

“Indemnities and Endorsements” – Protecting the Owner and Developer

Update on Indemnification, Anti-Indemnity Statutes
and Additional Insured Endorsements

CoreNet Global Network
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L. D. Simmons, II
McGuireWoods LLP
(704) 343-2062
lsimmons@mcguirewoods.com



Introduction

- Indemnity
 - Anti-indemnity statutes
- Contractual liability coverage for the contractor's indemnity obligations
- Additional insured endorsements
 - Recent ISO changes
 - Anti-additional insured statutes
- Tools for the tool box

Basics of Risk Transfer in Real Estate and Construction

- Primary ways to transfer risk:
 1. Require indemnity from the contractor
 2. Require the contractor to provide “additional insured” status
- Each method transfers risk downstream from owners to contractors or from contractors to subs

Indemnity Agreements

- An indemnity agreement obligates the indemnitor to assume the financial obligations of the indemnitee
 - The indemnitor must indemnify and pay the legal fees of the indemnitee
- Indemnity generally runs:
 - between the subcontractor (indemnitor) and the general contractor and/or owner (indemnitees); and
 - between the contractor (indemnitor) and the owner (indemnitee)
- ~~Indemnitee and indemnitor~~

Indemnity Agreements

- Benefits:
 - Agreements can be very broad
 - Protects owner or contractor from its own negligence and vicarious liability
 - Avoids disputes with insurance companies
- Risks:
 - Only as effective as the financial condition of the indemnitor

Contractual Liability Insurance

- Standard CGL policies exclude coverage for :

b. "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**. This exclusion does not apply to liability for damages:

- (1) That the insured would have in the absence of the contract or agreement; or
- (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.

- Insured Contracts often include:

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 liability that would be imposed by law in the absence of any contract or agreement

Additional Insured Endorsements

- An additional insured endorsement –
 - Is an *amendment to the insurance policy* of the contractor
 - It adds the third party as an additional insured to the contract
 - Extends the benefits of the policy to the third party and obligates the carrier to insure it
- Indemnification and additional insured status are separate and independent requirements

Additional Insured Status – Why is it Important?

- Transocean owned the rig and insured it -- \$50 million in GL and \$700 million in excess
- Transocean agreed to indemnify BP, but **not for pollution liabilities**
- Transocean agreed that BP Oil **was an additional insured** under the Transocean policies

- HELD: BP entitled to full coverage, even though there was no obligation to indemnify for pollution.
 - The insurance provisions and the indemnity provisions were **independent**
- BUT, now certified to Texas Supreme Court

Additional Insured Status

- Benefits:
 - Agreements can be very broad
 - Allows the owner or contractor to use the downstream party's insurance
 - Protects the owner from its own negligence and vicarious liability
 - Protects insurance limits and loss history of the owner
 - Owner can deal directly with insurer
- Risks:
 - Coverage only as broad as the contractor's policy
 - Limits may be insufficient

Let's Have It All . . .

If possible, secure both indemnity and additional insured status

Indemnity Agreements

- There are three forms of indemnity agreements
 - Limited
 - Intermediate
 - Broad

Limited Indemnity

- Indemnitor assumes only the responsibility for its **own negligence** – or “its share” of liability arising from the contract
 - E.g., “damages arising from a bodily injury claim are indemnified **only if, and to the extent that** the indemnitor **was negligent in causing** the employee’s injuries”
- Allowed in all states
- Provides the **least protection** to the owner
 - No protection if the owner is at fault

Intermediate Form Indemnity

- The owner is indemnified if the contractor is **solely** at fault, or **just partially** at fault
 - The owner receives indemnity if the loss was caused “in whole or in part” by the contractor
 - If the owner is **solely** at fault, no indemnity
- Two types of intermediate indemnity:
 - *Full indemnity* if the contractor was at fault – as long as the contractor is partially at fault, he pays
 - *Partial indemnity* – indemnity on a sliding scale based on the extent of the contractor’s negligence

Broad Form Indemnity

- Contractor transfers the risk of loss **regardless** of who is at fault.
- The contractor indemnifies for:
 - (1) contractor's sole negligence;
 - (2) owner's sole negligence; and
 - (3) joint negligence of contractor and owner
- Broad form indemnity agreements transfer the *entire* risk of loss to contractor

