Additional Insured and Indemnification Issues

Introduction

A fundamental purpose of construction contracts is to lay out the roles and responsibilities of each party in the performance of the work. Included in this document, the drafters usually attempt to delineate the liability of the parties to one another in the form of Indemnification clauses and insurance requirements which seek to clarify which party is responsible for its and in many cases the other parties liability. As contracts have evolved both clauses have been subjects of much discussion and disagreement and the same is true of various insurance forms which seek to meet the needs of the policyholders while at the same time trying not to offer coverage beyond the scope of what the insurance industry feels is prudent for its underwriting needs. This paper examines the current state of insurance industry thinking (at least as respects the most commonly used policy forms) and reviews proposed changes the industry is making in June of 2004.

Indemnification

Most construction contracts require some form of indemnification for the subcontractor to the draft or of the contractor.

FOR EXAMPLE:

As indemnification clauses became broader (to include sole negligence), many states passed forms of anti-indemnification statutes which did not allow such an extensive transfer of risk via indemnification clauses. Today, most states forbid "sole negligence" indemnification clauses and a number exclude "joint negligence" as well.

Most drafters of such contracts recognize that indemnification clauses may not adequately provide for financially viable transfer of risk. As a result, most contracts call for insurance requirements which reference the indemnification obligations and require Additional Insured status under various lines of insurance and in particular General Liability insurance.

How Commercial General Liability Policies Respond to Contractual Requirements:

In order to have a general liability policy respond to a contractually assumed liability several approaches evolved as policies were drafted.

1. Contractual Liability Coverage: Initially, policies were endorsed to include coverage for certain defined contracts. The effect of these was that if the insured was found to have signed a contract which was defined as an "insured contract" and the loss was his legal liability, then the policy would ultimately address the loss. Eventually the base CGL policy was amended to include "insured contracts" automatically. The current "insured contract" definition as contained in the ISO commercial general liability form **CG 0001 Edition 11/01** is excerpted as follows to show the portion of the Insured Contracts definition which covers most construction contracts:

> *9. "Insured contract" means (definitions a through e are purposely left off for this example)*
>
> *f. That part of any other contract or agreement pertaining to your business (including an indemnification of a municipality in connection with work performed for a municipality) under which you assume the tort liability of another party to pay for "bodily injury" or "property damage" to a third person or organization. Tort liability means a liability that would be imposed by law in the absence of any contract or agreement.*

The drafters of this policy have now decided to develop a new definition as an optional endorsement (CG 24 26 ed. 6 04) for insurance carriers to use and will insert wording which narrows this definition to exclude any assumption of sole negligence of another party. The new wording is as follows:

> *f. That part of any other contract or agreement pertaining to your business (including an indemnification of a municipality in connection with work performed for a municipality) under which you assume the tort liability of another party to pay for "bodily injury" or "property damage" to a third person or organization, provided the "bodily injury" or "property damage" is caused, in whole or in part, by you or by those acting on your behalf. Tort liability means a liability that would be imposed by law in the absence of any contract or agreement.*

As the highlighted portion of the endorsement indicates, it is the intent of the drafters to narrow the coverage to just those instances where the insured had an active role in the loss or if the insured directed others and the loss occurred. Sole negligence of the other party to the contract is specifically not covered.

Additional insured coverage:

As case law continued to evolve, many contracts went beyond requiring general liability including contractual liability coverage to requiring the naming of the contract drafter (and others as designated by the contract drafted) as "additional insureds" to the indemnitor's policy. Hence, the common requirement to have the owner or general contractor named as additional insured in many contracts. This approach significantly expanded the obligation to the additional insured beyond contractual coverage.

Specifically, it now gave the additional insured access to the coverages of the insurance policy. In many cases this was done without reference to either the contract or any restriction on the additional insured's coverage aside from loss arising out of the work for the additional insured.

ISO CG 20 10 Ed. 11-85

The endorsement for doing this was the ISO Form 2010 Edition 11/85. That endorsement is re-created below.

ADDITIONAL INSURED -- OWNERS, LESSEES OR CONTRACTORS (FORM B)

This endorsement modifies insurance provided under the following:

COMMERCIAL GENERAL LIABILITY COVERAGE PART.

SCHEDULE

Name of Person or Organization:

(If no entry appears above, information required to complete this endorsement will be shown in the Declarations as applicable to this endorsement.)

