CHAPTER 1

Insurance and Risk Transfer Basics for Construction Projects

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Introduction

Insurance does not exist in a vacuum. Effective insurance risk transfer requires a thorough understanding of both the risks to be transferred and applicable insurance products. This is no less true for construction than for any other commercial venture. Every construction project, regardless of size or scope, carries risks for interested parties, including owners, architects, engineers, construction managers, general contractors, subcontractors, and suppliers. Just as life is uncertain, there is simply no way to foresee exactly what will happen on a project, so it is crucial for each interested party to clearly understand the risks it faces, determine what and how much risk it is willing to tolerate, and analyze the strategies available to manage and finance those risks. Some of these multiple risks are insurable and some are not. This chapter provides an overview of the exposures inherent to the key players on any construction project and introduces the basics of insurance and risk transfer for construction projects.

Risk Management, Risk Transfer, and Risk Financing

The inherent uncertainty of events is commonly described in terms of risk. As Robert Jerry, dean of the University of Florida Levin College of Law, notes, "One of the great stories of humankind is how people developed a capacity to appreciate risk and measure it, and then used this information to make choices among competing alternative behaviors."[1] In making those choices, we typically speak of managing the risk, transferring the risk (where appropriate), and financing the risk.

Risk Management

Risk management is generally defined as the practice of identifying and analyzing loss exposures and taking steps to minimize the financial impact of the risks they impose.[2] In some organizations, risk management is little more than the implementation and oversight of the corporate insurance program, but in a more sophisticated sense it is the ongoing process of identifying, analyzing, and minimizing all risks—insurable, contractual, retained, and financial. Some organizations house risk management responsibilities within the finance or legal department. Other organizations have a separate and distinct risk management department.

Regardless of the form it takes, all good risk management programs start with a risk assessment. The purpose of the risk assessment is to ensure that all material risks faced by an organization are identified and treated in the most comprehensive and cost-effective way. From a philosophical standpoint, the purpose of risk management within any organization is to develop optimal risk prevention, mitigation, servicing, and financing strategies. Risk identification has been called the most important part of a risk assessment program, and it can also be the most difficult as "there is no sure-fire method to identify and classify all project risks."[3]

There are a number of tools and techniques used to identify and quantify the risks an organization faces. For example, risk assessment surveys and risk maps are mechanisms by which organizations identify risks that could affect their ability to achieve business objectives. Once a risk is identified, it is then evaluated based on the likelihood it will actually occur and if it does, the significance. The results of that assessment are then charted in a "risk map" and shared and relied upon by members of the organization. Ideally, a risk map or risk register will tabulate a description of the risk, the type of risk, the likelihood of occurrence, the severity of the risk, risk consequences, and mitigation techniques.[4] This process can be used at a macro level, to identify risks commonly faced by the organization, but it can also be done on a project-by-project basis.[5]

Once a risk is identified, it is important to understand the potential impact that risk will have on an organization, both in terms of its financial consequence and its organizational effect. Treatment of risks will vary depending on a multitude of external factors (e.g., industry, regulatory, environmental, and reputational) as well as internal factors such as the company's best practices, risk philosophy, and culture. Many organizations look to outside attorneys, brokers, and other consultants to help assess how the organization will best transfer, finance, or retain these risks.

Risk Transfer

A commonly employed method of managing risk is to transfer it to someone else. An organization's risk can be transferred through contracts, such as insurance contracts, vendor contracts, leases, and subcontracts. Generally,

the goal is to allocate the risk fairly within the contract to each party so that the responsible party retains the risks it can control and, if possible, insures the risk at a reasonable cost. There are circumstances, however, where a party other than the one who controls a risk assumes it, by reason of economic imperatives, because it has the ability to insure it most inexpensively, or otherwise. The procurement of builders risk coverage by an owner or general contractor by paying a premium to a third-party insurer to cover damage to the work caused by any project participant is a simple example.

Given every party's inherent bias to pass on as much risk as possible, it is difficult at times for the parties involved in a construction project to agree on the risk allocation. On a construction project, the owner typically transfers many risks arising from the work (other than design) to the general or prime contractor by means of indemnification clauses in the construction agreement.[6] Take, for example, Section 3.18.1 of the American Institute of Architects (AIA) Document 201:

> To the fullest extent permitted by the law the Contractor shall indemnify and hold harmless the Owner, Architect, Architect's consultants, and agents and employees of any of them from and against claims, damages, losses and expenses, including but not limited to attorneys' fees, arising out of or resulting from performance of the Work; provided that such claim, damage, loss or expense is attributable to bodily injury, sickness, disease or death, or to injury to or destruction of tangible property (other than the Work itself) but only to the extent caused by the negligent acts or omissions of the Contractor, a Subcontractor, anyone directly or indirectly employed by them or anyone for whose acts they may be liable, regardless of whether or not such claim, damage, loss or expense is caused in part by a party indemnified hereunder. Such obligation shall not be construed to negate, abridge, or reduce other rights or obligations of indemnity which would otherwise exist as a party or person described in this Section 3.18.

General or prime contractors, in turn, usually transfer risk to the subcontractors responsible for individual scopes of work.[7] Despite these efforts, all risks transferred can seldom be transferred downstream in this fashion. The details of what risks are retained by each entity (such as consequential damages flowing from defective work) are a frequent source of controversy.[8] Indeed, this flow-down concept does not always make practical sense, as small players may not be as well situated to handle larger risks.

Although there is some overlap, there are differences between transfer of risk by contract and transfer of risk by insurance. As noted above, the various participants in a construction project can transfer risk among themselves contractually. Again, a common example is an owner transferring certain risks of loss from defective workmanship to a general contractor, who in turn transfers the risks to the individual subcontractors responsible for each scope of work. Indemnification provisions and other contract clauses are utilized for this

purpose. (The relationship between contractual risk transfer and other limitation provisions is addressed throughout this book, in particular in chapter 2). Risk allocation in this sense is priced by project participants in their contracts.[9]

Insurance, on the other hand, involves the transfer of defined project risks to insurance carriers, who specialize in the pooling of such risks, rather than to other project participants.[10] Of course, there is a cost to such risk transfer, typically in the form of a premium. The insured pays a premium to the carrier to assume the risk and to reimburse the insured(s) for loss suffered to the covered interest. The insurer uses a portion of the premium and invests it. Warren Buffet, "the oracle of Omaha," describes the financial upside of this model for insurers:

> Insurers receive premiums upfront and pay claims later. In extreme cases, such as those arising from certain workers' compensation accidents, payments can stretch over decades. This collect-now, pay-later model leaves us holding large sums—money we call "float"—that will eventually go to others. Meanwhile, we get to invest this float for Berkshire's benefit. Though individual policies and claims come and go, the amount of float we hold remains remarkably stable in relation to premium volume. Consequently, as our business grows, so does our float.
>
> If premiums exceed the total of expenses and eventual losses, we register an underwriting profit that adds to the investment income produced from the float. This combination allows us to enjoy the use of free money—and, better yet, get *paid* for holding it. Alas, the hope of this happy result attracts intense competition, so vigorous in most years as to cause the P/C [property-casualty] industry as a whole to operate at a significant underwriting *loss*. This loss, in effect, is what the industry pays to hold its float. Usually this cost is fairly low, but in some catastrophe-ridden years the cost from underwriting losses more than eats up the income derived from use of float.[11]

For this model to work, the greater the level of risk transferred to insurance carriers, the higher the premiums that will be paid by project participants. Construction industry participants must always balance their appetite for risk with the cost of insurance, and consider what benefit they enjoy by financing their cost of risk with a third party.

Insurance carriers commonly insist that project participants retain some significant share of the risk, to ensure that they have an incentive to act safely and avoid loss. This is to avoid what is called a "moral hazard"—the problem where the party insulated from a risk "has less incentive to take precautions to prevent damage to its property if it has insurance to cover the damage."[12] Deductibles, self-insured retentions, and co-insurance requirements are the most obvious examples of ensuring that some risk remains with project participants. Of course, there are often uninsured exposures that accompany a covered loss, which provide an additional incentive for project participants to conduct their operations in a safe manner.

All interested parties in a construction project must understand not only their own particular risks but also those of the other parties. This understanding will help the parties deliver the project in the most cost-effective manner by negotiating risk transfer in project agreements before work commences, determining what insurance to purchase for the project, dealing with losses throughout the project term, and managing third-party claims during and after the project is complete. Intuitively, this makes sense. For example, if an owner fails, the contractor will likely not get paid; or if an owner without builders risk coverage works with a contractor with limited assets and the project is damaged, that owner is in a similar predicament.

Thoughtful risk management involves much more than just insurance procurement. The type and scope of insurance coverage that make sense for a project or an organization depend on its role in an individual project, as does any analysis of appropriate insurance limits and cost. As a simple example, architects and engineers are typically responsible for design services, and more commonly face third-party damage claims resulting from design errors, actual or alleged. As a consequence, a design professional will typically consider professional liability coverage whereas a contractor with no design responsibilities may not. While this basic proposition is rather obvious, it is important to note that an analysis of the organization itself and its particular project risks should be undertaken to determine the appropriate level of insurance and the type and scope of the coverage procured. For example, many contractors do face some design or other "professional" risk because they must have engineers stamp plans, or they provide design-assistance services. (These issues are discussed in chapter 6.) And an architect or engineer who must drive to visit a construction site for supervision purposes may face auto liability and some "premises" or operational risk by being present during the course of construction. Again, every organization must carefully evaluate, consider, and quantify its own unique exposures. One-size-fits-all rules do not work, and (as further discussed in chapter 2) talismanic reliance on form insurance procurement provisions can cause unintended and, sometimes, costly problems.

Placing insurance can be an intricate process even after an organization's risk assessment and determination of the appropriate insurance. At that time, an insurance agent or broker then presents those needs to various carriers who respond by offering a program of coverage at a particular price. Ideally the organization then negotiates with each carrier until it gets the broadest coverage at the lowest price. This process can be performed on a term basis, typically annually, where insurance is purchased to cover risks arising out of all of the organization's ongoing activities during that term. It can also be performed on a project-specific basis, where insurance coverage is procured to cover a single project or several discrete projects only.

Risk Financing

Risk financing refers to different types of funding mechanisms used by organizations (and individuals) to plan for the payment of possible future losses.

