

The right endorsement

Covering additional insureds in construction contracts

March 2018 • Lockton Companies

Adding other parties as an additional insured on to a general liability policy has become increasingly popular during the past twenty years. Almost every contract, especially in the construction industry, includes this requirement. To keep up with demand and pressure from the insurance industry, the Insurance Services Office (ISO) has issued various versions of the standard endorsements, CG 20 10 and CG 20 37, which have not always been advantageous to additional insureds, especially in the construction industry. Therefore, it is important to review construction contracts in full and pay special attention to the wording revolving around the additional insured endorsements.

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CONTRACT TERMS

- Almost every contract, especially in the construction industry, includes a requirement to add parties as additional insured.



WHAT IS AN ADDITIONAL INSURED?

- An additional insured is a third party that has been added to another party's general liability policy. This provides added benefits to the additional insured under the named insured's policy.



ENDORSEMENTS

- All additional insured endorsements do not provide equal coverage to additional insureds. Whether or not companies have proper coverage may depend on the endorsement used.



WHAT CAN COMPANIES DO?

- Vet insurance carriers and confirm what additional insured endorsements can be offered.
- Have an insurance professional with construction expertise review contracts prior to the contractor signing them.



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What is an additional insured?

An additional insured is a third party that has been added to another party's general liability policy. This provides added benefits to the additional insured under the named insured's policy. These include but are not limited to, access to the limits of insurance and defense. Essentially, being added as an additional insured grants the third party similar (but not the same) rights as the named insured.

Who typically asks to have additional insured status and why?

Additional insured status is typically sought by those entities not automatically included under the "Who is an Insured" provision of the general liability policy of another entity. In regards to contractors, this is typically an upstream party (such as an owner or general contractor) that has required the contractor to provide a certain degree of protection under the contractor's general liability policy. The reasons why a third party would want to be listed as an additional insured on a contractor's policy include:

- ❖ Provides safety net for hold harmless or indemnification agreements
- ❖ Affords direct rights under the other party's insurance
- ❖ Protects the additional insureds from subrogation
- ❖ May provide for higher total available limits (dependent on policy wording relating to horizontal exhaustion)
- ❖ Defers losses away from the additional insured's own insurance policies

What are the major changes that have occurred in the CG 20 10 and CG 20 37 endorsements?

There are various additional insured endorsements within the insurance industry. However, the most commonly requested additional insured endorsements are the ISO CG 20 10 and CG 20 37. These endorsements have changed drastically since their creation in ways that have not always been advantageous to contractors.

November 1985

ISO released the first additional insured endorsement in November of 1985, commonly known as the CG 20 10 11/85 endorsement. This endorsement was later labeled as the broad form endorsement as it includes coverage for "liability arising out of your work". This language proves important because it was deemed that the "arising out of" language did not require fault, and therefore this endorsement provided coverage to an additional insured even if the additional insured was 100% at fault. Also, this edition provided additional insured status for both on-going/premises liability and completed operations coverage in one endorsement.

October 1993

The second edition of ISO's additional insured endorsement, CG 20 10 10/93, was not commonly used as the language was changed from "liability arising out of your work" to "liability arising out of your ongoing operations." This edition effectively eliminated additional insured status for completed operations.

October 2001

To fix the completed operations issue, ISO released the CG 20 10 10/01 along with a new form, CG 20 37 10/01. The sole purpose of these forms was to bring back the ability to add an additional insured to the completed operations coverage. These endorsements were the last editions to use the "arising out of" language.

July 2004

The next editions released by ISO were the CG 20 10 07/04 and CG 20 37 07/04, which made minor changes to the wording that provided drastic implications for contractors and additional insureds. These editions changed the no-fault language of "arising out of" to "caused, in whole or in part, by: 1. Your acts or omissions; or 2. The acts of omissions of those acting on your behalf." As it states, this language requires the named insured on the policy to be at fault or partially at fault at the time of a loss. This language changed the broad form wording to an intermediate form as these editions are sometimes classified.

April 2013

The latest additional insured form editions released by ISO are the CG 20 10 04/13 and the CG 20 37 04/13. These forms use the same language as that of the 07/04 editions, however, they add language that has made them better known as the limited form editions. The additional language included is as follows:

"1. The insurance afforded to such additional insured only applies to the extent permitted by law; and 2. If coverage provided to the additional insured is required by a contract or agreement, the insurance afforded to such additional insured will not be broader than that which you are required by the contract or agreement to provide for such additional insured."