WHO IS AN INSURED (Section II) is amended to include as an insured the person or organization shown in the Schedule, but only with respect to liability arising out of "your work" for that insured by or for you.

This brief form seems relatively straightforward and has been widely used as the benchmark for all subsequent endorsements. It has even been inserted by form number into insurance requirement in many contracts. Almost immediately insurance companies began to interpret the meaning of this endorsement in different ways. Some felt it only applied to the vicarious liability of the additional insured. Some saw it as being further interpreted by the contract. Others saw it as a broad based insurance for the additional insured. Several court cases ruled that it could or should be interpreted to its most liberal meaning (any losses on the job regardless of fault i.e., the losses would not have occurred if the sub was not on the job). This trend toward broader interpretation caused ISO to begin to study revisions to the endorsement to narrow its meaning, as discussed in later sections of this document.

Over time a number of revisions were made to this endorsement and subsequent forms were split between "ongoing operations" and Completed Operations" as some carriers were not willing to grant additional insured status for both on one form. Instead they wanted the right to underwrite each job prior to agreeing to grant the coverage.

These endorsements- CG 2010 ed. 10 01 and CG 20 37 ed 10 01-(when put on the policy together and made to apply to "all contracts") basically achieved the extent of coverage granted in CG 2010 ed ll/85.

Current editions of the additional insured endorsements:

POLICY NUMBER: **COMMERCIAL GENERAL LIABILITY**

CG 20 10 10 01

THIS ENDORSEMENT CHANGES THE POLICY PLEASE READ IT CAREFULLY.

ADDITIONAL INSURED – OWNERS, LESSEES OR CONTRACTORS – SCHEDULED PERSON OR ORGANIZATION

This endorsement modifies insurance provided under the following:

COMMERCIAL GENERAL LIABILITY COVERAGE PART

SCHEDULE

Name of Person or Organization:

(If no entry appears above, information required to complete this endorsement will be shown in the Declarations as applicable to this endorsement.)

A. Section II – Who Is An Insured is amended to include as an insured the person or organization shown in the Schedule, but only with respect to liability arising out of your ongoing operations performed for that insured.

B. With respect to the insurance afforded to these additional insureds, the following exclusion is added:

2. Exclusions

This insurance does not apply to "bodily injury" or "property damage" occurring after:

(1) All work, including materials, parts or equipment furnished in connection with such work, on the project (other than service, maintenance or repairs) to be performed by or on behalf of the additional insured(s) at the site of the covered operations has been completed; or

(2) That portion of "your work" out of which the injury or damage arises has been put to its intended use by any person or organization other than another contractor or subcontractor engaged in performing operations for a principal as a part of the same project.

CG 20 10 10 01

ADDITIONAL INSURED – OWNERS, LESSEES OR CONTRACTORS – COMPLETED OPERATIONS

This endorsement modifies insurance provided under the following:

COMMERCIAL GENERAL LIABILITY COVERAGE PART

SCHEDULE

Name of Person or Organization:

Location And Description of Completed Operations:

Additional Premium:

(If no entry appears above, information required to complete this endorsement will be shown in the Declarations as applicable to this endorsement.)

Section II – Who Is An Insured is amended to include as an insured the person or organization shown in the Schedule, but only with respect to liability arising out of "your work" at the location designated and described in the schedule of this endorsement performed for that insured and included in the "products-completed operations hazard".

CG 20 37 10 01

The separate endorsements, while cumbersome, basically satisfied the contract drafters requirements for the CG 2010 11 85 or equivalent.

Proposed Changed to additional insured wordings

The most recent proposed changes to these endorsements and to the basic ISO CGL form seek to significantly narrow the intent of coverage under the "definition of insured contracts" and in the coverage provided to additional insures. The insured contract definitions were dealt with earlier and this section will specifically address the changes for the additional insured endorsements. ISO has revised other endorsements as well but this document deals with the CG 2010 and CG 2037 endorsement changes only.

The new ISO additional insured endorsement (editions to be effective 06/04 and on), seek to narrow the intent in a similar fashion as the definition of Insured Contracts discussed earlier. The wordings are intended to only address liability caused "in whole or in part" by the acts of the named insured or omission or the acts or omissions of those acting on its behalf".

The revised CG 20 10 edition 7/04 is recreated below.

THIS ENDORSEMENT CHANGES THE POLICY. PLEASE READ IT CAREFULLY.