Insurance is a form of risk financing in which (as Warren Buffet describes above) an insurance company takes other people's money, invests it, and then uses that combined pool of capital to pay losses in the future. In addition to insurance, risk can be financed using insurance-like products such as deductible insurance programs, self-insured retentions, captive insurers, alternative risk financing techniques, or self-insurance. Each of these approaches is described below.

In a deductible insurance program, a portion of a covered loss is paid by the insured. Typically, the deductible in an insurance policy is paid on each loss, often called "per occurrence" or "per claim" deductibles, at least until some total ("aggregate") level of loss is reached. Organizations routinely must assess and select the appropriate deductible level. Lower deductibles provide more cost stability and a higher degree of protection against losses, but the premiums charged will typically be higher than those insurance programs with larger deductibles. Programs with larger deductibles have lower fixed costs and offer a higher potential for savings, but have greater volatility.

Much like a deductible, a self-insured retention (SIR) is an amount specified on an insurance policy paid by the insured before the insurance policy will respond to a loss. A typical SIR program differs from a deductible program in several ways. [13] First, the policy's insurance limits stack on top of a SIR, while the amount of a deductible is subtracted from the policy's limit.[14] In other words, insurance coverage (including defense costs) may not apply until the insured has paid the SIR. Second, the insured pays the SIR directly to the claimant, while in a deductible program the insurance carrier will often pay the claimant and seek reimbursement of the deductible amount from the insured.[15] Some insurance programs utilize a hybrid approach, adopting elements of each. It should be clearly understood whether the deductible effectively reduces limits. As an illustration, if a policy has a per occurrence limit of $2 million and a $500,000 deductible, the true risk transfer from the insured to the carrier is only $1.5 million if payment of the deductible reduces the limits of liability.

Another risk financing tool used by many large contractors, owners, and developers is what is known as a "captive." A captive insurer is "a special kind of insurance company established by a parent company, trade association, or group of companies to insure the risks of its owners."[16] In other words, captives are typically created and controlled by a single business or by multiple organizations with similar risk characteristics, the purpose of which is to provide insurance coverage for that business or those organizations. Common advantages of forming and using a captive include less dependence on the cycles of the commercial insurance marketplace, greater access to insurance and reinsurance, more control over managing risks, broader coverage, tax benefits, and more efficient use of financial resources.[17] Of course, the organization's own resources fund the captive, so there is no real risk transfer to a third party, except to the extent that the captive's losses are reinsured. Captives, however, are expensive to form, and subject to state regulation and approval.[18]

Captives are most effective when created and managed by a sophisticated risk management team and when the organization requires less immediate policyholder protection than what is granted through traditional insurance policies. Since passage of the Terrorism Risk Insurance Act (TRIA), some larger insureds have created "TRIA captives" that are able to benefit from what is in effect federal reinsurance for 85 percent of the cost of reimbursing losses caused by designated acts of terrorism, and seek reinsurance from commercial insurers for the balance of that amount.[19] Cost, capital, and management requirements, however, are such that economic benefits may inure only to larger insureds, with greater risk to finance.

Alternative risk financing options are also available when traditional programs are not utilized. It is impossible to describe all alternative risk financing options because the market is evolving and new techniques are created on a regular basis. A few examples, however, follow: (1) capital market funding sources such as catastrophe bonds, credit derivatives, risk-linked securities, and special purpose entities; (2) finite risk programs that span over several years to incorporate investment income projections and include the time value of money; and (3) integrated risk programs that spread coverage over several risks in a single bundled arrangement to reduce cost and increase efficiency in handling claims.[20]

Lastly, risk financing can occur through self-insurance. Any exposure that is not addressed by some strategy is, by default, self-insured. When the risk is not addressed by the establishment of a reserve, this type of risk retention is better categorized as "doing nothing" because either the organization is not aware of the risk or has chosen to ignore it. [21] However, where an organization has truly evaluated a risk and decided not to finance or transfer the exposure, the company has deliberately chosen to retain the risk or self-insure.

Key Players on Any Construction Project

The key parties with direct involvement in a construction project are typically the owner, construction manager, general contractor, design professionals such as the architect and engineers, and subcontractors. (Sureties and lenders have important behind-the-scenes roles and have very real financial risks, but their risks depend on the parties whom they stand behind and of course may be affected by personal guarantees, security interests, and other commercial protections, not directly related to the construction process). As noted below, each has distinct risks on a project that must be analyzed and addressed either contractually or through insurance.

Owner

The owner of a construction project could be a developer, private business, private individual, or government entity whose role on the project is, generally speaking, to finance the construction. While some owners may have some limited oversight of construction-related activities, owners do not typically

self-perform any of the construction. Nonetheless, the owner is at risk for all damage to the project and faces liability for third-party injuries or damages resulting from construction activities, the quantum of which can differ depending on the state where the construction takes place.

Owners typically will attempt to transfer most of the risks related to construction activities to the design professionals, general contractor, or construction manager through contractual agreements, such as indemnity or insurance.[22] For example, and as explained in more detail below (and in chapter 10), the owner may choose to insure construction means and methods risks through a controlled insurance program (CIP), usually by purchasing the general liability and workers' compensation insurance for all project participants. Alternatively, if a CIP is not used, the owner may seek to transfer risk by requiring that it be named as an additional insured on the general contractor's policies and those of all lower-tier contractors. The owner can also procure builders risk insurance to cover losses to the project while it is under construction, or contractually require that the general contractor purchase builders risk insurance. In short, the owner will typically seek to transfer as much of the risk as possible from construction-related activities, using a combination of insurance and non-insurance risk transfer methods.

Construction Manager

Many people confuse a construction manager's role with that of the general contractor. Many companies perform both of these services but there is a distinction. A construction manager is an advisor to the owner on almost every aspect of a project, including financing, design, general construction, scheduling, contract negotiations, contractor awards, purchasing, and budgeting.[23] Further, a construction manager monitors the performance of the design and construction teams.

There are two types of construction managers: agency and at risk.[24] An agency construction manager is a fee-based advisor that works solely for the owner and does not contract directly with any of the consultants or contractors. Conversely, a construction manager at risk acts as an advisor to the owner during the design phase of a project and acts as a general contractor during the construction, although it may not self-perform any work.[25] Just as an owner can procure a CIP, a construction manager at risk can also place the CIP as it holds contracts with the general contractor and subcontractors. Which hat—pure agency or at risk—the construction manager wears will obviously result in divergent exposures to liability.

General Contractor

Also called the prime contractor on some projects, the general contractor is responsible for scheduling, directing, and supervising the work. The general contractor may self-perform work for some trades and subcontract other work. On many projects, however, a general contractor hires subcontractors

for all performed work. In any case, the general contractor is responsible for injuries to its employees and damage to its equipment, tools, and materials. The contractor is also at risk for damage to the project, third-party property damages, and injuries caused by its employees or subcontractors, including injuries to employees of subcontractors working on the project through third-party actions. (See chapter 5.) In addition, the general contractor may become contractually obligated for damage or injury incurred by the owner. Because of this exposure, the general contractor frequently attempts to pass this risk to its subcontractors through its subcontracts, including damages for failure to timely complete the project.

Subcontractors

Subcontractors are most often hired by the general contractor or a higher-tiered subcontractor to perform work in specific trades. Similar to the general contractor, subcontractors are at risk for injury to their employees, damage to their equipment, tools, and materials, to their own work or the work of others, and for injury or damage to third parties caused by their activities. They may be contractually liable to the general contractor or a higher-tiered subcontractor for injuries or damages caused by activities over which they have no real control.

Architects, Engineers, and Other Design Professionals

Architects, engineers, and other design professionals generally perform design work on a project. In addition, they can also perform environmental, project management, and supervisory services. If a general contractor acts in a design-build capacity, the architect, engineers, and design professionals are hired as subcontractors. Traditionally, though, these professionals are hired directly by the owner. Owners may also hire a project manager to oversee the project, act as an owner representative, and give added direction to the general contractor.

Architects, engineers, and other design professionals typically provide plans and specifications that guide the construction project but do not provide/perform actual construction means and methods.[26] Professional errors and omissions, however, can expose project owners, as well as other project participants, to enormous liabilities far in excess of the professional practice policies of the individual design firms. Relying on these practice policies alone may lead to unwanted results, as those individual policies tend to provide inadequate professional liability coverage for large projects. Among other things, they tend to have relatively low limits, which are reduced by defense costs and by claims on other projects.[27] Project-specific policies designed to ensure that adequate coverage is in place may need to be considered. (These issues are discussed in chapter 6.)

Some inherent construction risks, however, may arise, such as injuries to employees of the professionals when working at the project site in supervisory

roles. Therefore, these professionals usually carry workers' compensation, general liability, and other lines of coverage for liabilities that are not necessarily design-related.

Suppliers

While suppliers do not typically perform services or work at the project site, they are still exposed to loss from third-party bodily injury and property damage arising from their own operations, such as faulty fabrication of materials. Moreover, a supplier may visit the project site for deliveries or installment oversight, presenting limited construction exposure of their own employees to jobsite injuries.

Project Delivery Methods

Each of the key players on a construction project plays a role based on the agreed-upon project delivery method. The most commonly employed methods of delivery are described below and each chosen method dictates the relationship between the owner, design professionals, construction manager, and general contractor. Each of these project delivery methods brings a new risk strategy and requires a risk transfer technique unique to the project. This book is not a treatise on construction contract delivery mechanisms, and there are many other excellent resources available for the construction lawyer on these subjects (including several prepared under the aegis of the ABA Construction Forum). However, a theme throughout is that insurance must be understood by referring to the risk that it covers. One simply cannot determine the type of insurance needed for a construction project or professional without understanding the basic risks that are presented. To that end, a summary discussion of project delivery methods is set forth below, along with some thoughts on the insurance issues that they may raise.

Design-Bid-Build

The most traditional and most commonly used type of delivery method in the United States is design-bid-build.[28] In this method, an architect retained by the owner prepares plans and specifications and a contractor reviews those plans and specifications and prepares a bid to perform the job.[29] Contractors are to bid and construct the project as designed, and typically the lowest, most responsible bidder is awarded the work. The architect and contractor each have separate contracts with, and report directly to, the owner who maintains control over the design.

