

Notes on Edge-Howdens Insurance Round table – 15th July 2021

Note: The round table was held in accordance with the Chatham House Rule and comments are unattributed

State of Play:

- There is a significant problem at the moment for insurance for the construction industry – both PII & contracting.
- Construction has become loss making for insurers leading to many of them leaving the market. Losses now long-standing and construction 2nd worst performing class at Lloyds.
- The insurance market has become severely restricted with syndicates writing smaller levels of and greater restrictions on cover.
- All industry now effected by difficulty of getting insurance or high premiums
- Contractors increasingly under-insured or not insured at all
- Some surveyors and valuation firms now paying 27% of turnover in insurance costs just to stay in business
- Bigger businesses are aggregating their insurance in order to get cover
- SMEs are disproportionately affected by rise in PII costs and are really suffering
- At the same time professional fees have been getting lower & lower – it may no longer work financially
- Lack of confidence in the ability of construction to get it right
- Lack of confidence from contractors in consultants to get it right
- Some Institutions are attempting to protect their members by enforcing standards, protocols etc.
- The construction industry has got the insurance industry it deserves!
- The situation will not return to 'pre-Grenfell'

Causes:

- Grenfell & subsequent work of building safety investigations, inc. exposure of numerous failings
- The bankruptcy of Carillion
- Huge insurance losses on big project-based insurance schemes (e.g. Wembley Stadium)
- Traditional project procurement, with its focus on low cost/quality (see also value engineering) and adversarial approach, has led to massive losses
- Design & Build has resulted in low quality projects that are rapidly accumulating into a substantial risk (but D&B can work if the design team are appointed at the same time as the contractor).
- The normal soft/hard cycle lasts around 7-9 years, but the most recent soft market lasted 15 years and drove premiums down to an unsustainable level, eventually leading to market failure and a massive over-correction (it's not just Grenfell).

Issues:

Risks & information

- It is essential for clients to know that insurance will be there at point of claim
- Insurance is not a benefit to clients but a defensive mechanism for the construction industry
- Risk is being mispriced
- Inability of companies to provide adequate information to insurers
- Requirement for much greater diligence

- Losses principally due to structural errors, sourcing decisions, value engineering, poor auditing and overpromising: i.e. frequently bad project management.
- Liability – Net contribution clauses now very rare in appointment terms, sometimes still getting limits on liability
- Layers upon layers of insurance (with no single point of contact) means costs and costs of claims (and legal fees) cascading.
- It may be impossible to ever find final layer of insurance cover
- The wording of Contractor All Risk Insurance contracts both draconian and impossible to understand
- The self-reporting system has broken-down/failed

Availability

- EWS1 requirements causing extraordinary problems and pressures for both leaseholders and landlords. Leaseholders need help.
- Consultants and contractors not able to get cover for fire and cladding risks
- Clients &/or their PM advisors are insisting on high levels of insurance even for work (i.e. strategy advice) with negligible risk and only low fees. PII should be proportionate

Costs

- Cost overruns often have other insurance-related ramifications
- Getting sucked into a claim process can be extremely burdensome, costly and distracting for SME's so a great deal of effort put into avoidance
- Reputational damage to companies and the industry at large (a claim can close down a business)
- Very different levels of insurance available between major insurers and Managing General Agents (who cover SMEs)
- The Building Safety Bill, while welcomed, is going to lead to high levels of administrative/unproductive work at a time when the industry is already struggling. It will take time for its effects to play out, especially the new extended liability period

Performance & improvement

- Innovation and sustainability being stifled by inability to get cover (e.g. for using any flammable materials)
- Implications for materials choices for retrofitting and so barriers to reducing carbon etc.
- Performance monitoring (POE) is being prevented by the perception from the insurance industry that it will only dig up problems. Yet it is essential if the industry is going to improve its act
- How can the industry tackle issues like climate change if PII discourages innovation and is so resistant to change?

