



Advocates for Policyholders in Insurance Coverage Disputes

CONSTRUCTION WRAP UP POLICIES

Wrap Up Insurance Programs: An Innovative Approach

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I. INTRODUCTION

All business organizations are insured, and most companies typically carry commercial general liability (“CGL”) insurance and workers’ compensation/employer liability insurance, in addition to other specific policies for the individual business. In the context of a construction project that involves an owner, general contractor and multiple subcontractors, each party typically carries its own CGL and workers’ compensation policies which cover liabilities for the project as well as the insureds’ other liabilities. This is a traditional insurance program.

On large construction projects, it can be advantageous for the parties to participate in a consolidated insurance program (“CIP”), which is also referred to as a Wrap-Up.¹ A CIP or Wrap-Up insures interests of diverse entities brought together for a single project or purpose. A CIP enables the program Sponsor, usually the project owner or general contractor, to control elements of project risk and ensure that the benefits of a CIP are maximized. The typical participants in a CIP are the property owner/developer, construction manager, general contractor and subcontractors. Wrap-Ups can also include architects and engineers, especially where the project is structured as “design build.”²

The CIP concept has applications to various sectors of the construction industry. While incentives for each type of program differ, the end result is an insurance program which improves the quality and value of insurance as it applies to operational risks.

CIPs are often referred to as either an OCIP (owner controlled) or a CCIP (contractor controlled). Construction Wrap-Ups can be used for projects as diverse as civic or convention centers, state or district work such as highways and bridges, pipelines and electrical transmission lines, high rise buildings or office complexes, airports or residential developments. For purposes of this presentation, the focus is on the commercial development and building sector of construction.

II. CONSTRUCTION WRAP-UPS

A CIP is most effective for a large construction project. In this case, the program Sponsor would negotiate the appropriate price and terms of the various insurance policies for the specific project and the coverage would apply to almost all of the contractors who work on the project. The common types of coverage included in a construction Wrap-Up program are general liability and workers’ compensation/employer’s liability. Wrap-Ups sometimes may include coverage for builder’s risk and errors and omissions for architects, engineers and construction managers.

¹ Other varieties of CIPs in the construction industry include:

Rolling Wrap-Ups

Consolidated Insurance Program for Operations (CIPO, also abbreviated as ROCIP) is an ongoing Wrap-Up for contract work that is being done on operating facilities. The common insurance program remains in place indefinitely and contracted work is added as it occurs. CIPOs are also known as “rolling Wrap-Ups,” “perpetual Wrap-Ups,” or “gate Wrap-Ups.”

Dirty Wrap-Ups

Environmental Consolidated Insurance Program (ECIP), sometimes referred to as a “Dirty Wrap-Up,” is a Wrap-Up for environmental remediation projects. An ECIP can be written on a project basis or on a rolling basis, and may be contractor controlled (ECCIP), but is more commonly owner controlled (EOCIP).

International Wrap-Ups

International CIP or CIPO (ICIP/ICIPO) is any form of Wrap-Up in conjunction with projects or operations outside of the United States. Unlike domestic Wrap-Ups, they usually do not include coverage for worker injuries because of the unique laws applicable in different jurisdictions. However, auto and marine insurance are more usually included.

² “Design build” is a term used in the construction industry whereby the elements of the entire project, from design plans to final construction, are administered by one entity.

The benefits of a CIP, discussed in detail below, are best illustrated by an example which shows how various losses are handled under a CIP versus a traditional insurance program.

FACTUAL SCENARIO

Owner (“O”) hires general contractor (“GC”) to build a residential condominium complex consisting of 8 buildings with 48 units on an undeveloped piece of real estate. GC hires numerous subcontractors (“Subs”) to complete the work.

During the course of construction a Sub’s employee is negligently injured on the job.

Thereafter, the building is completed and GC turns the project over to O, who sells the units to residents.