Design errors may result in substantial liability, both for economic and noneconomic losses. Because the owner under this method retains design risk, it may seek to transfer some or all of that risk to the design professionals through contractual indemnity provisions and insurance requirements.[30] It may also seek its own independent insurance coverage using methods

discussed in greater detail in chapters 2 and 6. At the same time, the owner will seek to transfer liability to its construction manager and/or general contractor as to substantial construction-related liabilities arising out of execution of owner-provided plans and specifications.

Design-Build

In the design-build model, the owner develops a conceptual plan for the project and then hires one entity to both design and construct the project. The owner benefits by this method by having a single point of responsibility. For the contractor, however, there is both design and construction risk that must be protected against through contractual indemnity and insurance requirements. This project delivery method facilitates fast-tracking the project, as the design phase and construction phase can be executed simultaneously and overlap each other. Because of this, design-build is preferred for projects with a tight schedule and/or budgets, and has seen tremendous growth as a delivery system over the last few years.[31]

Design-Build-Bridge

The design-build-bridge method is similar to the design-build project delivery method except that the owner hires both an architect and a design-builder.[32] The owner assigns the architectural agreement to the design-builder once the project design documents are sufficiently developed to allow the owner to better understand the project's scope and/or budget (e.g., schematic design or design development stages). At that point, the design-builder becomes responsible for both design and construction.[33] This project delivery method presents unique issues with respect to the terms of the architectural agreement, as the owner and the design-builder each have an interest in those terms and will need to find them mutually acceptable.

Design-Build-Operate-Maintain

The design-build-operate-maintain method is most commonly used in heavy construction projects such as road construction.[34] This method is also similar to design-build, except it requires the design-builder to operate and maintain the project upon its completion. To compensate the design-builder for operating and maintaining the project, the design-builder often receives a portion of the operating revenues generated by the project (e.g., toll proceeds or lease proceeds).[35] Therefore, a single contractual relationship governs design, construction, operation, and maintenance.

Design-Build-Operate-Transfer

The design-build-operate-transfer method is similar to design-build-operate-maintain, but goes one step further by including the financing of the project in

the arrangement.[36] Specifically, the design-builder obtains the financing and is responsible for the construction loan, and typically the design-builder is paid from project proceeds after the project is complete. The project is turned over to the owner after the design-builder recovers its initial investment in the project, along with a negotiated amount of profit and interest.

Construction Manager at Risk

The construction manager at risk delivery method is typically divided into two phases: preconstruction and construction.[37] During the preconstruction phase, the construction manager reviews the owner-retained architect's design as it is being developed. As substantial portions of the design become complete, the construction manager solicits bids from trade contractors for those portions of the work. This project delivery method allows construction to begin before the design is complete, and because the construction manager holds the trade contracts, the owner is able to shift some of the project's risk to the construction manager. For example, the construction manager often contractually assumes liability for cost overruns and schedule delays.[38]

Construction Manager Not at Risk

Like the construction manager at risk delivery method, in the construction manager not at risk (or agency construction manager) method the construction manager is hired to both consult with the architect during the design phase of the project and manage the construction of the project.[39] In this way, the construction manager provides quality control during both the design and construction phases of the project, assisting the owner in making various project-related decisions. Unlike the construction manager at risk method, however, while the construction manager assists in the bidding process and manages the trade contractors during the construction phase, the owner contracts directly with the trade contractors. Furthermore, the construction manager does not guarantee the budget or the schedule.[40]

Insurance Basics for Construction Projects

Insurance plays a critical role in risk management, transfer, and financing on major construction projects. Despite its significance, however, construction insurance is often misunderstood. This section summarizes several basic insurance concepts that will allow a more complete understanding of the differences between the various insurance products discussed. Each of the different insurance products is described in greater detail in a separate chapter.

Bonds versus Insurance

Before we can begin discussing basic insurance concepts it is important to distinguish true insurance products from other construction-related instruments

such as performance and payment bonds. Although insurance carriers and sureties often cover what appear to be similar risks (and many companies offer both products),[41] in reality those risks are distinct.[42] Specifically, bonds stand behind, and financially guarantee, contractual risk transfers from owners to general contractors and from general contractors to subcontractors, including completion risks. [43] In a number of respects, bonds cover a wider range of performance exposures than traditional forms of insurance on construction projects.

Bonds do not necessarily transfer risk themselves. The bond is provided by the contractor-principal in favor of the owner-obligee and if a loss occurs under a bond, the surety is liable to respond to that loss.[44] Nevertheless, the principal-contractor has not transferred risk to the surety; rather, the principal remains liable for the loss at issue, typically through an indemnity agreement with the surety. By contrast, insurers pay covered losses with no right of recourse against the insureds beyond deductible obligations. Indeed, "the general rule is that the insurer may not bring a subrogation action against its own insured."[45] This is true even with respect to an insurer that has paid a loss for one insured, by reason of the negligence of another insured.[46]

First-Party versus Third-Party Insurance Coverage

Broadly speaking, insurance coverage can be classified according to the types of interests protected—that is, first party versus third party. First-party coverage applies to and protects an organization's own physical assets—for example, buildings, equipment, automobiles, mobile equipment, and personal property.[47] If a covered event damages these items, the insurance company provides the organization with the promised compensation, which is typically the actual cash value of the damaged item or the cost to repair or replace the damaged property, subject to the terms of the insurance contract. Other losses flowing from the event, such as business interruption or loss of rental income, can also be covered, typically through an extension of coverage that specifically covers such losses. The hallmark of first-party coverage is that the party suffering an injury, assuming that it is an insured, can submit the loss directly to the carrier for reimbursement. First-party policies generally do not protect the insured from claims by third parties.[48] Outside the construction context, coverage for fire damage to a home is an example of first-party coverage. Builders risk policies and equipment floaters are common examples of first-party policies on a construction project. An owner's permanent property policy also provides first-party coverage and can sometimes affect construction exposures.

Third-party coverage, on the other hand, is typically known as liability or casualty insurance and covers the insured's liability for damages to a third party. The two most common third-party coverages on a construction project are commercial general liability and professional liability policies.[49] For example, if an individual not employed by the organization or an entity not owned or operated by the organization makes a claim against the insured

organization for bodily injury or property damage, commercial general liability coverage may provide protection. In short, third-party coverage provides insurance for the insured's legal liability to a third party for losses or damages.

Many, but not all, third-party policies provide two distinct types of protection: a duty to defend and a duty to indemnify. The duty to defend, which is typically broader than the duty to indemnify, covers the cost of defending against third-party claims, while the duty to indemnify encompasses the cost of paying third-party claims.[50]

Coverage Triggers

A critical consideration, often misunderstood, is the time period for which insurance policies provide coverage. In other words, does an insurance policy with a 1998 to 1999 policy period cover losses that take place only during that time period? That are first reported during that time period? Where claims are first made during that time period? Here, some general principles can be distilled and, hopefully, basic misconceptions clarified.

Insurance begets jargon. An example is the commonly used term "trigger of coverage," which appears nowhere in insurance policies, but is used by lawyers as a shorthand to describe the circumstances under which the potential for coverage under an insurance policy arises.[51] In broad terms, third-party policies are triggered in different ways, and it is important to recognize and understand those differences.[52] An "occurrence" policy is triggered where damage or loss covered by the policy takes place during the policy period, regardless of when a claim arising from that loss or damage is made against the insured.[53] A simple example is a fire that occurs during the policy period. For sudden, one-time events like a fire, collapse, or automobile accident, the policy that is trigged is clear. Progressive losses over a period of years present more difficult issues and may involve coverage under multiple years. This is discussed in greater detail in chapter 3.

A "claims made" policy, by contrast, is triggered by a claim made against the insured during the policy period, regardless of when the loss or damage occurs.[54] Where a policy contains a "claims made and reported" requirement, a claim must be made against the insured *and* be reported to the carrier within the policy period.[55] Some claims-made policies contain additional limitations such as a "retroactive date." Where a policy has a retroactive date, only services performed or losses suffered after the retroactive date are covered.[56] Where a claim is made triggering a particular policy period, "related claims" made in later years are deemed to have been made during the initial policy period, at the time of the original claim. Whether two or more claims are "related" can determine whether more then one limit applies, whether more than one deductible must be paid, or even whether there is any coverage at all for later asserted claims.

An "extended reporting period" provides the insured with additional time to report claims after expiration of the policy period.[57] In professional liability policies, which are almost always claims-made rather than occurrence

policies, it is critical to include an extended reporting period extending coverage beyond the completion date of the project. This extension should cover claims made during the extended period, regardless of when the loss occurred, so long as the underlying work was performed in connection with the project. There are significant differences between the terms of individual extended reporting periods, so the terms of each must be carefully reviewed. Failing to timely report claims under claims-made policies can result in a loss of coverage, so particular diligence is required where policies of this nature are procured.

In recent years, "close of escrow" policies have become more common, especially for residential builders. A "close of escrow" policy covers homes or other buildings sold by the insured during the policy period for a specified period of time. For example, claims arising out of homes sold during the policy period may be covered for the period of an applicable statute of repose after the sale.

Project-specific insurance policies, as the name suggests, only insure claims arising out of the individual project or projects they are written to cover. Typically the policy period will be the anticipated length of the project, and the program will also include a completed operations tail (for occurrence policies) or extended reporting period (for claims-made policies) providing coverage for loss or damage occurring up to a specified number of years after project completion.

Per Occurrence, per Claim, and Aggregate Deductibles and Limits

The limits of many insurance policies, as well as deductibles (and SIRs) are often written on both a per occurrence or claim and an aggregate basis. As the name suggests, a per occurrence or per claim limit is the most the carrier will pay for all loss or damage arising out of a single occurrence or claim.[58] At the same time, a per occurrence or per claim deductible applies to each distinct occurrence of loss or claim.[59]

An aggregate limit is the most a carrier will pay under the policy regardless of the number of occurrences or claims made during the policy period, while an aggregate deductible is the highest amount that the carrier can withhold as deductible regardless of the number of occurrences or claims made during the policy period. Once an aggregate deductible is reached, the insured effectively has first dollar coverage for subsequent claims until policy limits are exhausted.

A simple example illustrates these points. If a policy has limits of $2 million per occurrence and $4 million aggregate, the carrier will pay or reimburse no more than $2 million in connection with any one claim or occurrence and a total of no more than $4 million for all covered claims or occurrences during the policy period. If this program had a per occurrence deductible of $250,000 and an aggregate deductible of $1 million, once the insured has incurred $1 million of the total deductible, the carrier must cover all future claims, losses, or damages falling within the policy and during the policy period until limits are exhausted.

