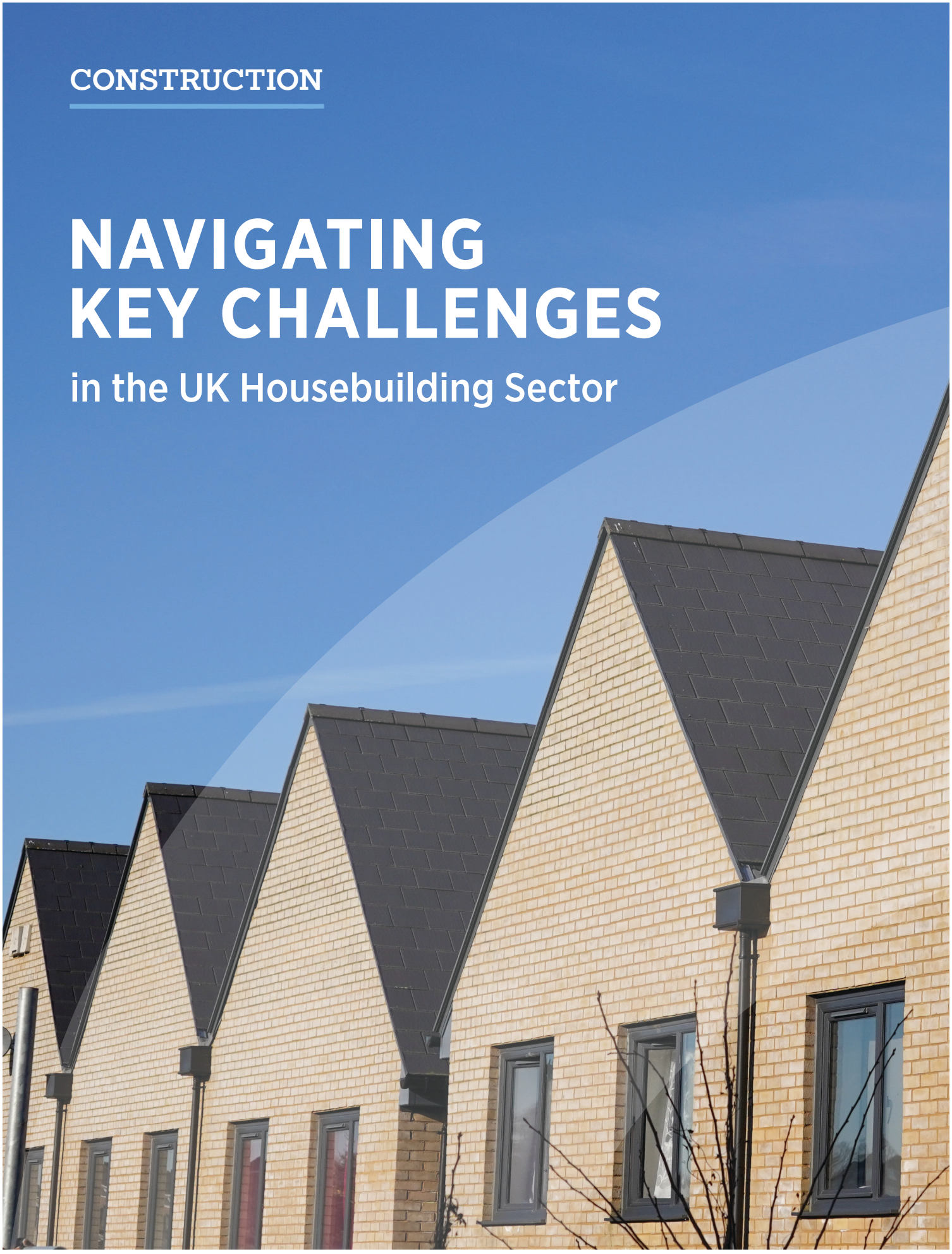
CONSTRUCTION

NAVIGATING KEY CHALLENGES

in the UK Housebuilding Sector



Gallagher SPECIALTY

The UK housebuilding sector is navigating a complex landscape characterised by ambitious growth targets, challenging planning environments, legacy build issues and labour shortages. These factors demand a nuanced understanding of the industry's unique risk profiles and insurance needs.

