PERSPECTIVES

Tariffs and Trade Series: Impact on the Insurance Industry for Construction Claims

Our perspectives feature the viewpoints of our subject matter experts on current topics and emerging trends.

This paper is the second installment in a series examining the multifaceted impacts of tariff and trade policies. By delving into the nuances of these policies, we aim to provide valuable insights and perspectives that will inform strategic business decision-making and foster resilience in an increasingly volatile global market. Future pieces in this series will explore the specific implications for key sectors such as agriculture, energy, and construction, offering targeted analysis and recommendations to help businesses navigate and thrive amidst evolving trade landscapes.

INTRODUCTION

The newly announced tariff policy from the United States has upended expectations for the global economy. The US tariffs are poised to potentially reshape global supply chains, impact regulatory compliance, and pressure companies and other governments worldwide to reassess their financial strategies in response to these changing economic dynamics. For the construction and insurance industries, uncertainty surrounding the fluctuating US tariffs and retaliatory tariffs from trading partners could have a significant impact on construction claims.

1. Rising Costs and Inflationary Pressures on Claims

One of the most immediate effects of tariff changes on construction insurance is the prediction of increased costs of building materials. Higher tariffs on imported steel, aluminum, and other essential construction materials may lead to inflated costs and cause project overruns. This inflation can directly affect insurance claims in the following ways:

- Higher Repair and Replacement Costs: Insurers typically consider increased costs for repairing or replacing damaged structures. Policies covering material damage or builder's risk insurance could see higher payouts due to elevated prices.
- Delays and Business Interruption Claims: Supply chain disruptions, such as those caused by trade restrictions, often delay projects, and can lead to increased business interruption claims. Contractors who fail to meet deadlines may also face penalties, such as liquidated damages.
- Rising Reinsurance Costs: As claims increase, insurers might adjust their reinsurance strategies, leading to higher premiums across the industry.

2. Increased Risk of Construction Disputes and Litigation

Tariffs and trade tensions can also contribute to contractual disputes between construction firms, suppliers, and developers. Many construction contracts do not account for sudden cost surges caused by tariffs, which may lead to conflicts about pricing adjustments and project feasibility. Potential issues that may arise include:

- Breach of contract disputes due to unexpected cost overruns.
- Claims for defective construction linked to substitutions of lower-quality materials.
- Legal battles over non-performance due to tariff-related delays.

> *"There should be more focus on contractual language including escalation and change clauses, including possible exemptions, so the contractor can maximize recovery and manage the risk to cover the cost increases."*
> *- Rob Strahle*
> *Senior Managing Director | Construction Advisory, United States Lead*

3. Supply Chain Disruptions and Increased Risk Exposure

Trade restrictions can lead to supply chain bottlenecks, forcing construction firms to potentially rely on alternative suppliers and / or lower-quality materials. This shift increases the risk of:

- Defects and safety hazards: Materials sourced from new suppliers may not meet original specifications, leading to potential conflicts and long-term liability concerns for the owners of property.
- Supply chain impacts may cause delays which lengthen exposure to increases in logistical expenses , such as higher energy costs.

- Project abandonment: When supply chain collapses due to trade restrictions occur, a construction project may be reevaluated according to changed economics.

POTENTIAL RISKS CREATED BY TARIFF CHANGES AND TRADE WARS FOR CONSTRUCTION INSURERS

> *"Increased tariffs create a ripple effect across the supply chain, potentially driving up the cost of materials and delaying delivery times. For the insurance claims and construction industries, this likely means higher claim payouts, prolonged project timelines, and added pressure on adjusters and contractors to manage budgets and expectations in a volatile market."*
> *- Andrea Korney*
> *Vice President of Sustainability*

1. Higher Claims

- Potential increased costs for materials and labor may result in higher claims for property damage and construction defects.
- Longer project delays could create compounded risks, raising claims under business interruption and delay-in-completion policies.

2. Regulatory and Compliance Uncertainty

> *"Project delays may lead to significantly increased costs - longer periods of business interruption, higher carrying costs, and, in a period of inflation, increased material and labor costs."*
> *- Timothy Gillihan*
> *Executive Vice President, Economic Damages & Valuations*

- As governments adjust trade policies, insurance contracts may need to adapt to the evolving risk landscapes, potentially requiring policy updates and legal reviews.
- Insurers may need to develop specific policy exclusions or endorsements to address tariff-related risks.

3. Reinsurance Market Tightening

- Rising claims may drive up reinsurance costs, potentially forcing insurers to either absorb higher expenses or pass them on to policyholders through premium increases.
- Some reinsurers may become reluctant to underwrite certain construction-related risks, potentially leading to capacity constraints in the insurance market.

POTENTIAL OPPORTUNITIES FOR INSURERS AMIDST TRADE TENSIONS

Despite the risks, tariff changes and global trade shifts may also create new opportunities for the insurance sector.

1. Growth in Specialty Insurance Products

- Trade Disruption Insurance: Insurers could introduce policies specifically covering trade-related supply chain disruptions.
- Tariff Risk Coverage: New insurance products could mitigate the financial impact of sudden tariff hikes on construction companies.
- Alternative Supply Chain Risk Insurance: Coverage could be developed to protect against risks associated with sourcing new materials or shifting production locations.

2. Increased Demand for Political and Trade Credit Insurance

- Given the heightened geopolitical risks, insurers offering political risk insurance may see increased demand from construction firms operating across multiple jurisdictions.

- Trade credit insurance may become more attractive as firms seek to protect themselves from financial losses due to contract disputes or supply chain failures.

CONCLUSION

As the US tariff strategy continues to evolve, so does the response from trading partners. As a result, the construction and insurance industries should prepare for potential fallout from the uncertainty surrounding the shifting global tariff landscape. At J.S. Held, we provide expert guidance to help businesses adapt to these challenges, ensuring compliance, financial stability, and long-term success.

ABOUT THE AUTHORS

Tim Gillihan is an Executive Vice President in J.S. Held's Economic Damages & Valuations practice. He brings nearly twenty years of forensic accounting and economics experience and is engaged as a consultant by attorneys, insurance companies, independent insurance adjusters, businesses, and municipalities. He specializes in the financial evaluation of damage claims and fraud cases, including first-party property losses, third-party liability cases, commercial litigation damages, partnership disputes, and fidelity matters. A certified public accountant, he has also provided analysis of business valuation, divorce, trust / estate, personal injury, death, and employment discharge cases.

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