

Workshop T2

Tuesday, October 30, 1:30–3:00 p.m. and 3:30–5:00 p.m.

ADVANCED RISK MANAGEMENT FOR RESIDENTIAL DEVELOPERS

Presented by



Toni Johnson
Senior Vice President
Construction Practice Leader,
Northern California
Beecher Carlson Insurance
Services, LLC



Jeffrey D. Masters
Partner
Cox, Castle & Nicholson LLP

Residential projects—including tract homes, ground-up condominiums, conversions, and mixed-use projects—present some of the most challenging and complex construction risk and insurance issues. From land acquisition to construction defect concerns, residential projects pose significant risks that successful developers must address and mitigate. Designed for those with extensive construction risk management experience, this workshop addresses both insurance and noninsurance techniques for managing residential construction risks.

- Provides strategies for land acquisition, entity structure, quality control, consumer sales agreements, warranties, and myriad other sources of risk.
- Describes techniques for avoiding construction defect litigation.
- Examines general and professional liability insurance challenges and alternatives for residential construction projects.



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Toni Johnson
Senior Vice President, Construction Practice
Beecher Carlson—San Francisco

Ms. Johnson is copresenting Workshop T2, “Advanced Risk Management for Residential Developers,” on Tuesday afternoon. She recently joined Beecher Carlson—San Francisco as Senior Vice President, Construction Practice. She was formerly Client Executive and Residential Controlled Insurance Program Zone Leader, responsible for construction-related sales in Marsh’s San Francisco office and throughout the zone. As zone leader she was responsible for driving the growth of the residential construction practice as well as coordinating the delivery of all Marsh resources to her clients, supervising the client team, developing marketplace strategies, and crafting creative solutions for unusual business and insurance risks. Ms. Johnson’s expertise with complex accounts includes the oversight of designing program placement and risk management programs for her residential and mixed-use clients.

Ms. Johnson joined Marsh in 2006. Previously she was chief risk officer for a large residential and commercial builder and served as an officer for a construction-focused risk management solutions firm. Ms. Johnson has held key roles for several insurance companies and as a construction producer at a large commercial brokerage. She has developed creative risk transfer programs that have reduced costs, enhanced value, and increased client control of their risk management programs. She is also a trusted resource to several leading construction focused law firms.

Ms. Johnson is a sought-after speaker to the risk management and insurance construction industry. She is an active volunteer in her community, including board membership to the San Francisco Symphony and executive board member to Girls Incorporated, a national nonprofit organization.

Jeffrey D. Masters
Partner
Cox, Castle & Nicholson LLP

Mr. Masters is copresenting Workshop T2, “Advanced Risk Management for Residential Developers,” on Tuesday afternoon. He is a partner in the Litigation Department and cochair of the Development Risk Management Practice Group at Cox, Castle & Nicholson LLP in Los Angeles.

He represents developers, home builders, contractors, and lenders in complex insurance coverage, construction defect, and real estate litigation matters. He also has extensive experience structuring insurance and risk management legal programs for projects of all sizes.

Mr. Masters is a frequent lecturer and author for real estate industry groups such as the Building Industry Association, PCBC, the National Association of Home Builders, and Urban Land Institute, as well as IRMI. He is coauthor of the educational materials and co-instructor for IRMI’s seminar series, “Construction Defect Risk Management and Insurance,” and for NAHB’s educational course, “Risk Management and Insurance for Building Professionals.”

Mr. Masters is rated AV, the highest rating available, by Martindale-Hubbell, which facilitates the peer review rating process for lawyers. He is a graduate of UCLA School of Law and UCLA Anderson Graduate School of Management.

