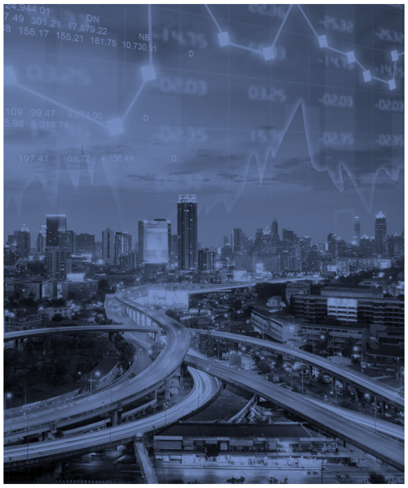
RYAN® TURNER SPECIALTY | new day

National Environmental and Construction Professional Liability Practice

2019 Market Update

NEWDAY.RTSPECIALTY.COM



The 2019 Market Update was developed to help the insurance industry at-large overcome environmental and construction-related professional liability challenges with best-in-class, strategic risk management solutions.

RT RYAN® TURNER SPECIALTY | new day

2019 Market Update

CONTENTS

Contact

RT SPECIALTY | RT NEW DAY

2465 Kuser Road

Suite 202

Hamilton, NJ 08690

P: (609) 298-3516

F: (609) 298-6254

newday@rtspecialty.com

NEWDAY.RTSPECIALTY.COM

Introduction

RT Specialty's Environmental and Construction Professional Liability Practice (ECP) is dedicated to helping agents, brokers, and their clients navigate the complex commercial insurance marketplace by identifying optimal risk management solutions. This includes providing the information necessary to make informed purchasing decisions on the numerous forms of environmental and construction-related professional liability coverages available in today's marketplace.

Our 2019 Market Update — an annual recap of the environmental and construction-related professional liability insurance industry with predicted trends for this specialty niche — represents the collective knowledge of RT's ECP specialists. This includes an annual survey of our staff to define the "state-of-the-marketplace," while offering insights into this highly-specialized field. In addition to uncovering specific market trends, the 2019 Market Update reviews the strategies needed to overcome challenges and protect against the risks that can potentially financially cripple businesses.

Throughout this report, the 2019 Market Update offers in-depth insights and trends information into the following environmental and construction-related professional liability coverages.

- ***Contractor's Pollution Liability (CPL)*** – In the CPL marketplace, carrier offerings remain abundant with expanding terms. The coming year will likely see stable premiums across all insureds for both project and practice programs. Leading motivators will continue to include pollution insurance requirements within contract specifications.
- ***Pollution Legal Liability (PLL)*** - Anticipate a generally stable, but competitive PLL marketplace for 2019. The underwriting trend of new PLL business continues to evolve with markets monitoring their offerings for various risk types. PLL activity during the last half of 2018 remained robust due to the advent of new markets, an up-tick in mergers and acquisitions activity and the continuous demand for real estate portfolios and one-off transactions. Continued coverage restrictions/pressures are expected as markets grapple with the significant mold claims of certain classes.
- ***General Liability/Pollution Legal Liability (GL/PLL)*** – While the capacity for the GL/PLL marketplace remains strong, markets are re-trenching in light of the industry's continued mergers and acquisitions. Form changes, re-underwriting and sensitivity to limits deployed is prevalent with all markets. Continued attention to excess line profitability will also be a key focus due to deteriorating auto underlying performances. Anticipate the appetites of carriers to be impacted as well as excess capacity.
- ***General Liability/Contractor's Pollution Liability/Professional Liability (GL/CPL/PL)*** - The market remains competitive with new players pushing for more share, while driving prices down. This is especially true where fleet exposures are limited. Accounts with fleet exposures, whether owned, hired or non-owned, anticipate increases. Carriers will continue to push pricing, while placing increased pressure on top-line growth. In addition, underwriting will push back on limits and coverages to counter increased claims activity. Auto-driven accounts will also remain highly scrutinized.
- ***Architects and Engineer's Professional Liability (A&E PL)*** - The buying habits of design firms are gradually changing. Firms specializing in structural or geotechnical engineering as well as organizations working on multi-unit residential or condominium projects can expect stiffer renewal terms and conditions due to the increasing number of exposures. Some carriers are even experiencing an up-tick in claims connected to roadway and intersection designs. Overall, however, these firms are likely to find alternate renewal options due to the sheer number of carriers participating in the A&E PL market.
- ***Contractor's Professional Liability (CPrL)*** - Look for 2019 to bring continued CPrL coverage expansions and competitive rates, provided the insured remains static. Although the frequency of CPrL claims is expected to rise in the coming year, this should not be a surprise since the number of buyers has also risen. The greater concern is the severity of the claims in the areas of civil, healthcare, commercial building, and habitational projects, where it is not uncommon to see eight-figure demands.
- ***Owner's Protective Professional Indemnity (OPPI)*** - OPPI continues to be the preferred method for managing professional liability exposures for owners and developers. The advantages of OPPI along with a wide range of applications make this a powerful tool for owners and developers. We anticipate that the frequency of OPPI purchases will continue to increase in 2019.
- ***Real Estate Developers (RED) Professional Liability*** - Exciting innovations will continue to emerge as RED Professional Liability becomes a more mainstream buy for real estate developers or construction professionals performing development activities as a compliment to their main operations. Recognized for their ability to provide the real estate industry with broader solutions than previously available, RED policies marry the features of professional liability insurance for design professionals, contractors and real estate development professionals.

To see examples of lawsuits, settlements, claims and incidents on any of these products, please visit RT's ECP blog.

Contractor's Pollution Liability

PRODUCT OVERVIEW: Contractor's Pollution Liability (CPL) provides coverage for pollution conditions that occur as a result of covered contracting operations performed by or on behalf of the named insured. Readily available on an occurrence based form, coverage can be purchased on a practice or project basis.

The standard CPL form typically contains the following coverages:

- Jobsite contracting operations
- Emergency response first-party coverage to minimize the impact of a sudden/accidental pollution condition
- Transportation by or on behalf of the Named Insured and typically all modes of transport
- Non-owned disposal site (NODS) coverage on a blanket basis
- Sudden/accidental Pollution Legal Liability (PLL) for locations owned/leased/rented by the insured in support of contracting services
- Defense (widely available via supplemental defense limit)
- Mold/bacteria coverage provided on most forms

INDUSTRY OVERVIEW

2018 continued to be a strong year for CPL coverage, with more carriers offering more CPL than ever before.

