CONTRACTOR INSURANCE: The Problem is Serious

Faced with serious underwriting losses, the insurance industry will be taking a hard look at contractors’ insurance rates

The problem of insurance coverage for wall and ceiling contractors is rapidly coming to the critical stage.

In the face of heavy underwriting losses by insurance carriers, contractors can expect some hefty jumps in premiums for all types of insurance—and in some cases they may not be able to get it at all.

“The problem is really serious,” a spokesman for the Insurance Information Institute told CONSTRUCTION DIMENSIONS. “Everyone has been reading about the malpractice situation facing doctors, but the truth of the matter is all liability and casualty writers are having a profound crisis.

“The nation’s 225-year-old property and casualty insurance industry, for example, has just completed the worst year in its history with 1975 losses of $4.8 billion compared to about $2.8 billion the year before.

“Last year alone, 30 small insurance companies failed—and unless something is done quickly, some adjustments are made, more will fail this year.”

Cutting Back

As a result, insurance companies are now trying to cut back on their less profitable operations, and hundreds of thousands of car and truck owners across the country are going to experience difficulty in getting new policies or renewing current ones.

The huge losses are attributed to the same basic causes that have caused such havoc in the medical professions. That is, the consumerism movement has hit the construction industry, too.

Just as very large losses in medical malpractice cases and the accompanying increase in the tendency for people to sue their doctors, the sweeping increases in Workmen’s Compensation benefits, high unemployment, and higher awards to workers for injuries and disabilities have likewise caused commercial insurers to sustain record losses.

Nor is the developing insurance crisis limited to contractors. One iaWCC associate member, a Midwest scaffolding company, admitted to CONSTRUCTION DIMENSIONS that premiums for the firm’s product liability insurance had risen from about $600 to a whopping $35,000 a year—in just a little over six years time.

Chuck Patterson, of the Fred S. James and Company, Inc., Chicago, iaWCC’s official insurers, confirmed his industry’s difficulties. “The problem right now,” Chuck said, “is placement. It’s certainly not the shortage of contractors who want property and liability insurance coverage.

“Had I been able to place the business with carriers last year, it could easily have been an outstanding year from the sales standpoint. But underwriting was the problem. Many companies, because of the vast losses they were experiencing, simply didn’t want the business.

“Some companies — well-known and respected in the industry—have simply stopped taking business. And others have cancelled contractor clients outright—and these contractors were not bad risks. They were outstanding companies with favorable histories, who suddenly found themselves shopping around for another insurance company to assume their risk.”

Benefits Liberalized

What has brought the insurance situation to crisis proportions is the liberalizing of insurance benefits while at the same time the various state insurance regulatory authorities have been reluctant to grant carriers rate adjustments adequate to cover the additional costs.

Much of the increased benefits can be traced back to the 1972 federal study commission on insurance. This commission issued some 19 major recommendations and distributed them to the states which, in turn, began implementing many of the recommendations.

A sampling of the federal recommendation indicates what has happened. Among other things, the commission recommended extended medical and rehabilitation benefits, increased maximum death benefits, extended disability payments with benefits pegged at a percentage of the average weekly wage in the state, the establishment of “second injury funds” (based on the premise that should an employee, say, lose an eye, the loss of the second eye would be more serious and thus a second fund should be set up for this possibility), mandatory systems.

Since the commission’s report most states now have unlimited, i.e., lifetime, benefits for total disability. More and more states are changing their laws to provide greatly expanded death benefits.

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Most states now have unlimited benefits for hospital and medical care.

Some 33 states peg their disability benefits to 66-2/3 percent of the average weekly wage, and 9 states have their benefits pegged at 100 percent.

The only states which today have time limits on the benefits for total disability are Alabama, Georgia, Indiana, Louisiana, Mississippi, New Jersey, New Mexico, Oklahoma, South Carolina, Tennessee, Texas, and Vermont.

Soaring Costs

During the last two years when so much has changed, insurance carriers are quick to point out that jury awards have soared, the cost of litigation has increased, and there is an increasing tendency for employees to sue for the benefits that are allowed to them.

Yet, again, the insurance companies have been generally unsuccessful in gaining regulatory authority to increase premiums to offset the vastly increased payout.

Contrary to popular opinion, the federal government has little, if any, control over the insurance industry. The administration of insurance within the states, policy approvals, rates, and the like are reserved for each of the states’ insurance commissions.

And the states reserve for themselves the right to establish what benefits will be. Insurance companies are unanimous in their promise that they will bring increasing pressure on state regulatory authorities for rate adjustments.

“Insurers must be profitable in order to increase their capacity for accepting additional risks (policy holders),” it was explained. “If capacity continues to diminish indefinitely, the availability of insurance will dwindle and qualified customers will find it increasingly difficult to obtain essential cover-

ages in the regular market."

The Insurance Information Institute projected that contractors should look forward to a minimum increase of 20-25% in property and liability insurance during the next six months. They should expect further increases, hefty increases in most cases, in the time period beyond that.

Weed Out Risks

In the absence of higher premiums, a New York State Insurance Department report states that “on the basis of whatever objective characteristics are in vogue at the time, an insurer faced with mounting losses will weed out ‘bad risks’ by whatever methods are at hand—refusal to write (a policy), by cancellation, by non-renewal and by steep rate increases.

“Such behavior may be legal and may be quite rational to the insurer, but it can be devastating to the policy holder.”

While contractors may find little consolation in the expected premium hikes they’ll be paying, at least modern insurance is not so severe as the legal code attributed to the Babylonian king Hammurabi, who lived shortly after 2000 B.C., and from whom liability insurance developed.

His code required that if any person caused an injury, he must suffer accordingly. So, if a stone fell from a roof of a house and killed a passerby, the builder of the house was put to death.

The liability system may date from Hammurabi, but the insurance industry itself dates back 1,000 more years—also to Babylon. Merchants worked out a plan for insurance 5,000 years ago to protect their camel caravans from robbers.

The Phoenicians utilized insurance to protect ships and cargoes from peril at sea. Insurance, referred to as the “handmaiden of commerce,” was used by ancient Greeks when the expansion of Greek commerce opened up trade routes across the known world.