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INSURANCE LAW

Additional Insured Coverage: Be Sure to Look Under the Hood

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Special to the Legal

Additional insured coverage is an important but often overlooked protection. Even where a party has heavily negotiated its indemnity rights, in the event of a significant loss, status as an additional insured can be critical.

By naming the primary policyholder's contractual counterparty as an additional insured, an insurance company purports to extend coverage to that counterparty as well as to the primary policyholder, i.e., the "named insured." Additional insured issues arise frequently in the construction industry, but also come up in manufacturing, information technology, energy and any other industry where vendors or subcontractors provide services pursuant to contract.

Where there has been substantial property damage, economic harm or bodily injury, plaintiffs



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often seek "deep pockets" to name as defendants, even where the culpability may be minimal (or non-existent). Regardless of the suit's merits or ultimate outcome, all defendants are likely to incur significant defense costs. Access to additional insured coverage for this type of expense is a vital but often overlooked component of any well-drafted service contract—and ensuring access goes well beyond simply requiring a counterparty to provide the coverage.

“ *Intelligent risk management demands thoughtful consideration of the intersection between indemnity rights and rights as an additional insured.*

CONTRACTUAL INDEMNITY: NOT A SUBSTITUTE FOR ADDITIONAL INSURED STATUS

Indemnification provisions—whereby at least one of the parties requires that the other party indemnify it for third-party claims arising from the project at issue—are present in most contracts for services. Wise counsel knows that securing the best possible indemnity language in their contracts is important; however, the corresponding additional insured provision does not always get the same level of attention. The “form” additional insured endorsements used by most

general liability insurance companies have narrowed the coverage available to additional insureds over time, making close scrutiny of a contract's insurance requirements vital.

Even with broad and unambiguous indemnity rights, the ability to access additional insured coverage can still be the difference between being made whole or being stuck with a loss. For example, where the indemnifying party (the indemnitor) is a small business, it may not have sufficient assets to satisfy its indemnity obligation in the event of a major loss, leaving the indemnified client (the indemnitee) with no recourse at all—unless it is also named as an additional insured, which would allow it to seek coverage from the indemnitor's insurance company. Additionally, many states have anti-indemnity statutes that limit the scope of indemnity one party may provide to another in certain situations, but the same limitations do not automatically apply to the corresponding additional insured coverage. Finally, the contract may limit the value of the indemnitor's obligation—often to the value of the contract—forcing the indemnitee to turn to its additional insured coverage when legal fees or a judgment exceed that limit.

For these and other reasons, negotiating a clear additional insured provision is key to shifting

the risk of loss in a services contract. Fortunately, there is ample room for negotiation over the terms of additional insured coverage.

CONSIDERATIONS IN NEGOTIATING ADDITIONAL INSURED PROVISIONS

When a deal is on the verge of closing, parties may be inclined to treat insurance as an afterthought, especially if one of the parties proposes seemingly “standard” language. However, insurance terms can vary greatly, leaving many opportunities to strengthen your potential coverage or, at a minimum, create bargaining leverage for other parts of the contract. Here are a few goals to keep in mind:

- **Maximize limits:** Maximizing limits seems obvious; however the devil is in the details, as policies often contain sub-limits for certain types of losses. Moreover, as an indemnitee, do not simply assume that the vendor's proposed limits are adequate—the lower the limits you agree to, the cheaper the policy is for your indemnitor. Think about the value of the particular contract—what is the anticipated exposure in the event of a loss? If the limits are not at least that high, consider negotiating the insurance terms.

- **Minimize deductibles:** In lower dollar value cases, an unnecessarily high deductible can render your additional insured coverage meaningless. For example, assume you are added as a throwaway

defendant and you are able to get yourself dismissed from the case for \$75,000 in attorneys fees. A \$100,000 deductible leaves you with nothing, while a \$25,000 deductible leaves you reimbursed for a substantial amount of your expense.

- **Require Completed Ops coverage:** Products Completed Operations Hazard coverage (completed ops) covers losses that occur after your work on a contract is complete. Most general liability policies include completed ops coverage for the named insured, but additional insured endorsements may exclude it. Ensure that your indemnitor has completed ops for a reasonable number of years after project completion.

- **Specify insurance provider requirements:** Smaller vendors may be inclined to purchase insurance from smaller insurance companies offering cheaper policies with more trap doors for policyholders, especially additional insureds. Indemnitees can require that the policies providing their additional insured coverage be issued by an insurance company meeting certain financial criteria.

LIMITS ARE NOT EVERYTHING

High limits, low deductibles, extended policy periods are all important factors. But at the end of the day, additional insured status is only as valuable as the actual coverage the policy provides.

Even if the indemnitor promises to name you as an additional insured under specified terms, the insurance company is only bound by the policy itself. There are many different types of additional insured policy language, and even the standard form endorsements drafted by insurance industry trade groups change frequently, often to the detriment of putative additional insureds.

For one example, look out for language that requires a direct contractual agreement between the named insured and the putative additional insured. While most often there is such a relationship, sometimes it is the bank financing a project, rather than the owner itself, that promises to provide additional insured coverage. Also beware of language limiting additional insured coverage to instances where the underlying loss is exclusively caused by the named insured's negligence. If possible, secure policy language that will provide additional insured coverage even if you may be partially at fault for the underlying incident—even if it means using something other than the most recent standard form endorsement. Savvy indemnitees can go as far as specifying the exact form number that must be used for the additional insured coverage.

As a general matter, do not be afraid to involve yourself as much as possible in the process of procuring

the additional insured coverage you may have to rely on at some point.

DOCUMENTATION: IT MIGHT SEEM LIKE HOUSEKEEPING, BUT IT CAN MAKE ALL THE DIFFERENCE

Given that an insurance company is only bound to provide additional insured coverage under the actual terms of its policy, indemnitees must ensure that their indemnitors purchase the coverage they say they will. Insurance companies will rarely provide the entire policy to a putative additional insured, but you should at least request a certificate of insurance confirming the policy numbers, the limits of liability, and your additional insured status. Be advised, however, that the terms of a certificate of insurance state that the certificate does not confer rights on any party—it is not the same as having the insurance policy. Also, ask that the insurance company, rather than the indemnitor's broker, issue your certificate of insurance. A certificate of insurance is not a guarantee of coverage no matter who issues it, but if it comes from the insurance company, it becomes harder to later deny your status.

If possible, obtain a copy of the policy's additional insured endorsement from your counterparty. That way you will know in advance when you will or will not have a plausible claim for additional insured coverage, which is especially helpful if your

services contract does not specify a policy form number. After all, you cannot evaluate the strength of your additional insured coverage, as discussed above, without having the actual policy language.

CONCLUSION

Intelligent risk management demands thoughtful consideration of the intersection between indemnity rights and rights as an additional insured. While a party may appear sufficiently protected on paper, having another source from which to seek recovery in the event the indemnitor becomes insolvent may prove vital. Therefore, be prepared to negotiate hard at the outset and act decisively when a claim arrives. ●