

Builder's Risk Insurance: Do You Know When Your Coverage Ends?

By Walter Schneider and Laila Louridas

Builder's risk insurance is a critical risk management tool for any owner or contractor seeking to renovate existing structures or build new ones. This coverage protects against loss to a construction project due to property damage sustained during the course of construction, subject to a variety of conditions and exclusions that vary by policy form. Construction contracts typically require the procurement of builder's risk insurance and hold either the owner or the contractor responsible for buying and maintaining it until the contract has been paid in full or the owner has accepted the buildings or structures covered by the policy. Because of the specialized nature of builder's risk insurance, it's important to select a knowledgeable broker to get the right policy. It's also important to procure adequate insurance based on the value of the overall project under construction, including sublimits for specific categories of losses. Finally, it's critical to understand what events can terminate coverage before the policy's actual expiration date.

Most contracts, including construction contracts, are negotiated at arm's length, put in writing and then signed by the parties. Insurance contracts are different. Coverage may be bound with a simple letter specifying the type of insurance purchased and the policy limits. The actual policy itself usually doesn't arrive until a later date and sometimes after there has already been a loss. This can create obvious problems if the coverage doesn't satisfy the construction contract or if coverage expires before a loss on the project.

Builder's risk policies, like other property policies, have a fixed expiration date, but they also have a list of other events that can terminate coverage before the full term. Failure to know and understand what events can terminate coverage, or the failure to renew a policy when a project is still under construction, can leave the project without insurance and the owner or contractor subject to uncovered losses and a breach of contract suit.

The first step in knowing how long your builder's risk coverage will last is to engage in a somewhat painful exercise: Read your policy. There may well be a conflict between the construction contract and the insurance ultimately procured with respect to duration of coverage or other issues like policy limits. If you have any concerns about how your builder's risk policy terminates or other coverage questions, consult with insurance counsel, preferably before you sustain a loss.

Here's a typical clause from a builder's risk policy, titled "When Coverage Ceases:"

- a. The insurance provided by this coverage form for each building or structure being worked on as part of a described project will end when one of the following first occurs:
 1. Your financial interest in the building or structure ceases;
 2. The building or structure is accepted by the purchaser as complete;
 3. You abandon the building or structure with no intention to complete it; or
 4. The building or structure is:
 - a. Put to its intended use; or
 - b. Leased or rented to others; unless we specify otherwise in writing.
- b. The insurance provided by this coverage form for

an entire described project will end when one of the following first occurs:

1. This insurance expires or is canceled; or
2. 90 days expire after the described project is completed, unless we specify otherwise in writing.

All builder's risk policies have such provisions, but don't assume they're identical. Recognize that coverage can end prior to the expiration date of the policy either through acts of the general contractor, the owner or both parties. Under this particular policy, there's a distinction between individual buildings or structures that are part of a project versus coverage for the entire project itself. For a project with a single building, this won't make a difference, but for a group of buildings and other structures, you have to know how these provisions determine when coverage ends.

Under the first section, if the owner accepts a building or structure as complete, occupies it or rents it to others, coverage will end for that part of the project. Likewise, if the contractor is fully paid for that individual structure or building, the contractor no longer has a financial interest in it and coverage will end. The same result occurs if the contractor abandons the project. The owner and contractor need to carefully consider the number of buildings or structures involved, the payment schedule for the project and to monitor the progress of construction closely. As buildings are substantially completed, the owner should not occupy those buildings or lease them without getting the consent of the insurance carrier. Also, check your construction contract for provisions about use or occupation of buildings during construction. Otherwise, early occupation of a building could terminate coverage even though the contractor still has remaining work to be done.

The second section addresses when the policy will terminate for the entire project instead of its component parts. The first item seems simple enough. All builder's risk policies have an expiration date and, under certain conditions, the policies can be canceled. Where this presents a particular problem is where completion of a project is delayed and the owner or contractor fails to renew the policy. If that happens, the party responsible for procuring coverage now becomes the insurer for the project in the event of a loss. The 90-day expiration date after a project is completed is another potential problem if the construction has reached a point of substantial completion, 90 days passes and then a loss is sustained prior to actual completion as defined in the construction contract.

Failure to understand your builder's risk policy or failure to make sure that its terms are consistent with your construction contract requirements can lead to substantial uncovered losses, especially toward the end of a project. Reading your policy for the first time after a major loss can be quite unpleasant—so don't put it off.

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