Anti-Indemnity Statutes

- Anti-indemnity statutes limit or prohibit indemnity
- History and purpose of statutes:
 - Construction industry – particularly subcontractors - sought legislative changes
 - Designed to correct inequality in bargaining power
- So 44 states have enacted anti-indemnity statutes

Anti-Indemnity Statutes - Summary

- 17 states prohibit broad form indemnity provisions (but allow intermediate form)
 - Alaska, Arizona, Arkansas, Georgia, Hawaii, Idaho, Indiana, Maryland, Michigan, New Jersey, South Carolina, South Dakota, Tennessee, Utah, Virginia, Washington and West Virginia
- In these states the owner CAN be indemnified if he is partially at fault

Anti-Indemnity Statutes - Summary

- 27 states **prohibit** intermediate form indemnity provisions
 - California, Colorado, Connecticut, Delaware, Florida, Illinois, Iowa, Kansas, Kentucky, Louisiana, Massachusetts, Minnesota, Mississippi, Missouri, Montana, Nebraska, New Hampshire, New Mexico, New York, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, Texas, and Wisconsin.
- The remaining 6 states **do allow** a contractor to indemnify the owner even if the owner is 100% at fault

North Carolina General Statute 22B-1

§ 22B-1. Construction indemnity agreements invalid.

Any promise or agreement in, or in connection with, a contract or agreement relative to the design, planning, construction, alteration, repair or maintenance of a building, structure, highway, road, appurtenance or appliance, including moving, demolition and excavating connected therewith, purporting to indemnify or hold harmless the promisee, the promisee's independent contractors, agents, employees, or indemnitees against liability for damages arising out of bodily injury to persons or damage to property proximately caused by or resulting from the negligence, in whole or in part, of the promisee, its independent contractors, agents, employees, or indemnitees, is against public policy and is void and unenforceable. Nothing contained in this section shall prevent or prohibit a contract, promise or agreement whereby a promisor shall indemnify or hold harmless any promisee or the promisee's independent contractors, agents, employees or indemnitees against liability for damages resulting from the sole negligence of the promisor, its agents or employees. This section shall not affect an insurance contract, workers' compensation, or any other agreement issued by an insurer, nor shall this section apply to promises or agreements under which a public utility as defined in G.S. 62-3(23) including a railroad corporation as an indemnitee. This section shall not apply to contracts entered into by the Department of Transportation pursuant to G.S. 136-28.1.

(1979, c.

597, s. 1; 1991, c. 636, s. 3; 1993, c. 553, s. 12.)

Do Anti-Indemnity Statutes Apply to AI Endorsements?

- It is important to read both the applicable statute and the cases interpreting it.
- Two states have applied anti-indemnity statutes broadly to additional insured endorsements: Tennessee and Michigan
 - Michigan court of appeals found that while the anti-indemnity statute was **silent** regarding insurance, **it was contrary to public policy** for an owner to avoid liability by requiring a third-party to buy insurance for it. *Peeples v. Detroit*, 297 N.W.2d 839 (Mich. App. 1980)

Statutes Prohibiting Additional Insured Endorsements

- Ten states have expanded their statutes to prohibit owners from securing additional insured protection from downstream contractors:
 - California, Colorado, Kansas, Louisiana, Montana, New Mexico, Oklahoma, Oregon, Texas and Utah
- The count -- **12 states now bar** additional insured endorsements either by case law or statute

Additional Insured Endorsements -- Why the Change?

- Conflicting appellate decisions led ISO to examine its key CGL policy forms and endorsements
- SO – in 2013 ISO made significant changes to its policy forms

Additional Insured Endorsements – The Industry’s Reaction to Change

- The entity being added as an additional insured
- The nature of the transferred risk -- e.g., sole, contributory, and/or gross negligence
- The operations for which coverage will be provided; e.g. continuing or completed
- Additional exclusions contained in the endorsement

ISO CG 20 10 – Evolution

- Original ISO endorsement CG 20 10 11 85
 - Very broad coverage
 - Entity listed on the endorsement often is “any party as required by written contract”
 - The upstream party receives coverage for “only with respect to liability arising out of [the named insured’s work]”
 - “Arising out of” -- Courts generally have found that this term includes **both** the sole and concurrent negligence of the owner
 - “Work” includes both ongoing **and** completed operations

ISO CG 20 10 – Evolution

- CG 20 10 10 01
 - Similar to the 1985 edition, BUT -- **no coverage for completed operations.**

ISO CG 20 10 – Evolution

- CG 20 10 07 04
 - Like the 2001 edition, it **does not provide coverage** for the additional insured's **completed operations**
 - **Does not provide coverage** for the additional insured's **sole negligence**

Changes to the 2013 Additional Insured Endorsements - - -

Coverage Under the AI Endorsements Limited “To the Extent Permitted by Law”

Additional Insured—Owners, Lessees Or Contractors—Scheduled Person Or Organization” (CG 20 10 04 13)

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.

