Insurance-Indemnity – What’s The Difference?

Two of the primary mechanisms for construction risk transfer are indemnity provisions and insurance agreements. Both indemnity provisions and insurance agreements require one party to stand good for the loss of another. But there are significant differences, both practical and legal. In the following article we’ll discuss the different types of indemnity, anti-indemnity statutes, insurance coverage for liability coverage, and additional insured endorsements.

What is Indemnity?

Indemnity provisions, also known as hold harmless agreements, are the most prevalent means of risk transfer in the construction industry and are found in just about every construction agreement. Indemnity provisions involve a promise by one party to protect another party from claims for damages by a third-party. The intent of an indemnity provision is to transfer the risk of third-party claims to the party best-suited to bear the risk.

In a construction setting, indemnity demands most often result from an injury on the construction site that results in a third-party claim. For example, owners have certain non-delegable duties to ensure that their property is safe. Therefore, if a person is injured on a construction site, the owner is often named as defendant in any litigation. An indemnity agreement operates to transfer the liability of the owner, the indemnitee, to the contractor, the indemnitor. As the contractor is in possession and control of the construction site, the contractor is in the best position to manage risk of injury on the site and, therefore, is the party best-suited to bear the risk.

What Are Anti-Indemnity Statutes?

The vast majority of states have enacted anti-indemnity statutes that limit the permissible breadth and scope of indemnity provisions. If an indemnity clause is too broad, it may be declared void and unenforceable under a state’s anti-indemnity law. When drafting an indemnity provision, a party must first know the permissible level of indemnity in the subject state. To assist in that regard, there are three classifications of indemnity provisions—broad form, intermediate form, and limited form. Each classification, or type of indemnity, shifts a different level of liability to the indemnitor.

Broad Form Indemnity

Under a broad form indemnity provision, the indemnitor assumes an unqualified obligation to hold harmless the indemnitee for all liability arising out of the contract, regardless of which party was actually at fault. Even if the indemnitee is solely at fault for the loss, the indemnitor has an obligation to indemnify. A broad form indemnity provision shifts the entire risk of loss arising out of the contract to the indemnitor.

By way of example, assume a pedestrian walking by the construction site slips and falls, resulting in $100,000 in damages. Assume further that the owner, the indemnitee, was solely at fault for the loss. Under a broad form indemnity agreement, the contractor, the indemnitor, would be required to indemnify the owner for 100 percent of the...
damages, or $100,000.

A broad form indemnity agreement may be drafted in many ways. However, there is certain clear and concise language that indicates a broad form provision. The following language provides broad indemnity:

To the fullest extent permitted by law, the Contractor [Indemnitor] shall indemnify and hold harmless the Owner [Indemnitee] … from and against all claims, damages, losses and expenses, including attorney’s fees, arising out of or resulting from the performance of the work, whether or not such claim, damage, loss or expense is caused in whole or in part by the Owner [Indemnitee].

The language that indicates a broad form indemnity provision is in use is the phrase “caused in whole” "by the Owner [Indemnitee].” Essentially, the Contractor has agreed to indemnify the Owner for the entire loss even if caused “in whole” (100 percent) by the Owner. (The language “caused ... in part” indicates intermediate form indemnity and addresses the situation where both the parties contribute to the loss. See discussion below.)

Presently, broad form indemnity is permitted in only eight states. That said, many of these states have certain requirements that must be met in order to enforce the provision. For example, Florida permits broad form indemnity. However, to be enforceable the contract must “contain a monetary limitation on the extent of the indemnification that bears a reasonable commercial relationship to the contract,” and the use of broad form indemnity must be “part of the project specifications or bid documents, if any.” Fla. Stat. Ann. § 725.06.

Intermediate Form Indemnity

Under an intermediate form indemnity provision, the indemnitor assumes an obligation to hold harmless the indemnitee for all liability arising out of the contract, so long as the indemnitor is partially at fault—even one percent at fault. Using the injured pedestrian example, assume that the owner was 99 percent at fault and the contractor was one percent at fault for the pedestrian’s damages. The percentage allocated to each party is irrelevant as long as the indemnitor has some level of fault. Under an intermediate form indemnity agreement, the contractor would be required to indemnify the owner for any liability allocated to the owner, 99 percent or $99,000, plus any liability allocated to the contractor, one percent or $1,000. So long as the contractor is even one percent at fault, the owner receives 100 percent indemnity.

An intermediate form indemnity provision may be drafted in many ways. However, there is certain clear and concise language that indicates an intermediate form provision. The following language provides intermediate indemnity:

To the fullest extent permitted by law, the Contractor [Indemnitor] shall indemnify and hold harmless the Owner [Indemnitee] … from and against all claims, damages, losses and expenses, including attorney’s fees, arising out of or resulting from the performance of the work, whether or not such claim, damage, loss or expense is caused in whole or in part by the Contractor [Indemnitor]
The language that indicates an intermediate form indemnity provision is in use is the phrase “caused … in part” “by the Contractor [Indemnitor].” Essentially, the Contractor has agreed to indemnify the Owner for the entire loss so long as the loss is caused “in part” by the Contractor.