Notes

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Advanced Risk Management For Residential Developers

IRMI
October 30, 2007

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OVERVIEW AND SESSION OBJECTIVES

- Understand the residential liability landscape
- Identify the developers
 - Production homebuilders (public and private)
 - Investors and their advisors
 - Developers of other real estate product types entering the residential market

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OVERVIEW AND SESSION OBJECTIVES

- Recognize different residential product types
 - SFD
 - Attached
 - Mixed use
 - Mid-rise and high-rise
 - Condo hotels
 - Condo conversions

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OVERVIEW AND SESSION OBJECTIVES

- Offer strategies to avoid, minimize, shift, insure and retain liabilities
 - How to design and implement non-insurance risk management strategies
 - How to employ insurance structures and strategies

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LIABILITY ISSUES

- Claim trends
- How residential construction defect litigation starts

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LIABILITY ISSUES

- Plaintiff tactics developers will confront

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LIABILITY ISSUES

- Need to anticipate homeowner and HOA claims and proactively manage liability risks

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LIABILITY ISSUES

- Why implement a risk management legal program?
 - Litigation threat
 - Large SIRs
 - The New Underwriting
 - Protect brand equity
 - Enhance loss history
 - Preserve limits

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NON-INSURANCE RISK MANAGEMENT STRATEGIES

- Site acquisition
 - Environmental issues – onsite and offsite
 - Environmental insurance tools
 - CPL
 - PLL
 - Cost cap
 - Lenders' coverage

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NON-INSURANCE RISK MANAGEMENT STRATEGIES

- Site acquisition
 - Due diligence may generate information that must be disclosed
 - How to capture this information

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ENTITY RISKS

- Practical tips for minimizing alter ego risks
 - Capitalization
 - Formalities
 - Provisions for post-dissolution claims

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ENTITY RISKS

- How and when to dissolve the entity?
 - Reasons to dissolve
 - Handling post-dissolution issues
 - Customer service and warranty operations
 - Payment of SIRs
 - Claims management

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QUALITY ASSURANCE PROGRAMS

- Four main components
 - Design peer review
 - Construction observations
 - Closure
 - Document retention and retrieval systems

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QUALITY ASSURANCE PROGRAMS

- Pre-qualifying the QA consultant
 - Experience with the product type
 - Closure and re-observation procedures
 - Observers as employees
 - Flexible regarding SOW and sampling
 - Handling discrepancies
 - What does the price include?

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QUALITY ASSURANCE PROGRAMS

- Practical issues
 - Plan review tends to reduce discrepancies
 - Conducting pre-construction meeting(s)
 - Documenting peer review changes and value engineering

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QUALITY ASSURANCE PROGRAMS

- What does your CGL program require?
 - May be only a minimum standard
 - What did you commit to in the application?

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QUALITY ASSURANCE PROGRAMS

- QA sample size and other developer decision points

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QUALITY ASSURANCE PROGRAMS

- Documenting closure of open items

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QUALITY ASSURANCE PROGRAMS

- Document retention and retrieval systems

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QUALITY ASSURANCE PROGRAMS

- Negotiating contracts with QA consultants – practical tips
 - Is it realistic to expect risk transfer?
 - Insurance and indemnity obligations
 - Observation and reporting timelines
 - Who is the QA consultant reporting to?

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PROTECTIVE PROVISIONS IN CONSUMER SALES AGREEMENTS AND CC&RS

- Recap of major protective provisions
 - Dispute resolution – contractual rights of:
 - Notice of defects
 - Access
 - Inspection
 - Testing
 - Repair
 - Need to coordinate with state NOR statute requirements

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PROTECTIVE PROVISIONS IN CONSUMER SALES AGREEMENTS AND CC&RS

- Maintenance obligations and education
- Maintenance manuals

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PROTECTIVE PROVISIONS IN CONSUMER SALES AGREEMENTS AND CC&RS

- Disclosures
 - How to build a better disclosure
 - Think broadly
 - Don't editorialize
 - Finish strong

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PROTECTIVE PROVISIONS IN CONSUMER SALES AGREEMENTS AND CC&RS

- Project reconfiguration rights

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PROTECTIVE PROVISIONS IN CONSUMER SALES AGREEMENTS AND CC&RS

- HOA pre-litigation requirements
 - Written notice and disclosure to homeowners of nature of dispute, anticipated costs, prospects for success
 - Opinion from independent counsel
 - Special meeting of homeowners
 - Majority or supermajority vote required to authorized litigation
 - Reserve funds may not be used for litigation (HOA must specially assess)

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ADR ENFORCEABILITY ISSUES

- Enforceability of ADR provisions, particularly arbitration provisions

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ADR ENFORCEABILITY ISSUES

- Unconscionability attacks on arbitration provisions
 - Procedural
 - Substantive
- Strategies for defeating unconscionability attacks – how to build a better arbitration provision

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ADR ENFORCEABILITY ISSUES

- Can subsequent purchasers be bound to the ADR provisions?