Procurement

- Not necessarily one guiding hand throughout the design to delivery process – Design and build can work if the architect is appointed at the outset and remains to completion
- Lack of clarity about responsibility, hard to manage risk – passing the buck is endemic
- Major insurers need to start practicing non-adversarial procurement on their developments
- Tier 1 contractors are dead (Ref-Mark Farmer)

Basic housekeeping

- Don't operate outside core competencies
- Pay attention to appointment and contract terms
- Keep accurate records
- Ensure subcontractors have adequate insurance
- Credit control
- Client requirements to be adequately defined. Limit scope of appointments so not to take on more responsibility than required
- Check whether projects under-funded or not
- Reduce/mitigate risk/exposure to risk
- Need for a close relationship with underwriters – they must know & understand their clients' businesses
- Be pro-active

Short-term challenges:

- How to mitigate risk
- How to provide/share far more information
- How to increase transparency
- Getting clients to accept appropriate levels of insurance for their project
- Dealing with the Building Safety bill

Long-term challenges:

- How to prevent excessive off-loading of risk down the supply chain (the current system is designed to achieve just this)
- Size (of businesses) matters more that it should. How should SMEs/microbusinesses be supported? (Note: 50% of architectural practices are 5 or less).
- Developing an insurance market that offers a wider range of products
- Developing a stable working response to the Building Safety Bill that achieves its ends
- Finding solutions that work for the collective industry – including clients

Actions required

- Risk mitigation/reduction – an industry that is more risk-aware and risk based
- Means for information sharing, interpretation and alarm raising on near misses and emerging problems
- Finding new ways to enable innovation and creativity in the industry without attracting unsustainable insurance costs
- Thinking boldly and imaginatively

Barriers & blockages:

- The insurance industry recoils at change and is not facing up to gathering challenges
- Insurance is backwards looking based on a claims-made approach
- BIM requires sharing information – anathema to insurance companies
- Insurers focusing on individual companies rather than integrated (and long-standing) teams or project by project
- Risk & responsibility transfer (dumping) rather than risk reduction
- Consultants are being deskilled by a procurement process that separates concept design (for planning) from delivery and detailed design. A 'golden thread' does not run through the whole process.
- The complexity of the design and contracting process requires everyone/thing to be right together and the insurance process must understand and support this.
- It is difficult to achieve change and look forward in a hard market

Potential solutions

- IT and digital systems for design and management and particularly for the provision & sharing of information (e.g. obtaining relevant information from digital twins)
- Project insurance & IPI
- A change in process to Project Team Alliancing with single insurance cover and incentives for collective success → no claims bonus → no PII → projects signoff → inherent defect insurance going forward
- MMC – generally a good thing (ref. Farmer), but with the risk of single defects being replicated and massively multiplied.
- Collaboration across the industry and especially between design and contracting is key to improving our product and reducing risk
- Government taking responsibility on risk for post-Grenfell remedial work in order for the industry to be able to carry out the necessary work.

Questions:

- Is current problem a cyclical issue or a downward spiral? Does it represent permanent change?
- Why do we have a high claims problem in the first place?
- Is it possible to split insurance calculations to prevent double cover (e.g. for both PII and IPI)?
- Can insurance cover reflect better performance/higher quality?
- What should the industry look like in 3 or 4 years time?
- What model of insurance would work for it?

Messages

- The current procurement processes are building up problems and it needs to be thoroughly altered.
- Industry change in response to issues, including Grenfell, climate change etc., is coming fast and insurers must play their part
- The insurance market must use its collective muscle to change the construction industry for the better
- There is a case for Government intervention if it leads to longer-term solution. Change may need to be driven by legislation
- Importance of work on system change to mitigate risk
- Joint and several liability needs to be rethought
- Re-establishing the golden thread and carrying through from project inception to delivery is essential
- Post occupancy evaluation (POE) must be encouraged by the industry and the POE period should not form part of the 'service period' for liability.
- Insurance calculations should reflect alternative approaches (e.g. IPI on some projects) – no double counting
- The true financial benefit of good practice may be a massive saving on lawyers' fees rather than lower insurance
- Agreement that IPI is a great idea – but it now needs to be rolled out on all sizes of projects
- After 300 years of insurance it's time for something different/radical
- Covid has shown that it is possible to work in dramatically different ways – this could be fundamental in achieving change