

BOGGS RISK & INSURANCE CONSULTING

Understanding and Reviewing Contracts and Contractual Risk Transfer

Christopher J. Boggs, CPCU, ARM, ALCM, LPCS, AAI, APA, CWCA, CRIS, AINS
President - Boggs Risk & Insurance Consulting

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Today's Fun

- Warning(s)
- The Purpose: What is Contractual Risk Transfer
- Where Insurance "Fits" into Contractual Risk Transfer
- Managing Contractual Risk Transfer
- "Ancient" Language We Still See
- Internal "Best Practices"

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Warning(s)

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Warning(s)

- Do NOT assume the duties and responsibilities of a lawyer
- Do NOT confuse the contractually required limits with a coverage limit recommendation
- Look "UP" and Look "Down"

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The Purpose: What is Contractual Risk Transfer

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Risk Management Options

- Control
 - Risk management
 - Loss prevention
 - Loss reduction
 - Risk financing
- Avoid
- Retain
- **Transfer**
 - Insurance
 - **Non-Insurance**

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Why is Contractual Risk Transfer Necessary

Contractual Risk Transfer

Contractual Insurance Requirements

The "Upper Tier" Contractor!
(At ANY "Level!")

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Why is Contractual Risk Transfer Necessary

The Responsibility of the "Upper Tier" Contractor!
(General Contractor)

↓ ↓ ↓

The Responsibility of the "Lower Tier" Contractor!
(Sub-Contractor)

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Why is Contractual Risk Transfer Necessary

The Responsibility of the "Upper Tier" Contractor!
(General Contractor)

↓ ↓ ↓

The Responsibility of the "Lower/Upper Tier" Contractor!
(Sub-Contractor)

↓ ↓ ↓

The Responsibility of the "Lower Tier" Contractor!
(Sub-Sub-Contractor)

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Why is Contractual Risk Transfer Necessary

- Vicarious Liability
 - Relationship
 - Position
 - Contract

NOTE: Requires the Right, Duty or Ability to Control the Actions of the Other Party

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Key Purpose of Contractual Risk Transfer

- Place the financial burden on the party closest to and best able to control the chances of a loss
- The person/entity doing the work is in the best position to avoid the loss
- Contractual Risk Transfer is fair and appropriate

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Parties to Contractual Risk Transfer

- Transferor
- Transferee
- Payor/Financer

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Enforceability of Contractual Risk Transfer

- Contracting parties can generally agree to anything...legal
- Courts generally prefer to not alter or overturn contracts with two major exceptions:
 - The contract violates statute based on level of transfer allowed:
 - Limited
 - Intermediate
 - Broad
 - Exculpatory contracts - The contract attempts to transfer or avoid a statutory duty, common law duties, criminal penalties or sole negligence in torts
 - Waiver of Liability vs Acknowledgement of Risk
 - "Not Responsible for Broken Windshields"

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Potential Misuses of Contractual Risk Transfer

- Exculpatory contracts
- Violates statute
- Transferor violates its own contract

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Where Insurance "Fits" into Contractual Risk Transfer

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Where Insurance "Fits"

- The CGL ignores contractual risk transfer – at first...

2. Exclusions
This insurance does not apply to:

- b. Contractual Liability
"Bodily injury" or "property damage" for which the insured is obligated to pay damages by reason of the assumption of liability in a contract or agreement.

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Where Insurance "Fits"

- Exception "gives back" coverage for contractually-assumed risk

This exclusion **does not apply** to liability for damages:

(2) Assumed in a contract or agreement that is an "insured contract", provided the "bodily injury" or "property damage" occurs subsequent to the execution of the contract or agreement. Solely for the purposes of liability assumed in an "insured contract", reasonable attorneys' fees and necessary litigation expenses incurred by or for a party other than an insured are deemed to be damages because of "bodily injury" or "property damage", provided:

- (a) Liability to such party for, or for the cost of, that party's defense has also been assumed in the same "insured contract" and
- (b) Such attorneys' fees and litigation expenses are for defense of that party against a civil or alternative dispute resolution proceeding in which damages to which this insurance applies are alleged.

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Where Insurance "Fits"

- "Insured Contract:

"Insured contract" means:

- f. That part of any other contract or agreement pertaining to your business...under which you assume the tort liability of another party to pay for "bodily injury" or "property damage" to a third person or organization.