Key Insurance Industry Players

Most insurance transactions in the construction context include the insured (contractor, subcontractor, owner, etc.), an insurance broker or agent, and the insurance carrier representatives. Insurance agents and brokers act as intermediaries between the insured and insurance carrier. Although the terms are sometimes used interchangeably by courts, it is generally understood in the industry that an insurance agent represents the insurance company whereas the broker represents the insured.[60] An agent often has the power to bind the insurer, issue policies, and accept risks on its behalf.[61] While some agents use exclusive arrangements with particular carriers, it is not uncommon for an "independent" agent to work on behalf of many carriers to carry out the administrative tasks of placing coverage. An agent typically does not have the responsibility to examine the needs of the insured or to determine the appropriateness of coverage; that is where a broker comes in.

In representing the insured, a broker performs a wider array of functions for the insured. A broker will typically solicit proposals for coverage and, upon securing an order from the insured, will place the order with the carrier.[62] In addition, a broker may also offer other products or services outside of placing insurance coverage. For example, a broker can be involved in claims advocacy, loss prevention services, risk management analysis, captive management, CIP administration, and other complementary services related to risk management. The precise scope of the broker's obligations should be delineated in a written agreement with the client because "acts of an agent are imputable to the insurer, [and] acts of a broker are imputable to the insured."[63] Additionally, not all brokers have access to all insurance markets. As an illustration, the retail broker retained by an owner or contractor to negotiate and procure the necessary insurance may in turn need to retain a wholesale broker to access certain surplus lines markets—markets established for insuring unique or hard-to-place risks.

Insurance carriers employ several categories of individuals who are involved in the insurance program of their insureds. Underwriters, for example, determine the insurability of a particular risk, that is, whether insurance should be provided and, if so, under what terms and at what price. More specifically, underwriters identify and calculate the insured's risk of loss, determine whether a policy can be written for a potential insured, determine the appropriate premium, and then formulate a policy to cover the risk in whole or in part by assembling a policy with appropriate terms, conditions, and exclusions.[64] Underwriters who are too conservative can cause insurers to lose business to other carriers. Underwriters who are too eager can expose the insurer to excessive liability.

Insurance carriers also employ claims adjusters. When a loss occurs, a claims adjuster representing the insurance company will review the details of the loss, provide an interpretation of the coverage wording, accept or deny the loss, and if accepted, offer a payment for the loss. Many insurance carriers have distinct underwriting and claim departments. Other carriers employ

independent third parties to act as other claims adjustors on their behalf.[65] (See chapter 11 for a detailed discussion of this process.)

Development of Standard Forms of Insurance for Construction Projects

The origins of modern insurance derive from the marine shipping and transportation industry, which was the first to invoke the act of transferring risk by having others guarantee against loss of a shipment.[66] As the insurance industry evolved, insurance companies created policy forms, coverage enhancements, and exclusions based on their loss experience, case law, and appetite to respond to the various risks posed by their clients. Many of today's policies, especially inland marine and builders risk policies, have evolved from these early forms, and as a consequence contain archaic maritime language even to this day.[67]

It is important to understand that not all insurance policies have the same terms, even for identical lines of coverage. This may seem obvious, but is frequently overlooked by even the most experienced construction project participants when facing complex issues of insurance coverage. Nevertheless, the vast majority of general liability policies sold in this country utilize language drafted by an insurance trade association, the Insurance Services Office (ISO).[68] ISO was formed in 1971 to provide customers and insurance professionals with information on property and casualty risks. Their services include issuing standard policy language, and that standardized language, particularly the commercial general liability policy, is relied upon to insure all types of business, not just construction risks. ISO uses a numbering system, typically in the lower left hand corner of the form, to differentiate among these amended and distinct forms.[69] The standard ISO commercial property forms are also frequently encountered.

One advantage of using ISO policy forms is that the policy language is used in common practice nationwide. It is also critical to recognize that ISO will periodically issue new language for both basic policy insuring agreements and endorsements, which amends existing forms in material ways. For this reason, reviewing the policy's drafting history to glean the parties' intent—and especially the insurer's intent—is a common practice in insurance coverage cases.[70] Indeed, in our experience, much of the confusion reflected in the case law and elsewhere over the scope of coverage provided by ISO forms arises out of a failure to recognize critical changes in policy language over time.

When an insurer does not use an ISO or other standard form, the carrier creates its own policy form known as a "manuscript" form.[71] Manuscript forms are more common with property, umbrella, professional liability, and excess liability coverages. An organization may receive broader coverage under a manuscript form, but it is particularly important to review all the language of a manuscript form and perform a detailed coverage analysis on that form prior to purchasing the policy. Note that endorsements modifying the terms of the policy are often manuscripted, even though they are attached to a standard form policy. Many manuscript forms include ISO language or may rely upon U.K. policy forms, including the Lloyd's Market Association (LMA) and Lloyd's forms.

Choice of Law

Choice of law can be critical to any insurance coverage analysis even though most insurance policies contain no choice of law clauses. Indeed, the same policy provisions can be interpreted differently depending on the state law that applies. Because of variation in state law regarding a variety of insurance coverage issues, this can affect the scope of coverage provided in a material fashion.[72]

Occasionally policies expressly identify the law to be applied to an interpretation of the policy. Where the policy is silent, however, the insurer and insured must look to the choice of law rules of the jurisdiction in which the dispute is centered to determine what law to apply.[73] There are four main approaches that courts throughout the United States have adopted when resolving choice of law questions with respect to contracts, including contracts of insurance: (1) *lex loci contractus* (the law of the place of contracting); (2) the "balancing of interests" or "most significant relationship" test (reflecting the *Restatement (Second) of Conflict of Laws* §§ 6 and 188); (3) governmental interest analysis (comparing competing states' interests); and (4) the "choice-influencing considerations" or "better rule of law" approach. The majority of jurisdictions employ variations of the first two approaches.[74] Under the first, the traditional *lex loci contractus,* the law of the state where the insurance policy was formed or entered into governs.[75] This is typically a fact-intensive question, and can be the place where the insurance policy was executed, where it was delivered to the insured, or where the last act that established a binding contract was performed.[76]

Under the second approach, the law of the state that has the most significant relationship to or contracts with the particular coverage dispute is the law that applies. Under this more modern and flexible approach, the factors considered include the location of the insured property, the place of performance, the location of the insured and insurer, and where the policy was issued or entered into.[77]

Regardless of what approach is utilized, it is important for all project participants to understand how choice of law may affect coverage.

Subrogation

Another important concept to understand in the context of insurance procurement is that of subrogation. Generally speaking, subrogation occurs when a party's insurer pays for a loss that was caused by, or the responsibility of, another party. The paying insurer is then subrogated to the rights of its insured and can pursue a direct action against that responsible party to recover that payment.[78]

In the construction context, subrogation claims are often waived by contract. Indeed, the industry recognized long ago the disruption that would ensue if there was constant finger-pointing on a project site.[79] Standard form AIA agreements were developed to include waiver of subrogation language to enable parties to look to their own insurance or specific insurance for certain claims without having to litigate fault or cause. Specifically, AIA Documents

B141 and A201 each contain waiver of subrogation language whereby each project participant agrees to waive all rights against the others "to the extent damages are covered by property insurance."[80] These waivers have been upheld as valid risk-shifting mechanisms.[81]

Where the owner and general contractor or other project participants utilize the standard AIA contracting documents or draft a contract that includes waiver of subrogation language, it is important for the insurers insuring the project to acknowledge these waivers and agree to forgo their rights of subrogation in the event of a paid loss because most policies expressly include a provision that states that the insured will not act in a way that would limit or otherwise diminish the insurer's rights of subrogation.[82] Therefore, it is critical to advise an insurer in advance of a claim of what subrogation rights, if any, have been waived in the contracting documents to ensure that the policy recognizes this waiver.[83]

Again, separately as a matter of law, an insurer cannot seek subrogation from its own insured.[84] Therefore, to further ensure that project participants and their respective insurers cannot subrogate against one another, it is common for project participants to be added as insureds on the others' policies.[85]

Common Construction Insurance Coverages

Each of the different insurance products described below is the subject of a separate chapter. In addition, special contract drafting considerations are discussed in chapter 2. For this introductory chapter, however, we provide a summary description of the common coverages used for construction projects in the United States, and the reader is directed to each individual chapter for more detailed treatment.

Builders Risk Insurance

Builders risk insurance is first-party property insurance typically covering loss or damage to the work during the course of construction, including losses arising from the negligence of contractors as well as certain "acts of God."[86] Builders risk coverage is often provided on an "all risk" basis, meaning that it covers all risks of physical loss or damage to property unless that risk or cause of loss is expressly excluded.[87] A builders risk policy should name the owner, contractors, and subcontractors of every tier, design professionals, and any necessary financing parties as insureds. The policy should also be written to cover the full value of the completed project, with the term of the policy extending to the anticipated date of project completion (including extensions for delayed completion). Permanent property coverage should be put into place as of the completion of the project, when builders risk coverage typically expires. No gap between the effective dates of these coverages is acceptable.

"All risk" builders risk policies cover costs incurred to repair physical damage caused by an accident or other covered event during construction.[88]

Coverage issues may arise over the extent to which the policy covers other costs flowing from the accident, such as delay-related damages, acceleration costs, disruption, and other "ripple" effects. The basic insuring agreements of most builders risk policies exclude "consequential" and similar losses except to the extent added back by a coverage extension. Accordingly, what coverage extensions are purchased to supplement coverage for the cost of repairing physical damage, and the terms of those extensions, are critical, and their effects must be carefully reviewed and considered.

It is also important to consider what exclusions are contained in the policy. Unlike commercial general liability policies, most builders risk policies are not written on standard industrywide forms.[89] Therefore, it is important to review the exclusions in both the basic insuring agreement and those added by endorsement. Conceptually, the purpose of an "all risk" policy is to cover most risks of physical damage to the work during construction, but if exclusions barring coverage of the principal risks faced by a project are added, the "all risk" nomenclature becomes nearly meaningless. In general, as with all insurance policies, the exclusions should be reviewed in their entirety to ensure that no unusual gaps in coverage are created. (See chapter 8 for an in-depth discussion of builders risk insurance issues.)