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ADR ENFORCEABILITY ISSUES

- Binding HOAs to ADR provisions

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HOA INSURANCE REQUIREMENTS

- CGL and excess/umbrella
- Property
 - WOS in favor of developer?
 - EQ, flood, windstorm?
- D&O
- Auto
- Crime

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REDUCING SALES AND MARKETING RISKS

- Disclosures revisited
 - Square footage
 - Acoustical
 - Pricing and sales concessions
 - Project reconfiguration
 - Assessment, fees and taxes
- Training and management of salespeople in the new market environment
- E&O insurance?

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TRANSITION FROM DEVELOPER CONTROL

- HOA budgets as a source of risk
- Mitigation tactics
 - Qualified budget preparer
 - Regulatory minimums
 - Reflect the reality of the project
 - Link to HOA maintenance obligations and maintenance manual

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TRANSITION FROM DEVELOPER CONTROL

- Developer presence at the project
 - Fiduciary duty concerns
 - Should the developer retain membership on the HOA board?
 - Developer liaisons to the HOA
 - Training of homeowner board members
 - D&O insurance concerns

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TRANSITION FROM DEVELOPER CONTROL

- Selection of HOA property management company and HOA counsel

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TRANSITION FROM DEVELOPER CONTROL

- Formal protocols for turnover of common area
 - Include in CC&Rs
 - Walkthrough procedures
 - Inspection reports and punchlists
 - Photo or video documentation
 - Board resolution
 - Opportunity for disclosure and education

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DESIGNING AND IMPLEMENTING EFFECTIVE INSURANCE PROGRAMS

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INSURANCE STRUCTURES

- Conventional annual renewal policies
- Wrap-ups
 - Project specific
 - Rolling
- Drivers for wrap-ups

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WRAP-UP COVERAGES TO CONSIDER

- CGL and excess liability
- Builder's risk
- CPL or PLL
- BI/PD coverage for professionals
- Project PL programs
- WC/EL

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CGL INSURANCE MARKET REPORT

- Who is writing residential developers?
 - Domestic and non-domestic markets
 - Primary markets
 - . ACE/Westchester
 - . American Home (AIG)
 - . Arch
 - . Arrowhead (Safety Mutual)
 - . C&F
 - . Gemini

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CGL INSURANCE MARKET REPORT

- Primary markets
 - . Glencoe
 - . Interstate
 - . Investors
 - . Lexington
 - . Lloyds (Wellington Aspen, Caitlin)
 - . Navigators

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CGL INSURANCE MARKET REPORT

- Umbrella/excess markets
 - . AIG
 - . Axis
 - . AWAC
 - . CV Starr (Everest)
 - . Endurance
 - . Gerling
 - . Lloyds (Wellington, Aspen, Caitlin)

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CGL INSURANCE MARKET REPORT

- Umbrella/excess markets
 - . Scor Re
 - . Westchester
 - . XL (Dublin)

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CGL INSURANCE MARKET REPORT

- Conventional annual renewal
- OCIPs
 - Project specific
 - Rolling
- CCIPs
- Project PL programs

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ALTERNATIVE RISK APPROACHES

- Finite risk programs
- Captives

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THE APPLICATION AND UNDERWRITING PROCESS

- What are underwriters looking for?
- How to craft an effective submission

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PRACTICAL TIPS FOR SUCCESSFUL RESIDENTIAL INSURANCE PLACEMENTS

- Practical tips for successful placements
 1. Start early
 2. Use specialized resources
 3. Tell your risk management story
 4. Beware nonstandard forms and endorsements
 5. Recognize different coverage structures (occurrence vs. claims made vs. close of escrow)
 6. Avoid nonconcurrency