Although not as common, an intermediate form indemnity provision may be tied to the Owner. For example, an intermediate form indemnity provision may read: “caused in whole or in part by the Owner.” The words “in whole” must be removed or the provision reverts to broad form. Presently, intermediate form indemnity provisions are permitted in over thirty states.

**Limited Form Indemnity**

Under a limited form indemnity provision, the indemnitor assumes an obligation to hold harmless the indemnitee only to the extent of indemnitor’s fault. Using the injured pedestrian example, assume that the owner was 70 percent at fault and the contractor was 30 percent at fault for the pedestrian’s damages. Under a limited form indemnity agreement, the contractor is required to indemnify the owner for the contractor’s percentage of fault, 30 percent or $30,000.

There is certain clear and concise language that indicates a limited form provision. The following language provides intermediate indemnity:

> To the fullest extent permitted by law, the Contractor [Indemnitor] shall indemnify and hold harmless the Owner [Indemnitee] … from and against all claims, damages, losses and expenses, including attorney’s fees, arising out of or resulting from the performance of the work, but only to the extent caused by the negligent acts or omissions of the Contractor [Indemnitor].

The language that indicates a limited form indemnity provision is in use is the phrase “but only to the extent caused by … the Contractor [Indemnitor].” Essentially, the Contractor has agreed to indemnify the Owner for that portion of any loss caused by Contractor. Limited form indemnity provisions are permitted in every state.

**Does General Liability Insurance Cover Indemnity Obligations?**

The Standard Insurance Services Office or ISO CGL policy provides coverage of the insureds indemnity obligation. The coverage is afforded through an exception to the “contractual liability” exclusion. Under the contractual liability exclusion, coverage is eliminated for “assumption of liability” in a contract or agreement. This exclusion is intended to eliminate coverage for the insured’s contractual obligations, including liability arising out of indemnity or hold harmless agreements.

Through the exceptions to the exclusion, the exclusion is not applicable to “insured contracts.” An insured contract is defined in the policy. The definition begins by listing five types of contracts:

- Lease of premises (but not for a promise to pay fire damage to a
premises you rent or occupy)
• Sidetrack agreement
• Easement or license agreement (not for construction or demolition
  on or within 50 feet of a railroad)
• Indemnify a municipality (except for work for the municipality)
• Elevator maintenance agreement

In addition to the above five enumerated contracts, a blanket clause
is included in the definition of “insured contracts,” which states as
follows:

That part of any other contract or agreement pertaining to
your business (including an indemnification or a municipality
in connection with work performed for a municipality) under
which you assume the tort liability of another party to pay for
“bodily injury” or “property damage” to a third person or
organization. Tort liability means a liability that would be
imposed by law in the absence of any contract or agreement.

The blanket contractual clause extends coverage to any contract
pertaining to the named insured’s business under which they
assume the tort liability of another, that is, an indemnity obligation.
But insurance companies may remove coverage for contractual
liability using the Contractual Liability Limitation Endorsement, Form
CG 21 39.

Additional Insured Endorsements

An individual or organization can be covered under another party’s
general liability policy as an additional insured by way of a policy
endorsement. Additional insured status gives the additional insured
direct access to the other party’s insurance—they are treated as an
insured under the policy. However, the coverage that is afforded to
the additional insured differs depending on which endorsement form
is used to add a party as an additional insured.

It is important to keep indemnity obligations and insurance coverage
separate. For example, an owner may require a contractor to provide
intermediate form indemnity. In general, the contractor has coverage
for this indemnity obligation. At the same time, an owner may further
require a contractor to add the owner as an additional insured to the
contractor’s CGL policy. As an additional insured under the
contractor’s CGL policy, the owner is insured for third-party claims.
This gives the owner two avenues to be made whole from a third-
party claim.

1. Require the contractor to provide full indemnity based on the
intermediate indemnity provision. The contractor has insurance
for this obligation through the exception to the contractual
liability exclusion. The contractor’s CGL carrier would indemnify
the contractor by making a payment on contractor’s behalf to the
owner.

2. As an additional insured, tender the third-party claim to the
contractor’s CGL carrier. As an additional insured, the
contractor’s carrier would indemnify the owner by making a
payment on the owner’s behalf to the third-party.

While the net result can be the same under either avenue of
recovery, the legal mechanics are completely different. It is possible
to have a situation where the net result under the two avenues of recovery is different. This usually occurs when a limited form indemnity provision is used, but the upstream party is added as an additional insured using an endorsement that provides full coverage to the additional insured. This situation is commonly referred to by insurance carriers as the “additional insured loophole.” Insurance carriers frown on such a situation and have pushed for statutes to address this discrepancy. Presently, six states prevent a party from seeking coverage as an additional insured greater than the amount the carrier would be obligated to pay for the insured’s indemnity obligation. For that reason, it is important to know the scope of coverage that is provided under each additional insured endorsement form.