One year later, property damage is discovered, there is mold and moisture build-up in the walls of several units, windows leak and the roof, which also leaks, has started to warp. The Condominium Association (“Association”) and the unit owners (“Residents”) allege that the property damage is the result of faulty HVAC installation and operation, improper window installation, and failure of the GC to properly dry out the building before enclosure.

The manner of resolution of these disputes is significantly different under a traditional insurance program versus a Wrap Up program.

Example 1: Traditional Insurance Program

O maintains a CGL Policy. GC, pursuant to its contract with O, is also required to maintain its own CGL Policy that names O as an additional insured (via endorsement) and includes completed operations coverage. The additional insured requirement in the O/GC contract reads:

Contractor, the Owner and other entities as may be reasonably requested shall be named as an additional insured under these policies of insurance. It is expressly agreed and understood by and between Subcontractor and Contractor that the insurance afforded the additional insureds shall be primary insurance and that any other insurance carried by Contractor shall be excess of all other insurance carried by the Subcontractor and shall not contribute with the Subcontractor’s insurance. Subcontractor further agrees to provide endorsements on its insurance policies which shall state the foregoing.

The additional insured endorsement to the GC’s policy reads:

Name of Person or Organization:
Owner

WHO IS AN INSURED (Section II) is amended to include as an insured the person or organization shown in the Schedule, but only with respect to liability arising out of “your work” for that insured by or for you.³

³ Additional insured endorsements are also written in a “blanket” format indicating that any person or organization shall be an additional insured if the named insured has agreed to do so in writing.

The O/GC contract contains an indemnity clause which reads:

The subcontractor hereby assumes entire responsibility and liability for any and all damage or injury of any kind or nature whatever (including death resulting therefrom) to all persons whether employees of any tier of the subcontractor or otherwise and to all properties caused by, resulting by, arising out of, or occurring in connection with the execution of the work or in any preparation for the work or any extension, modification or amendment to the work by change order or otherwise.... the subcontractor agrees to indemnify and save harmless the contractor and the owner, their officers, agents, servants and employees from and against any and all such claims and further from and against any and all loss, costs, expense, liability, damage, penalties, fines, or injury including legal fees and disbursements that the general contractor and the owner, their officers, agents, servants, or employees may directly or indirectly sustain, suffer, or incur as a result thereof and the subcontractor agrees to and does hereby assume on behalf of the owner and the general contractor, their officers, agents, servants and employees the defense of any action at law or in equity which may be brought against the general contractor and/or the owner, their officers, agents, servants or employees upon or by reason of such claims and to pay on behalf the general contractor and the owner, their officers, agents, servants, and employees upon demand the amount of any judgment that may be entered against the general contractor and/or the owner, their officers, agents, servants or employees in any such action.

Subs, pursuant to their contracts, are required to carry the same insurance coverage as GC, naming GC and O as additional insureds, and carry completed operations coverage. The Subs' contracts also contain the same additional insured requirement, additional insured endorsement and indemnity clause identified above.

As a result of the above bodily injury and property damage claims, when a traditional insurance program is in place, there are several levels of litigation that usually result.

a. Bodily injury

i. Employee vs. Subcontractor

Injured employee files a claim for workers' compensation benefits with his employer. Employee cannot sue the Sub who is his employer for negligence because his exclusive remedy is workers' compensation.

ii. Employee vs. O, GC and Subs ("Initial Action")

Employee will generally file a suit against O and GC for negligence. The employee may also sue one or two other Subs who could also be liable for his injuries. This often results in cross-claims being filed between the defendants.

iii. Contractual Indemnity; GC vs Sub

When the GC is sued in the Initial Action, the GC is entitled to indemnity from the Sub for costs incurred in defending the Initial Action and for any judgment or settlement paid in the Initial Action, pursuant to the GC/Sub contract. In many instances, GC is forced to sue Sub. GC can file a separate action against Sub, but a third-party action is more common.

iv. Contractual Indemnity; O vs. GC

When the Initial Action is filed, GC is obligated to indemnify O for defense costs that O incurs, pursuant to the contractual indemnity provision in their contract. O may have to file suit against GC for indemnity.

v. Insurance Claims; GC vs. GC Insurer; Sub vs. Sub Insurer

Litigation scenarios (iii) and (iv) can result in coverage litigation between GC and its insurer and/or between Subs and their insurers regarding coverage for contractual indemnity.

