



RISING PREMIUMS

# How Tariffs Affect Construction, Insurance Costs

**P**RESIDENT TRUMP'S far-reaching tariffs are starting to bleed into building costs as many of the main materials used in construction are now subject to import taxes.

And as construction costs increase due to tariffs, so does the cost of repairing or replacing materials if damage occurs during construction. Rising repair and replacement costs make claims more expensive, and, in turn drive up the cost of property and casualty insurance for contractors.

Inputs for construction have already been on the rise for the last six years — particularly in 2020-2022, when the COVID-19 pandemic devastated global supply chains — and now many materials used in building or to build equipment and tools have been hit with hefty tariffs.

### Effects on insurance

These policies' premiums are tied to the cost of materials and the length of a project. If building materials like lumber and steel cost more due to tariffs, the insured value of the project increases.

Example: A contractor is constructing a \$25 million office building. If the tariff on imported steel and lumber increases the project cost by 10%, the insured value would increase by \$2.5 million. The insurer accounts for that higher replacement value in its premium calculation, which will result in a larger premium.

Another factor that could result in higher claims costs is snarled supply chains — builders will have to wait longer for materials. That, in turn, can increase the building timeline, and if that happens, the contractor will need to extend their builder's risk policy.

That will cost more as well, as the insurer will charge for the extension due to the longer exposure it will face.

See 'Be Sure' on page 2

## Recent construction material tariff hikes

- **Aluminum** – 25% tariff as of March 12.
- **Lumber and timber** – There is a 14.58% tariff on Canadian lumber, a rate that could rise to nearly 35% in coming months. The administration is studying whether to impose a 25% tariff from on lumber from all nations.
- **Steel** – 25% as of March 12.

Prices for building inputs may rise even higher if tariffs start snarling supply chains, which is a possibility. Higher tariffs can make imported goods harder to source and more expensive, forcing contractors to find new suppliers or wait longer for deliveries.

That can slow down a construction project, which costs money and increases exposure to a number of risks, including:

- Fire,
- Weather damage,
- Theft, and
- Vandalism, among others.




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## CONSTRUCTION RISK

# Check Subcontractors' Insurance Policies

**D** ID YOU know your firm can be held liable under your own workers' comp policy if a subcontractor's employee is injured? Courts have ruled time and again that if a company hires a subcontractor without coverage and an employee gets hurt on the job, the injured worker can seek coverage under the hiring company's policy.

In many cases, an injured worker may even be a third- or fourth-level contractor, but if none of your subcontractors are carrying workers' comp, a claim can hit your own policy.

This scenario is even more likely if your firm, as the main contractor, has substantial control over the sub's employees.

To determine coverage, courts generally start with the sub whose employee was injured and move up the chain until they find a valid workers' comp policy.

Protect yourself by requiring your subcontractors to have a certificate of insurance. But don't stop there; you should call the insurance carrier to see if the certificate is valid.

You can also check with your state's contractor licensing board to see if your subcontractor has workers' comp coverage. ❖



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## Be Sure to Get Copy of Any Maintenance Contracts

**General liability coverage extension** — If delays occur, so will the exposure to increased worksite injuries, damage or third party claims. For each additional day a project takes to complete, the risk of an accident also increases.

Example: If a project extends past its deadline, the general liability policy would need to be extended for the additional time. And it's unlikely that extension will be priced at the same rate as the original liability policy. Insurers will often reprice the policy extension based on the extended exposure and the kinds of subcontractors or equipment that will be on site.

### The takeaway

Higher cost of materials and insurance costs will make their way into project budgets, bids and profit margins. Another risk is that insurance certificates are delayed or found to be non-compliant, which can delay payments, result in expensive work stoppages and breaches of contract.

With all this in mind, you will need to work closely with your broker well in advance for new projects to ensure that your coverage reflects the reality of higher material costs, the possibility of delays due to procurement issues and more. ❖

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## COMMERCIAL FACILITIES

# Managing Higher Property Insurance Deductibles

**A**S COMMERCIAL property insurance rates have climbed steadily in the last five years, insurers have been increasing deductibles, sometimes for all risks, but sometimes for specific perils, such as hail.

Often, business owners fail to notice these increased deductibles until they file a claim. Sometimes, their dollar-amount deductible has been replaced by a deductible that covers a certain percentage of a claim's value, sometimes as high as 5% to more than 10%.

The result for businesses is that their premiums have climbed, and they now have more skin in the game. But these changes can be costly, particularly ones that are based on a percentage of a claim. Navigating these higher premiums may require some negotiation with the insurer — something we can help with.

