Talking Points Newsletter *March Vol. #25*

TSIB's Talking Points Newsletter covers recent top industry articles in the following categories:

- Insurance Market
- Construction Industry
- Claims
- Trends

This newsletter is a guide to assist you on the most important current events. We share insight on each topic and how it can affect you directly.

If you have any questions about any of these articles, other insurance & surety concerns, or have specific topics you would like to learn more about, please reach out to us directly at contact@tsibinc.com or visit our website.

Insurance Market

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Q1 Market Ups and Downs

In a new report, Amwins State of the Market, Amwins states that commercial insurance buyers will be facing a "roller coaster" ride at renewal in 2023. Some lines are softening but some lines are experiencing the worst market conditions in decades.

There is no softening in the foreseeable future for the property market, as capacity continues to shrink and deductibles rise. In addition to the rate increases that we are seeing, the carriers will start pushing the insurance to Value. This creates a double whammy as insurers feel building values are off by as much as 30%. With underwriters aware of the valuation issue, they will push values for this renewal.

Even though there have been three years of property rate increases, most reinsurers still feel that the pricing on CAT exposed programs is insufficient. The reinsurers are facing uncertainty with the macroeconomic shocks, investor fatigue, and volatile underwriting results. However, unlike the last hard market cycles after 9/11 and Hurricane Katrina, new capital is not flowing into the market.

TSIB Talking Point: Casualty accounts are getting better but the market is still in flux. Real Estate insurance remains difficult as the realities of climate change and changing weather patterns continue to cause massive losses for the insurance industry.

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Hard market prompts formation of cell captives

The hard market is driving more insureds to form protected cell captives as buyers are becoming more sophisticated and looking to access the reinsurance markets on their own.

A protected cell captive is a vehicle that allows the insured to form a protected cell within a larger captive and take advantage of the benefits of the captive without having to create a separate company. This can be much more affordable than a single parent captive. There is some concern over mingling risks between the cell owners within the protected cell company. However, there are built-in structures that prevent any issues.

TSIB Talking Point: The current market dynamics are pushing companies to utilize captives. A protected cell captive can be a useful vehicle that would help the insured to access the reinsurance markets directly. This captive can provide an economic benefit for the insured as well. It is important to note that protected cell captives are not standalone vehicles. You must have access to a larger captive that will allow you participate in their program. This can be accomplished by creating a cell within a larger captive that is presumably related to your company or if that is not available, there are captive programs set-up specifically to allow this type of transaction, they are called "Rent-a-Captive" Cells.

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San Francisco Buildings are Vulnerable in a Huge Earthquake

In February, a major 7.8 magnitude earthquake struck Turkey and Syria, killing over 42,000 people and destroyed thousands of buildings in the region.

Right now, in San Francisco, CA there are over 3,900 buildings that are as vulnerable as the neighborhoods that were destroyed in Turkey. The issue is due to buildings that are constructed using non-ductile concrete that are highly susceptible to pancaking. Non-ductile structures are brittle concrete structures that lack the steel reinforcement needed to protect against pancaking that occurs when the building is shaken from side to side in an earthquake. Pancaking is when one floor collapses on top of the other causing a chain reaction that brings down the entire building.

The city of San Francisco is in the process of developing a program to update and upgrade the buildings that are exposed. Although it has other programs in place for retrofitting unreinforced masonry and soft-story buildings, it currently does not have a formal program in place for non-ductile concrete buildings.

TSIB Talking Point: The cost to retrofit non-ductile buildings can be high. In addition, retrofitting may take many months to complete, and the process displaces the building's tenants.

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OSHA Fines to Increase as Multiplier Goes into Effect

In March, the Occupational Safety and Health Administration (OSHA) plans to increase the penalties that it levees on employers who repeatedly violate workplace health & safety rules. The program will now allow OSHA to apply "instance-by-instance" penalties on employers.

For example-
If an employer is found to have 10 employees without hardhats on the jobsite, and the fine per incident is $15,625, the employer would be fined a total of $156,250. There will likely be an increase in companies fighting OSHA fines.

TSIB Talking Point: OSHA's new mentality is an important shift, as its goal is to enforce employee safety rules. The enforcement will also apply to record keeping and logs.

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California Expands on Scope of Coverage for Soft Cost Claims

Some of the most debated claims in the builder's risk arena relate to soft cost claims. Soft costs are indirect expenses associated with project delays caused by the related property damage and repair efforts (for example, increased payments of loan interest or real estate taxes). Disputes often arise as to what is covered, along with debate on methodology as to how financial burdens have been calculated.

A California federal court addressed these issues in *KB Home v. Illinois Union Insurance Co.* and provided guidance on cases involving builder's risk insurance claims for soft cost coverage. In that case, the builder of residential home sites suffered damage and delays as a result of a severe rain event. A portion of the project suffered delays as a result. The policy purchased by the builder included both hard and soft costs. The carrier essentially denied all soft cost claims because the delays incurred did not span the entirety of the project, rather only a portion of it. In addition, the carrier denied costs associated with the interest incurred on the loans to fund the development because the financial sourcing was not that of traditional lending.

The court ruled in favor of the insured as the policy did not distinguish between delays arising from the whole project vs a portion of the project. In addition, the policy did not specify the form a construction loan should take, and, therefore, any financial instrument that required the payment of interest could be considered a construction loan. Lastly, the courts also rejected the carrier's argument that the insured's increased costs for marketing and real estate taxes were not proven.

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TSIB Talking Point: Soft cost claims are some of the most complex claims to present to a carrier. It is critical to keep detailed records of the financial impact that may arise as a result of direct physical damage. It may be prudent to consider hiring a forensic accountant to help present a claim for soft costs. Many policies contain a provision containing a sublimit for claim preparation costs.

One thing is certain, there will always be grey areas when presenting a soft cost claim. However, this case sets good precedent to help support insureds' claims in the future.

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Does High-Speed Rail Really Meet U.S. Transportation Needs?

Rail travel is getting a boost from the Infrastructure Investment and Jobs Act with $22 billion earmarked for Amtrak. This money will be used to replace Amtrak's entire fleet. In addition, another $44 billion will be allocated to light rail, passenger, and subway lines.

There are currently a few high-speed rail projects in the U.S. The most notable is the California High Speed Rail project that seeks to build a 500-mile route that connects Los Angeles and San Francisco. The cost is projected to be $113 billion. There is also another California high-speed rail project in the works, which will take passengers from Los Angeles to Las Vegas.

With speeds close to 230 miles per hour, proponents of the high-speed rail system are quick to point out that, while the cost to build these systems is high, the investment in high-speed rail is a sound one.

TSIB Talking Point: The costs are relative when you compare them to equally costly road and bridge projects. This is a smart addition to the transportation system in the U.S., as it will reduce road and air traffic.

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Department of Energy Addressing Cyber Risks

The U.S. Government Accountability Office (GAO) recently issued a report that stated that the U.S. power grid is "increasingly at risk for cyberattacks". Although the nation's grid's distribution system, which carries electricity from the transmission systems to the consumer, is primarily regulated by the individual states, the GAO has identified this as an area that the federal government must urgently address.

The systems are exposed and more vulnerable due to industrial systems increasing connectivity, which allows threats to get in and potentially disrupt operations.

TSIB Talking Point: Cyber criminals pose a significant risk to our infrastructure. In addition to the power grids, the other areas that are at risk are the communications sector, oil and gas, infrastructure, and schools, K-12. The Departments of Homeland Security, Justice, and Energy all need to enhance their interagency coordination and work together.

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