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Risk Management Bulletin

Subcontracts – Insurance Coverages

A properly executed subcontract agreement between an owner and contractor or contractor and lower tiered subcontractor is vital to ensure a successful project. After all, it outlines the responsibilities for each party, the scope of work, payment structure, and the indemnification provisions. It should also include detailed insurance requirements to help ensure there is financial protection in the event there is an unforeseen event leading to a claim.

Over the past several years insurance company underwriters have begun to dictate very specific requirements in these subcontracts to help ensure proper risk transfer is in place and mitigate potential claims costs for their insureds. The primary reason is that most all insurance provisions now include the verbiage “as required by contract”. So if the wording is not in the agreement the subcontractors’ policy may not respond. These requirements start with adequate insurance limits. Following is an overview of these coverages, their importance, and typical limits required for each line of coverage.



The Commercial General Liability (CGL) is a very broad coverage offering and is designed to cover bodily injury or property damage that the insured is legally liable to pay. It does not cover every type of liability event, but it does provide the foundation for the liability exposures an organization might face. There are three key limits provided on this policy that should be referenced in the subcontract agreement. The “Per Occurrence” limit which applies to bodily injury or property damage under Coverage A of the policy (primarily third party claims arising from activities on your premises), the “General Aggregate limit” which is the maximum amount payable during the policy term for Coverage A claims, and the “Products / Completed Operations” limit which is the annual aggregate limit for damages arising from the products or your completed operations exposure (e.g. a building or electrical work in a building). The expectation of most insurers is that the subcontractors should maintain \$1 million per occurrence, \$2 million general aggregate and \$2 million products / completed operations limits. Some contracts also include a requirement for “Personal and Advertising” coverage, typically at a \$1 million limit. This addresses exposures outlined under Coverage B of the policy including defamation, slander, or copyright infringement. Some contracts may reference higher limits of coverage, depending on the nature of the risk and the specific insurance company they may offer a higher per occurrence, general aggregate or products/ completed operations limit, but for most insurers the standard offering is \$1M / \$2M / \$2M limits. Higher limits are secured through an Excess or Umbrella policy, which “sits on top” of the CGL limits. The CGL excludes coverage in several areas which then warrant securing policies to address these exposures.

The CGL specifically excludes bodily injury to an “employee” of the insured arising out of employment or in the course of performing their duties for the insureds business, therefore a Workers Compensation policy must be secured to address this exposure. The Workers Compensation policy has two coverage parts. Part 1 is “statutory” workers compensation coverage which are prescribed by the State. It provides coverage for lost wages and medical bills for an injured worker. It has no limit other than by statute, the policy responds for the total lost wages and medical bills no matter the cost. Workers compensation coverage is an “exclusive remedy” for work related injuries, meaning an employee cannot sue their employer if injured on the job. State work comp laws provide an exception to the exclusive remedy if there is gross negligence on the part of the employer and the injury is severe (in Texas it pretty much requires a fatality to trigger the employers liability coverage). This exposure is addressed in Part 2 of the policy, the “employers’ liability” coverage. This coverage has a defined limit, similar to the CGL. Contracts typically require \$1M in limits, occasionally we see a requirement for \$500,000 limits for lower risk trades. Both coverage parts should be outlined in the subcontract agreement to help ensure proper coverage is in place.

The CGL also specifically excludes bodily injury or property damage arising out of the ownership, maintenance, use or entrustment to others of any auto, therefore a Commercial Auto policy must be secured to address legal liability arising from owned, hired, or non-owned vehicles used in the course of work. We typically see a requirement of \$1 million limits, again, higher limits would need to be addressed via an excess or umbrella policy.

Many contracts require higher limits of coverage due to the nature of risk or the exposures associated with the work. This is achieved through the aforementioned Umbrella or Excess Liability policy. This policy is designed to increase the limits of coverage for each of the policies mentioned above. The Umbrella policy should be “following form” to help ensure continuity of coverage from the primary policy to the Excess policy.

The CGL also excludes environmental / pollution exposures (although some policies provide a sublimit for sudden and accidental pollutants) aircraft (including drones), and professional liability. Depending on the nature of work, separate coverage may be required to address these exposures and should be spelled out in the contract accordingly.

There are many other nuances and complexities related to the insurance provisions required in a subcontract agreement, but hopefully this information provides a good overview of the coverages, policy limits, and why they are each important to help ensure financial responsibility to respond to an unforeseen event. If you have questions about your insurance program structure, or need assistance with other loss control or risk management issues, please feel free to call or drop me a note.

THANKS,

Mark

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