## The deductible buydown

A key strategy emerging to manage rising deductibles is the use of deductible buydowns, also called buybacks.

A deductible buydown is a separate insurance policy that allows a property owner to “buy back” a portion of their large deductible. For an additional premium, the buyback policy kicks in after a covered loss to offset the out-of-pocket amount the business must pay under its main property insurance policy.

For example, if a hurricane causes \$100 million in damage to a factory with a 5% deductible, a buydown policy could reduce that deductible exposure to a much more manageable figure, such as \$1 million, with the insurer covering the rest of the deductible.

## Pros and cons

Buydown coverage can dramatically reduce financial exposure after a large loss without requiring the company to pay prohibitively high base insurance premiums.

In areas highly exposed to natural disasters, a buydown can make the difference between recovering quickly after a storm or facing devastating financial strain.

Buydown policies are not cheap and businesses must carefully weigh whether the likelihood of a claim justifies the added expense.

In relatively low-risk areas, or for companies with sufficient cash reserves to cover a large deductible, the additional cost of a buydown may not be worthwhile. Also, buydown policies come with their own terms and exclusions that must be reviewed to avoid coverage gaps.

## Which businesses benefit most?

- Companies with high-value properties exposed to frequent natural disasters (e.g., resorts, coastal hotels and manufacturing plants in Tornado Alley).
- Businesses with tight cash flows or low cash reserves that would struggle to pay a high deductible after a loss.
- Firms with lender requirements capping allowable deductible amounts.
- Organizations with a significant concentration of properties in high-risk geographies, where natural disasters could trigger multiple losses simultaneously.

Businesses with strong balance sheets, low-risk property locations or highly diversified property portfolios may be better off absorbing the risk or structuring their primary insurance policies to limit their exposure through narrower deductible applications.

## The bottom line

Buydown costs between 6% and 15% of the insured value, depending on factors like location, property type and peril-specific risks.

You may also be able to purchase a buydown for only specific locations or perils. You can identify sites that may have a higher exposure to a natural catastrophe and purchase buydown coverage for your properties in that area and for the specific peril.

We can help you negotiate language that limits the percentage and the geographic region to which it applies. ❖



## CONSTRUCTION PREP

# Preparing for Surety Bond Underwriter Queries



**I**F YOU'VE been involved in a large construction project, you are familiar with surety bonds and all of the underwriter's questions you need to answer. If you're new to the game, it can be daunting.

Many small contractors pass on bidding for projects if they require a surety bond. But it doesn't have to be that way as long as you are prepared and know what kind of questions the surety insurer's underwriter will be asking.

Surety bonds protect project owners from loss if the contractor's work is defective or of poor quality, or if the contractor fails to complete the work or follow the terms and conditions in the agreement.

For example, if the contractor fails to finish a project due to a shortage of workers or financial problems, the surety company has to step in and perform in the contractor's place. Obviously, it's in the carrier's best interest to insure projects where they won't be asked to perform. As a result, the questioning can feel like an inquisition, but it's worth it to be prepared so that the insurer underwrites the bond and you can get to work.

## TYPICAL QUESTIONS

- Have you, the principal, ever worked with this owner or general contractor (if you're a subcontractor)? What was that project, and was it successfully completed?
- Can we confirm financing on any private project? This question aligns with Section 2.21 on the American Institute of Architects Document A201.
- What is the project scope? Have you worked on a similar project before, and what was the outcome of that project?
- Geographically, are there any constraints that could impact your ability to complete the project? For example, if you're working in a state with proprietary workers' compensation laws, can you obtain the necessary insurance coverage to comply with that state's statutory workers' compensation requirements?
- What is the warranty period? Is it a typical time period or longer than usual?
- Name any material manufacturers involved in the warranties, and do the contract terms allow the contractor to tender claims to them?

## Other areas of scrutiny

Besides the questions in the box, the insurer will also likely want to know:

- If the start and completion dates in the contract are feasible.
- The amount of the bid bond if there is one.
- Any warranty terms and if they are sensible.
- The payment terms and if they will allow the owner to manage expenses during the life of the project.
- If there is any retainage, or the withholding of the final contract payment for a specific time period, to ensure that the job has been properly completed.
- If there are any damages set out in the contract in case of non-performance or shoddy workmanship.
- If the contractor's costs to complete other projects it is working on are sufficient to ensure that it can cover its general and administrative costs in the following year.

The above list is not exhaustive, and some surety insurers may have different areas of interest.

The bottom line is you'll want to make sure your finances are up to snuff and that you have a strong track record. ❖