

'Green' Coverage In Builders' Risk Insurance

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Residential and commercial construction is being transformed by the movement towards "green." Green features are specifically designed to make structures more energy efficient, presumably resulting in a less adverse impact on the natural environment.

An outgrowth of this developing technology and change in construction methodology is the evolution of builders' risk coverage to manage the new property risks created by green construction.

Builders' risk is a traditionally uncontrolled, or "nonfiled," class of inland marine insurance providing first-party property coverage for structures as they are being erected. Builders' risk is also known as "course of construction" insurance, a label more commonly used in Canada and Europe.

Fireman's Fund in October 2007 may have been the first major builders' risk insurer to introduce a green builders' risk form. The form insured, among other things, loss of earnings, "soft costs" and rental income attributable to green construction's unique concerns and conditions. Zurich, ACE and several other carriers followed suit with their own versions of green builders' risk endorsements.

Finally Some Standardization

The American Association of Insurance Services (AAIS) in July 2009 introduced the first two "standardized" green builders' risk endorsements. The "**Green Building Coverage**" and "**Delay in Completion Coverage Part - Green Building Form**" created an opportunity for carriers to offer green coverage without having to develop proprietary forms.

When attached to a standard builders' risk form, the "**Green Building Coverage**" endorsement provides four additional coverages increasingly sought by insureds seeking to build environmentally sound and energy efficient structures:

- "**Indoor Air Quality**" coverage pays costs necessary to restore the air quality within a damaged structure to the standard set in an "air quality management plan" (but only to the extent achieved prior to the loss);
- "**Recycling Debris**" pays the additional costs required to divert delivery of the debris from damaged property to a recycling facility rather than a landfill;
- "**Recertification**" pays the cost of recertifying a structure as meeting the "green" standards of one of the leading environmental building organizations (but only to the level of certification achieved prior to the loss); and
- "**Electricity and Water Replacement**" covers the expense of purchasing replacement electricity or water from a public utility made necessary by an insured loss to renewable energy generating equipment or water conservation systems.

Each of these four coverages is triggered only by a cause of loss covered in the underlying builders' risk form; and each carries a separate limit as indicated on an accompanying "Green Building Schedule." These green coverage limits apply separately from any limits scheduled in the underlying builders' risk form.

The "**Delay in Completion Coverage Part - Green Building Form**" can be used in place of a standard delay in completion form. This new green delay in completion form incorporates the policy provisions AAIS introduced in 2008 to clarify questions regarding what were loosely called "soft costs."

AAIS's 2008 Builders' Risk forms specifically distinguished between additional "construction expenses" and increases in "soft costs." "Construction expenses," such as fees, are generally incurred in a lump sum where additional "soft costs," such as interest and taxes, increase over time.

This distinction is retained in the new green delay in construction form. In addition "Green Coverage Extensions" are introduced to cover additional construction expenses, additional soft costs, loss of rental income, and loss of net income attributed to an extended delay due to procedures and processes required to retain green certification.

"Energy Generating Income" is also protected in this new green delay in construction form. Covered under this extension is the loss of income experienced due to the lost sales of surplus power during the delay period. To garner coverage under this extension, an insured loss must render an insured's renewable energy generating equipment inoperable.

Green Builders Risk Compared to Green Property Coverage

Green coverage is not an innovation of AAIS. As an advisory organization, AAIS works to standardize the structure and phrasing of coverages that emerge in the marketplace. The purpose of standardized forms is to introduce consistency and clarity to policy language allowing buyers and sellers to make an "apples-to-apples" comparison between or among forms, and to limit the number of claim disputes that arise when losses occur.

The introduction of "green" coverage into builders' risk insurance poses different considerations than "green" coverage in building property forms. This caveat applies to both the AAIS forms and the proprietary builders' risk forms that preceded them.

In the first place, there is no "upgrade" coverage in the AAIS green Builders' Risk forms or in the proprietary builders' risk forms. When green building coverage was introduced in commercial property forms a few years ago, buyers were offered the option of replacing damaged property with property built to green specifications. For a price, such policies will go beyond the principle of indemnity to put the insured in a better position than existed before the loss.

Buildings are, in many cases presumably, constructed to the specifications desired by the project owner, so upgrade coverage should not be necessary in builders' risk insurance. In the AAIS forms, the coverages generally pay increased costs needed to reconstruct up to the level a project attained before an insured loss.

That leads to a second, more fundamental question: "If the 'green' aspects of a project are already incorporated into it, why is a green builders' risk forms needed?" Wouldn't all the green components of a building project, like any other components, be covered under a standard builders risk form?

"Theoretically, that could be the case," says Robert Guevara, AAIS vice president of inland marine. "But there are advantages to providing the green coverages explicitly."

Guevara points out that some principles of green construction contradict longstanding practices in builders' risk insurance. For example, loss recovery for debris removal has typically been adjusted on the basis of the least expensive means of removing and disposing of damaged property, which

typically involves taking it to a landfill. The now-standard "green" coverage pays the additional cost for recycling the debris of damaged property.

In other cases, the green forms explicitly establish coverages that have not been typically provided under builders risk forms, such as the coverage for compensating an insured for loss to energy generating and water conservation systems.

Finally, says Guevara, the presence of specifically identified green coverages makes it easier for agents to market them and for carriers to charge for the added exposure, if desired.

Over time, some of the building features and construction processes which stand out as "green" today may become routine or incorporated into local building codes. While new features and certification standards will almost certainly arise, "green" coverage, whether in property forms or builders' risk policies, will have to evolve with those changes.

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AAIS is a national advisory organization that develops standardized policy forms and rating information used by more than 600 property/casualty insurers throughout the U.S. AAIS is the successor organization to a series of inland marine rating bureaus, and its Inland Marine Guide is a widely used source of standardized forms, rating procedures, and other information for the non-filed classes.