

Construction Insurance

Article by Richard Ollis
Written for the Springfield Business Journal
March 14, 2006

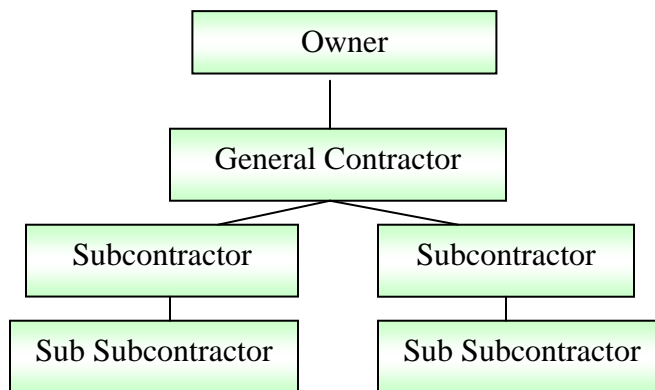
The construction business offers unique challenges, contracts and insurance coverages. Contractors typically have to deal with owners, architects, subcontractors and many regulations. Being good at your trade is just part of the increasingly complex process of building.

Probably the most overlooked and under appreciated area is the necessity of contracts between the owner and general contractor and their subcontractors. The days of a verbal bid and a handshake are long gone.

All jobs should have written contracts between the owner and general contractor. In addition, the general contractor should have written contracts with all of their subcontractors. The contracts should address:

- Specific scope of work and performance standards
- Time for completion of the project
- Payment terms
- Risk of loss to ongoing work (typically covered under a builder's risk policy)
- Indemnification and hold harmless agreements
- Insurance requirements

Oral contracts can be valid and enforceable, but they are extremely difficult to prove if something goes wrong. In addition, they tend to focus on price and scope of work and often fail to address risk and the transfer of risk. The most commonly used methods of risk transfer include indemnification, hold-harmless agreements, insurance requirements and additional insured endorsements. The following chart is the normal "flow" of risk transfer:



Indemnification agreements transfer risk and responsibility to other parties. These agreements are a critical part of construction contracts. A property owner may require the general contractor on a project to sign an indemnification agreement, a hold harmless agreement and name the owner as an additional

insured on the contractor's liability policy. The general contractor then needs to require the same of their subcontractors and the subcontractor would require the same for their subcontractors.

Many look at this process as excessive; however, it reduces exposure from both higher and lower tier contractors (up and down the "flow chart"). There are several types of indemnification agreements:

- Broad Form Agreement – The indemnitor (party that assumes the risk) assumes all risk described in the contract, regardless of fault even if the indemnitee is entirely at fault.
- Intermediate Form Agreement – The indemnitor assumes all risk of loss described in the contract except when the loss is caused by the indemnitee's sole negligence. Just 1% of fault will trigger the obligation of the indemnitor to be responsible for all damages.
- Limited Form Agreement – The indemnitor is obligated to reimburse for the extent of the damage described in the contract. It is typically calculated on a percentage basis and is sometimes referred to as a comparative fault agreement.

Often, construction contracts include hold harmless agreements stipulating the party that assumes the risk agrees not to recover any portion of the damages from the other party.

As you can probably tell, the contractual process is complex, but critical. Also, not all risk transferred by an indemnification agreement is covered by insurance and state statutes treat indemnity agreements differently.

Another important part of construction contracts is the insurance requirements. There are two basic provisions that need to be addressed. One is the minimum limits of liability and coverages required and the other is the additional insured provision. Normally, minimum limits of liability and coverages required include:

- \$1,000,000 each occurrence for bodily injury (GL) and property damage; \$2,000,000 aggregate
- \$1,000,000 combined single limit for auto liability.
- 500,000/500,000/500,000 or statutory for workers compensation
- 30 days written notice if the policy is cancelled

Additional insured status is normally addressed in the contract. Being named as a "primary" additional insured on a contractor's policy obligates their policy to respond first in the event of a covered claim and protects you (as Primary Additional Insured) under their policy for covered damage caused by them. In addition, language stipulating that completed operations are included is preferable to protect the higher tier on the flow chart.

Construction contracts are one of the most important documents to address on a building project. Make sure your insurance agent and attorney advise and approve every document you are required to sign. It will ultimately determine the outcome if something goes wrong.

Richard Ollis is CEO of Ollis and Company, an employee-owned, independent insurance agency.