Commercial General Liability Insurance

Commercial general liability (CGL) coverage is third-party coverage designed to protect the insured against third-party claims and lawsuits for bodily injury or property damage arising out of its business operations.[90] Typically, CGL insurance is structured with a primary policy written on a standard ISO form. Most CGL coverage is written on an "occurrence" basis, and for nearly all construction risks occurrence-based coverage is preferable to claims-made coverage. Under standard industry forms, defense costs are in excess of limits (i.e., do not reduce them), while indemnity payments exhaust coverage limits.[91] Incurring costs to defend third-party claims is a significant risk in connection with any construction project, and not infrequently the insured's defense costs exceed indemnity paid for actual losses under the policy. This exposure should be carefully considered before an insured agrees to a CGL policy form that puts defense costs within rather than in excess of limits.[92]

Excess and umbrella coverage, typically written on a carrier-specific or manuscript form, may then be purchased to provide additional coverage over the primary layer of coverage.[93] As a general observation, it is important to have adequate limits, and to ensure that all policies (primary and excess) have relatively consistent provisions. Follow-form excess (sometimes called pure excess) policies, as the name suggests, follow the terms of the underlying policy, except where there are express differences. "Umbrella" policies provide broader coverage than the underlying policy in some respects, and effectively become primary when a loss triggers the broader umbrella coverage (often subject to a SIR).

Unlike builders risk policies, where the scope of coverage extensions is often a point of controversy, the most significant controversies with respect

to general liability policies often arise in connection with exclusions added by endorsement or included as part of a manuscripted policy, and the scope of those exclusions. Examples of exclusions commonly used by carriers in connection with large construction projects include mold/pollution and professional liability, but in both of these cases there are materially different forms of the exclusion in use. Some pollution exclusions leave contractors with a significant amount of coverage for pollution risks created during construction, while other exclusions seek to eliminate all coverage of "pollution" in all circumstances.[94] Coverage for property damage arising out of defective work is often hotly contested either under the policy terms themselves or endorsements. These issues are discussed in chapter 3. Likewise, there are significantly differing types of professional liability exclusions, and which form is utilized can be the determinative factor in whether damage arising from errors in stamped submissions by subcontractors is covered. Thus, it is critical to study what changes a carrier seeks to make by endorsement to the coverage provided by a standard form ISO insuring agreement.

Coverage for Environmental/Pollution Exposures

Many environmental and pollution exposures, including mold, are commonly excluded from general liability, builders risk, and professional liability policies. Specialized policies covering environmental risks, sometimes called contractors' pollution liability (CPL) and pollution legal liability (PLL) policies, can provide coverage to fill those gaps. CPL and similarly named policies typically cover pollution conditions resulting from operations performed by or on behalf of the named insured at a jobsite, but do not cover existing pollution conditions at a site owned by an insured. PLL and similarly named policies typically cover pollution conditions at or extending beyond owned property or caused by transported cargo. Unless a project is on an undeveloped site, obtaining CPL and/or PLL coverage should be considered. Of course, the scope of the required coverage can be determined only in conjunction with environmental studies of the particular site. These coverages are discussed in detail in chapter 7.

Professional Liability Coverage

Another third-party liability coverage commonly obtained for major construction projects is professional liability coverage. This is coverage for loss arising from services deemed "professional" in nature, such as architectural, engineering, and other design services. Unlike CGL coverage, professional liability coverage commonly covers pure economic loss, such as a delay in completion of the work independent of any physical damage to it. Most professional liability coverage is written on a claims-made basis and the limit of liability is always stated in terms of a per claim limit and an aggregate limit.

Many professional liability policies include both a duty to defend and a duty to indemnify. Unlike CGL occurrence policies, however, defense costs are typically within (i.e., reduce) the limits of professional liability policies.

This significantly impairs limits available to pay claims and has significant ramifications both for the insured and for third-party claimants.

On large projects, project-specific professional liability coverage is often procured. The alternative is to rely upon the practice policies of individual design firms. Unfortunately, those individual policies are often inadequate. They tend to have relatively low limits, which, as stated, are reduced by defense costs and by claims on other projects. Professional errors and omissions can expose project owners, as well as other project participants, to enormous liabilities far in excess of individual practice policies. Therefore, the extent to which losses arising from professional services are excluded from coverage of other project policies is very important and emphasizes again the need for a coordinated approach to coverage, one that focuses upon the interplay of various project policies

While nearly all design professionals are required to have professional liability coverage by project agreements, many construction managers procure it as well. Some services performed by construction managers may be deemed to be professional in nature, and thus may be outside the coverage provided by CGL policies with professional liability exclusions. Subcontractors whose work includes a significant design element may also incur, and expose general contractors and construction managers to, professional exposures. Where a contractor provides design-build services, ensuring that the design-build entity has professional liability coverage is critical. See chapter 6 for a discussion of professional liability insurance related to the construction industry.

Workers' Compensation/Employers' Liability Coverage

Workers' compensation policies cover injuries to employees suffered in the course of their employment. Since state law mandates the policies and benefits, it is often considered first-party coverage. All project participants who have employees working on the site must be covered by workers' compensation policies providing statutorily required limits. This can be accomplished through a project-specific insurance program, or by each project participant's own policies. While limits are statutorily prescribed, how the coverage is structured and financed can have significant cost implications for the project.

Most CGL policies exclude coverage of claims arising from injuries to the insured's own employees, but workers' compensation policies do not cover all such claims. Employers' liability policies issued as a part of the workers' compensation policy can fill the gap between workers' compensation and CGL policies. Procuring employers' liability coverage is commonly mandated by project agreements, together with workers' compensation coverage. Workers' compensation coverage is addressed in chapter 4.

Other Risks and Insurance Products

In addition to traditional "accidents" and "acts of God," owners face risks in connection with land acquisition and condemnation, zoning, financing, and

other aspects of construction, and satisfaction of performance requirements. Insurance and financial products are sometimes available in alternative markets (e.g., offshore and other surplus lines) to cover these risks, although those products tend to be extremely expensive. For the right price, and in the right insurance market, however, unique coverage can often be negotiated.

Certificates of Insurance

Certificates of insurance play a common role in construction projects and have for many years. Contractual agreements among the various parties outline insurance coverages, limits, and policy provisions required during the project term and through a specified time period after completion of the project. Rather than each party supplying copies of its entire insurance program, including all coverage forms and endorsements, each party usually requests certificates of insurance from the others to verify that appropriate coverage has been placed in compliance with governing contractual agreements.[95]

A certificate of insurance is an informational document identifying the insurance policies of the insured listed on that form. Similar to ISO, the Association for Cooperative Operations Research and Development (ACORD) has created standard form certificates commonly used to provide this information. A certificate of insurance does not amend the terms of the policies listed on the certificate. Rather, it certifies to the certificate holder and the entity requesting proof of insurance that the insurance coverage is in place at the limits and conditions listed on the certificate. But unless the certification is by the insurer or a party with actual or apparent authority to execute it, the certificate is not a guarantee that coverage is actually in place.

Routinely obtaining and reviewing policies by all project participants is seldom feasible, but sometimes the effort may be warranted given the size and nature of the risks presented. Thus, aside from receiving a certificate, in some circumstances a party may be well advised to seek independent verification that it has in fact been named an additional insured under the referenced policies and the terms on which that status has been afforded. Copies of policies and additional insured endorsements can provide this proof.

Additional Insured Status

Insurance policies may cover different categories of insureds. The "named insureds" are typically parties who are specifically identified in the policies and are entitled to all coverages provided by the policies.[96] The first named insured is commonly the party that procured the policy and is responsible for premium payments and the satisfaction of other conditions.[97]

Chapters 2 and 5 discuss the substance and mechanics of "additional insurance" status. In short, an "additional insured" is an individual or entity that is added as an insured under a policy with respect to certain projects or exposures in conjunction with a business relationship.[98] Requesting to be named as an additional insured is a generally accepted risk management tool for the

transfer of certain categories of risk to other parties on construction projects. The status of an additional insured gives those parties direct rights under the other party's insurance.[99] In addition, it should protect parties who obtain additional insured status from subrogation claims by the carrier, even where they were responsible in whole or in part for a covered loss, because generally carriers cannot subrogate against insureds.[100]

The coverage provided to additional insureds depends on the provisions negotiated on a case-by-case basis, making generalizations difficult. The protections provided to an additional insured can range from coverage only for claims arising from a narrow scope of work over a short period of time, to coverage nearly identical to that of the named insured. Typical examples of additional insured status are lessors under the liability policies of lessees; mortgagees, lenders, and owners under the liability policies of general contractors; and general contractors under the liability policies of subcontractors. Under builders risk policies, the term "additional insured" is not generally used, but similar status is often given to contractors and subcontractors of every tier. This is accomplished either specifically by endorsement or in the general description of an additional insured in the basic insuring agreement.

As noted, most additional insured endorsements contain limitations with respect to the coverage they provide. In the construction industry, for example, some endorsements used in connection with general liability policies provide the additional insured with coverage for completed operations claims, while others provide protection only against claims arising during construction.[101] In addition, a coverage aspect that receives considerable attention is the degree, if any, the additional insured is entitled to coverage for its own negligence. The failure to understand these issues, and insist on broader endorsements, can leave construction industry participants without the coverage they anticipated. Following up on the immediately prior example, general contractors who simply require that they be named as an additional insured on their subcontractor's general liability policies are likely to obtain that status during construction only. Requiring additional insured status for ongoing and completed operations, and collecting insurance certificates confirming that status, is far more likely to result in the general contractor having a more complete range of coverage for claims arising out of the work of subcontractors. Additional insured status does not replace the need for strong contractual hold harmless and indemnification provisions, as the obligation to indemnify is independent of the existence of insurance. Even if a loss does not trigger coverage or the loss is excluded from the policy terms, even if limits are inadequate or exhausted or if the insurer is insolvent or out of business, the indemnitor's obligation to indemnify remains intact as long as the provision is enforceable.

Wrap-ups or CIPs

Under a traditional construction industry insurance program, each project participant purchases its own insurance, and passes insurance costs to the owner in its bid.[102] The contractor's and design professional's own insurance

policies are typically called their "practice" policies. As an alternative, a sponsor (at times the owner, developer, construction manager, or general contractor) can purchase a master insurance program for an individual project or series of projects called a wrap-up or controlled insurance program (CIP), also referred to as a consolidated insurance program under the same acronym. A wrap-up or CIP "enables the program sponsor . . . to control elements of project risk and ensure that the benefits of a CIP are maximized."[103] This topic will be taken up in greater detail in chapter 10, but we introduce some broad principles of CIPs now because of their growing importance in large construction projects.