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Where Insurance "Fits"

- Dangers to the definition of "Insured Contract"

1. **CG 21 39-Contractual Liability Limitation:** Removes "f." from the definition of "Insured Contract," Effectively deleting contractual risk transfer
2. **CG 24 26-Amendment of Insured Contract Definition:** Only allows acceptance of contractual risk transfer where permitted by law

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Where Insurance "Fits"

- Insurance is a "Slave" to the Contract – Sort of!
- Two Key Questions
 - What did the insured contractually agree to?
 - Does the CRT agreement compel the insurance carrier to do anything?
- Insurance is ONLY a Risk Financing mechanism – NOTHING ELSE

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Managing Contractual Risk Transfer and Insurance

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General Liability – Indemnity Agreement

Limited State Indemnity Wording:

“For and in exchange for fair and equitable consideration, [Lower Tier] agree to indemnify, defend and hold harmless [Upper Tier] for and against any and all liabilities, costs, expenses, damages and losses (including any direct, indirect or consequential losses, loss of profit, loss of reputation and all interest, penalties and legal and other reasonable professional costs and expenses) suffered or incurred by [Upper Tier] arising out of or in connection with [the construction contract in question] except with respect to claims arising from [Upper Tier’s] separate negligence or willful acts.”

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General Liability – Indemnity Agreement

Intermediate State Indemnity Wording:

“For and in exchange for fair and equitable consideration, [Lower Tier] agree to indemnify, defend and hold harmless [Upper Tier] for and against any and all liabilities, costs, expenses, damages and losses (including any direct, indirect or consequential losses, loss of profit, loss of reputation and all interest, penalties and legal and other reasonable professional costs and expenses) suffered or incurred by [Upper Tier] arising out of or in connection with [the construction contract in question] except with respect to claims arising from [Upper Tier’s] sole negligence or willful acts committed individually or jointly with any other party.”

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General Liability – Waiver of Subrogation

[Upper Tier] and [Lower Tier] mutually agree to waive any right of recovery either may have against the other as a result of payments made for injury or damage arising out of the contracted construction project committed individually or jointly.

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Liability Coverages and Contractual Insurance Requirements

- Minimum Commercial General Liability limits
- Requirement to name upper tier (and possibly additional parties) as Additional Insured
 - Premises/Operations
 - Products/Completed Operations (?)
- "Primary and Non-contributory"
- Requirement to attach a "Waiver of Subrogation" endorsement
- Business Auto Liability requirements (covered auto symbols and limits)
- Work Comp and Employers' Liability requirements
- Other relevant coverages and requirements
- Cancellation provisions

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General Liability – Additional Insured

Additional Insured endorsement language is of utmost importance!

Exposure	Scheduled AI Endorsements	Privity of Contract AI Endorsements	Contractually Require AI Endos
Premises/Operations	CG 20 10	CG 20 33	CG 20 38
Completed Operations	CG 20 37	CG 20 39	CG 20 40

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General Liability – Additional Insured

Effects of Adding an Additional Insured:

- 1) To end one myth, naming an Additional Insured does not affect the named insured's per occurrence limits (necessarily), but an AI might negatively affect the aggregate limits.
- 2) Remember, the named insured must still be a (not just "the") cause of the injury or damage.
- 3) The Additional Insured may be covered even if coverage for the named insured is excluded. (Separation of Insureds)
- 4) Addresses the primary vs. excess question.
- 5) Gives the AI the ability to be "covered" by ISO's Primary and Noncontributory endorsement.

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General Liability – Additional Insured

Endorsement limits amounts available to the additional insured - unless otherwise addressed:

With respect to the insurance afforded to these additional insureds, the following is added to Section III - Limits Of Insurance:

If coverage provided to the additional insured is required by a contract or agreement, the most we will pay on behalf of the additional insured is the amount of insurance:

1. Required by the contract or agreement; or
2. Available under the applicable limits of insurance;

whichever is less.

This endorsement shall not increase the applicable limits of insurance

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General Liability – Additional Insured

Contractual wording to potentially overcome the limitation:

The coverage terms, requirements, and limits of liability coverage presented within this Contract are not intended nor are they to be applied as limitations on the Subcontractor's responsibility or liability under the Contract. The terms, requirements, and limits presented herein are the minimums necessary. If the Subcontractors insurance provides broader coverages, better coverage terms, or insurance limits in excess of the minimum limits set forth herein, the Contractor will receive the broader or additional benefits.

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General Liability – Additional Insured

Form Language Matters:

BLANKET ADDITIONAL INSURED

A. Under SECTION II - WHO IS AN INSURED is amended. The following provision is added.
 A person or organization is an Additional Insured, only with respect to liability caused, in whole or in part, by "your work" for that Additional Insured by or for you:

1. If required in a written contract or agreement; or
2. If required by an oral contract or agreement only if a Certificate of Insurance was issued prior to the loss indicating that the person or organization was an Additional Insured.

