

## Manager/Supervisor Risk Management

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A twice weekly e-mail training for YCPARMIA members

### TOPIC: INSURANCE LIMIT COMPLAINTS

A public entity contract generally requires that the contractor purchase certain types and amounts of insurance to guarantee that they have the financial ability to fulfill their contractual duty to defend and indemnify. Probably the most common risk transfer complaint that we hear is that a member entity is requiring insurance limits that are perceived as too high. Insurance premiums are a significant business expense, and the higher the limit, the higher the premium cost (though the cost per dollar of protection is proportionately cheaper as the limits go up). A business often looks at their risk tolerance for that allusive balance between maximizing protection while controlling cost.

One of the issues that might be missing from the contractor's risk assessment is the hold harmless promise that they made in their contracts. The promise to defend and indemnify the entity is basically unqualified and unlimited. It is a "whatever-it-takes" contractual duty. If the insurance coverage is inadequate, the business, and possibly personal assets of the owner, will be called on to respond to the indemnification promise. To beat a dead horse, the Indemnification Clause and the Insurance Clause are totally independent of each other and stand on their own. The duty to defend and indemnify continues regardless of insurance.

It is therefore a bit incongruous to hear a contractor, who has made an unlimited contractual commitment of his business assets (and possibly personal assets) to defend and indemnify, try to limit their ability to respond. The realization of the consequences of their risk decisions often emerges when we tender a claim or suit. The tender demand is made to both the insurance company, and the insured contractor. The contractor is told that if the limits prove inadequate, YCPARMIA will be looking to them to make up the difference per their contractual promise regardless of the effect on their business.

It should also be understood that the entity's choice of required limit amounts should not be relied on by the contractor as an indication of adequacy. The insurance requirements are usually stated in minimum terms rather than an exact amount. For example the insurance clause would state "with limits of not less than \$2 million" as opposed to "with limits of \$2 million." The only thing that the entity's insurance requirement does is to establish a floor of minimum coverage limits.

In conclusion, the minimum limits found in the entity's insurance requirements not only protect the entity, but sometimes protect the contractor from making short sighted financial decisions on risk. The desire by some entity employees to lower the requirements in an effort to "help" a contractor can lead to disaster if the indemnification provisions are triggered without adequate financial protection. Fortunately most contractors that regularly work with public entities have insurance programs in place that are structured to satisfy the risk requirements found in our member's standard contracts.

Next topic: Insurance Limits - How much?