ADDITIONAL INSURED – OWNERS, LESSEES OR CONTRACTORS – SCHEDULED PERSON OR ORGANIZATION

This endorsement modifies insurance provided under the following:

COMMERCIAL GENERAL LIABILITY COVERAGE PART

SCHEDULE

Name Of Additional Insured Person(s) Or Organization(s): Location(s) Of Covered Operations

Information required to complete this Schedule, if not shown above, will be shown in the Declarations.

A. Section II – Who Is An Insured is amended to include as an additional insured the person(s) or organization(s) shown in the Schedule, but only with respect to liability for "bodily injury", "property damage" or "personal and advertising injury" caused, in whole or in part, by:

1. Your acts or omissions; or

2. The acts or omissions of those acting on your behalf;

in the performance of your ongoing operations for the additional insured(s) at the location(s) designated above.

B. With respect to the insurance afforded to these additional insureds, the following additional exclusions apply:

This insurance does not apply to "bodily injury" or "property damage" occurring after:

1. All work, including materials, parts or equipment furnished in connection with such work, on the project (other than service, maintenance or repairs) to be performed by or on behalf of the additional insured(s) at the location of the covered operations has been completed; or

2. That portion of "your work" out of which the injury or damage arises has been put to its intended use by any person or organization other than another contractor or subcontractor engaged in performing operations for a principal as a part of the same project.

To complete the additional insured status often called for (including completed operations) the following endorsement needs to be used in conjunction with the CG 20 10 ed. 7-04.

THIS ENDORSEMENT CHANGES THE POLICY. PLEASE READ IT CAREFULLY.

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ADDITIONAL INSURED – OWNERS, LESSEES OR CONTRACTORS – COMPLETED OPERATIONS

This endorsement modifies insurance provided under the following:

COMMERCIAL GENERAL LIABILITY COVERAGE PART

SCHEDULE

Name Of Additional Insured Person(s) Or Organization(s):	Location And Description Of Completed Operations

Information required to complete this Schedule, if not shown above, will be shown in the Declarations.

Section II – Who Is An Insured is amended to include as an additional insured the person(s) or organization(s) shown in the Schedule, but only with respect to liability for "bodily injury" or "property damage" caused, in whole or in part, by "your work" at the location designated and described in the schedule of this endorsement performed for that additional insured and included in the "products completed operations hazard".

What To Do Now?

Perspectives are important when looking at indemnification and additional insured requirements. From the general contractor's standpoint, its interest is to be defended and have claims addressed by the responsible subcontractor(s). Indemnification provisions over time have been narrowed by statute to the point where additional insured endorsements were required to assure the general contractor (and others) that claims would be directly addressed by insurance carriers.

Subs on the other hand, have felt that they have unfairly been asked to shoulder responsibility for liability beyond the scope of their work.

The recognition that many subs will not be able to provide the additional insured wordings specified by current contracts (including the requirement to defend the general contractor even when they may be wholly or partially responsible) may lead to several outcomes:

1. General contractors and owners may seek to expand their programs to do more OCIP's and CCIP's Wrap-ups are one tool on larger jobs and programs to assure that all claims are handled efficiently with one cover and one set of claims adjusters.

2. Additional insured requirements may have to be modified to reflect the reality that many subcontractors will not be able to comply with the sole negligence of the additional insured or those acting on behalf of the additional insured.

3. Larger subcontractors who can still negotiate broader wordings, due to their buying power, could use this as a competitive advantage as more owners and general contractors scrutinize these wordings.

Impacts Of The New Endorsements And Contractual Definition

It is clear that these new wordings are an attempt by ISO to narrow the coverage granted to avoid picking up the sole negligence of other parties. While many General Contractor's have indicated that they were not intending to transfer their actual sole negligence, but instead just coordinate defense on a claim, the impact of these changes will clearly reduce the likelihood of sole negligence transfer. Also, there is a well established principle that defense obligations under General Liability are often broader than indemnifications obligations. The new wordings may call into question how broad the defense obligation is for the additional insured.

As an example, claims or suits often site damages occurring out of multiple causes. It has become common that insurance carriers would defend most aspects of a case as long as some of the allegations relate to the coverage provided. This can take some stress off contract negotiations but the general contractor may also have to closely review its obligations to owners.

In addition, generals will need to closely review claims passed to subs previously and try to quantify how much of those claims awards will now be handled by the General Contractor's program. This could increase the General Contractor's cost and needs to be recognized in accruals for cost of risk.