In scenarios (iii) and (iv) above, the defense costs and damages incurred by O should be paid by GC. Similarly, the defense costs and judgment or settlement values incurred by GC should be paid by Subs. These payments by GC and Sub become their respective indemnity claims with their insurers, pursuant to the insured contract coverage typically in place in a CGL policy.

vi. Additional Insured Litigation (O vs. GC; GC vs. Subs)

O is an additional insured (“AI”) on GC’s and Subs’ insurance policies. O and GC are AIs on each Sub’s policy. Therefore, GC’s insurance carrier must defend O, and each Sub must defend GC and O in the Initial Action.

Although less frequent in the bodily injury scenario, litigation with the insurers may result because the insurers often dispute that O’s and GC’s liability arises out of the insurer’s Sub’s work.

b. Post Construction Property Damage

The levels and amount of litigation in a construction defect property damage claim tend to be more complicated. They can be broken down as follows:

i. Association and Residents vs. O and GC

Association and Residents file suit for defects. O and GC defend the suit and pay out any damages.

ii. GC vs Subs (liability)

As a result of the suit filed by the Association and Residents, GC typically adds all potentially liable Subs via third-party actions. The third-party claims inevitably result in cross-claims among the third-party defendants (Subs) and counterclaims against the GC where the GC performed a portion of the work.⁴

iii. Contractual Indemnity; GC vs. Subs

Each Sub, pursuant to its contract, is obligated to indemnify GC for its defense costs in the litigation filed by the Association and Residents. GC may end up filing suit against Subs for indemnity.

⁴ Many larger GCs do not self-perform any work on a project, which may eliminate counterclaims.

The Subs now have indemnity claims against their insurance carriers.

iv. Contractual Indemnity; O vs. GC

GC is obligated to indemnify O for defense of O, pursuant to the contractual indemnity provision in their contract. O has a claim against GC for this indemnity. This can be the subject of a separate lawsuit or can be filed as a cross-claim in the initial lawsuit filed by the Association and the Residents, if GC does not willingly comply with its contract.

v. GC vs. GC's Insurer

GC now has a claim against its insurer for indemnity based on the defense costs it paid on behalf of O.

vi. Additional Insured Litigation (O vs. GC; GC vs. Subs)

O is an AI on GC's and Subs' insurance policies. GC is named as an AI on each Sub's policy. Pursuant to the AI endorsements, GC's insurer must defend and indemnify O, and each Sub's insurer must defend and indemnify GC and O in the Initial Action.

The additional insured issues often results in litigation between the various parties, because more often than not, the Subs' insurance carriers deny coverage based on the additional insured endorsements. The issues that often arise in this context include:

- a. inability to identify carriers for competed operations claims;
- b. denials of coverage;
- c. O and/or GC not named as AI, which is a breach of contract by the Sub, requiring expanded litigation;
- d. The Sub's policy is excess for AIs, based on the policy language or the endorsement.

The proper end result of the property damage claim should be that the Subs' liability insurers pay proportionately for the defense and indemnity of Sub, GC and O in the Initial Action. Reaching this point, however, often requires significant litigation amongst the parties at great expense. It is worth mentioning that the attorneys' fees incurred in seeking *coverage* for these underlying lawsuits are not insured and O, GC and each Sub has to pay these costs out of their own pocket.⁵

Example 2: Wrap Up Program

When a Wrap-Up insurance program is in place, the Sponsor (O or GC) arranges for all of the necessary insurance coverage for the Project. This always includes CGL and workers' compensation coverage, and depending on the Project, other coverages would be included. There is only one insurer for the Wrap-Up and O, GC and each Sub are named as insureds. Administration and claims handling is all under the control of the Sponsor.

The significant benefit that results from a Wrap-Up when there is bodily injury or property damage is the instant elimination of most of the litigation identified above. The bodily injury and property damage claims are itemized below.

