standalone wrap ups are typically for very large projects, up to $150 million, and very expensive. They can offer professional liability for the design team and an extended reporting time of ten years. Arch Insurance has recently begun to advertise a wrap up policy that offers true professional liability insurance, bodily injury/property damage, economic loss and errors and omissions. The policy is very expensive, and can only be bought by owners and contractors. However, if an architect has a solid working relationship with the owner, the design team can be covered.

Traditional carriers understand that it is currently a soft insurance market, and faced with competitive pressures they are becoming more flexible. Premiums and deductibles, while remaining costly until a track record of losses is established, are dropping from all time highs. Meanwhile, surplus lines carriers, which can only be accessed through wholesale brokers working with retail brokers, are filling the void and providing viable solutions.

Background and Research Methodology

In order to accurately assess available policies and underwriting criteria, a questionnaire was sent to contacts known by members of the Forum group within the insurance industry. The objective of the questionnaire was to identify carriers writing project and/or OCIP/OPPI policies for residential/multifamily/condos and if those carriers track loss history based on construction type.

Contact was made with Terry Canela, AIA, and Bill Nichols, Chair of the AIA National Risk Management Committee. Bill's committee recently surveyed 15 carriers on Professional Liability issues. The survey contains information on underwriting restrictions, including residential and condo based; restrictions on specific hazards; policy terms and limits of liability; a ranking of premium determinations in order of importance; and, project specific insurance. Results have been sent to Paul Welsh and are available.

The survey did not specifically address multi-family/condo project policies, OCIP /OPPI policies, or tracking loss histories relative to construction types and building height. Therefore, a slightly amended AIACC questionnaire was sent out to the national survey participants, followed by telephone conversations with several of the respondents.

Surplus lines vendors and brokers can only be reached through retail brokers, and Tim Corbett, a risk management consultant, was instrumental in bringing this information to light. Leslie Pancoast, IOA Insurance Services also offered contacts for follow up. There is more specific information and contacts per company at the specific company websites and through the Surplus Lines Association of California.

Project Specific Policies and Underwriting Criteria

As stated, traditional carriers have moved away from writing project policies because they are very risky, expensive and usually not commercially viable. When project policies are written, and only 5 out of the 15 carriers surveyed by AIA will consider them, the closest they come to residential is mixed use projects, preferably in combination with a hotel that will be responsible for overall building maintenance. Loss histories are not tracked by building type because they do not write enough policies to make it worthwhile, but projects must be of commercial grade construction. None of the traditional insurance carriers I contacted have written a condo project policy in California.

Here is an overview of traditional companies:

Avreco: Linda Deiss, VP , stated that Avreco will write project policies, however they are only on an annual basis, are for small jobs, and they would not do condos. They do not write OCIPs.

Schinnerer: Kate Enos, VP of underwriting from Schinnerer (VOSCO on the AIA survey) shared that they do not do project policies for multi-housing because for every dollar that comes in, three go out and therefore, they cannot afford to offer them. They will consider project policies with a lot of underwriting for long term clients and projects with which they are comfortable and which the firm normally handles, and they may offer excess/supplemental insurance on a limited basis. They do not write a lot of OCIPs, but will for specific projects.

St. Paul Travelers: Both John Droutsas and William Farron, Practice Leader, responded to the questionnaire with negatives throughout. They write over 7000 policies nationwide but not project policies or OCIPs. They do not track loss histories by building type.

XL Insurance: Tom Bongi only offers practice policies, no OCIPs or project policies. He states “Condos are too high a risk to take on.”

Euclid: Brian Van Cleave responds they do not write any project policies and little condo.

Arrowhead: Jack Doran responds much the same. They do not write any project policies, no OCIPS, and therefore do not have relevant claims data. Jack used to run the project policy group at DPIC but had very bad experiences with them.

Benchmark Professional: Kitty Dimit, President, responded that due to the severe adverse loss experience with condo projects, Benchmark discontinued offering project specific policies and practice policies with significant condo projects 20 years ago. However, even with strong risk management procedures in place, 38% of their claims are on residential projects. Of that number, 10.2% were condos. Further, 52.2 % of the claims were made by the client, 15.6 by a 3rd party, and 11.2% by the general contractor. While they do not track the # of stories they do track construction values and histories show that the larger the project, the more severe the damages. Interestingly, smaller projects seem to have the same frequency of claims. The stats appear to reflect that those design professionals who occasionally design residential projects are just as likely to have a claim filed against them when compared to design firms specializing in residential projects. Benchmark looks at proper client selection, good contract language, contingency funds, insured sub-consultants and HOA manuals when assessing risk on residential projects.

