

## Commercial Risk Transfers in Construction

Construction projects usually start with a contract outlining the project details and the duties and responsibilities of the parties. There are standard contracts, such as the ones provided by the American Institute of Architects (AIA) and the Construction Owners Association of America, and agreements (often templates) developed by owners, contractors, and architects. Both can be modified to address different projects and circumstances.

Commercial risk transfers are a way to allocate risk among the parties to an agreement. As such, they are often used in construction contracts. When done correctly, commercial risk transfers shift the responsibility to pay for claims and claim-related expenses (such as attorney fees) to someone else, stabilizing or reducing liability insurance premiums – loss payments and reserves are a primary rating factor for the commercial general liability policy.

### CONTRACT REVIEW – IDENTIFYING OBSTACLES AND OPPORTUNITIES

Some things to consider:

- Contract terms favor the drafter.
- The upstream party has greater bargaining power.
- Standard contracts or documents produced by an organization or association benefit its members or subscribers.
- Contracts can contain unenforceable or unobtainable terms.

When you are the downstream party (such as a subcontractor), your goal is to limit your exposure and accept a *minimal* degree of risk – an acceptable allocation that is consistent with your responsibilities under the agreement and in line with your existing insurance coverage. Elements of the contract to review include: indemnification and hold harmless language should be consistent with the law and not overreaching; requested insurance coverage and limits should reflect the nature of your work; required forms and endorsements should be proper and obtainable (the New York State Department of Financial Services does not allow the use of unauthorized certificates of insurance forms and prohibits language that reflects terms and conditions not contained in the actual policies).

As the upstream party (such as a general contractor), your goal is to reasonably *allocate* risk to the party performing the work. Besides using indemnification and hold harmless clauses, you want to make sure a subcontractor carries the correct coverages and limits of insurance.



This is particularly important when subcontractors are performing specialty work, or work that carries a higher level of risk, for example:

|  |  |   |
|--|--|---|
| <b>Abatement</b>   | Asbestos/Lead Abatement Liability                                    | \$2 million each occurrence and aggregate |
| <b>Crane Operators</b>                                   | Excess/Umbrella Policy   | \$25,000,000                              |
| <b>Contractors Cleaning-Up Toxic Materials or Spills</b> | Contractors' Environmental Coverage                                  | \$2,000,000 each occurrence and aggregate |
| <b>Marine/Barge Operators</b>                            | Protection & Indemnity<br>Towers Liability<br>Marine Umbrella Policy | \$1,000,000<br>\$1,000,000<br>\$5,000,000 |
| <b>Testing Companies</b>                                 | Errors & Omissions   | \$2 million each occurrence and aggregate |

#### **INDEMNIFICATION AND HOLD HARMLESS AGREEMENTS**

If drafted properly, courts will enforce these agreements. Regardless of a party's position in the contracting process, indemnification and hold harmless agreements should be reviewed by an attorney before drafting and/or signing.

#### **CERTIFICATE OF INSURANCE REVIEW**

Whether an upstream or downstream party, insurance certificates and other documents need to be reviewed and checked for compliance. Pitfalls include:

|   |   |
|---|---|
| <ul style="list-style-type: none"> <li>➤ Missing coverages</li> <li>➤ Insufficient limits</li> <li>➤ Nonlicensed insurers</li> <li>➤ No additional insured status or, additional insured status without primary and noncontributory language</li> </ul> | <ul style="list-style-type: none"> <li>➤ Policies with unacceptable exclusions</li> <li>➤ Expired policies</li> <li>➤ Missing or deficient additional insured endorsements</li> <li>➤ No waiver of subrogation</li> </ul> |
|---|---|

*This document contains general information about Commercial Risk Transfers. It is not intended as legal advice. For assistance with risk transfers, contact your insurance broker, attorney or Gramercy Risk at 516 750-9364.*