Another approach is the Owners and Contractors Protective policy. This does address vicarious liability of the general contractors (and/or owner) arising out of subcontractors activities but will not respond to completed operations claims. OCP's have had a reduced role in risk transfer as additional insured clauses have become more common in the last 15 to 20 years, but many sub contractor groups believe this approach should be sufficient to defend at least ongoing issues which are created for the general contractors and owners.

COMPARISON OF ISO ADDITIONAL INSURED FORMS

CG 20 10 11 85	CG 20 10 10 01	CG 20 37 10 01	CG 20 10 7 04	CG 20 37 7 04
▸ Ties Additional Insured status to liability arising out of "your work" – i.e., the named insured's work – for the additional insured. ▸ Applying the coverage to "your work: encompasses liability incurred while the named insured's work is in progress and also the named insured's completed operations. ▸ Addresses a coverage requirement that is frequently imposed by project owners on contractors doing work for them – the contractor will provide the owner with additional insured status for claims against the owner arising out of completed work. ▸ Later versions of CG 20 10 were revised to take away completed operations coverage, but the 11/85 version continued to be used regularly until the last three years.	▸ Grants coverage only with respect to the named insured's ongoing operations (i.e., there is no coverage for completed operations) ▸ Limits the term of additional insured coverage to the time period in which operations are actually being performed by the named insured. This language is a concern because coverage could potentially be eliminated if operations are still in progress but a claim arises against the additional insured after their operations are completed. ISO adopted the CG 20 37, which can be used in conjunction with CG 2010 to fill this gap (see next column) ▸ The endorsement also contains a design professional liability exclusion.	▸ Provides additional insured status with respect to the products-completed operations hazard in connection with the named insured's work. ▸ Coverage applies only for completed operations claims, there is no coverage for premises and operations, which can be included by adding the CG 2010 10 01. ▸ By applying the CG 20 37 and the CG 20 10 (10 01) endorsements, ISO developed a way to essentially receive similar coverage to the CG 20 10 11 85	▸ Only applies to ongoing operations ▸ Only covers liability for BI, PD and Personal and Advertising Injury caused in whole or in part by: ○ Your acts or omission or the acts or omission of others acting on your behalf Goal is to narrow the grant of coverage to the additional insured to true vicarious liability arising out of the sub contractors ongoing operations for the additional insured.	▸ Only applies to completed operations. ▸ No coverage for "personal injury or advertising liability". ▸ Only applies to liability arising out of acts or omissions of the named insured or others acting on its behalf. Needs to be used in conjunction with CG 2010 7/04 to meet contract requirements for additional insured status for both ongoing and completed operations. Again, endorsement is trying to narrow scope of coverage to the additional insured to just address vicarious liability of the general from the sub contractors operations.

One additional outcome would be that the indemnification clause is significantly broader than the Additional Insured protection available. In this case the GC could choose to seek direct defense from the subcontractor (where allowed by statute) and eventually rely on the balance sheet of the subcontractor for defense. This could then create issues in the relationship of the parties or additional thinking about using surety or subcontractor default insurance to try to bridge this issue.

Other Additional Insured Endorsements Being Re-Filed by ISO in July 2004

Some carriers will use other versions of the additional insured endorsements which are also being re-filed as of July 2004. In addition, special use endorsements are also being re-filed. These include the following:

CG 20 28 ed. 7-04 Additional insured-Lessor of leased equipment
CG 20 15 ed. 7-04 Additional insured-Vendors
CG 20 26 ed. 7-04 Additional insured-Designated person or organization
CG 20 32 ed. 7-04 Additional insured-Engineers, Architects or Surveyors not engaged by the named insured-NOTE: This is used when the contract calls for naming the owners professionals but doesn't cover any professional liability of those professionals.
CG 20 31 ed. 7-04 Additional insured-Engineers, Architects or Surveyors-NOTE: This is used when the named insured hires a professional and covers that professional except it specifically excludes all professional services provided.

Copies of these endorsements are available from your Willis representative.

Summary

It is important that all contractors be aware of the revised ISO wordings as respects contractual definitions and the new additional insured endorsements. Insurance carriers will begin using these endorsements widely starting in mid 2004 and it is expected that most will adopt those in their standard contractor coverages. It is expected that larger contractors (i.e. those with significant buying power and large deductibles) will still have some flexibility to get expanded forms (closer to current wordings). Now is the time to discuss this issue with Willis and your carrier. A quick review summary of the form changes in the additional insured wordings is included below for reference.