Insurance specifications requiring CPL coverage will remain the biggest buying motivator for contractors. We envision contracts will increasingly require CPL coverage in 2019 and at an increased per claim/aggregate limit than experienced in 2018.

As with many middle- to large-sized insurance buyers, asset protection will become the prevalent driver as contractors increase in size. Exposure education, claims, and the scope of coverage terms will also attract buyers looking beyond typical contractual requirements.

CPL claims on RT's ECP book of roughly 1,200 contractors (both general contractors and specialty trades) were analyzed between 2014 and 2017. This included the type and total number of claims. Some of the most notable findings follow:

- There was a 60% increase in the number of claims from 2014/2015 to 2016/2017
- 1 in 16 contractors experienced a claim during the 2016/2017 time period - up from 1 in 21 the period before
- 29% of the claims were related to microbial matter with the disburbance of utility lines a close second
- Pre-existing asbestos-containing materials (ACM)

Claims under $1 million continued to increase when compared to last year, countering the common perception that CPL is a low frequency/high severity line of coverage. The trend is likely due to the broad coverage terms currently provided by carriers under the microbial matter – mold, fungi, bacteria, and legionella categories of exposure.

CPL claim responsiveness remains a concern. Advantages exist for carriers using in-house claims staff in comparison to third-party claims vendors.

MARKET OVERVIEW

Approximately 45 markets offer CPL with the coverage continuing to broaden with carrier competition. Premiums for both practice and project programs assessed on less than $100 million in construction revenue will remain stable. Carriers will remain aggressive for the larger practice/project business ($100 million+), largely due to carrier competition.

Contractor's Pollution Liability

Continued from page 4.

Capacity is not an issue, both in terms of primary and excess. Some carriers offer as much as a $50 million limit with the average carrier typically providing between $10 million and $25 million.

Occurrence CPL coverage is common with a minimal price reduction for a claims-made product. Carriers will also continue to provide varying coverage for bacteria, mold, microbial matter, legionella, silt/sedimentation, silica, petroleum hydrocarbons, low-level radioactive waste, illicit abandonment, escape of methamphetamines, medical/infectious/ pathological wastes, and electromagnetic fields.

Coverage for microbial matter/mold/bacteria varies upon the risk, but is commonly offered on a claims-made basis, especially for high hazard projects.

Annual practice policies will also continue as the preferred CPL product. However, more markets are offering two- and three-year policy duration options. Project policies tend to extend to the 10- to 15-year plus completed operations/extended reporting period.

Supplemental defense expenses are available from most carriers. Some even provide unlimited defense limits outside the limit of liability.

Additional coverage enhancements will continue to be available for Emergency Remediation, Crisis Management, Litigation, and Subpoena Expenses. Some carriers are even providing coverage for the "green building" and/or sustainable/energy-efficient materials used in restoration events.

RT'S ECP 2019 OUTLOOK

Overall, expect CPL availability to remain abundant, while continuing to expand. Expect premiums to stabilize (risks less than $100 million) or to be aggressive (risks $100 million+) for 2019. The migration of insureds moving from a monoline pollution liability product to a combined professional/pollution liability program will also continue. Due to the increase in mold claims, look for carriers to restrict mold coverage via a claims-made trigger, higher retentions or the removal of mold terms altogether for high risk classes.

Coverage for microbial matter/ mold/bacteria varies upon the risk, but is commonly offered on a claims-made basis, especially for high hazard projects.

Pollution Legal Liability

PRODUCT OVERVIEW: Pollution Legal Liability (PLL) continues to be a key risk management tool for facilitating transactions related to contaminated properties as well as buoying the balance sheets of large real estate assets. In 2018, this claims-made coverage consistently managed on- and off-site clean-up/remediation expenses; third-party bodily injury, property damage; and defense expense.

Coverage enhancements such as contingent business interruption and first-party diminution of value are readily available for inert real estate portfolios; while indemnity triggers were utilized to address the known pollution conditions identified in contaminated property transfers.

Coverage terms have been impacted over the past year, depending on the type of risk, by a combination of high profile mold claims and natural disasters ranging from Hurricanes Harvey and Irma to the wildfires in California. As a result, the marketplace responded with restrictive coverage terms and increased underwriting scrutiny.

INDUSTRY OVERVIEW

A Deloitte survey of 500 global investors recently identified the key influencers behind their Commercial Real Estate (CRE) investment decisions. It found that:

1. A large proportion of respondents planned to increase their capital commitment to CRE with the United States, Germany, and Canada leading the way.
2. Many of the surveyed investors expected to prioritize their investments in existing and potential investor companies that respond rapidly to business model changes, while adopting a variety of future-ready building technologies.
3. Survey respondents also expected technology advancements to significantly impact legacy properties of three years or less.
4. 97 percent of the survey respondents plan to increase their capital commitment to CRE over the next 18 months.
5. U.S. respondents plan to increase their capital commitments by 13 percent with the same time frame.[1]

RT's ECP expects the demand for PLL to remain strong as global and domestic investment in U.S. real estate is projected to remain strong in 2019. The commensurate up-tick in PLL claims over the past several years will also continue the drive PLL coverage.

POLLUTION LEGAL LIABILITY CLAIMS

PLL claims on RT's ECP book of roughly 750 insureds who purchase PLL were analyzed from 2014 to 2018. This included the type and percentage of claims impacting the spectrum of real estate industries including Commercial and Habitational Real Estate; Hospitality, Healthcare; Education; Manufacturing and Transactional. Some of the most notable findings follow:

- 104 PLL claims were made between 2014-2018
- 36% of the claims were related to Microbial Matter
- 24% were from spills/leaks
- 19% of the claims resulted in soil/groundwater contamination
- The remaining claims include Legionella, asbestos/lead based paint, vapor intrusion, transportation and underground storage tanks.

PLL claims frequency increased from 2017 to 2018 with most caused by microbial matter in the habitational, hospitality, healthcare and education classes. Over 80% of these claims were for clean-up and restoration costs, although few of the claims included indemnity payments. Suspected reasons for the up-tick in claims frequency for these categories include:

- Increase in renovations and capital improvements due to 10 years of continued economic growth
- Continued high-profile media coverage of microbial matter cases

[1] *Deloitte Center for Financial Services - 2019 Commercial Real Estate Outlook*

Pollution Legal Liability

Continued from page 6.