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General Liability – Waiver of Subrogation

Is a Waiver endorsement necessary if additional insured status granted?

Argument: The insurance carrier cannot seek reimbursement from its insured, thus, because the upper tier is an additional insured there is no need to attach a waiver of subrogation.

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General Liability – Waiver of Subrogation

Reality: Two different purposes

- 1) Endorsement waives subrogation and contribution
 - Subrogation: The ability of the financially harmed party to recover from the fully at fault party.
 - Contribution: The ability of one party who was jointly liable with another party to recover the amount from the joint wrongdoer (tortfeasor) such that each pays their share of the damage.
- 2) NO insurance protection is provided by the waiver.

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General Liability – Waiver of Subrogation

Reality: Some loss situations may fall outside the protection granted by additional insured protection:

- The injury or damage falls outside the scope of the additional insured endorsement
- Loss exceeds the contractually required limits
- Loss results from an activity outside the insured's normal operations
- Not every policy can include an additional insured endorsement
- Losses fall outside the breadth of contractually agreed to transfer

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General Liability – Waiver of Subrogation

Reality: Subrogation has likely already been waived in the contract, so just attach the endorsement.

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General Liability – Reporting Limits

Should the actual policy limits or the contractually-required policy limits be listed?

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General Liability – Statute of Limitations

Post-Completion Coverage (“Statute of Limitation”): Some contracts require the lower tier to provide proof of coverage for up to a certain amount of time after the work is completed:

- The agent cannot guarantee this beyond notifying the insured of the requirement
- This is a function of the upper tier’s record keeping
- Lower tier must confirm compliance to avoid breach of contract

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Business Auto – Coverage Symbols

Coverage Symbols

- Symbol 1 – Any Auto is preferable – the “King” of all symbols
- If any Symbol other than “1,” require use of Symbols 8 and 9.

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Business Auto – CA 20 48

Is the CA 20 48 necessary?

- Upper tier looking for their name in “lights”
- A wholly unnecessary endorsement

Who is an Insured (BAP)	CA 20 48
I. Who Is An Insured ***** c. Anyone liable for the conduct of an “insured” described above but only to the extent of that liability.	Each person or organization shown in the Schedule is an “insured” for Covered Autos Liability Coverage, but only to the extent that person or organization qualifies as an “insured” under the Who Is An Insured provision contained in Paragraph A.1. of Section II - Covered Autos Liability Coverage in the Business Auto and Motor Carrier Coverage Forms and Paragraph D.2. of Section I - Covered Autos Coverages of the Auto Dealers Coverage Form.

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Business Auto – Excluded Drivers

Varies by State

Approximately 40 states and DC allow driver exclusions by either statute or common law

Approximately 10 states do NOT allow driver exclusions (not even “gentlemen’s agreement”)

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Business Auto – Excluded Vehicles

May be a function of the Symbols used

Still a way to get “Any Auto” even if a vehicle is excluded- CA 99
40-Exclusion or Excess Coverage Hazards Otherwise Insured

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Umbrella/Excess

- Which is it?

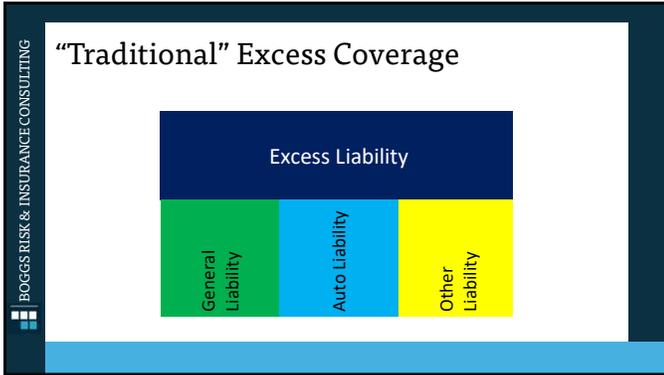
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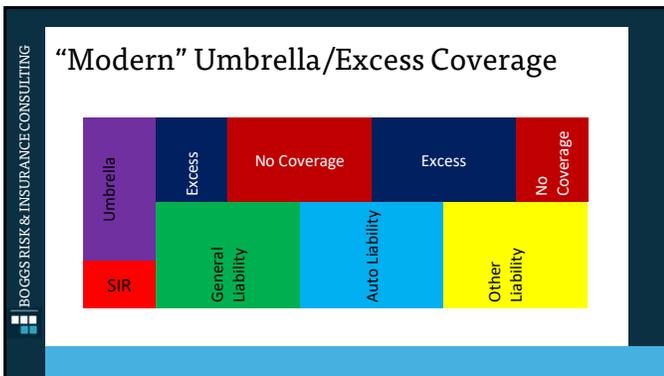
“Traditional” Umbrella Coverage