<u>Zurich</u>: Ray Bustamante, Product Manager, responded that they do not insure stick frame or attached residential construction under either their project a/e or OPPI program. They will insure residential units that are part of a commercial project on an OPPI basis. Mike Davis, also a Product Manager, added that Zurich will write project policies, but they are so expensive many view them as "contingency funds" or "risk funding" because premiums on a $3 million dollar limit can be as high as $2 million. Mike added that Zurich does not write residential or condo exclusions on their policies and does not place restrictions on the project. Zurich writes very few project policies, preferring to write OCIP/OPPI policies which can offer some protection to the architect in excess to their practice policies. Some of their OCIP policies include professional liability as well as general liability and excess coverage.
While underwriting criteria is proprietary information, Mike shared that they look at locations, high end vs. low and do not track by type I, II, III. Knowing the developer and the design team, having a current practice policy with Zurich and a clean track record are critical. He added that Zurich has a 10% cap on condos across the board for practice policies, but is flexible on individual policies citing the unprofitability of the class as a whole and the need to limit exposure on the books. Mike is open for discussion on policies and understands the architect's needs.

<u>Liberty's</u> Rob Cunningham, VP of Underwriting, states that they have 25 project policies on the books for schools, court houses and convention centers, but no residential because they are cost prohibitive. However, they have insured a mixed use project in San Diego with a $2 million dollar limit. Rob would like to do more project policies and offers the following tips: brokers need to ask more questions on applications to clearly identify the stakeholders, the scope and type of project (mixed use is less risky than straight residential). While they have not written a project policy for a condo, they have a self funded "alternative risk policy" on a project in Nevada. It is a 10 year policy with the limit fully funded by the developer. Liberty sets up the fund and provides claims handling services. Rob also writes excess project policies. He would like to see brokers take the lead (or maybe the AIA) on forming a "pool" of carriers who would mitigate the risk on project policies by partnering on larger projects and each taking a portion of the risk and the premium.

Bearsdley: Jerry Sullivan, Product Manager, says they do not write project policies, and they do not offer OPPI or OCIP policies because they feel it is not good for the architect. (This was expressed by several responders) Jerry used to write project policies and directed me to Bob Rogers @ Lexington because he thinks they are the only company really writing these programs.

Lexington Insurance takes a different approach. Instead of staying away from project policies they took a more active role in managing them and are actively looking for more. Bob Rogers, AVP Architects and Engineers, estimates they write 40-50 project specific policies per year of which 3-4 are mixed use (hotel with condos) and maybe two are residential. Except for apartments, which are considered commercial, they have never written a residential project policy in California primarily because of the 10 year statute of repose and the aggressive legal environment.

Project policies from Lexington are primary policies and offer professional liability. They cover only the lead design professional and sub consultants. This "team coverage" means that all are bound by a joint defense policy that provides one remedy and eliminates "finger pointing". The policies do not cover owners, contractors or developers, and a lone sub-consultant cannot buy one. Policies are offered independent of whether or not there is a practice policy in place; however, an existing relationship is a definite advantage.

- Pricing: 20-25% rate on line, premium over limit which means a policy with a 5 million dollar limit would carry a 1.25 million dollar premium and a $250,000 deductible (ball park number). This is cost prohibitive in many cases and may not be commercially viable which is why so few are written.

- Endorsements: all project specific policies carry a material variation endorsement with a specific allowed variance. This endorsement keeps the cost of construction within the contracted guidelines and guarantees that the risk at the beginning of the project remains essentially the same throughout. All projects are inspected on a regular basis (6 month intervals) to insure compliance. In addition, projects in California are required to contract with an inspection company like Quality Built who will make site visits, take photos during construction, create a paper trail and provide a "stamp of approval".

- Apartment policies carry a condo conversion endorsement that will either negate the insurance or raise the premiums.

Underwriting: Risk assessments include information about the design team, owner, contractor, construction value and scope of the project. Single family tract housing is the least desirable, followed by condos and townhouses. They will not cover frame housing and usually require commercial grade steel construction. There are currently 5 regional underwriting team members for project policies.

The quality of the contract with other stakeholders is also examined. They look for a "professional" standard of care vs. heightened, and a fair allocation of responsibilities.

