SPECIALTY LINES MARKETS

NAILING DOWN OPPORTUNITIES IN CONSTRUCTION

Agents, underwriters and specialist intermediaries adjust to "the new normal"

By Dave Willis

The average annual 2010 unemployment rate for the construction industry was 20.6%, according to U.S. Labor Department figures cited by construction trade group Associated Builders and Contractors (ABC) in its January 2011 *Construction Economic Update.* That compares to 19.0% in 2009 and 10.6% percent in 2008. One bright spot, according to ABC: The nonresidential building sector, while still losing jobs in December, was up from the same time a year earlier—the first year-over-year growth since August 2008.

Such statistics tend to track construction insurance industry observations. "We've seen our customers' payrolls stop falling as dramatically as they had been," says Mark Jorgenson, executive vice president, Bituminous Insurance. "We actually did start to see a bit of an uptick in the latter part of the year in the oil and gas segment."

Jim Jinhong, senior vice president, underwriting, NBIS, has seen pockets of increased activity, too. "For the most part, they're isolated to firms working in the petrochemical refinery business," he explains. "We're also seeing a bit of an increase in commercial construction in Midwestern states as it pertains to equipment leasing operations."

According to the economic update, ABC Chief Economist Anirban Basu says the construction sector is poised to underperform in the year ahead, due to a number of factors, including dwindling direct impact from stimulus spending and an ongoing malaise in commercial real estate.

Another factor is a recent U.S. House of Representatives vote rescinding guarantees that Highway Trust Fund reserves would be spent on highway and transit programs. The move met with widespread disapproval from groups ranging from the American Association of State Highway and Transportation Officials to the U.S. Chamber of Commerce. "That has some of our highway and bridge contractors pretty concerned," says Jorgenson. "We'll keep a finger on that."

With construction projects in short supply, competition is intense. "It's hyper-competitive, because the work is so thin," says Jorgenson. "We're seeing a lot of new entrants—for example, specialty commercial contractors looking to do work they've never done; but because they might have some equipment, they're willing to try. So they bid." Projects that may have drawn three or four bidders before attract 10 or 12 or more now, he notes.

In such an environment, owners and large general contractors tend to have the upper hand. "Additional insured issues continue to be a challenge," says Jorgenson. "Owners and GCs continue to look to include in contracts insurance terms that are in their favor."

A drop in work brings with it risk management implications. When contractors don't have as much revenue or cash reserves, it's tough to maintain an emphasis on safety and risk management. Equipment maintenance, safety plan compliance and even adequate site supervision suffer.

In some situations, a silver lining exists, according to Jorgenson. "We have customers that have the best of their workforce left," he explains, "and that has a positive effect. Contractors are not out hiring new people, and new people are the ones who tend to get hurt most often. That means frequency of losses, workers comp losses in particular, is declining even more dramatically than you might expect."

Insurance impact

Construction insurers are directly affected by the state of their clients' business. "We're operating in what seems to be a new normal," notes Tim Cappellett, vice president, sales and marketing, at Oryx Insurance Brokerage. "The market continues to be soft. Premiums follow payrolls. But overall, our (January 1st) renewals were flat."

Jinhong concurs. "For the most part, we're maintaining rates, but with a decrease in ratable revenues, we're still seeing premiums go down." He finds this distressing because, he says, severity doesn't necessarily diminish just because ratable revenues are down. "Actually, we're getting less rate for the overall exposure," he explains. Thorough, well-informed underwriting is key to a profitable book of business.

Admitted insurance markets are active in the construction arena, Cappellett notes. "I don't see much E&S movement, which would indicate a hardening of the market," he says. "Companies are figuring out ways to be profitable."

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Risk management diligence is key. "We're a managing general underwriter," says Jinhong, "but we take a very large share of the risk in each account we write, so we don't skimp where risk management is concerned." Among the firm's tactics are thorough contract reviews. "One thing we do that delivers proven, quantifiable results is review the daily business contracts each one of our clients signs," he adds, from rental agreements to bills of lading or cartage agreements.

"Having a carrier available and willing to support contractual review is a significant value-added service for contractors," he adds. "This is especially true as they're cutting back and, for example, instead of having four or five site supervisors they have one or two hustling around."