⁵ Some States, by Statute or common law, allow for the recovery of attorneys fees incurred for the successful prosecution of coverage litigation.

a. Bodily injury

i. Employee vs. Subcontractor

Injured employee files a claim for workers' compensation benefits with his employer.

ii. Employee vs. O, GC and Subs

Employee will generally file a suit against O, GC, and perhaps one or two Subs for negligence.

b. Post Construction Property Damage

i. Association and Residents vs. O and GC

Association and Residents file suit against O and GC for the defects.

In a Wrap-Up, the suits filed by the employee, the Association and the Residents result in two claims being filed with one insurance carrier. There are no contractual indemnity claims or AI claims, multiple insurance carriers do not have to get involved and the level of litigation and costs to each party are significantly reduced. Cross-claims and counterclaims are not necessary, and allocation of liability is not relevant because a single insurer covers all contractors on the project. Comparing the charts on pages 7 and 10 with the charts on pages 12 and 13 illustrates the differences between litigation with a traditional insurance program versus a Wrap-Up.

The Wrap-Up manual, which is generally incorporated into the various contracts for the Project, often contains a waiver of subrogation clause.⁶ This language typically reads:

Waiver of Subrogation. Where permitted by law, Subcontractor hereby waives all rights of recovery by subrogation because of deductible clauses, inadequacy of limits of any insurance policy, limitations or exclusions of coverage, or any other reason against Owner, Contractor, the Indemnified Parties, the CIP Administrator, its or their officers, agents, or employees, and any other contractor or sub-subcontractor performing Work or rendering services on behalf of Contractor or Owner in connection with the planning, development and construction of the Project. Where permitted by law, Subcontractor shall also require that all Subcontractor's maintained insurance coverage related to the Work include clauses providing that each insurer shall waive all of its rights of recovery by subrogation against Subcontractor together with the same parties referenced immediately above in this Section. Subcontractor shall require similar written express waivers and insurance clauses from each of its sub-subcontractors. A waiver of subrogation shall be effective as to any individual or entity even if such individual or entity (a) would otherwise have a duty of indemnification, contractual or otherwise, (b) did not pay the insurance premium directly or indirectly, and (c) whether or not such individual or entity has an insurable interest in the property damaged.

⁶ The waiver of subrogation clause reinforces that an insurer cannot sue its own insured for losses that it pays. In a Wrap-Up, because there is one insurer for all participants, the insurer would be prevented from suing an insured after paying out on behalf of a different insured.

While a Wrap-Up may seem advantageous based on this example, other factors must be considered before determining which insurance program to choose.

III. WHEN IS A WRAP-UP RIGHT FOR YOU?

The Sponsor has to determine whether a Wrap-Up would provide the economic savings as compared to the traditional insurance program, and whether the Sponsor wants to have more control over the insurance that is secured for the project. Even if the potential savings of the Wrap-Up program are not substantial, a Wrap-Up may be beneficial simply because it allows the Sponsor to ensure that necessary coverage limits are in place and provides the Sponsor with control of the claims and reporting process.

Some commentators suggest that Wrap-Ups provide the most financial benefit on a project of at least \$100 million, or on a project that would generate at least \$1 million in workers' compensation premiums. Every owner or contractor will have a different value for the overall cost of a project that they would consider sufficient before concluding that a Wrap-Up should be utilized.

In addition, Wrap-Up insurance programs are regulated differently in every state. Therefore, the program Sponsor has to ensure that the Wrap-Up is permissible in the state where they are seeking coverage. Some states prohibit the use of Wrap-Ups all together, while other states restrict their use under "fictitious grouping" laws, direct limitations on persons or entities that qualify to employ Wrap-Ups or monopolistic worker compensation insurance systems. Other states allow Wrap-Ups only for certain types of entities such as government entities.