The diagram illustrates the structure of traditional umbrella coverage. It consists of a large purple rectangle at the top labeled "Umbrella Liability". Below this, there are four vertical bars of different colors: a red bar on the left labeled "SIR", a green bar labeled "General Liability", a blue bar labeled "Auto Liability", and a yellow bar labeled "Other Liability". To the right of the yellow bar is another red bar labeled "SIR". The purple umbrella bar spans across all these four bars, indicating that the umbrella coverage applies to all the underlying policies shown below it.

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Umbrella/Excess

- What coverages does it "sit over" (don't assume)?
- Confirm additional insured status applies to umbrella/excess policy.
- Vertical vs. Horizontal exhaustion of limits: Contract should state that the upper tier's policy is excess over all other collectible coverage

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Workers' Compensation – Experience Mod Reporting

Is it proper to request the Experience Mod?

Is the experience mod truly an indication of the level of safety practiced?

Do not release the mod without client permission

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Workers' Compensation – Any Excluded Employees

Entity type matters

There is more than one type of “employee”

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Workers' Compensation – The Out of State Problem

Can you or should you ask?

An Extraterritoriality and Reciprocity issue

Potential for No Coverage in a non-3.A. state

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Workers' Compensation

False Statements and Scary Situation

- "We are not required by statute to have work comp."
- A "ghost" policy

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Workers' Compensation

Waiver of Immunity language:

"...regardless whether such claim is presented by an employee of the subcontractor...."

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Workers' Compensation

Request that CANNOT be satisfied (well, maybe one...)

- "Additional Insured": Only one "level" of insured in Work Comp
- Alternate Employer endorsement

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"Ancient" Language We Still See

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Language Nearly 40 Years Old

- "Comprehensive" General Liability
- Broad Form Contractual Liability
- No XCU Exclusion
- Broad Form Other States Endorsement

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Language That is 30 Years Old

- CG 20 10 11 85

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Internal "Best Practices"

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Who Must Pay Attention

- "Upper Tier" Clients
- "Lower Tier" Clients

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Internal Checklist

- All parties contracting work to others utilize contractual risk transfer
- Keep most current copy of contract in the client's file
- Have insured confirm indemnity agreement complies with relevant statute (may require an attorney). Get this in writing. Based on level of transfer allowed (Limited, Intermediate or Broad)
- Confirm all contracts signed BEFORE work begins
- Review contract for insurance requirements ONLY
- Advise client of insurance-related contractual obligations that cannot be satisfied

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Internal Checklist

- Confirm that indemnity wording precludes the insurer of the direct employer's ability to assert sole remedy in third-party over suits
- Look for, recommend and expect the "belt and suspenders" of Waiver language coupled with the request to attach the "Waiver of Subrogation" endorsement applicable to all liability policies
- Coverage limits included in the contract are the required minimums and NOT the recommended "maximums"
- General Liability:
 - Confirm Additional Insured status granted to correct parties
 - Confirm Additional Insured status granted for correct exposures
 - If your insured is the Additional Insured, confirm they have access to whatever limits are purchased - not just those required by the contract
 - Report the actual policy limits, not the contractually-required policy limits
 - Develop minimally-acceptable limits for all subcontractors

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Internal Checklist

- Business Auto:
 - Ask for Symbol 1 for Liability
 - Confirm no excluded drivers or vehicles being used on site
 - Set minimum acceptable limits
- Umbrella/Excess:
 - Confirm the underlying policies over which the policy sits or is required to sit.
 - Contract specifies that the upper tier's policies are excess over all other policies provided by the lower tier (underlying and umbrella/excess)
- Workers' Comp / Employers' Liability
 - Require workers' compensation even if not required statutorily
 - Confirm/require the state in which work is being performed is listed as a 3.A. state or in compliance with extraterritoriality/reciprocity requirements
 - Set minimum employers' liability limits

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Christopher J. Boggs, CPCU, ARM, ALCM, LPCS, AAI, APA, CWCA, CRIS, AINS
President - Boggs Risk & Insurance Consulting
chrisboggs@windstream.net
(704)685-6207
