

# Construction Zone Warning: Contractor Exposures Ahead

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Construction subcontractors come with significant advantages to builders, enabling them to supplement their workforce and augment their core offerings. At the same time, they bring added exposure to risk, which can be costly.

Granted, subcontractors often operate in a dangerous, high-risk, high-volatility environment. But all too often, avoidable residual losses arise when subcontractors are not carefully vetted and selected.

## UNDERSTANDING THE IMPACT OF EXPOSURES

Keeping a project on time, on budget and executed to the highest of safety standards are key objectives for any competitive builder. But, even the most competently, diligently managed construction projects are subject to accidents, project delays, errors or mishaps. This can be a significant hit to the bottom line—and more importantly, a company's reputation. Particularly when selecting subcontractors, it's important to understand exposures and their long-term impact to the business. While competitive pricing is understandably a key factor in evaluating subcontractor bids, making a decision on price alone can potentially expose builders to high risk in the following areas.

## RESIDUAL EFFECT OF ACCIDENTS AND INJURIES

Nearly 6.5 million people work at approximately 252,000 construction sites across the nation on any given day, according to OSHA. The fatal injury rate for the construction industry is higher than the national average in this category for all industries.

Construction workers face primary exposures to safety hazards and compliance issues, as well as personal and business liabilities. In today's litigious climate, contractor credibility, compliance and safety data have become key qualifiers—and they can be deal breakers. Now, it's considered routine that RFPs require contractors to elaborate on their safety program. OSHA searches reveal the number and type of past violations. A company's Experience Modification Rating (EMR), a measurement of its relative workers' comp history, is a standard request.

Developers and builders simply cannot hire contractors with high injury rates or compliance credentials that fall outside of industry standards, especially when they have another contractor in better standing at their disposal that can handle the project.

## INDIRECT LIABILITY COSTS

The direct costs of accidents and injuries are straightforward. These exposures can translate to millions of dollars in hospital bills. The loss is even greater in cases where the injured is not covered by insurance. Lack of proper coverage can lead to lawsuits, which translate to significant loss of time and money.



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Workers' comp is one of the most expensive lines of coverage, and more claims equate to higher insurance rates. As a result, insurance costs on large general contractors and construction managers are getting so high that they've become non-competitive. This is a big problem for companies, especially in a market like New York City, where there's a huge amount of construction and claims are high. Some indirect costs related to workers' comp may include:

- third-party liability;
- worker's pain and suffering;
- various legal fees;
- OSHA fines;
- wages not covered;
- administrative fees; and
- hiring and training replacement employees.

### LONG-TERM PR/REPUTATION DAMAGES

Construction generates high-interest media coverage. There's a large construction accident with injuries and it's all over the media. An accident not only causes significant financial loss, it damages reputation. The old adage, "A good reputation is more valuable than money," has some merit. In a highly competitive market, PR issues drive a difference in costs. A bad reputation harms the company's immediate status and it can prevent it from getting work in the future.

Needless to say, these risks are not all-inclusive and understanding the landscape requires a deeper dive. The point is it's essential to have a handle on the risk exposures and related costs associated with hiring contractors. And more importantly, it's best to take proactive steps to manage them.

### TOOLS FOR SUCCESS: KEY STEPS TO SAFEGUARD AGAINST POTENTIAL LOSS

1. **Select only qualified subcontractors.** Screen subcontractors properly to make certain workers are experienced and adequately trained. Put processes in place to vet licensing and certification, experience (project size and scope) and expertise. To reduce the risk of the financial loss as a result of injuries, procure contractor prequalification services to verify whether a contractor is maintaining adequate workers' compensation coverage. Contractor screening enables verification that a contractor's insurance contains the right coverage throughout the project's life, and that the proper safety procedures and training are in place to protect the business.
2. **Obtain appropriate insurance coverage.** Insurance is a primary method of managing a range of construction contract-related risks. Quality subcontractors should be Insured for accidents and bonded for payment and performance. Industry standard coverage includes:
  1. workers' comp;
  2. commercial general liability;
  3. business auto;
  4. umbrella/excess liability;
  5. additional insureds protection;
  6. primary and non-contributory;
  7. policy changes cancellation; and
  8. surety bonds or other payment and performance guarantees.

The utilization of captive insurance can be a supplement or alternative insurance vehicle to traditional commercial insurance, which prices its premiums based on claims data for broad business categories such as construction, manufacturing, health care and related sub-sectors within those categories. This is an attractive option for construction companies with higher construction volumes and favorable claims history relative to industry peers.

3. **Create a positive safety culture.** Taking a proactive approach to safeguard the firm and manage risk means more than simply obtaining insurance coverage. Establishing risk control guidelines, developing training and implementing safety programs, along with reinforcing and measuring results can be valuable tools in creating a safer work environment, reducing costs and establishing a favorable position in contract negotiations and business development.

Consider the advantages of obtaining risk management consultants as a viable approach to jumpstarting a risk management program efforts, providing expertise in areas such as:

- developing and reviewing safety plans;
- helping with accident investigation;
- program design to prevent safety issues and accidents in the future; and
- developing a risk management philosophy.

Appropriate foresight, planning, training and reinforcement can reduce the impact of contractor risk exposures, safeguard against loss, and achieve safer, more efficient and profitable project execution. Build higher levels of trust in business dealings, negotiate better contracts and ensure a competitive advantage in an exceedingly competitive marketplace.