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PRACTICAL TIPS FOR SUCCESSFUL RESIDENTIAL INSURANCE PLACEMENTS

7. Understand coverage restrictions and their impact on your operations
8. Assess lender, investor and municipality requirements
9. Enlist the contractor and design professionals early
10. Be prepared to make fast decisions

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PRACTICAL TIPS FOR SUCCESSFUL RESIDENTIAL INSURANCE PLACEMENTS

- Are you binding what you ordered?
- Watch subjectivities and commitments made in the application

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SELECTED OCIP COVERAGE ISSUES

- Non-standard policy forms revisited
- Modifiability of the forms and endorsements

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SELECTED OCIP COVERAGE ISSUES

- Extended products-completed operations coverage

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SELECTED OCIP COVERAGE ISSUES

- Coverage for post-completion repair work
 - How is repair work defined?
 - Duration of the coverage
 - Substitutability of contractors and subcontractors

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SELECTED OCIP COVERAGE ISSUES

- Cancellation

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SELECTED OCIP COVERAGE ISSUES

- Exclusion J(2): premises you sell
 - "... This exclusion does not apply if the premises are 'your work' and were never occupied, rented or held for rental by you."

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SELECTED OCIP COVERAGE ISSUES

- Exclusion L: Your work

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SELECTED OCIP COVERAGE ISSUES

- Property damage to the project during COC

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SELECTED OCIP COVERAGE ISSUES

- Insured versus insured; cross-suits
 - BI implications
 - PD implications

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SELECTED OCIP COVERAGE ISSUES

- Earth movement and subsidence

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SELECTED OCIP COVERAGE ISSUES

- Professional services and professional liability

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SELECTED OCIP COVERAGE ISSUES

- **Deductibles and SIRs**
 - Per occurrence vs. other structures
 - How is the deductible or SIR eroded?
 - Special notice and reporting requirements
 - Who may satisfy the SIR?

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SELECTED OCIP COVERAGE ISSUES

- **Limits of liability**
 - Selection of limits
 - Reinstatement of aggregates

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SELECTED OCIP COVERAGE ISSUES

- Coverage for past projects when using a close of escrow CGL form
 - The problem
 - Possible approaches
 - Availability of prior CGL coverage
 - Special servicing protocols
 - Prior operations buyout policies

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SELECTED OCIP IMPLEMENTATION ISSUES

- Need for comprehensive OCIP exhibit to design and construction contracts
 1. Eligible and ineligible parties
 2. Summary of coverages and limits afforded by the OCIP
 3. Enrollment process
 4. Responsibility for contribution toward the policy SIR

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SELECTED OCIP IMPLEMENTATION ISSUES

5. Calculation and collection of insurance credits
6. Disclaimers by Sponsor; representations and warranties by enrolled parties
7. Joint defense agreement
8. Discontinuation or modification of the OCIP coverages

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SELECTED OCIP IMPLEMENTATION ISSUES

9. Statement of coverages not provided by the OCIP
10. Handling subrogation claims which might affect the OCIP coverages
11. Enrolled parties' duty of cooperation; compliance; record retention and disclosure; audits
12. Dispute resolution provisions

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SELECTED OCIP IMPLEMENTATION ISSUES

13. Effect on indemnity obligations?
14. Obligations regarding safety, loss control and quality assurance programs imposed by developer, contractor and/or OCIP insurers
15. Compliance with recommendations and requirements of OCIP insurers and their representatives

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SELECTED OCIP IMPLEMENTATION ISSUES

- Disclosure issues
 - California SB 195

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SPECIAL ISSUES IN CONDOMINIUM CONVERSION PROJECTS

- Liability trends
- Disclosure issues
- Coverage issues

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LIABILITY TRENDS

- What is the converter liable for?
 - New construction
 - Original construction

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DISCLOSURES

- Need for enhanced disclosures
- Mandatory disclosure statutes
 - Example: California Civil Code §1134

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SELECTED INSURANCE COVERAGE ISSUES

- Prior work exclusions
- Prior defects and damages exclusions
- "Your work" limitation in PCO definition
- Exclusion J(2): premises you sell

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