- Rising litigation resulting from microbial matter claims, particularly involving bodily injury
- More intensive lender-required environmental due diligence, which increasingly leads to the “discovery” of microbial issues

MARKET OVERVIEW

New business underwriting trends continue to evolve with markets monitoring their offerings for various risk types including the prospective (ongoing) vs. the legacy coverage for development/redevelopment projects and deals. These markets are also reviewing their mold capabilities with several retracting full coverage for hospitality/habitational risks.

Policy terms remained consistent during 2018. For transactional purchases, terms varied between 5 and 10 years with a few carriers offering 10-year policies for operational coverage, while others offered 10-year terms for transactions. In regard to hospitality, habitational, and healthcare risks, markets are continuing to tighten their options due to an increase in frequency and the severity of claims, particularly around mold. Most markets offer a maximum term of 3 years for these risks. For prospective coverage, the average term remained 3 years. The availability of 10-year policy terms for prospective coverage has all but disappeared from the landscape.

With the increase in claim activities, rates continue to rise depending on the market and risk type. Carriers are pushing rates and increasing deductibles related to mold in the hospitality, habitational, and healthcare space. Rates and deductibles are also increasing rapidly in the energy/oil & gas space. Finally, minimum premiums have risen for site redevelopment deals.

Overall, this represents a market capacity of over $300 million with a few carriers still able to provide $50 million limits; however, maximum limit deployment has been curtailed throughout 2018.

Buying motivators for PLL continue to fall into four categories: regulatory, contractual, lender requirements, and risk management.
The frequency and severity of claims dramatically increased during 2018 with seven- and eight-figure microbial matter/mold claims in the hospitality, habitational, and healthcare spaces. Natural disasters have also led to several large clean-up/remediation events in the seven and eight figure range. Claims have also plagued the energy sector involving pipeline risks as well as oil & gas wells.

Underwriting scrutiny remains high for site redevelopment deals, hospitality exposures and the energy space. Significant underwriting information is now required to provide competitive terms for these risks, including but not limited to Environmental Site Assessment (ESA) Phase I’s and/or mold and legionella management plans.

Broad coverage is still available and widely used in the PLL marketplace including the following:

- **Defense Expense** in addition to the Aggregate Limit of Liability for risks seeking a lower limit
- **First-Party Diminution in Value** coverages applied to the insured’s owned location for property damages resulting from pollution conditions
- **Contingent Business Interruption** coverage applied to an insured for an event impacted by off-site pollution conditions

However, with the recent drastic rise in mold and clean-up claims during site development, several markets are deploying the following coverage restrictions:

- Sublimits and higher deductibles or per “door” deductibles for microbial matter/mold
- Exclusions for mold discovered during capital improvements
- Voluntary Site Investigation and Capital Improvement exclusions for site development/redevelopment risks

RT’S ECP 2019 OUTLOOK

Although the increased frequency of various pollution losses continues to plague the marketplace, competition remains robust due to the advent of new markets. Policy terms are expected to remain consistent throughout 2019 with a maximum term of 10 years. Policy terms for prospective/ongoing coverage are anticipated to remain in the 1 to 3 year range. PLL activity during the last half of 2018 was robust in all market segments including mergers and acquisitions (M&A), real estate portfolios, and one-off transactions. Expect a continued increase in underwriting scrutiny for industrial and hospitality/habitational/healthcare risks as well as in the energy sector.

The frequency and severity of claims dramatically increased during 2018 with seven and eight-figure microbial matter/mold claims in the hospitality space. Natural disasters have led to several large clean-up/remediation events also in the seven- and eight-figure range. In addition, claims involving pipeline risks as well as oil and gas wells continue to plague the energy sector.

General Liability/Pollution Legal Liability

PRODUCT OVERVIEW: The Combined Pollution Legal Liability (claims-made) and General Liability (occurrence) forms provide coverage to chemical manufacturers, distributors, waste management facilities, and any other manufacturer of “environmental” products, including but not limited to storage tanks, pressure vessels, liners, pumps/valves and pollution control equipment. Significant market expansion has occurred over the past 10 years. Coverages include: General Liability (GL) for Products Pollution; Pollution Legal Liability (PLL); Contractor’s Pollution Liability (CPL) (for incidental contracting services); and Professional Liability (for waste brokering and other miscellaneous professional exposures).

INDUSTRY OVERVIEW

While the capacity for the General Liability/Pollution Legal Liability (GL/PLL) marketplace remains strong, markets are retrenching in light of the continued mergers and acquisitions within the industry. Form changes, re-underwriting and sensitivity to limits are prevalent within all markets.

Market pressures continue to evolve with some developing programs for recyclers and chemical distributors and others continually searching for new ways to compete against the traditional marketplace.

In 2019, the continued attention to excess line profitability in support of GL/PLL products will be a key focus due to deteriorating auto underlying performances. Anticipate the appetites and excess capacity of carriers to be impacted.

Market pressure continues in this class as new markets push to grow their books. Middle-tier markets are taking advantage of leadership changes and re-underwriting accounts to grow business outside their normal framework.

Smaller markets are also lowering premium thresholds to support competitive growth.

In addition, the pricing for high-hazard, construction-related products and mass tort products will continue to remain defensive in this marketplace.

Capacity remains strong despite market disruptions, but the greater concerns are how capacity and coverage restrictions are enforced by carriers, particularly on long-time site pollution exposures, as markets seek to manage their loss ratios.

The motivators for this policy form will remain consistent. The main driving forces are (1) regulatory compliance for waste facilities where financial responsibility is needed; (2) asset protection; and (3) products with pollution exposures.

Additional motivators include insureds seeking coverage for unique or unusual exposures that are not readily available in the traditional marketplace. These include products pollution, site time elements for non-owned locations, and odor problems. Tailoring coverage in this arena remains a viable strategy for showcasing the policy’s value and distinguishing products from competitors.

Private equity acquisitions for environmental accounts continue to occur as industries such as recyclers, emergency response contractors and chemical manufacturers continue to evolve and expand.

MARKET OVERVIEW

Carriers are increasingly scrutinizing the site pollution risks that had previously been underwritten. As a result, stricter standards have been put in place due to legacy loss and preventive underwriting issues. This includes auto loss severity, which continues to penetrate into excess and impact how fleets are classified with the allowed capacities.