1. Benefits of Construction Wrap-Ups

The greatest benefit of a Wrap-Up is the cost savings, due to reduction of administrative costs, procurement costs, loss control costs and related expenses. Other benefits of a Wrap-Up are:

Benefit	How
Reduced Litigation	Mitigate opportunity and need for cross-litigation.
Compliance with Regulatory Standards	Enforce high standards for loss control, safety and health requirements.
Control of Insurance Coverage and Claims Handling	Sponsor can control coverage terms, choice of insurers and defense of claims, which can mitigate many potential problems.
Improved Productivity	Safer conditions can produce better overall morale and higher productivity.
Cost Control	CIPs can prevent and mitigate injuries and damages.
Ability to Employ Small Contractors	Bid opportunities can be made available to a broader range of service providers.

2. Limitations on the use of Wrap-Ups

Although the Wrap-Up has many benefits, it is not for every project. An owner or general contractor should not automatically engage a CIP program without considering the benefits as well as the limitations. This needs to be done on a project by project basis. It may be that a Wrap-Up is not the best insurance program for a particular project.

If the CIP's potential Sponsor is not well-versed in CIPs, it is generally good advice to hire a broker or consultant. Since the decision should not be taken lightly, a CIP feasibility analysis should be conducted prior to choosing service providers. The following are some limitations when deciding on whether to use a Wrap-Up policy.

Limitation	Why
Project Size	Volume of contracted work must meet the needs of the program Sponsor.
Control of the Work	Capability to overcome the geographic, legal, regulatory, cultural or contractual limitations on the Sponsor's loss control measures.
Legal Jurisdiction	Wrap-Ups must be legally permissible in the state where the work is being performed.
Ability and Inclination to Administer Wrap-Up Features	The Sponsor must be able and willing to rigorously enforce safety and loss control measures and to obtain appropriate insurance for all participants.

IV. INSURANCE PROGRAM DESIGN

Formal details of a Wrap-Up program should be developed and an insurer to underwrite the program should be chosen before the procedure manuals can be written. A CIP can be written on a manuscript form when risks are suitably unique. In addition, a CIP simplifies the Sponsor's administrative duties, such as verifying contractors' compliance with insurance requirements and dealing with brokers and insurers. Even if certificates of insurance are needed for non-CIP coverages, the task of confirming compliance is much simpler. Having one policy and one insurer in a CIP allows for fewer coverage disputes and faster, less complicated claims handling, where the task of identifying and corresponding with multiple brokers and insurers is made considerably simpler. This is illustrated in the property damage example discussed above.

V. WHAT IS THE RIGHT COVERAGE FOR THE PROJECT?

The specifics of the particular project will dictate the types of coverage that should be included in a Wrap-Up program. The sponsor should analyze every aspect of work to be performed in order to provide a comprehensive program that would protect all participants. Some of the more common coverages are identified on the next page.

Coverage	Purpose
Contractual Liability	Coverage should be “joint and several,” since Wrap-Up participants under one policy are still considered separate legal entities with the ability to bring suit against one another.
Damage to the Work	Coverage provides protection regarding liability for damage to the work.
Completed Operations	This coverage is a major concern for contractors in that a contractor’s CGL policy is typically endorsed to remove completed operations coverage for the Wrap-Up project.
XCU Coverage	Covers explosion (property damage resulting from blasting operations or other explosions; collapse (structural property damage resulting from excavation and other demolition work); and underground property (damage to wires, pipes, tunnels and sewers, resulting from mechanical digging, pile driving, excavating or similar work by heavy equipment).
Personal Injury Liability	Coverage includes protection for claims against a person other than for actual physical injury, such as libel, slander, false arrest, detention or imprisonment and invasion of privacy.
Employee as Insured	Covers employees as insureds and permits suits by one employee against another.
Workers’ Compensation Coverage	Part A covers the employer’s statutory liability under the laws of the states listed in Item 3.A. of the policy information page. Part B provides employers liability coverage for an employer’s non-statutory liabilities resulting from its status as an employer.
Excess/Umbrella Policies	Major construction projects should ideally include excess or umbrella policies.
Builder’s Risk Coverage	Should include an all-risk builder’s risk policy for all parties to the project.