

INFORMATION RELEASE 93-1

CONSTRUCTION PROJECTS

April 19, 1993

INTRODUCTION

This Information Release has been prepared because of the great deal of confusion regarding insurance coverage relating to construction projects of Member Districts. It is often the case that the Member District assumes that the Contractor either was required to provide course of construction coverage or has provided such coverage and neither fact was true. In other words, the construction contract was prepared by an architect who either put in no insurance requirement or an inadequate insurance requirement relating to course of construction. Even if the contract requires that the Contractor obtain insurance, the Contractor may fail to provide a certificate or a copy of the policy to the Member District evidencing coverage. Each of these failures could have a significant adverse impact on the Member District because coverage under the property coverage provisions of the OSS policy are generally limited to \$500,000 (except as noted under Section 2.3 with respect to remodeling or reconstruction projects).

Section 1 of this Information Release generally requires that a Contractor of a Construction Project consisting of the construction of new buildings or structures obtain a "Builders Risk" policy covering the risks of loss due to fire, lightning, theft, vandalism and extended coverage endorsement, and all risk of physical loss excluding flood and earthquake. Failure to do so may result in the Member District being liable for any damages which may be incurred in excess of the \$500,000 coverage provided under the present OSS policy. In new Construction Projects Member Districts should require the Contractor to furnish them with a copy of the Builders Risk policy and to review it with their insurance carrier with respect to the amount of coverage, types of coverage, whether the coverage is primary and whether notification of termination or cancellation of a Contractor's insurance policy is required to be given to a Member District. The Member District should also review and compare the Contractor's policy with the OSS policy to determine what risks of loss are covered and whether there is a nonconcurrency between the policies.

Section 2 of this Information Release is substantially similar to Section 1 except that these provisions apply when the Construction Project consists of remodeling, reconstruction or additions to existing buildings. The Member District should be familiar with Section 2.3 of this Information Release which provides that if the estimated cost of completing a Construction Project is in excess of \$500,000, the Member District is required to report this to Industrial Indemnity (or the company then providing property coverage insurance) within sixty (60) days after commencement of such Construction Project. If the Member District fails to do so, the endorsement to the OSS policy which increases coverage from \$500,000 to \$3,000,000 would not be effective.

1. CONSTRUCTION ON NEW BUILDINGS OR STRUCTURES

- 1.1 Many construction contracts for a new building or structure require the Contractor of a given Construction Project to assume all risks of physical loss or damage to the Construction Project during the course of construction. Such risks of loss include the perils of fire, theft, vandalism and the like. Further, most construction contracts require the Contractor to obtain and maintain a policy of Builders Risk insurance to provide primary coverage against these same risks. Such policies of insurance are required to protect both the Member District and Contractor as their respective interests may appear in the property lost or destroyed.
- 1.2 When the Construction Project contract for constructing a new building or structure requires the Contractor to provide evidence that it has obtained a "Builders Risk" policy of insurance, such policy should cover risks of loss to the Construction Project due to fire, lightning, theft, vandalism and extended coverage endorsement, and all risk of physical loss excluding flood and earthquake. Both the Contractor and the Member District should be named as insureds under the policy.

- 1.3 Under the present OSS policy relating to property coverage for newly acquired property, each Member District has only \$500,000 of coverage for direct losses from any one occurrence (by a peril not otherwise excluded) for newly acquired buildings or structures, including those under construction. Since many new Construction Projects will exceed \$500,000 it is imperative that the Member District in its construction contract for a new building or structure require the Contractor to provide coverage for all risks of loss as outlined above in sections 1.1 and 1.2. It is possible that the Member District in the course of construction could pay the Contractor sums substantially in excess of \$500,000 and if the Contractor did not provide such coverage or such coverage should lapse, and there is no requirement that the Contractor notify the Member District on lapse, then the Member District could neither recover the funds expended nor would the Member District have insurance in excess of the \$500,000 provided under the OSS policy.
- 1.4 Each Member District is strongly advised to require that the Contractor or his insurance company furnish the Member District with a copy of the Builders Risk policy obtained by the Contractor and to have such policy reviewed by the Member District's insurance agent with respect to the amount of coverage, types of coverage, whether such coverage is primary and whether notification of the Member District is required in the event of any termination or cancellation of the policy for any reason.
- 1.5 Under the OSS policy providing for property coverage the coverage described hereinabove terminates on the anniversary date of the policy following the date on which the new construction is complete and such property becomes the risk of the Member District, unless the Member District files a declaration with Industrial Indemnity (or the company then providing property coverage insurance) declaring by location the additional value of the new construction. The insurer will charge an additional premium thereafter for the new property added to its coverage.
- 1.6 Care must be taken with respect to the amount of coverage for each construction contract for a new building or structure. For example, if a Contractor provides a certificate of insurance for \$10,000,000 but he has \$50,000,000 of new construction projects, then the coverage on the Member District's Construction Project would only be 20% of the loss. This analysis applies to every loss submitted. For example, if the Contractor's policy was for \$1,000,000 but your project was \$2,000,000 and there was a \$500,000 loss on a Member District's Construction Project, only \$250,000 of that loss would be covered under the Contractor's policy since the policy only covered one-half (1/2) of the total Construction Project cost.
- 1.7 In addition to all of the concerns outlined in the preceding sections of this policy, it is also important to review and compare the Contractor's policy with the OSS