General Liability/Pollution Legal Liability

Continued from page 8.

Carriers are increasingly scrutinizing the site and pollution portion of risks that had previously been underwritten. As a result, stricter standards have been put in place due to legacy loss and preventive underwriting issues.

In addition, GL/PLL is increasingly being scrutinized with capacities limited depending on exposures. There is also little, if any, tolerance for oil and gas related products.

The underwriting of these products tightened significantly in 2018. New markets and middle tier markets have tempered heavier underwriting approaches; however, markets are pushing increases. Anticipate coverages that were previously thrown in or offered on an occurrence basis to be scrutinized more heavily and in some cases converted to claims-made coverage forms. Additionally, anticipate that higher deductibles will be employed on core coverage such as hostile fire, which can also impact pollution terms and coverages.

Professional liability coverage (added as an additional coverage part or by endorsement to the GL/PLL) is still available for industries related to waste brokering and limited waste operations. Insureds are continuing to expand the scope of the professional services covered in this space. In addition, business interruption (BI) coverage has become more prevalent in environmental casualty forms as a result of increased uninsured BI losses in the traditional property marketplace.

RT'S ECP 2019 OUTLOOK

The continued narrowing of appetites by individual carriers can be anticipated as the market expands and pushes competition, resulting in rate increases. Mature markets are also still in a heavy underwriting mode with books challenged by middle-tier carriers, who benefit from the narrowing appetites, market disruption, and pricing push.

General Liability/Contractor's Pollution Liability/Professional Liability

PRODUCT OVERVIEW: The Combined Environmental Casualty Program (GL/CPL/PL) provides general liability (GL), contractor's pollution liability (CPL), and professional liability (PL) to a specific market segment consisting of environmental contractors, waste transporters, environmental consultants or a combination thereof, and oil/gas/energy contractors. Only a few insurers offer complementary coverage such as Workers' Compensation, Auto, and Excess.

INDUSTRY OVERVIEW

The market remains competitive with new players pushing for more share, while driving down prices. This is especially true where fleet exposures are limited. In general, accounts with fleet exposures, whether owned, hired or non-owned, are anticipating increases. Most markets are on the third year of auto filings increases. Smaller, secondary markets continue to push the envelope and write larger accounts with mature carriers re-underwriting their books. Appetites for environmental considerations are also being scrutinized with carriers. Particular attention is being paid to professional liability risk.

Contracting accounts with site pollution exposures are also undergoing the same stringent underwriting that exists in monoline markets for site pollution, making it more difficult to move these accounts.

Leadership changes and acquisitions have also impacted underwriting approaches, while narrowing appetites. For instance, most environmental carriers have pulled back from offering coverage to oil and gas accounts. Many carries are also rewriting their forms to narrow coverage. In addition, the decreasing number of carriers in the auto marketplace, along with limited workers compensation, have emboldened all-lines markets to remain firm on their pricing and programs. As a result, middle-tier carriers have continued to capitalize on the changing market with low-cost options that helped support their growth. One new dynamic is the request for primary auto with at least $2 million limits especially on heavy transportation risks and hazardous auto fleets. Many environmental markets are still working on pricing, while struggling to treat these buffer layers with the proper excesses.

Additionally, the markets continue to re-underwrite New York-based risks with several markets stepping out of the marketplace entirely due to the severity of action-over claims. Because of the refined carrier appetites, pricing remains inconsistent, especially on new business. That said, carriers are looking for increases related to auto exposures including 5% to 10% on primary and equal amounts on excess. This not only applies to hazardous waste haulers, but also to consultant related fleets. In addition, the market is increasingly seeking to buffer auto layers to accommodate accounts with heavier fleets.

Although stable, individual markets are keeping to a narrow bandwidth, but are likely to expand with selective product offerings. The re-underwriting of capacities impacted or subjected to higher-layer premiums will result from continued mergers. Carriers will also carefully manage capacity with the market depth creating opportunities for new markets to push on capacity.

Throughout the year, many accounts are expected to look for the benefits of a combined program that offers economies of scale and sometimes broader coverage than split lines. These accounts will continue to stretch the environmental space as carriers seek to maintain market share by considering this competitive environment. The contractual requirements of many business partners will also motivate the purchase of combined environmental policies with flat and non-auditable coverage forms providing additional cost controls as GL/CPL/PL becomes increasingly popular among contractors.

MARKET OVERVIEW

The market will continue to apply a conservative underwriting approach with mature markets looking to refine their appetites and protect loss ratios especially when auto coverage forms are concerned.

General Liability/Contractor's Pollution Liability/Professional Liability

Continued from page 10.

Some carriers will also seek to grow their books with a focus on higher layer excesses. In addition, small markets and newer markets as well as carriers will offer all-lines approaches, while increasingly offering coverages that are more in line with monoline placements to help sell accounts. This includes expansions such as defense outside the limit coverage or adding pollution products to a contractor form.

The coverage form itself is expected to remain conservative with many carriers carefully deploying limits and rewriting forms.

This also includes:

- Fleet exposures of all types being scrutinized
- Impact to excess policies as a result of auto exposures remaining a key concern
- Professional liability lines carefully underwritten to cover exposures beyond environmental
- Contractors and consultants who provide both design and product installation services continuing to heavily scrutinize in this increasingly tightening marketplace

Small and newer markets as well as carriers will offer all-lines approaches, while increasingly offering coverages that are more in line with monoline placements to help sell accounts. This includes expansions such as defense outside the limit coverage or adding pollution products to a contractor form.

RT'S ECP 2019 OUTLOOK

We expect the market to remain competitive in 2019. Carriers will continue to push pricing, while placing increased pressure on top-line growth. In addition, underwriting will push back on limits and coverages to counter increased claims activity.

The focus on auto-related accounts will also remain high. However, while competition will be rampant, the auto accounts with loss issues will also continue to struggle with the accompanying excesses reflecting the changing market.

Architects & Engineers Professional Liability

PRODUCT OVERVIEW: Architects and Engineers Professional Liability (A&E PL) insures design professionals against damages resulting from the acts, errors and omissions committed while rendering professional services including damages that can result from design mistakes and project delays. Expect most admitted carriers to offer coverage for pollution incidents arising out of professional services within the base policy form, with a growing number of markets also incorporating some degree of coverage for technology services and cyber liability. Industry segments facing these exposures include architectural design firms, engineers, construction management agency firms, interior designers, space planners, and surveyors.

