Manager/Supervisor Risk Management
#100– 10/23/12
A twice weekly e-mail training for YCPARMIA members

TOPIC: INSURANCE LIMITS – AGGREGATES CAN BE BAD

A liability insurance limit establishes the maximum amount of money that the insurance company will pay for each and every occurrence. An aggregate limit establishes the maximum amount of money that the insurance company will pay under the policy cumulatively for all occurrences or claims.

In practice an entity requires that the contractor have a minimum insurance limit – commonly $1M per occurrence. The contractor will provide proof of coverage that they have a policy with the required $1M limit, but subject to a $2M aggregate limit. They appear to be in compliance with the contract requirements, but what happens if they have had other claims made against that policy. If the policy has already paid out $1.5M there is only $500K left under the aggregate limit, so in effect the entity is only getting half the level of protection that they required in the contract.

Aggregate limits cap the insurance carrier's exposure for the policy, and as a result lower the premium that the contractor pays for the coverage – the contractor is spending less because they are getting less protection. At the same time, when the entity accepts a policy from their contractor with an aggregate, they usually do not know how much protection they are really getting – it might be everything that they require, or it might be nothing.

Remembering that while the contractor probably has a pre-existing insurance program that discourages flexibility or modification the entity does have options. Depending on their bargaining position, they can require that there be no aggregate, a higher aggregate, or that the aggregate not apply to their project. They can require that the contractor provide a list of all claims made against the policy including payments and reserves so that the adequacy of the protection can be assessed. They can ask for a history of claims made against prior policy terms to see if the aggregate limit appears reasonable. Of course all of these options require negotiation and can slow down the contracting process.

What happens in real life? Hopefully someone does a risk assessment to see if the aggregate for this particular contractor fits with the entity's risk tolerance. More likely, the person reviewing the insurance for the entity sees that the required limit per occurrence is there, and ignores the aggregate and its potential dangers – a simple and painless approach unless something goes wrong.

Next topic: Insurance Limits – deductibles, retentions and self-insurance