This paper explores two critical areas that are shaping the future of housebuilding: mergers and acquisitions, and cladding and fire safety. By examining these topics, we aim to provide insights into the evolving challenges and opportunities within the sector.

MERGERS & ACQUISITIONS

M&A activity in the residential construction sector has increased significantly in recent years, driven by economic stability, government housing initiatives, and the need for sustainable construction innovation. These factors have led to strategic mergers and acquisitions as businesses diversify to smooth market volatility, vertically integrate for competitive advantage, acquire niche expertise and enhance their brand reputation.

Another key driver in M&A activity is recognition of the value in operating multiple brands targeting distinct customer segments. Multiple branding gives companies access to a wider customer base, can reduce build times and make larger sites viable. This, in turn, provides enhanced return on assets, accelerated cash generation and improved returns of capital for the business.

With housebuilders lined up to deliver the ambitious growth targets set by the UK government, and further M&A activity likely, now is a good time to consider the impacts that both organic and acquisitional growth can have on your insurance and risk management strategies.

TYPE OF ACQUISITION

Initially, it is important to consider the type of acquisition. Whilst there are many different types, they are generally share purchases, asset purchases or the acquisition of defined assets and liabilities. In housebuilding, we have seen many recent examples of whole company share purchase acquisitions, while asset acquisitions are also common on land and even equipment when it comes to vertical integration into the supply chain, such as manufacturing capabilities.

The different types of acquisition will impact a business in a variety of different ways, and whilst the focus of the business may be operational integration, supply chain efficiencies, synergy savings, etc., your insurance broker should be working with you to consider the implications for insurance and risk management strategy.

> Integration of insurance programmes enables the Insured to realise economies of scale, leading to substantial recurring cost savings and broader cover, whilst also avoiding the operational pitfalls caused by policy overlap.

INFORMATION GATHERING

Through the due diligence process, insurance information such as current policy schedules and claims listings is often uploaded to a data room. It is often assumed that this level of information is sufficient for an insurance broker to provide advice on a planned acquisition; however, much more detail is required to provide strategic advice at this critical phase. Historic and current information should be obtained for each class of insurance, such as policy schedules, wordings, claims experiences (including claims run-off), details of any 'stand-alone' placements and underwriting submissions. Information should also include 'go forward' estimates, historic exposure information, details of core business activities and joint venture participation. These lists are not exhaustive, but they do give a feel for how much information is required to undertake a thorough review and provide guidance on behalf of the acquiring entity. Important examples for housebuilders to consider would be the provision of any cladding and fire safety reviews undertaken and the scope of historic reviews and claims notifications under a professional indemnity policy.

Also, giving due consideration to the contractual liability and insurance obligations of the business to be acquired through the due diligence phase will be imperative to shaping the go-forward insurance and risk management strategies. This may require the provision and review of contracts or agreements.

RISK PROFILE

One of the most obvious things to consider is changes to the risk profile of the business, at past, present and future. An example could be the introduction of new risks or exposures previously unfamiliar to the acquiring business, for example, a timber frame manufacturing facility. Insurers' appetite to provide cover can change with the introduction of different activities, exposures or risk management approaches. Insurers may also be subject to certain underwriting restrictions that inhibit their ability to meet the needs of your business going forward. This can change the landscape dramatically in terms of your relationship with your partner insurers and emphasises the importance of maintaining healthy relationships with several sector specialist insurers. Examples of risks associated with housebuilding that could impact upon insurer appetite or ability to provide cover are high-rise development, use of timber frame and Modern Methods of Construction (MMC).

HOW CAN GALLAGHER HELP?

From experience in managing some of the largest acquisitions and mergers in the housing market, Gallagher can play a crucial role in helping you navigate the insurance risks that arise from an acquisition.

We can assist you in:

- The due diligence process
- Review insurers' reserving practices and, where required, advise on the reservation of rights to protect insurance cover
- We are aware of the challenges in obtaining claims data, particularly historic run-off, and can help you pull together an accurate claims picture of the combined entity to ensure you get the cover and terms that accurately reflect the merged business
- Depending on how integrated the business is post-acquisition, an option could be to run concurrent programmes, and we can help ensure coverage is aligned and you still get the benefits of scale in insurance pricing
- A combined group will present a different insurance risk, and we can advise on alternative structures, limits, retentions, appetite or alternative risk transfer strategies
- Procedures — insurers in-house handling, client appointments such as TPAs and loss adjusters
- Help maintain strong relationships with insurers and, importantly, ensure you get the competitive benefits that derive from economies of scale

CLADDING AND FIRE SAFETY

Ever since the Grenfell Tower tragedy in 2017, challenges relating to cladding and fire safety have been high on the agenda for firms operating in the UK residential sector. The market for construction Professional Indemnity (PI) insurance has been particularly difficult, reflecting underwriters concern around the potential for historic design liabilities to develop into future claims. An influx of claim notifications followed on a scale not previously seen in the UK PI market. This was further exacerbated by the extended limitation periods applicable for claims under the Building Safety Act 2022 (1).