INDUSTRY OVERVIEW

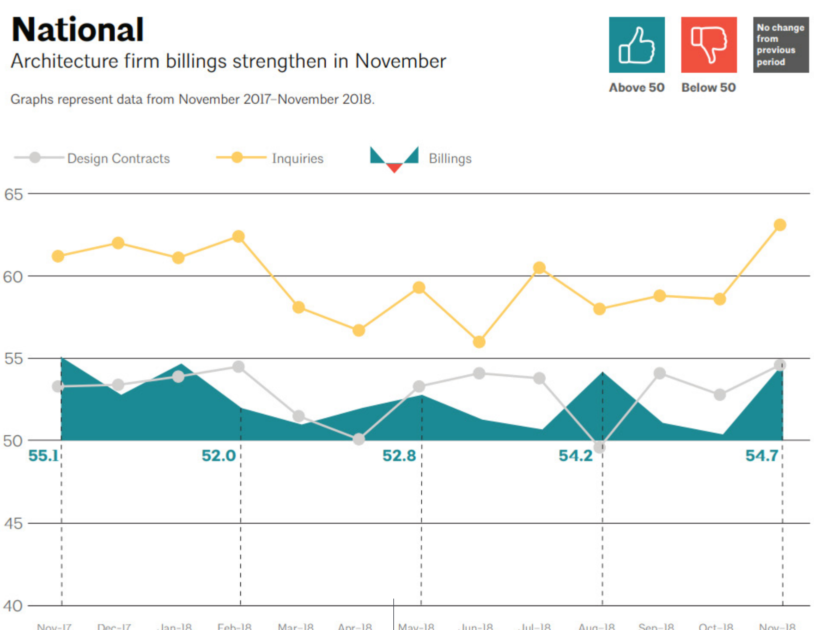
In November 2018, the American Institute of Architects (AIA) released their Architecture Billing Index (ABI). Serving as a leading economic indicator of U.S. construction activity, the ABI surveyed month-to-month, design firm billing trends. For the most part, the previous year's predictions were actualized over the past 12 months. Key takeaways include:

1. **Regional Activity** - While all regions posted growth during the year, design firms operating out of the South and Midwest saw stronger growth than those in the Northeast and West.[2]

2. **Growth by Sector** - The momentum in billing growth seen in 2017 continued in 2018. All specializations (residential, commercial, institutional) showed growth; however, design firms with a focus on residential projects grew the most.[2]

3. **Positive Outlook** - Growth trends are likely to continue for the next few months, with design firms generally reporting growth in the value of new design contracts as well as new project inquiries.[2]

4. **Obstacles** - Two of the three most common concerns reported by design firms in 2017 were also reported in this year's survey: increasing firm profitability and the identification of new, qualified staff. The number three ranked concern was coping with an unpredictable economy.[2]



Courtesy of the American Institute of Architects

MARKET OVERVIEW

The soft market for A&E PL remained in effect during 2018 and will likely continue into the near future. Design firms are beginning to see higher contractual requirements for A&E PL coverage; fortunately, most major A&E PL insurers report limit capacities of $5 million to $10 million on admitted paper. Increased competition among carriers in this soft market has led to several favorable outcomes for design professional firms purchasing A&E PL including:

- Standardized policy language among most carriers for core A&E coverages
- Stable renewal ratings, despite industry wide increases in overall billings (exception: structural and geotechnical engineers as well as any discipline engaging in multi-unit residential project)
- Multi-year policies available with fewer underwriting restrictions
- Broadening of coverage among some forms to include

[2] *Source: AIA December 2018 ABI*

Architects & Engineers Professional Liability

Continued from page 12.

differing levels of technology and cyber liability coverage
- Risk management offerings including complimentary contract review services and webinars

Firms specializing in structural or geotechnical engineering as well as organizations offering services on multi-unit residential or condominium projects can continue to expect stiffer renewal terms and conditions due to typically heightened professional liability exposures associated with these services or project types. Overall, however, claims trends in the market have stabilized and these firms are likely to find competitive alternate renewal options due to the abundance of available admitted products.

The marketplace interest and availability for project-specific A&E policies affording dedicated PL limits to the A&E for a given project remain scarce on small projects (those generating less than $100 million in construction values).

The need for diligent policy review and coverage assessments remains as strong as ever with many carriers resorting to various "throw-in" coverages such as technology errors and omissions, cyber liability, directors & officers, and employment practices liability insurance as a way to attract and retain buyers. While design professionals may appreciate these provisions, it is important for insurance professionals to closely review the coverages for quality, while considering carrier claims expertise before touting the benefits of such extensions. This includes preserving their A&E PL policy limits, A&E PL claims and entertaining a separate policy for cyber, directors and officers, employment practice liability and other inclusions.

RT'S ECP 2019 OUTLOOK

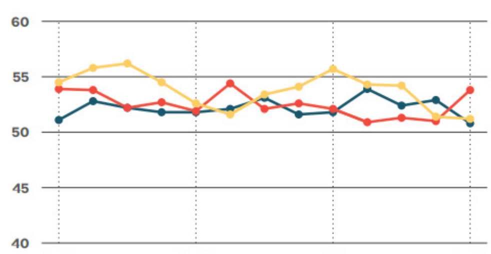
Looking forward, we have a stable outlook for the A&E PL marketplace. No major players have exited the market and we expect competition among the carriers to extend into 2019. Pricing rather than coverage will be the focal point of purchase decisions.

Although no looming claim trends appear on the horizon, it is worth noting that A&E PL claim activities typically follow the construction industry. In addition, the number of A&E PL claims per construction dollar spent should remain steady but the overall amount of litigation is likely to increase in step with the economy. This, combined with stagnant rates, could spell hardship for some carriers carrying smaller or less mature books of business, while affording advantages to more established markets.

Sector

Firms with commercial/industrial specialization report strongest billings growth

Graphs represent data from November 2017–November 2018 across the three sectors. 50 represents the diffusion center. A score of 50 equals no change from the previous month. Above 50 shows increase; Below 50 shows decrease. 3-month moving average.



