

Manager/Supervisor Risk Management

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A twice weekly e-mail training for YCPARMIA members

TOPIC: INSURANCE REQUIREMENTS

In a contract the Indemnity Clause serves to transfer risk; it is a relatively simple statement of intent and scope. The Insurance Clause serves to provide a partial guarantee that the contractor has the financial where-with-all to fulfill their contractual promise to defend and indemnify. While the indemnity and insurance clauses work together, they are independent obligations; each clause stands on its own. Most importantly, the promise to defend and indemnify continues independently of any insurance; the contractor remains personally responsible for fulfilling their promise to hold the entity harmless regardless of available coverage.

When you look at the risk elements of a contract you will often find that the indemnification clause is confined to a single paragraph, while the insurance clause contains multiple paragraphs. It helps to understand that indemnification involves two parties, the contractor and the entity, and a single promise to defend and indemnify. Insurance requirements add a third party, the insurance company, to the mix. The insurance clause lays out the requirements that the contractor must negotiate and purchase from their insurance carrier. Since the entity is not part of that process, these requirements have to be carefully spelled out using the terms and language of the insurance industry.

It is important to be sensitive to an underlying truth: contractors have their own pre-existing insurance programs that are hopefully designed to meet their business needs, and any requirements of their usual customers. It is doubtful that the contractor has the flexibility or resources to change or modify their insurance program every time they enter into a contract. Fortunately the insurance requirements of YCPARMIA members are consistent with the vast majority of other California public entities. If the contractor commonly does work for public entities in this state, it should be relatively easy for them to meet the requirements without significantly modifying their preexisting insurance coverages.

As a practical matter, contract risk transfer problems shared by our members usually involve insurance issues rather than indemnification issues. In the bid process the contractor takes on the obligation to fulfill the insurance requirements as laid out in the contract specifications. After agreeing to those terms a contractor will occasionally seek to modify the insurance requirements. This issue goes straight to the entity's risk tolerance. Is the entity willing to lower or modify the agreed insurance requirements and take on more risk? Additionally, if the entity subsequently agrees to the modification are they giving the contractor an unfair advantage over other bidders who may have factored the cost of the required insurance into their price bid?

A possible answer to these questions might turn on whether the requested modifications are material, or merely incidental. To make that determination it is necessary to understand what the various insurance elements entail.

Next topic: Insurance Limit Complaints