Under a CIP, the sponsor procures given lines of coverage for enrolled parties. Most CIPs include at least workers' compensation and general liability coverages (both primary and umbrella/excess liability insurance), although there are CIPs that provide general liability coverage only. Builders risk, professional, pollution, and other coverages can also be provided through the CIP. The sponsor of the CIP requires all enrolled parties to remove the cost of insurance from their bids, with respect to the lines of coverage being centrally purchased. These are significant sums since in today's world, insurance costs can be 5 percent of the hard costs of construction, or even more. The CIP sponsor uses the deductions of enrolled parties to offset the costs of the CIP (premium, deductibles, administration, etc.). The difference between the contractors' traditional cost of insurance, as reflected in bids made on projects without a CIP, and cost of the sponsor's CIP program plus any losses for which it becomes responsible can result in program savings (avoided costs) or losses for the sponsor.

An OCIP, or owner consolidated or controlled insurance program, is a CIP sponsored and administered by the owner. A CCIP is organized and administered by the general contractor or construction manager. Savings and risks of loss arising from use of a CIP are often shared by the owner and general contractor/construction manager in project contract documents.

Notes

1. Robert H. Jerry II, *What is Insurance?*, *in* New Appleman on Insurance Law Library Edition § 1.01[3] (Dec. 2009).

2. *See, e.g.*, IRMI, Glossary of Insurance and Risk Management Terms, http://www.irmi.com/online/insurance-glossary/default.aspx. *See generally* Mark Siwik & Randall Davis, *Emerging Corporate Governance Standards for Risk Management and the Lawyer's Role*, 14 Coverage 1 (2004) (discussing adaptation of the traditional risk management role with business development strategy). Practically applied, risk management is "taking deliberate action in accordance with the company's strategic objectives . . . to increase the odds of good outcomes and reduce the odds of bad outcomes." *Id.* The point is not to become a risk manager, but to become a better risk manager, since we are all risk managers already. *Id.*

3. Philip L. Bruner & Patrick J. O'Connor Jr., Bruner & O'Connor on Construction Law § 7.2 (2002). Indeed, most construction projects involve a host of risks, some of which are reasonably foreseeable by parties, and others more "peculiar," specific to a particular project and site. *Id.* The Construction Industry Institute (CII) has identified 13

"best practices" for identifying the most common risk on a construction project, upon which Bruner & O'Connor elaborate in some detail. *Id*. at § 7:24 n.2.

4. Risk assessment templates can be downloaded from a number of online resources and are available through software programs, such as Microsoft Office. For additional information on risk management services, consider these online resources: Insurance Services Office, Inc. Risk Management Services, available at http://rm.iso.com; Construction Weblinks, available at http://www.constructionweblinks.com; Construction Risk Management Portal and Library, available at http://www.constructionrisk.com; and the International Risk Management Institute (IRMI)'s guide, Risk Management for Business Executives, available at http://www.irmi.com.

5. For a case study employing risk registers for the management of tunneling projects, see Robert J.F. Goodfellow & Terry W. Mellors, Cracking the Code—Assessing Implementation in the United States of the Codes of Practice for Risk Management of Tunnel Works (Rapid Excavation & Tunneling Conference (RETC) 2007). For a case study on determining liquidated damages premiums, see F.H. (Bud) Griffis & Symeon Christodoulou, *Construction Risk Analysis Tool for Determining Liquidated Damages Insurance Premiums: Case Study*, 126(6) J. Constr. Eng'g & Mgmt. 407–13 (Nov./Dec. 2000). For additional construction risk management case studies, see IMRI, Risk Management Construction Case Studies, http://www.irmi.com/expert/topics/riskmanagement/constcaestudies.aspx, and Am. Soc'y of Civil Eng'rs, Construction Risk Analysis Tool for Determining Liquidated Damages Insurance Premiums: Case Study, http://cedb.asce.org/cgi/WWWdisplay.cgi?0004040.

6. *See generally* Vic Oblas, *Claims Avoidance and Dispute Management*, *in* Construction Law Handbook § 44.03 (Richard K. Allen & Stanley A. Martin, eds., 2d ed. 2009) ("[T]he contractor is usually well aware of the risk that has been allotted to their own activities (and likely has priced these in his bid). Where the trouble usually begins is when the contractor feels he is being asked to cover the cost of risk that he feels was originally allotted to the owner. This defaults to the importance of a clear delineation of risk ownership from the outset[.]"

7. For example, by requiring the subcontractor to indemnify the general contractor and name the general contractor and owner as additional insureds on the subcontractor's liability insurance and affording it coverage that is primary to, and non-contributory with, any other insurance available to them. *See* Bruner & O'Connor, *supra* note 3, § 10:20 (discussing flow-down indemnity liability and citing cases). *See generally* Donald S. Malecki, Pete Ligeros & Jack P. Gibson, The Additional Insured Book 55–105 (IRMI, 5th ed. 2004) (identifying several issues incidental to additional insured coverage). Additional insured coverage complements contractual indemnity running from general contractor to subcontractor. *Id*. at 67.

8. A common component of risk-shifting is the potential for the general contractor to require a subcontractor to defend against liability to the owner. *See* Advanced Ground Sys. Eng'g., Inc. v. RTW Indus., 388 F.3d 1036, 1043 (7th Cir. 2004) (subcontractor's indemnity obligations included a duty to defend its general contractor). Where risk has been successfully transferred downstream, controversy may also arise over whether the risk is insured. *See, e.g.*, Am. Home Assur. Co. v. Libby-Owens-Ford Co., 786 F.2d 22, 27–29 (1st Cir. 1986) (insurance policy covered consequential damages flowing from physical property damage to insured's defective work and discussing like cases); *see generally* Bruner & O'Connor, *supra* note 3, § 10:27.

9. In other words, the contractor includes the cost of the risk-shifting into its contract price.

10. *See* The Law of Performance Bonds 4 (Lawrence R. Moelmann & John T. Harris eds., Am. Bar Ass'n 1999).

11. Berkshire Hathaway 2009 Annual Letter from Warren Buffet, http://www.berkshirehathaway.com/letters/2009ltr.pdf (last visited Nov. 19, 2010).

12. Patrick J. Wielinski, Insurance For Defective Construction 157 (IRMI 2000, 2005). To illustrate, a "moral hazard" of procuring workers' compensation coverage might consist of reduced worker safety controls on the jobsite. *See* William J. Warfel, *Additional Insureds and the Moral Hazard*, Risk Mgmt., Jan. 1, 2006. Or, in the general liability context, employing a construction method that costs less for the contractor but increases the risk of third-party property damage.

13. Barry R. Ostrager & Thomas R. Newman, Handbook on Insurance Coverage Disputes § 13.13[a] (15th ed. 2010).

14. *Id*.

15. *Id*.

16. Jerry, *supra* note 2, § 1.09. Notably, "[t]he difference between a business that forms a captive and a business that self-insures the risk is that premiums paid to the captive may be tax-deductible, where contributions made by the self-insured business to a reserve fund are not; " *Id*. at § 1.09[3].

17. *See* Couch on Insurance 3d § 39:2 (1995).

18. Vermont, the largest U.S. captive domicile, and New York have robust captive programs. *See generally* Vt. Dep't of Econ. Dev., Captive Insurance, http://www.thinkvermont.com/Programs/CaptiveInsurance/tabid/120/Default.aspx; N.Y. Ins. Dep't, New York Captive Insurance Solutions for the Global Business Community, http://www.ins.state.ny.us/website3/captives/captive0.htm.

19. *See generally* Pub. L. No. 107-297, § 201, 116 Stat. 2,322, 2,337 (codified at 28 U.S.C. § 1610). TRIA was first enacted in 2002. It was extended in 2007 through 2014.

20. For further reading, see Practical Risk Management: The Handbook for Risk & Financial Professionals (IRMI 2010); U.S. Gen. Accounting Office, GAO-02-941, Catastrophe Insurance Risk: The Role of Risk-Linked Securities and Factors Affecting Their Use (Sept. 2002); U.S. Gov't Accountability Office, GAO-05-199, Catastrophe Risk: U.S. and European Approaches to Insure Natural Catastrophe and Terrorism Risks (Feb. 2005); Basel Comm. on Banking Supervision, Bank for Int'l Settlements, Report on Special Purpose Entities (Sept. 2009), http://www.bis.org/publ/joint23.pdf (last visited Nov. 22, 2009); Neil A. Doherty, Integrated Risk Management: Techniques and Strategies for Reducing Risk (McGraw Hill 2000).

21. Couch on Insurance 3d § 1:4 ("Strictly speaking, [a self-insurer is] an entity which rather than purchasing insurance, undertakes to guard against its own risks by assessing the risks and establishing sufficient reserves to pay any losses which occur. In practice, the term self-insurer tends to be applied to any party who does not purchase insurance, regardless of whether formal risk assessment has occurred or reserves established."); Eugene R. Anderson, Jordan S. Stanzler & Lorelie S. Masters, Insurance Coverage Litigation § 1.13 (2d ed.) (Aspen, 2d ed. 2010) ("Self-insurance has aptly been described by legal authorities as 'no insurance,' 'noninsurance,' the very 'antithesis of insurance.'").

22. *See, e.g.*, AIA Doc. 201 § 3.18.1.

23. AIA, The Architect's Handbook of Professional Practice, Glossary (14th ed. 2008).

24. Design Professionals and Construction Manager Law 246–47 (Steven A. Hess et al. eds., 2007).

25. *Id*.

26. AIA, The Architect's Handbook of Professional Practice 369–77 (14th ed. 2008); Philip L. Bruner & Patrick J. O'Connor Jr., Bruner & O'Connor on Construction Law § 11:287 (2010).

27. Bruner & O'Connor, *supra* note 26, at § 11:290.

28. Design-Build Contracting Claims 4 (Barry B. Bramble & Joseph D. West eds., 1999).

29. Bruner & O'Connor, *supra* note 3, § 6.1 (2002); Chuck Eastman et al., BIM Handbook: A Guide to Building Information Modeling for Owners, Managers,

Designers, Engineers and Contractors 3 (2008) (reporting that in 2002 almost 90 percent of public buildings and about 40 percent of private buildings were built using design-bid-build).