Courtesy of the American Institute of Architects

Contractor's Professional Liability

PRODUCT OVERVIEW: Contractor's Professional Liability (CPrL) provides coverage for the damages arising from professional service acts, errors, and omissions performed by or on behalf of any construction firm. Some CPrL programs offer first-party coverage, such as "protective" or rectification coverage (otherwise known as mitigation). Protective coverage indemnifies the named insured for the costs it incurs (in excess of the design professional's (DP's) professional liability insurance) and is legally entitled to recover as a result of the negligent acts, errors, and omissions committed by design professionals under contract with the named insured. Whereas contractor's protective coverage supplements the DP's professional liability insurance, rectification coverage essentially replaces the DP's insurance solely with respect to the costs incurred by the named insured to remedy the design errors discovered during the course of construction and would have otherwise resulted in professional liability claims.

INDUSTRY OVERVIEW

1. It is predicted that total U.S. construction starts for 2019 will be $808 billion, staying essentially even with the $807 billion estimated for 2018.[3]

2. The President's $1 trillion infrastructure plan remains on the table. The Wall Street Journal has reported an increase in public agency spending on infrastructure investments.

3. Commercial building is likely to retreat 3%, after experiencing 2% gains in 2017 and 2018, which had followed prior increases. 2018 market fundamentals for offices and warehouses are healthy. 2019 numbers are anticipated to decrease due to vacancy rate increases in response to an expected economic slowdown.[3]

4. While single family housing is predicted to be unchanged in dollar terms, multi-family housing is predicted to decrease 6%.[3]

Recession fears exist throughout the marketplace, although 2019 predictions for the horizontal and vertical construction industries offer the promise of continued premium growth for the year.

Claims on RT's ECP book of roughly 1,000 contractors (general contractors, specialty trades, construction managers, design/builders and A&Es) that purchased CPrL coverage were analyzed between 2014 and 2017. This included the type and total number of claims. Notable findings revealed:

- There was a 23% increase in CPrL claims during the 2016/2017 time period compared to the period before.
- Construction management (as a process rather than delivery method) claims led the trend with about 60% of total claims.
- Construction management claims included safety issues, mismanagement of subcontractors, poor inspection of work product and misidentification of environmental hazards.
- Of the remaining 40% of claims, the following trends were identified:
  - Most of the remaining claims included errors in subcontractor design
  - Other claims included in-house engineering performed in support of contracting services, a more prevalent trend than actual third-party design services
  - Surveying and value engineering claims are a prevalent trend across the book of business

Statistics support the idea of CPrL as a catastrophic coverage with nominal claims frequency although high severity. It is estimated that claims will continue with historical catastrophic trends with demands being in the six- to seven-figure range. However, as the number of buyers increase, frequency is also likely to increase.

MARKET OVERVIEW

We continue to see a competitive marketplace with approximately 25 domestic carriers and another 5 to

[3] *Source: Dodge Data & Analytics, 2019 Dodge Construction Outlook*

Contractor's Professional Liability

Continued from page 14.

7 foreign markets offering CPrL products and one or two new entrants entering the field every year. Most major players report an on-average, limit capacity of $25 million with ease of structuring follow-form excess layers offered via other carriers. However, some carriers now offer up to $50 million in capacity. Increased competition has also led to favorable outcomes for many firms purchasing CPrL:

- Expanding first-party coverages with carriers loosening restrictions on: protective and rectification coverage; definitions covering professional services representing a more accurate deipiction of the risks contractors face; and more consistent offerings for defense outside the limit terms, among other benefits
- Competitive pricing despite growth in revenues. Carriers remain aggressively priced with rate reductions offered to firms showing revenue increases pending the absence of adverse claims and static service offerings
- Increased project-specific coverages for smaller-sized projects (construction values under $100 million) with more markets willing to provide dedicated limits with reasonable pricing. Stable pricing and coverage outlook remain for larger projects, though some carriers are hesitant when it comes to heightened limits.

Firms specializing in single-family home construction as well as multi-unit residential or condominium projects should expect to see limited market interest and coverage restrictions due to the heightened professional liability exposures found within in these project areas.

RT'S ECP 2019 OUTLOOK

With a stable to expanding market, look for 2019 to bring continual expansions in coverage and competitive rates, provided the insured remains static (no large revenue swings, change in services, claims, etc.). The competitive nature of the market has pushed many carriers to be creative and flexible with their products. Limited coverage for faulty workmanship and recall expenses have been introduced within the professional ranks of construction carriers, and merit further scrutiny to see if such offerings become common. It should be noted that such products should be carefully evaluated for true intent of coverage as they often differ greatly from traditional CPrL policies providing coverage for the economic damages arising from the provision of professional services.

The need for diligent policy review and coverage assessments is critical as new carriers emerge and existing players emulate competitors with the addition of first-party coverages. The modification of forms by carriers seeking to remain competitive further supports the need for diligent review. While this expansion benefits buyers, it is equally important for carriers to clearly understand the terms they are providing and the handling of claims under these first-party coverage parts. Due to the relatively limited amount of staff who have actually handled and adjusted first-party claims, attention must be paid to the quality of claims personnel amongst the carriers.

As the number of CPrL buyers continues to increase, the frequency of CPrL claims is expected to grow in the coming year; first-party coverages (rectification/mitigation type claims have a shorter payout period) are regularly producing new claims. Quite simply, the coverage is broad.

The frequency of CPrL claims is expected to grow in the coming year; first-party coverages (rectification/mitigation type claims have a shorter payout period) are regularly producing new claims; and quite simply, the coverage is broad.

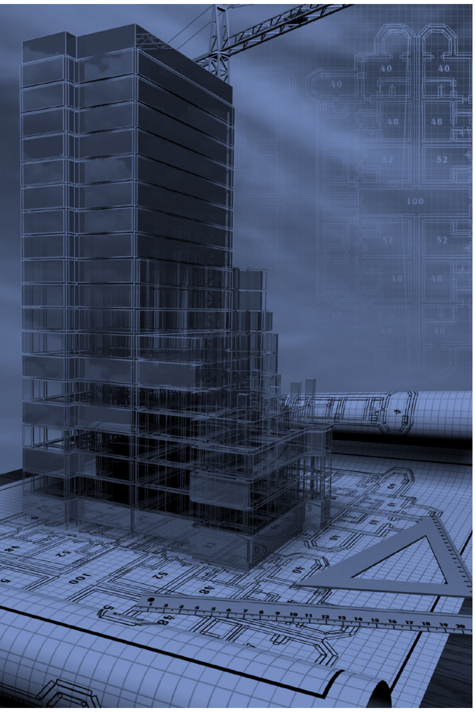
The greater concern is claims severity. Significant claims have risen in the areas of civil, healthcare, commercial building, and habitational projects. Eight-figure demands are common on CPrL claims. As more buyers enter the marketplace, first-party coverages will become more prevalent.