Delivering extra value is important, Cappellett notes, particularly as insurance professionals adjust to the "new normal" he described. "You really have to adjust business to what it is now, and concentrate on what you can do to better your situation," he explains. "There's no sense looking outward and hoping things will change—that the construction business will change, that the insurance marketplace will change, that pricing will change.

"You can't control that," Cappellett adds. "What you *can* control is what you provide your customers. That's the direction we've taken." As his firm marks its 15th year as a construction specialist, he points to a clear focus on delivering underwriting, loss control and claims administration as factors contributing to the company's success.

Practical advice

Cappellett encourages retail agents to take the same approach. "Agents who want to succeed, who want to set themselves apart, can't just touch construction accounts anymore at a six-month review or at renewal," he says. "They need to work every single customer, all year long. They need to understand how to integrate claims and loss control, how to proactively work with carriers to keep a program healthy."

Jinhong says agents can better serve clients by helping with contracts. "Construction firms are concerned about maintaining a competitive marketplace advantage without assuming onerous contractual requirements," he explains. "When there is very little work, companies and general contractors are asking for broad indemnification provisions, onerous additional insured requirements and other amendments that adversely affect the insured—and the carrier."

Agents can work with the client's legal team and carrier to help insureds negotiate the best possible contract, Jinhong adds. "The agent needs to make sure coverage is in place that satisfies whatever terms and conditions end up in the contract," he says.

Adds Cappellett, "If I were an agent, I'd want to be able to make sure the insured was not breaching any contracts they've signed."

According to Cappellett, success in the construction marketplace calls for a high degree of specialization. "Agents need to be able to speak the contractors' language, understand their business, and help them succeed," he says. "You can't be a generalist if you want to grow your business in the construction markets."

Agents should be versed in coverage options and carrier strengths, as well, to help contractors through difficult buying decisions. Marketplace options, Jinhong notes, range from large, national carriers to boutique firms focused exclusively—or nearly so—on the market. Price versus after-the-sale service and specialization are factors an agent needs to understand and explain, he adds.

When dealing with carriers, agents should understand what kind of risk management support systems will be included with the policy, Jinhong says. "Also, explore the company's experience in running a particular class of business. Many classes of contractor business are increasingly appetizing to carriers because of the big rate. But with a big rate comes severity."

Underwriter expertise is critically important. "I've been underwriting our classes of business, high severity business, for 15 years, and I still learn new things every day," Jinhong says. "I shudder to think what's happening in the minds of underwriters at carriers that come in and chase this high premium.

"We stick to a very specific subset of classes in which we've spent the time and energy to achieve proven proficiency," he adds. "Once you start roaming into uncharted territories, you start assuming risk you cannot contemplate or that wasn't contemplated in the underwriting process."

Jinhong encourages agents to make sure the carrier claims force is specialized and equipped to handle high severity issues. "If you have an inexperienced adjusting staff out there, claims could show up on loss runs that shouldn't be there," he says. "Plus, contractors risk lost time on the job or lost work due to a bad reputation if a carrier isn't walking in lockstep, supporting the insured."

He also warns about chasing the lowest premium. "Buying insurance from the lowest price carrier doesn't necessarily contemplate onerous deductibles that may be applied for claims that, quite possibly, the insured shouldn't be liable for," Jinhong explains.

"A carrier may be cheapest this year, but five years ago they wouldn't touch the class of business," he adds. "The adage goes, 'Accounts won on price will be lost on price.' If you want to undercut the market and write an account for a single year, go ahead. I'd rather be a fairly priced, well-informed underwriter."

Jorgenson concurs. "Our very best agency partners are those that earn trust over time and, as a result, have something to sell other than just price."

Finally, Jinhong explains, compare apples to apples. "A lot of carriers out there, particularly in this market, will offer a very basic type coverage—a CGL policy that may have some enhancements," he explains. "But do they offer things like riggers liability, upset and overturn pollution coverages or sudden and accidental pollution coverage? Is their policy going to conform to over-the-road regulatory requirements for contractors mobile equipment?

"Agents need to know their customers, know the coverages they need, and know the best way to meet those needs," he concludes. ■