30. Dennis Brand, *Design-Build Contracts*, ConstructionWeekOnline.Com, Aug. 1, 2010, http://www.constructionweekonline.com/article-9090-design-build-contracts/1.

31. Philip Bruner and Patrick O'Connor report that a number of industry professionals estimate "that design-build will ultimately eclipse the more traditional delivery approaches and respect more than half of the United States' construction market by 2015." Bruner & O'Connor, *supra* note 3, § 6:15. For a comprehensive discussion of design/build contracting, see The Design Build Deskbook (John R. Heisse II & James S. Schenck IV eds., 3d ed. 2004).

32. Design Professionals and Construction Manager Law 247 (Steven A. Hess et al. eds., 2007).

33. *Id*.

34. Design-Build Contracting Claims 18 (Barry B. Bramble & Joseph D. West eds., 1999).

35. *Id*. at 19.

36. Bruner & O'Connor, *supra* note 3, § 6:9 (2002).

37. Design Professionals and Construction Manager Law 260 (Steven A. Hess et al. eds., 2007).

38. *Id*.

39. *Id*. at 259.

40. *Id*. at 259–60.

41. In a similar vein, courts may at times treat sureties as insurers under a state's insurance code. *See, e.g.*, Snow v. Jim Rathman Chevrolet, Inc., 39 So. 3d 368 (Fla. 5th Dist. Ct. App. 2010) ("[A] surety is considered by the courts to fit within the definition of insurer and to be subject to the same regulations as insurers in the Florida Insurance Code.") *But see* Eagle Fire Prot. Corp. v. First Indem. of Am. Ins. Co., 145 N.J. 345 (N.J. 1996) (surety contracts do not fall under New Jersey's court rule R.4:42-9(a) permitting the recovery of attorney's fees in actions "upon a liability or indemnity policy of insurance").

42. Couch on Insurance 3d § 1:18 ("the nature of the risk assumed by the party in the role of the "insurer" is a major distinction between insurance and arrangements of . . . surety. As a broad general rule, the risk can be characterized in terms of the degree to which the contingency is within the control of one of the parties.") See also The Law of Performance Bonds 4–6 (Lawrence R. Moelmann & John T. Harris eds., Am. Bar Ass'n 1999) for a discussion of the contrasts in underwriting considerations between performance bonds and casualty insurance policies.

43. *See* U.S. Fire Ins. Co. v. J.S.U.B., 979 So. 2d 871, 887–88 (Fla. 2007) ("The purpose of a performance bond is to guarantee the completion of the contract upon default by the contractor. Thus, unlike an insurance policy, a performance bond benefits the owner of a project rather than the contractor. Further, a surety, unlike a liability insurer, is entitled to indemnification from the contractor."); *see also* Sheehan Constr. Co., Inc. v. Cont'l Cas. Co., No. 49s02-1001-cv-32 (Ind. Sept. 30, 2010).

44. Commonly used bond forms include AIA A312 Performance Bond and Payment Bond; AIA A311 Performance Bond and Labor and Material Bond; and AIA 310 Bid Bond.

45. *See* Ostrager & Newman, supra note 13, § 5.06[c][2] (citing 16 Couch on Insurance 2d § 61:133 (1983)) ("No right of subrogation can arise in favor of the insurer against its own insured, since by definition subrogation only arise with respect to the rights of the insured against third parties to whom the insurer owes no duty.").

46. *Id*.

47. Bumberger v. Ins. Co. of N. Am., 952 F.2d 764 (3d Cir. 1991). For a thorough comparison of first-party property and third-party liability insurance, see Ostrager & Newman, supra note 13, § 21.01.

48. *See* Standard Fire Ins. Co. v. Spectrum Cmty. Ass'n, 141 Cal. App. 4th 1117, 1136 (Cal. App. 4th Dist. 2006) ("[insurer] is mixing apples and oranges—by attempting to apply principles of first party property insurance contract interpretation to third party liability insurance contracts."); Couch on Insurance 3d § 101:56. Notably, some policies do include both first-party and third-party protections. Auto liability policies and some pollution policies are examples.

49. *See* Port Auth. of N.Y. & N.J v. Affiliated FM Ins. Co., 311 F.3d 226, 233 (3d. Cir. 2002); Newmont Mines Ltd. v. Hanover Ins. Co., 784 F.2d 127 (2d Cir. 1986) ("A liability policy is intended to protect an individual or a business from liability for their tortious conduct").

50. *See, e.g.*, Perdue Farms, Inc. v. Travelers Cas. & Sur. Co., 448 F.3d 252, 257 (4th Cir. 2006) ("It has been uniformly held that the policy covenant to defend is 'separate from' and 'broader than' the covenant to indemnify.").

51. *See* Scott M. Seaman & Jason R. Schulze, Allocation of Losses in Complex Insurance Coverage Claims § 2:2 (2d ed. 2007).

52. Couch on Insurance 3d § 102:21 ("Under a liability policy providing coverage for each 'accident' or each 'occurrence' during the policy period, a risk insured against by the policy must occur during the policy period in order for coverage to be triggered.").

53. *Id*.

54. Holmes' Appleman on Insurance 2d § 130.1, at 218 (LexisNexis 2002) ("Focusing on the discovery, some call the policy a "discovery" policy rather than "claims made.")

55. Extended reporting periods are typically made available under a specified set of conditions, for example if the policy is canceled or not renewed by either the insurer or the insured; the insurer renews or replaces the policy with one specifying a later retroactive date; or the insurer renews or replaces the policy with one that is not claims-made (i.e., occurrence). IRMI, Commercial Liability § II.C.8–9 (describing ISO Form CG 00 02 § V—Extended Reporting Periods).

56. Holmes' Appleman on Insurance 2d § 130.1, at 226.

57. Extended reporting periods are typically made available under a specified set of conditions, for example if the policy is canceled or not renewed by either the insurer or the insured; the insurer renews or replaces the policy with one specifying a later retroactive date; or the insurer renews or replaces the policy with one that is not claims-made (i.e., occurrence). IRMI, Commercial Liability § II.C.8–9 (describing ISO Form CG 00 02 § V—Extended Reporting Periods).

58. *See, e.g.*, ISO Form CG 00 01 10 01 § III.5 ("the Each Occurrence Limit is the most we will pay . . . because of all 'bodily injury' and 'property damage' arising out of one 'occurrence.'").

59. Where one party on a construction project procures insurance for a number of project participants, which party bears responsibility for any deductibles is often a point of contention, and should be clearly stated in project agreements. The most common dispute is whether the deductible should be incurred by the party that procures the policy (and thus benefits from a higher deductible by reason of a lower premium) or by the party that caused the loss. In many cases a cap is negotiated so that the party procuring the coverage bears the deductible above a certain specified level. For example, project agreements may require the owner to purchase builders risk coverage, and cap the deductible obligation of a contractor responsible for a covered loss to $25,000 per occurrence, even though the policy deductible is higher. The owner is responsible for deductible in excess of that sum, but presumably has benefited from lower premiums.

60. *See* Couch on Insurance 3d § 45:1.

61. Holmes' Appleman on Insurance 2d § 44.2.

62. *See id*.

63. Couch on Insurance 3d § 45:1.

64. *See id*. at § 13 ("Underwriters affect (a) the existence of coverage, by approving or disapproving applications for insurance, and (b) the terms of the insurance agreement by determining the nature and magnitude of the risk involved, which directly determines the premium that the insurer will charge a particular insured.").

65. *Id*.

66. *See id*. at § 1:2.

67. Take, for example, "sue and labor" clauses, such as the one at issue in *American National Fire Ins. Co. v. Mirasco, Inc*., 249 F. Supp. 2d 303, 326 (S.D.N.Y. 200), requiring the insured "to sue, labor, and travel for, in and about the defense; safeguard and recovery of said goods and merchandise . . . without prejudice to [the] insurance." *See also* Swire Pac. Holdings, Inc. v. Zurich Ins. Co., 845 So. 2d 161, 168 (Fla. 2003) ("to sue, labor and travel for, in and about the defense, safeguard and recovery of the insured property . . .").

68. *See* French v. Assurance Co. of Am., 448 F.3d at 697 (4th Cir. 2006) (citing Hartford Fire Ins. Co. v. California, 509 U.S. 764, 772 (1993)) ("ISO develops standard policy forms and files or lodges them with each State's insurance regulators; most CGL insurance written in the United States is written on these forms."); Sheehan Constr. Co., Inc. v. Cont'l Cas. Co., No. 49S02-1001-CV-32, at *1 (Ind. Sept. 30, 2010) ("Most CGL policies are written on standardized forms developed by an association of domestic property insurers know as the Insurances Services Office.").

69. Most primary policies in today's construction market are written on the CG 00 01 ISO "occurrence" forms. As those forms evolve, the updated version is reflected by the ISO form number. The 2001 ISO occurrence form is CG 00 01 01, the 2004 version is CG 00 01 04, the 2007 version is CG 00 01 07, and so on.

70. *See, e.g., French*, 448 F.3d at 701; United States v. Fire Ins. Co. v. J.S.U.B., Inc., 979 So. 2d at 887; Kerr-McGee Corp. v. Admiral Ins. Co., 1995 Okla. 102, 905 P.2d 760 (1995) (citing an exhaustive review of drafting history in *Morton Int'l, Inc. v. Gen. Accident Ins. Co*., 134 N.J. 1, 36, 629 A.2d 831, 851 (1993).)

71. IRMI Online Glossary, "Manuscript Form or Policy," http://www.irmi.com/online/insurance-glossary/terms/m/manuscript-form-or-policy.aspx.

72. Coverage for pollution losses is one example where state law variations are potentially consequential, though not necessarily dispositive. *See* Apana v. TIG Ins. Co., 574 F.3d 679, 682 (9th Cir. 2009); *see, e.g*., MacKinnon v. Truck Ins. Exch., 31 Cal. 4th 635 (Cal. 2003); Am. States Ins. Co. v. Koloms, 177 Ill. 2d 473 (Ill. 1997); Belt Painting v. TIG, 100 NY 2d 377 (2003); *see, e.g*., Deni Assocs. of Florida, Inc. v. State Farm Fire & Cas. Ins. Co., 711 So. 2d 1135 (Fla. 1998); Owners Ins. Co. v. Farmer, 173 F. Supp. 2d 1330 (N.D. Ga. 2001).