The main additional insured forms offered by ISO, identified by year, are as follows: the ’85, ’01, ’04 and the ’13 forms. Below is summary of coverage, or lack of coverage provided under each form.

‘85 Form

When it comes to being named as an additional insured, the broadest coverage afforded is under ISO Form 20 10 11 85, or equivalent forms. Under the ’85 form the additional insured is provided coverage for liability arising out of the insured’s work and coverage for claims arising out of the additional insured’s work. Coverage is afforded during ongoing operation and in a completed operation setting.

Most states have interpreted the ’85 form as providing coverage as long as the additional insured’s negligent act had a close and direct connection with the operations of the named insured. The coverage afforded to the additional insured is essentially identical to the named insured. Some carriers will no longer underwrite an ’85 form. This is because the ’85 form arguably provides coverage for the additional insured’s own, or sole, negligence.

‘01 Forms

In 2001, ISO divided coverage for ongoing and completed operations into two separate forms, CG 20 10 10 01 and CG 20 37 10 01. Form CG 20 10 10 01 provides coverage during ongoing operations and form CG 20 37 10 01 provides coverage with respect to the completed operations. In order to achieve similar coverage to the ’85 form, which provided coverage for both ongoing operations and completed operations, both the CG 20 10 and CG 20 37 forms must be procured.

‘04 Forms

In 2004, ISO again divided coverage for ongoing and completed operations into two separate forms, CG 20 10 07 04 and CG 20 37 07 04. Form CG 20 10 07 04 provides additional insured coverage during ongoing operations and form CG 20 37 07 04 provides additional insured coverage with respect to the completed operations.

However, unlike the ’85 form or ’01 forms, the ’04 forms remove coverage for the additional insured’s sole negligence by replacing the language “arising out of” with “caused in whole or in part by your work.” As a result of this change, the ’04 form does not provide coverage if the additional insured is solely negligent.
Use of the '04 forms may increase the likelihood of coverage litigation. Third-party plaintiffs do not always identify the acts and omissions of every entity involved with a loss. If the plaintiff fails to name the downstream party in a suit and/or fails to allege acts or omissions by that party, the carrier may deny a defense and/or indemnification to the additional insured party because the loss was not alleged to be caused in whole or in part by the named insured.

'13 Forms

In 2013, ISO again divided coverage for ongoing and completed operations into two separate forms, CG 20 10 10 13 and CG 20 37 10 13. Form CG 20 10 10 13 provides additional insured coverage during ongoing operations and form CG 20 37 10 13 provides additional insured coverage with respect to the completed operations.

Unlike the '04 forms, the '13 forms do not automatically remove coverage for the additional insured’s sole negligence. The '13 forms remove coverage for the additional insured’s sole negligence “if not permitted by law.” The additional insured is not covered for the additional insured’s sole negligence if the applicable law does not permit coverage. The intent of removing coverage for the additional insured’s sole negligence if not permitted by law is to address those states, for example Texas, that have enacted “anti-indemnity” statutes, where the statutes further declare as void the additional insured status of the indemnitee. This is commonly referred to as closing the additional insured loop.

In addition under the '13 forms, coverage is limited to what is required by the contract. If the contractor has greater limits of insurance than what is required in the contract, the additional insured does not benefit from the additional coverage. Since the policy is tied to the contract, the contract arguably functions as part of the endorsement. Under a '13 form carriers may scrutinize the contract every time additional insured coverage is requested. What if insurance requirements change during construction? Would an increase in limits be binding? There are many issues related to tying the policy to the contract. When using a '13 form, it is important to carefully define the contract’s insurance requirements. If they are vague in any way, the carrier may construe the '13 form as limiting coverage.

A Closing Example

There can be significant differences between indemnity and additional insured obligations in the same contract. Using the injured pedestrian example, assume the owner and contractor used a limited form indemnity provision in the construction contract, and the owner was added as additional insured to the contractor’s CGL policy using an ‘85 form. Assume further that the owner is 70 percent and the contractor is 30 percent at fault for the $100,000 in damages.

Pursuant to the indemnity provision, the contractor is required to indemnify the owner only for its level of fault, 30 percent or $30,000. The contractor has insurance coverage for this obligation through the exception to the contractual liability exclusion. The contractor’s CGL carrier would pay the owner $30,000 on behalf of the contractor.

But as an additional insured, the owner will tender the claim to the contractor’s CGL carrier. Because an ’85 additional insured endorsement was used, the carrier is required to defend and fully
indemnify the owner for the claim—just as the carrier would for the named insured. The CGL carrier pays the third-party $100,000 on behalf of the owner. Even though the contract required only limited form indemnity, the owner is fully compensated for the third-party claim.

This inconsistent result is currently prevented by statute in only six states. In the remaining states, the upstream party can receive full protection for a third-party claim with the use of a broad additional insured form, even if broad or intermediate indemnity is prohibited by statute.