Notwithstanding these challenges, PI market conditions have improved markedly over the past 24 months. This is driven by increased capacity and a strong desire for growth among insurers, leading to heightened competition. As a result, significant rate reductions and a loosening of coverage restrictions, particularly concerning fire safety and cladding, have been observed.

The market has now widely adopted the IUA Cladding and Fire Safety restricted coverage clauses, the key features of which are

- Negligence trigger
- Single aggregate limit
- Exclusion of consequential losses

Despite these safeguards against substantial new claims activity, we are aware of multiple residential construction firms that have been unable to secure cladding and fire safety cover for their current activities at a competitive premium and reasonable level of excess. In many cases, cladding and fire safety liabilities had been fully excluded during the hard market cycle, with any reinstatement over recent renewals being partial (lower limit, higher excess) or secured at unfavourable terms. This can be a barrier to winning work, both on new residential schemes and external wall remedial works.

Another frustration for many PI buyers is the slow pace of progress on cladding and fire safety claims. It is indicative that a significant proportion of claims notified in 2018 and 2019 have still not reached settlement. There is a notable deficit of specialist insurance and legal resources to deal with an unprecedented volume of claims, and while this goes some way to explaining the delays in achieving settlements, we have also seen progress frustrated by:

- Slow or contested coverage decisions
- Insurer challenges around the scope and timing of notification
- Reactive broker approach to claims management

All of these factors contribute towards unsatisfactory outcomes and spiralling legal costs.

Challenges around cladding and fire safety are not confined solely to the PI market, however. With a vast number of remedial works planned over the coming years, residential developers and contractors are now focusing on the terms and conditions which will apply to these schemes. Contractual negotiation around property and injury risks can be complex, especially where works are undertaken in occupied apartment blocks.

Key considerations include the allocation of risk and liability for damage to the existing structure and for any resultant consequential losses such as rehousing occupiers, as well as the insuring obligations of each party, which are likely to span property, construction all risks and third-party liability insurances as a minimum.

HOW CAN GALLAGHER HELP?

Gallagher have represented a number of large housebuilder clients throughout the 2017-2025 market cycle. Our deep experience enables us to maximise claims returns from historic policies and capitalise fully on the current softening conditions. We can assist you in:

Retaining or reinstating cover for cladding and fire safety

- We use a data-driven approach to secure the optimum PI renewal outcomes for our clients, achieving average rate reductions of 15% in 2024, which increases to circa 25% for new clients.
- We have successfully reinstated cladding and fire safety cover for several new clients on a limited retro basis. This cover can often be achieved at negligible or nil additional premium and at no increased policy excess.
- To achieve these outcomes, it is critical to demonstrate a solid understanding of your cladding and fire safety exposures, and Gallagher can assist in this process.

Optimising claims outcomes

- Specialist knowledge of our claims team, which includes qualified lawyers and a former insurer's head of construction claims.
- Protocols which remove claims roadblocks, e.g., (1) limiting knowledge of claims/circumstances to key individuals at Insured, (2) pre-agreed timescales for designated steps in the process and (3) dispute resolution.
- Support in securing recovery from the supply chain.

(1) Defective Premises Act 1972 amendments:
- Five years for claims regarding works completed after 28 June 2022;
- 30 years for claims regarding works completed before 28 June 2022.

Ensuring that risks associated with remedial works are appropriately allocated and that sufficient insurance cover is in place

- AJG provides education and guidance notes. Highlights key liability and insurance considerations.
- Includes options ranging from the preferred solution to various alternative positions — agreed with client senior management.
- Support in third-party negotiations.

If you want to discuss any of the issues covered in this paper or would like to see what Gallagher can do to help your business, please contact:

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