73. *See* Klaxon Co. v. Stentor Elec. Mfg. Co., 313 U.S. 487, 496 (1941).

74. For useful surveys of how choice of law rules are applied, see Symeon C. Symeonides, Choice of Law in the American Courts in 2009: Twenty-Third Annual Survey (Am. J. Comparative Law 2010); Stephen D. Coggins, Fifty State Survey of Choice of Law Rules in Insurance Coverage Litigation (1995), http://www.abanet.org/tips/iplc/fiftytates.html.

75. Fioretti v. Mass. Gen. Life Ins. Co., 53 F.3d 1228, 1235 (11th Cir. 1995) (under Florida law, "in the absence of a contractual provision specifying the governing law, a contract (other than one for the performance of services) is governed by the law of the state in which the contract is made, i.e., where the last act necessary to complete the contract is done.")

76. Commercial Union Ins. Co. v. Porter Hayden Co., 630 A.2d 261, 266 (Md. 1993) (under Maryland's application of *lex loci contractus*, the last act in forming an insurance

policy is typically delivery and payment of premium.). In contrast, in *Fioretti*, the Eleventh Circuit determined that where a carrier agreed to underwrite a life insurance policy, contingent only upon the insured's execution of the statement of good health, "this one event (as opposed, to say, his tendering of the first required premium)" was the last event necessary to complete the contract. *Fioretti*, 53 F.3d at 1236.

77. Specifically for contracts, under § 188, courts consider (1) the place of contracting, (2) the place of negotiation of the contract, (3) the place of performance, (4) the location of the subject matter of the contract, and (5) the domicile, residence, nationality, place of incorporation, and place of business of the parties. Significantly, however, when dealing with insurance contracts, under § 193, the principal location of the insured risk is given greater weight than any other single contract in determining the state of applicable law provided that the risk can be located in a particular state. Section § 193 provides in pertinent part:

> The validity of a contract of fire, surety or casualty insurance and the rights created thereby are determined by the local law of the state which the parties understood was to be the principal location of the insured risk during the term of the policy, unless with respect to the particular issue, some other state has a more significant relationship. . . .

Id. § 193.

78. Eugene R. Anderson, Jordan S. Stanzler & Lorelie S. Masters, Insurance Coverage Litigation § 19.04[A] (Aspen 2010) ("Under subrogation, an insurer that pays its policyholder's loss is placed in the position of its policyholder, allowing the insurer (and not the policyholder) to recover from any third party responsible for the loss."); Patrick J. Wielinski, Insurance for Defective Construction 329 ("This common law doctrine allows a party who has paid a loss or debt on the part of another to succeed to the rights of that other party to pursue recovery from a third party who was responsible for causing the loss.")

79. Wielinski, *supra* note 78, at 330 ("A waiver of subrogation allows the parties to allocate the risk of damage to the work during construction to a third-party insurer with the reasonable certainty that payment for the loss will stay [for example] with the builders risk insurer, and not be passed on to contractors on the project."); Haemonetics Corp. v. Brophy & Phillips Co., 23 Mass. App. Ct. 254, 501 N.E.2d 524 (Mass. Ct. App. 1986) (quoting Tokio Marine & Fire Ins. Co. v. Employers Ins., 786 F.2d 1010, 104 (2d Cir. 1986)) ("A waiver of subrogation is useful in such projects because it avoids disruptions and disputes among the parties to the project. It thus eliminates the need for lawsuits, and yet protects the contracting parties from loss by bringing all property damage under the all risks builder's risk property insurance."); Donald S. Malecki, Pete Ligeros & Jack P. Gibson, The Additional Insured Book 325 (IRMI 2004) ("Subrogation is a particularly crucial issue in builders risk insurance because the parties to a construction contract usually intend for the builders risk insurance to be their sole remedy for covered damage caused by the negligence of any of the parties.").

80. *See* AIA Doc. B141 § 1.3.7.4; AIA Doc. 201 § 11.3.7.

81. Wielinski, *supra* note 78, at 331 ("The broad scope of the AIA waiver of subrogation is generally upheld and enforced") (citing Temple Eastex, Inc. v. Old Orchard Creek Partners, Ltd., 848 S.W.2d 724 (Tex. App. 1992, writ denied)).

82. IRMI, 2 Commercial Property Insurance § IX.J.41 ("Virtually all types of insurance policies contain a provision restricting the insured from taking actions that will impair the insurer's ability to seek reimbursement from negligent third parties for damages paid under the policy (i.e. its ability to subrogate).").

83. *Id*. ("Most builders risk policies allow pre-loss waivers of subrogation, either affirmatively or impliedly. An implied waiver of subrogation says that the insured must

do nothing *after loss* to impair any recovery rights against others. An affirmative waiver of subrogation specifically states the insured may waive recovery rights against another party in writing prior to loss." Specifically, the sample affirmative waiver provided therein includes the language "The Company will have not rights of subrogation against: A. Any person or entity, which is a Named Insured or an Additional Insured; B. Any other person or entity, which the Insured has waived its rights of subrogation against in writing before the time of loss.")

84. *See supra* note 43.

85. *See supra* note 83; *see also*, Wielinski, *supra* note 78, at 330.

86. Couch on Insurance 3d § 132:20 ("A builder's risk policy is a species of property loss insurance by which the builder seeks to insulate himself from liability occasioned by damage to or loss of the structure which the builder has contracted to produce. Such coverage is necessitated by the fact that commercial general liability policies generally except for coverage damage to the insured's work product."). *See also* Wielinski, *supra* note 78, at 315 ("The primary means to insure property exposures during the course of construction is through first-party property insurance, usually builders risk coverage.").

87. Ariston Airline & Catering Supply Co., Inc. v. Forbes, 511 A. 2d 1278, 1282 (N.J. Super 1986) ("a policy of insurance insuring against 'all risks' is to be considered as creating a special type of insurance extending to risks not usually contemplated, and recovery will usually be allowed, at least for all losses of a fortuitous nature, in the absence of fraud or other intentional misconduct of the insured, unless the policy contains a specific provision expressly excluding loss from coverage.")

88. 4 Douglas L. Patin, Law and Practice of Insurance Coverage Litigation § 45:25 (2008) ("Builder's risk insurance is issued to a contractor or property owner to insure against the risk of loss or damage to the construction work during the construction process, regardless of the insured's fault. This coverage generally extends until the placement of permanent property insurance to cover the completed work.").

89. IRMI, Commercial Property Insurance § IX.J.4. ("The vast majority of builders risk policies are written on nonstandard inland marine forms. . . . As is true of most inland marine coverage lines, there is no such thing as a standard builders risk coverage form . . . The only way to know what a specific policy does or does not provide is to read the policy carefully.")

90. Holmes' Appleman on Insurance 2d § 129.1.

91. Standard CGL policies also provide coverage against what is known as "Coverage B—Personal and Advertising Injury." These include injury arising out of such things as false arrest, malicious prosecution, wrongful eviction, and infringing upon another's copyright, trade dress or slogan." ISO CGL Form CG 00 01 10 01 § V.14. Those coverages are only infrequently triggered in the context of a major construction project.

92. Prejudgment and postjudgment interest, taxed costs, and other exposures are also in excess of policy limits under the "Supplementary Payments" provision of a standard ISO CGL policy. Again, these exposures can exceed the indemnity limit in some circumstances.

93. Ostrager & Newman, supra note 13, § 6.03[a] ("Excess or secondary insurance is coverage that attaches only after a predetermined amount of primary coverage has been exhausted" while umbrella policies may provide broader coverage than what is contained within an underlying primary policy.); Commercial Union Ins. Co. v. Walbrook Ins. Co., 7 F.3d 1047, 1053 (1st Cir. 1993) ("Umbrella policies differ from standard excess insurance policies in that they are designed to fill gaps in coverage.").

94. Compare the "absolute" pollution exclusion in the ISO standard CGL form, which preserves coverage for certain incidental pollution (including hostile fire) damages, certain off-premises operations, and the products-completed operations hazard with the Total Pollution Exclusion Endorsement, ISO Form CG 21 49 09 99, which "is used by gen-

eral liability insurers to virtually eliminate all coverage for pollution incidents." IRMI, Commercial General Liability § VI.I.32 (10th Reprint Aug. 2009).

95. Donald S. Malecki, Pete Ligeros & Jack P. Gibson, The Additional Insured Book 345 (IRMI, 5th ed. 2004) ("The certificate of insurance is the primary vehicle for verification that insurance requirements have been met.").

96. *Id*. at 9 ("Named insureds are those individuals or entities to whom the policy is issued. Named insureds typically have more rights and responsibilities than additional insureds and are also subject to more exclusion.").

97. For example, in addition to paying premiums, named insureds "have more stringent loss reporting requirements." Likewise, some policies give them broad cancellation rights. *Id*. at 12.

98. *Id*. at 9 ("Additional insured status is usually provided either by endorsement or . . . by way of a policy provision that is triggered by a requirement for additional insured status in the underlying contractual agreement.").

99. *Id*. at 73 ("[O]ne of the most important reasons for seeking additional insured status in addition to contractual indemnification is to secure direct rights in the indemnitor's insurance policy" in order that the indemnitee may avoid funding defense costs or paying settlements and judgments first and wait to recover under an indemnification clause.).

100. See *supra* sections "Bonds versus Insurance" and "Subrogation."

101. For example, ISO Form CG 20 10 (Additional Insured—Owners, Lessees or Contractors—Scheduled Person or Organization) and ISO Form CG 20 33 (Additional Insured—Owners, Lessees or Contractors—Automatic Status When Required in Construction Agreement with You) provide additional insured coverage but "only with respect to liability for [injury caused by acts or omissions] in the performance of your ongoing operations for the additional insured."). In contrast, ISO Form CG 20 37 07 04 (Additional Insured—Owners, Lessees or Contractor—Completed Operations) provides additional insured coverage but "only with respect to liability for [injury caused by your work] at the location designated . . . performed for that additional insured and included in the products-completed operations hazard."

102. Tracy Alan Saxe, *Construction Wrap-Ups: Owner and Contractor Controlled Insurance Programs*, *in* Construction Law Handbook 627 () (Richard K. Allen & Stanley A. Martin eds., Aspen, 2d ed. 2009).

103. *Id*.