However:

- 1. The insurance afforded to such additional insured only applies to the extent permitted by law[.]***

(emphasis added)

Coverage “Will Not Be Broader Than” The Contract Requires.

Additional Insured—Owners, Lessees Or Contractors—Completed Operations” (CG 20 37 04 13)

***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” 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”.*

However:

2. If coverage provided to the additional insured is required by a contract or agreement, the insurance afforded to such additional insured will not be broader than that which you are required by the contract or agreement to provide for such additional insured.

(emphasis added)

Limits Are The Lesser Of The Contract Requirement Or The Policy Declarations

Additional Insured—Designated Person Or Organization” form (CG 20 26 04 13)

B. 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 shown in the Declarations; whichever is less.***

This endorsement shall not increase the applicable Limits of Insurance shown in the Declarations

(emphasis added)

Other Insurance Endorsement – Primary and Non-Contributory

CG 20 10 04 13

Primary And Noncontributory Insurance

This insurance is primary to and will not seek contribution from any other insurance available to an additional insured under your policy provided that:

*(1) The additional insured is a Named Insured under such other insurance;
and*

(2) You have agreed in writing in a contract or agreement that this insurance would be primary and would not seek contribution from any other insurance available to the additional insured.

(emphasis added)

Tools for the Tool Box – The Lawyering of Indemnity Issues



Blocking and Tackling

- Review your existing contracts
- Read your current policies
- Understand how your counterparties do business
- Tailor your agreements to your risks and the laws in the controlling jurisdiction

Solutions in Anti-Indemnity States

It is still possible for an owner to transfer risk downstream – even in the face of an anti indemnity statute

- “Even though the indemnity agreement violated Nebraska’s anti-indemnity statute, the provision requiring the subcontractor to provide additional insured status for the contractor was valid” *Federated Serv. Ins. Co. v. Alliance Constr., LLC*, (Nebraska 2011)

Solutions:

- Require additional insured status and get the policy
- Draft contracts to “bypass” statutes
- Make your contracts compliant

Solutions in States That Restrict Both Indemnity and Additional-Insured Status

- Consider a “wrap” policy -- OCIPs and CCIPs
 - Names all parties to the construction project as insureds
 - Consists of GL, auto, workers’ compensation and excess coverage
 - Provides completed operations coverage
- Benefits – allocates costs between owner and contractor

Choice of Law and Venue

- Venue is very important in insurance litigation
 - Controlling law could determine the result
- Forum state's choice of law rules apply
 - In most states, that is the law of the state where the contract was formed
- Insurers are subject to suit in most every state – there can be many options
- The venue for the underlying case is **not** the only option for the battle over indemnity and insurance

Making it Work . . .

Drafting Contracts and Managing Insurance

- Identify all states in which you operate.
- Understand the laws in each state
 - Anti-indemnity statutes *and* common law
 - Anti-additional insured statutes *and* common law
- Add choice-of-venue and choice-of-law provisions to your agreement
 - **Force** the application of law that benefits your client and avoids the anti-indemnity and anti-additional insured laws
- Add “to the extent allowed by law” to your indemnity and additional insured language.

Making it Work – Drafting Contracts and Managing Insurance

- Understand the new AI endorsements and how they work
- Decide which ones are best for your business and request them
 - Specifically name the AI endorsement you want to apply
 - Do not name the endorsement by “or similar to XYZ20”
- Do not rely on a certificate of insurance – these are unenforceable and for “informational purposes only”

Making it Work . . .

Drafting Contracts and Managing Insurance

- Require the appropriate limits of liability
- Require that the insurer give you notice of cancellation
- If you need completed operations coverage, make sure the downstream policy includes it
- Clearly separate indemnity and insurance in contractors
- Require **primary and non-contributory** insurance

Making it Work . . .

Drafting Contracts and Managing Insurance

- Separate limits
 - Require that the policy limits apply separately to the named insured and the additional insured
- Require that deductibles be paid by the named insured

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