Project specific vs. OPPI: AIG writes OPPI policies for residential, however they prefer to write project policies and write more of them because of better quality and easier to defend against suits because there is no need for multiple defendants and lawyers. They are considered to be "excess funds" and all available insurance must be exhausted first.

Bob Rogers is the contact for multifamily/condo and residential projects at this time, rather than the regional rep.

OCIP/CCIP Policies

These "wrap insurance" policies were originally designed for residential projects; single family, townhouse and condo. Most do not offer professional liability, but do provide general liability insurance that cover bodily injury and property damage, insure everyone on the project, and terms that cover the statute of repose. Endorsements are available for mixed use and commercial, but typically exclude residential. However, the market is expanding, the rates are dropping and terms are being extended. Different terms and premiums are available, and while some traditional carriers will write them, the feeling by the professional liability people is that there is a conflict involved for architects and engineers in that the practice policy must be exhausted before the OCIP coverage can be accessed. OCIPs are typically written by different departments within the company than professional liability and many retail brokers are not aware of them. The real players in this market are the surplus lines carriers and surplus lines brokers who feel that the OCIPs are a "clean" way to handle liability, and as noted above, one carrier, Arch, has begun to advertise a policy that includes professional as well as general liability.

Surplus Lines Insurers (Non-admitted)

While many traditional carriers have moved away from both project specific and OCIP/OPPI/CCIP policies, surplus lines, or non-admitted insurers, have moved into the gap. These carriers offer products and policies that traditional carriers find too risky, and can only be accessed through wholesale brokers who in turn work with retail brokers. They are a growing segment of the insurance marketplace and have outperformed general commercial lines over the past 10 years.

Tim Corbett, an AIA member and risk management consultant in Pasadena, works with architects and wholesale brokers to obtain project specific policies on condos and residential projects. Stating that 80% of all claims are driven by non-technical business practices and come from owners/clients, Tim works with clients to assess and mitigate risk so that surplus lines carriers, who focus on the design team and management experience, will accept them. Tim has written several project policies that cover professional liability and 10 year tails to cover the statute of repose. Typically, these carriers will require a third party vendor such as Quality Built to inspect projects at certain milestones and present a portfolio for inspection. A list of current residential projects that are insured either by a project specific policy or wrap policy from surplus carriers is attached. Jason White, a surplus broker specializing in A/E policies works mostly with Admiral and Aspen. He is extremely experienced in this area, shared policy information found in the above executive summary, and offers many solutions. His brochure on these programs is attached.

Jett Abramson, a wholesale broker specializing in wrap and OCIP policies, reports that traditional carriers are excluding or limiting residential projects from even their practice policies, so surplus lines vendors are advising architects to go back to their carrier and ask that only the bodily injury and property damage be removed. This gives them coverage for economic loss and professional liability on their practice policies, and they can then go to a surplus carrier for the BIDI on a wrap policy. He states that project policies he has written do not include sub contractors and he always looks to make sure the right management processes are firmly in place.

Here is a partial list of surplus lines insurers who write project specific and OCIP policies on residential projects: Interstate, Rockhill, American Safety, Arch, Navigator, Aspen, Liberty (a London company) and West Chester. A complete list of insurers can be found on the Surplus Lines Association of California website www.sla-cal.org

Next Steps

The information in this report identifies key insurers for project policies. At this time the admitted company representatives have been personally contacted, however, the surplus lines information has come from brokers and consultants, not the companies discussed. I do have contacts that can be made, and the committee may want to consider sending a questionnaire, with follow up, to non-admitted insurers for more information.

Contact List for this Report

For more information on California surplus lines and risk management services contact:

Tim Corbett (risk management consultant) @ 626-665-8150.

Or have your retail broker contact the following wholesale broker:
For OCIP policies:
Jett Abramson Bliss & Glennon 310-372-9115 ext. 1355

For project policies:
Jason White Managing Director: Swett and Crawford 213-439-3417
Ken Miller (retail broker who does a lot work with surplus brokers) 310-526-1810

For more information on traditional carriers writing project policies, contact:
Lexington: Bob Rogers, Lexington is located in Boston @ 617-330-8564.
The contact for OCIPs is Tom Grandmaison @617-345-4130
Liberty: Rob Cunningham, VP Underwriting 212-208-2814 New York
Zurich: Mike Davis, Product Manager 215-979-6639 Philadelphia
Schinnerer: Kate Enos 301-951-6919 Washington, DC
Avreco: Linda Deiss 312-294-5475 Chicago