The late reporting of claims by insureds will also continue to trend. Contributing factors include CPrL buyers who:

- Do not understand that the coverage is in place to insure against incidents and claims
- Do not understand the importance of formally reporting incidents and errors
- Apply the "we screwed up, we should fix it" mentality, while failing to report the claim after the fact

Insurance buyers should review, understand and comply with the claims reporting provisions outlined by their policies to avoid unnecessary coverage denials. Furthermore, it is critical to not assume liability since this assumption could violate CPrL policy provisions.

We expect to see a consistent increase in 2019 claims activity as the CPrL market matures.



Owner's Protective Professional Indemnity

PRODUCT OVERVIEW: Two core insuring agreements are available and include First-Party Indemnity and Third-Party Defense. First-party indemnity, referred to as Protective, indemnifies the named insured for damages in excess of available design professional insurance. This coverage part should drop down in the event a design professional's practice policy has eroded or is less broad than the coverage offered under the Owner's Protective Professional Indemnity (OPPI). Third-party defense protects owners from the actions arising from the vicarious liability assumed through the contracting of design professionals. Optional excess Contractor's Pollution Liability (CPL) is available from most markets.

Purchase of OPPI includes the policy period, which generally matches the construction period, and an Extended Reporting Period (ERP) along with a retroactive date, which generally matches the first date of design. OPPI policies are often auditable but should allow for automatic extension for project delays. OPPI can be purchased for a single project or be structured to enroll additional projects over a multi-year policy period.

INDUSTRY OVERVIEW

There are currently 10 carriers writing the "primary" with a few secondary markets offering coverage excess of the initial OPPI layer. Most markets can provide $10 million to $15 million on the primary layer, while a select few can write a full $25 million. Total market capacity is between $100 million and $150 million, depending on the type of project.

Benefits

Design professionals often carry low limits of professional liability insurance. Much of this is shared among all the work performed on an annual basis. This is brought to light in ACEC's (American Council of Engineering Companies) 2018 annual insurance survey whereby firms generating $49.9 million in fees or less purchase professional liability limits at $5 million or less. Even more alarming, 32% of the firms this size buy $3 million or less. To exacerbate the concern, there are an estimated 60 markets insuring design professionals with varying scopes of coverage. It is extremely difficult to verify the quality of coverage carried by those design professionals unless you construct a lengthy insurance specification but even then, who's to say that the form complied with the specification. As excess and difference-in-conditions of the contracted design team professional liability policies, OPPI can relieve these concerns. Additional benefits to owners and developers include Named Insured status, a defense against third-party claims and significant reduction in cost.

Another benefit of the OPPI is the defense coverage part for third-party claims. With the continuing trend for architects and engineers (A&Es) to remove defense provisions from their professional service contract leaving the owner or the general contractor to fend for themselves when legal actions are brought against them as a result of the services performed by the A&E. Lastly, as excess insurance, OPPI pricing is often 50% or less than the cost of primary project specific professional liability (PSPL) placements.

Claims

As an excess insurance designed as a catastrophic backstop, the frequency of claims has remained limited. Future loss activity may increase as residential projects increasingly become a larger portion of the OPPI marketplace.

MARKET OVERVIEW

Demand remained strong throughout 2018. We expect this to continue into 2019.

With continued demand and profitable underwriting results, rates continue to decrease.

Owner's Protective Professional Indemnity

Continued from page 16.

We are seeing interest in OPPI on smaller projects and the market has responded with an improved appetite for projects under $50 million in construction value.

Most markets have now removed the self insured retention (SIR) obligation under the Protective coverage part. An SIR typically only applies to third-party defense coverage.

Habitational risks continue to pose challenges. The risk associated with residential construction along with concerns from homeowner's association litigation continue to affect market interest. Third-party defense becomes a key insuring agreement on habitational projects due to the increased chance of claims against the owner. When quoting habitational projects, markets may remove this coverage part, provide a sublimit or attach a higher SIR. The definition of professional services under OPPI continues to expand and track more closely to the A&E forms.

OPPI forms often contain exclusions not found in the policies they are in excess of. Recognizing and negotiating amendments is performed on a case-by-case basis.

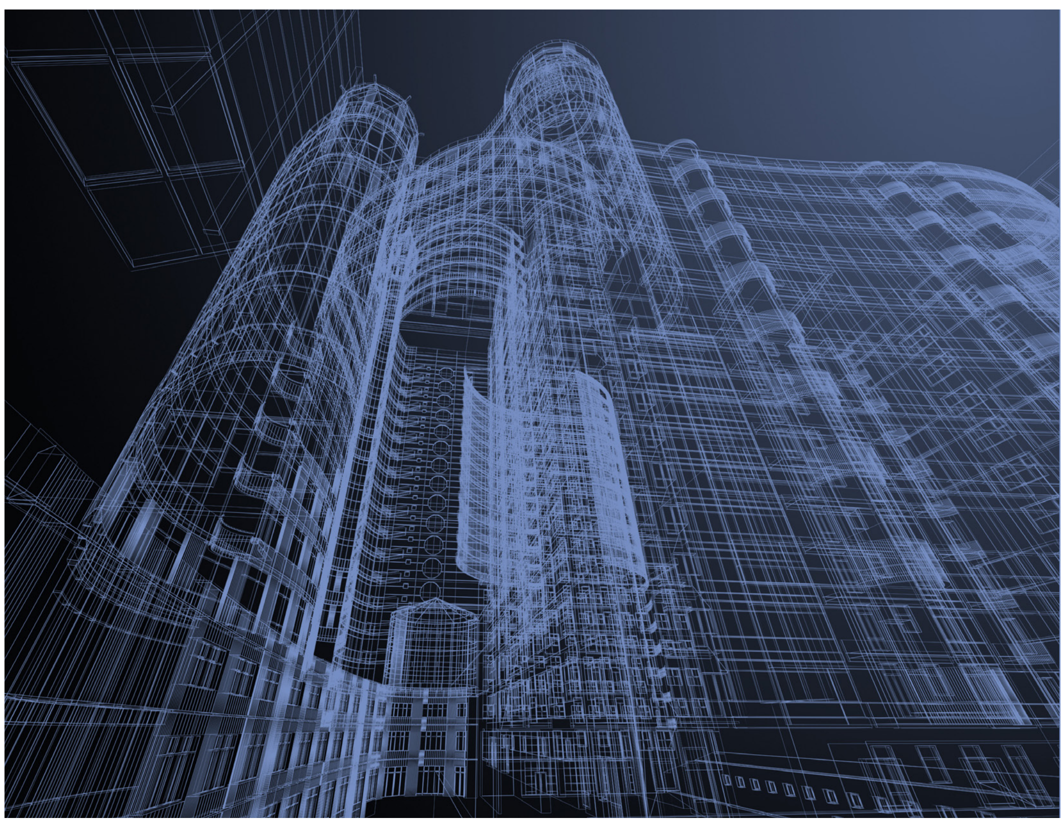
Lastly, there has been an increased interest and purchase of "rolling" OPPI programs or blanket programs over the past year. This concept makes better financial sense for those owners and developers who have committed to the capital expenditures and will build versus choosing which projects to insure.