policy issued by Industrial Indemnity (or any company then providing property coverage insurance). It is possible that the two policies may not cover all of the same risks and if a loss occurs that is only covered in one of the policies, the insurance carrier providing that coverage may not cover the damage based upon nonconcurrency between the two policies. For example, if policy A covers fire, lightning and windstorm damage and policy B covers only fire and lightning damage and, during the course of construction a building is severely damaged or lost because of windstorm damage, the carrier who included windstorm damage in its policy would cover only the percentage of loss that its policy covers compared to the total coverage. So for example, if each policy were for \$1,000,000 and the windstorm damage totalled \$1,500,000 then the company that covered windstorm damage would only pay \$750,000 of the \$1,500,000 loss (50% of the total coverage).

2. REMODELING, RECONSTRUCTION OR ADDITIONS TO EXISTING BUILDINGS

- 2.1 Many construction contracts for remodeling, reconstruction or additions to existing buildings require the owner of a given Construction Project to assume all risks of physical loss or damage to the Construction Project during the course of construction. Such risks of loss include the perils of fire, theft, vandalism and the like. Further, most construction contracts require the owner to obtain and maintain a policy of Builders Risk insurance to provide primary coverage against these same risks. Such policies of insurance are required to protect both the Member District and Contractor as their respective interests may appear in the property lost or destroyed.
- 2.2 Under the present OSS policy relating to property coverage, each Member District has only \$500,000 of coverage for direct losses from any one occurrence (by a peril not otherwise excluded) for remodeling or reconstructing existing buildings.
- 2.3 If the estimated completion cost of a Construction Project consisting of a remodeling, reconstruction or addition to an existing building is over \$500,000, the Member District is required to report this to _____ (or the company then providing property coverage insurance) within sixty (60) days after commencement of such Construction Project. If it is not reported, the endorsement to the OSS policy which increases coverage from \$500,000 to \$3,000,000 would not be effective. Notice to the insurance carrier should include the location, project description and anticipated cost of the Construction Project.
- 2.4 Under the OSS policy providing for property coverage the coverage described hereinabove terminates on the anniversary date of the policy following the date on which the Construction Project is complete and such property becomes the risk of the Member District, unless the Member District files a declaration with

Industrial Indemnity (or the company then providing property coverage insurance) declaring by location the additional value of the Construction Project. The insurer will charge an additional premium thereafter for the new property added to its coverage.

- 2.5 The Contractor is advised that any agreement entered into between Member District and Contractor shall include language similar to the following:

The owner will be responsible for providing the insurance during the re-construction or remodeling of an existing building, or additions to an existing building, and will protect the interest of the Contractor only on property that has become a part of the building. In other words, it will not cover supplies and materials which are on the premises but have not become a part of the building. The coverage will be fire, lightning, vandalism, malicious mischief, and extended coverage endorsement, and all risks of physical loss excluding flood and earthquake. If the Contractor wants to protect its interest against flood and earthquake, it may buy a separate policy from its agent.

There will be no insurance on any of the Contractor's equipment on the job. The Contractor will be responsible for insuring its own equipment and materials before they become a part of the building.

3. LIABILITY INSURANCE

Member Districts shall require that a Contractor who enters into a contract with the Member District for a Construction Project to provide evidence of insurance coverage for liability exposure with liability limits of \$3,000,000 for new Construction Projects, or \$2,000,000 for re-construction or remodeling of existing buildings, or additions to existing buildings. These limits should be a combined single limit of \$3,000,000 or \$2,000,000, respectively. The policy shall also provide coverage for broad form property damage. If the policy provided by Contractor contains a General Aggregate, then the liability limits should be at least the same as are required under the liability exposure policy. The policy must also contain an endorsement which makes each job site a separate aggregate limit.

4. DEFINITIONS

- 4.1 For purposes of this policy, "Construction Project" means the construction of a new building, additions to an existing building, and reconstruction or remodeling of any existing building, including the placement or relocation of portable buildings.

- 4.2 For purposes of this policy, "Contractor" means any person who enters into a contract with a Member District to undertake to construct a Construction Project.
- 4.3 For purposes of this policy, "Member District" means any school district which has become a member of OSS pursuant to the provisions of the OSS Agreement and Bylaws.
- 4.4 For purposes of this policy, "owner" means Member District.

251700DJ.F03