"If coverage provided to the additional insured is required by a contract or agreement, the most we will pay on behalf of the additional insured is the amount of insurance: 1. Required by the contract or agreement; or 2. Available under the applicable Limits of Insurance shown in the Declarations; whichever is less."

The above language has limited the coverage available to the additional insured to the lesser of the amount of coverage required by the written contract or agreement, or the limits included within the policy.

Potential implications of the latest CG2010 & CG2037 editions and solutions to obtain adequate coverage

As noted, there are various changes to the ISO additional insured endorsements which have resulted in a range of coverages afforded to the additional insureds. Some of the most notable changes, their implications and solutions are below.



"Arising Out Of" vs. "Caused in Whole or In Part By" language

When ISO made the change from the CG2010 and CG2037 10/01 editions to the 07/04 editions, they created a gap in coverage that was previously provided to an additional insured. In a case of a general contractor and a subcontractor relationship, the liability is typically pushed down to the subcontractor via an additional insured endorsement. The outcome can vary depending on what edition date is included on the subcontractor's policy.

EXAMPLE 1

To further explain this issue, imagine there is a contract in place between the general contractor and the subcontractor which requires the general contractor to be included on the subcontractor's insurance policy as an additional insured regardless of fault. Now envision there is a loss in which the general contractor was 100% at fault. If the correct edition is not used, the subcontractor's general liability policy may not provide coverage as required.

Scenario 1

The subcontractor includes the general contractor as an additional insured on their general liability policy via ISO endorsements CG2010 and CG2037 10/01.

In this scenario, the subcontractor's general liability policy will pay the entire loss since the 10/01 endorsement editions do not require there to be fault.

Scenario 2

The subcontractor includes the general contractor as an additional insured on their general liability policy via ISO endorsements CG2010 and CG2037 07/04.

In this scenario, the subcontractor would have to pay the loss out of pocket depending on the language found in the contract. The 07/04 endorsement edition dates would not provide coverage under the general liability policy for the subcontractor because they were not at fault or partially at fault.

A solution to this change in wording is to confirm the insurance requirements found within the contract language match the insurance coverage that will be provided by the additional insured endorsement requested. Also, the contract language and additional insured endorsements must stay consistent to confirm appropriate risk transfer continues downstream. Unfortunately, this is not always that simple because the older editions of the CG2010 and G2037 are getting harder to obtain.



Additional stipulations included on the CG2010 04/13 and CG2037 04/13

ISO included additional wording limitations from the CG2010 and CG2037 07/04 to the 04/13 editions as noted previously. This additional language proves to be detrimental to both named insureds and additional insureds as it could potentially cause a gap in coverage for both parties.

EXAMPLE 2

Imagine a contract between a general contractor and a subcontractor that requires general liability coverage with a \$500K per occurrence/general aggregate limit. In addition, this contract requires the subcontractor to include the general contractor as an additional insured (no specific edition date required). Now imagine a \$1M loss occurs where both the general contractor and subcontractor are at fault. Depending on which additional insured endorsement is used, the outcome at the time of a loss can be substantial. For purposes of this example, the subcontractor has general liability limits of \$1M per occurrence / \$2M general aggregate.

Scenario 1

The subcontractor includes the general contractor as an additional insured on their general liability policy via ISO endorsements CG2010 and CG2037 07/04.

In this scenario, the subcontractor's general liability policy will pay the entire loss first as the risk was properly transferred to the subcontractor.

Scenario 2

The subcontractor includes the general contractor as an additional insured on their general liability policy via ISO endorsements CG2010 and CG2037 04/13.

In this scenario, the subcontractor's general liability policy will only pay for the first \$500K of the loss only because the 04/13 editions provide coverage up to the limit required by the contract. The remaining \$500K of the loss would not be covered by the subcontractor's general liability policy and would ultimately go back to how the contract is worded. In a case like this, either the subcontractor would have to pay the \$500K out of pocket or the general contractor's general liability insurance would pay the remainder of the loss. Additionally, the subcontractor's umbrella liability policy will not respond as the underlying general liability limit was not exhausted.

A solution to this potential gap in coverage is to make sure the contract does not include language that limits the coverage to what is required by the contract, but rather, the contract should include language which requires the additional insured to maintain coverage up to what is required in the contract or up to the limits included on the additional insureds policies, whichever is higher.

How can Lockton help?

Vetting insurance carriers and confirming what additional insured endorsements can be offered will help companies ensure they have proper coverage. The best way to avoid the issues regarding the various additional insured endorsements is to have an insurance professional with construction expertise review the contracts prior to the contractor signing them. Lockton's associates are trained in contract review and can be an advocate for making sure the insurance policies are providing the coverage that is being required in the contract.

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