RT'S ECP 2019 OUTLOOK

A continually undersold and under-purchased product, the OPPI economic outlook remains strong. Our success with this product has dramatically increased over the past several years. We attribute this success to owner/developer education and understanding of OPPI benefits when comparing to alternatives. Look to owners and developers taking an interest in "rolling" or blanket programs.

As insurers continue to see profitable results and buyers become more aware of the benefits, strong competition is expected in 2019.

We are seeing interest in OPPI on smaller projects and the market has responded with an improved appetite for projects under $50 million in construction value.



Real Estate Developers (RED) Professional Liability

PRODUCT OVERVIEW: Real Estate Developers (RED) Professional Liability provides a financing mechanism to protect against the losses arising from the negligent acts, errors and omissions committed during the performance of real estate development professional services. RED policies marry the features of professional liability insurance for design professionals, contractors and real estate development professionals with broader solutions that were previously unavailable. The product can be customized for all real estate professionals including those with modest ownership, firms providing services to third party investors, or sophisticated real estate developers and owners looking for a comprehensive risk management program.

All real estate developers face professional liability stemming from four major areas: investors, clients/tenants, design and construction professionals, and third parties who are adversely affected by ongoing development activities. RED professional liability can be structured to address each of these areas of risk and may include coverage for services provided to properties owned or unowned by the real estate developer.

INDUSTRY OVERVIEW

With 2018 construction spending ending on a high note, the consensus within the construction industry is that spending across many sectors will again be on the rise in 2019.[4]

In spite of generally favorable economic conditions nationally and solid AEC industry trends, apprehension exists for the market's future conditions. At this stage of the business cycle, economists are generally speculating that there are more downside than upside risks. The concerns include:

- A nine-year economic expansion that has run about twice as long as the typical expansion cycle.
- The construction industry is at capacity with a projected $1.2 trillion dollars in business coupled with industry unemployment at an all-time low. Given the lack of additional skilled labor, the problem is exacerbated by an aging construction labor force.[4]
- Steadily rising interest rates are projected to continue to increase over the next 18 months;[5]
- Wages and material costs continue to be on the rise.[5]
- Federal immigration policies that threaten one of the most reliable sources of labor for the AEC industry.

Uncertain economic trade winds will increasingly incentivize real estate developers to protect the assets they have grown over the past eight years. This includes the strategic purchase of real estate focused professional liability coverages.

MARKET OVERVIEW

The Real Estate Developers (RED) Professional Liability market has slowly emerged since the initial introduction of a standalone product in 2009. RED is comprised of three markets offering standalone

[4] *Source: 2019 AGC/FMI Industry Risk Survey*
[5] *Source: Federal Reserve Bank of St. Louis*

Real Estate Developers Professional Liability

Continued from page 18.

products and a host of construction and miscellaneous professional liability carriers offering coverage on an ad hoc basis. Primary players report an on-average, limit capacity of $5 million with ease of structuring follow-form excess layers offered via other carriers. There are many first-time buyers or insureds “graduating” to more expansive coverage beyond the more typical property manager or contractors’ professional liability products. This involves:

- Expanding first-party coverages with carriers offering coverage features more common with the contractor’s professional liability arena. This includes protective and rectification; definitions highlighting a wide scope of all professional services such as “coupling” of real estate fund E&O coverage parts; and defense outside the limit terms, among other benefits.
- Competitive pricing despite growth in revenues. Carriers have remained aggressively priced with rate reductions offered to firms showing revenue increases pending the absence of adverse claims and demonstration of consistent development strategies.
- Unlike many construction professional liability markets, RED markets are generally more bullish on residential projects and less critical of project delivery methods. Rather, these carriers focus on the quality and nature of real estate services, the expertise of the firms providing such services and their strategy for development in the unique regional markets in which they trade.

RT’S ECP 2019 OUTLOOK

With a volatile and uncertain economic environment coupled with a burgeoning RED Professional Liability insurance market, look for 2019 to bring continual expansions in coverage and competitive rates as many first-time buyers look to shore up their risk management portfolio.

With the expansion of rectification and protective coverage forms, increased attention should also be paid to the quality of claims personnel employed by carriers. Education on key issues (exposures, claims, coverage, program structure, transition from more limited coverage offerings, etc.) will continue to play an important role in the development of this insurance line.

The need for diligent policy review and coverage assessments remains very important with marked coverage disparities among standalone RED and miscellaneous professional liability carriers.

Claims trends continue to be severity driven, yet overall favorable industry-wide. With historical performances meeting or exceeding carriers internal expectations, look for new RED carriers to enter the marketplace and more traditional construction professional liability carriers to expand existing coverages with real estate-focused professional liability terms and conditions.

RYAN® TURNER SPECIALTY | new day

CONTACT
RT SPECIALTY | RT NEW DAY
2465 Kuser Road
Suite 202
Hamilton, NJ 08690
P: (609) 298-3516
F: (609) 298-6254
newday@rtspecialty.com

NEWDAY.RTSPECIALTY.COM