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REAL ESTATE DISRUPTOR

New Heights for Real Estate and Construction Firms Bring New Risks

It's more challenging than ever for firms that specialize in acquisition and ground-up development to make deals pencil out. Increased labor and construction costs resulting from today's strong economic climate, workforce shortages and highly valued assets trading are all impacting return on investments. Many companies that once invested independently are now considering alternative and more complex financing and partnership arrangements such as joint ventures, syndications and private investment funds to attract individual investors. These changes in deal complexity are often overlooked with respect to risk transfer.

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What insurance challenges are real estate firms and their investors facing today?

Property

The real estate insurance market has hardened over the past 12 to 18 months. Multiple consecutive years of adverse losses are causing insurance rates to increase, which has forced greater underwriting discipline. In some cases, this can make finding coverage more difficult. Several insurers have exited the real estate space, and this attrition is simply fueling the fire. In addition, double digit increases in property rates are not uncommon.

Firms with multiple investors or partners can consolidate coverages for their projects. By leveraging more premium with their insurer partners, they can create administrative efficiencies and realize cost savings.

Liability

Skyrocketing rates are frustrating habitational insurance buyers. Insurers are focusing on internal underwriting metrics such as "crime scores," which are determined by historical data, local jurisdiction and court rulings on violent crimes in a particular zip code—all of which affect the rate. As an underwriting example, it is not uncommon in today's marketplace for an insurer to sublimit or even exclude coverage for assault and battery claims.

Additionally, the lead umbrella layer pricing is out of control; the increases we're seeing aren't proportionate to the underlying rate increase.

Executive Risk

As more firms employ unique and diverse structures to finance their projects, they also face new risks that traditional Directors and Officers Liability (D&O) policies aren't built to cover. Since principal partners and their personal assets are targeted by investors and partners, this is a significant coverage gap especially for firms that raise private capital. There are better coverage options available to address the risk created by having a varied mix of investors, funds and joint venture partners.

Professional Liability

Many firms assume that because their subcontractors carry professional liability coverage, they are protected from claims alleging professional errors. Not so. For instance, if an architect goes bankrupt or if their professional policy is already maxed out due to losses, the real estate owner/developer could be left holding the bag.

Environmental Liability

Owners and contractors often overlook environmental coverage when they shouldn't. Whenever dirt is moved, an environmental hazard is created. Pre-existing conditions on acquisitions can also present environmental exposures; for example, mold continues to be a major issue for owners and property managers alike.

How should real estate firms approach an insurance purchase?

Given the hardening property market, real estate development firms should be mindful that rates are increasing, and at the same time the terms and conditions may not be as broad as in recent years. For instance, deductibles and limits provided for water damage on a builder's risk policy aren't what they once were. It's critical for an owner/developer to structure a builder's risk program that addresses their exposures appropriately, keeping in mind that they'll likely be paying more for potentially less coverage. Owners may also want to avoid relying on the general contractor's insurance program to provide the builder's risk policy, as this can be problematic when interests are not aligned.

How is Valent Group protecting complex real estate firms from industry-specific exposures?

We believe that developing a risk management strategy should precede any discussions of insurance. Our real estate team is experienced in handling risks for Fortune 1000 companies with property schedules in the billions of dollars. When we structure risk financing programs, we interface with clients to understand not only what they need or want for coverage this year, but we also need to know their plans for the next three to five years. This allows us to design their risk transfer program to match their future goals.

What makes Valent Group uniquely positioned to consult for the real estate industry?

Our clients benefit from working with a risk consultant who understands the real estate industry as both a buyer of insurance and a broker. As a division of EBSCO Industries, a global corporation with a variety of real estate holdings including multi-family and hospitality portfolios, we deploy EBSCO's knowledge, technology, processes and resources, creating a competitive advantage for our clients.