



2021 CLM Construction Conference

Sept 22nd – 24th 2021

San Diego, CA

Wrap it up: Don't let a WRAP cause you to come UNWOUND!

I. Introduction

Wrap policies have become ubiquitous in construction insurance over the last two decades years. The theory of one policy covering all potential liability claims on a construction project is sensible, cost-effective, and efficient. In practice, however, Wraps can be cumbersome, inefficient, and problematic. This seminar will address the good, the bad, and the ugly of wrap policies, and discuss potential options, workarounds, and examples of real-life issues on claims involving wrap policies. The discussion will include coverage matters, including potential gaps in coverage, the question of conflicts and assignment of counsel, including joint defense agreements, and best practices for resolving claims involving wraps efficiently, effectively, and economically.

II. The Good: How it Started

For large projects, contractors and subcontractors may choose to be insured through a wrap insurance program, such as an Owner Controlled Insurance Program ("OCIP") or Contractor Controlled Insurance Program ("CCIP"). Under either an OCIP or CCIP, the developer, general contractor and all of the subcontractors are named insureds for a single construction project. In contrast, without an OCIP or CCIP each contractor purchases their own policy which typically names the general contractor and owner as an additional insured on their policy and the contacts between the general contractor and subcontractors contain broad indemnity agreement that attempt to shift the responsibility for losses arising out of the project to the subcontractor.

A. The Wrap Administrator

Whether your client is an Owner/Developer or General Contractor, a thorough evaluation of all of the various options should be undertaken. There are projects that lend themselves better to a CCIP and other projects where an OCIP makes more sense. There are other projects where neither one is a good option. As part of the Scenario Based Risk Assessment that should take

place on every project, identification of the goals of the parties is paramount to being able to make the right recommendation for the parties.

OCIP's, CCIPs and Project Specific policies are filled with potential pitfalls and potential gaps in coverage. More importantly, the program itself can be filled with potential pitfalls. The policy is just one part of the puzzle. Understanding the project and the goals of the participants is a good starting point to build the right program. Once those goals are defined, you are in a better position to evaluate the various products in the marketplace (i.e., CCIP and OCIP and Project Specific policies). Evaluating the right partners including the technical abilities of the broker, carrier and administrator are as important as evaluating the project itself due to the fact that this space is unique.

B. The Wrap Policy

1. Everyone is Covered! (Are they?)

Both OCIPs and CCIPs provide consolidated insurance to all parties involved in a construction project. OCIPs and CCIPs have certain advantages such as guaranteeing certain coverages are in place with the correct limits. This is often an issue when subcontractor's insurance policies do not have the correct policy limit, the wrong additional insured endorsement or lapse when the subcontractor goes out of business.

Typically, OCIP and CCIP policies have professional liability exclusions. This excludes coverage for claims arising out of "the rendering of or failure to render any professional services by you," and, unlike the "Contractors – Professional Liability" exclusion, broadly defines "professional services" as including all supervisory, inspection, architectural, and engineering activities, as well as the "preparing, approving, or failing to prepare or approve, maps, shop drawings, opinions, reports, surveys, field orders, change drawings or drawings and specifications." This type of professional services exclusion has consistently been held to be valid by courts across the country. *E.g., Alpha Therapeutic Corp. v. St. Paul Fire and Marine Ins. Co.*, 890 F.2d 368 (11th Cir. 1989); *Carpenter, Weir & Myers v. St. Paul Fire and Marine*, 1998 WL 976309 (D. Kan. 1998) ("Commercial general liability coverage and professional liability coverage 'serve significantly different functions within the insurance industry.' CGL offers comprehensive coverage to the insured and may even cover the provision of services in general. A professional liability policy is designed to insure members of a particular professional group from the practice of liability arising out of a special risk inherent in the practice of the profession."). In addition, professionals such as architects, engineers and threshold inspectors are typically not included as enrollees in the OCIP or CCIP.

2. Everything is Covered! (Is it?)

Most OCIP's and CCIP's will include the policies that you would need for just about any construction project and these coverages will be "wrapped-up" into your package. These include General Liability, Workers Compensation, and Builders Risk coverage. Other coverages you can consider are those that are specific to the project and the region in which the project is taking place, such as protection from natural disasters such as floods and earthquakes, pollution and environmental liability, and other industry-specific coverages that might be needed.

General Liability Insurance: General Liability policies, including those that are part of an owner-controlled insurance package, provide protection from injury claims, advertising claims, and property damage claims. They will also cover defense costs in a lawsuit brought against you or anyone else involved in the project in addition to judgment and settlement monies. Contractors who enroll in an OCIP will likely already have their own general liability policy. If they do, they will have to discuss options with their existing insurance provider. Ideally, the contractor will be able to adjust their coverage to not overlap or conflict with the OCIP. However, contractors who have inflexible insurance providers will be forced to carry overlapping policies or even cancel their existing policy.

Workers Compensation Insurance: Workers Compensation is another primary component of an owner-controlled insurance package. The policy provides compensation to contractors and employees who are injured on the construction jobsite. It covers medical bills, rehabilitation, and wage losses in the event of an injury. Including workers compensation insurance within the OCIP is one of the biggest drivers of cost savings for the whole package. When a worker's comp policy is added to the OCIP, the insurance provider will evaluate the owner's vetting process for contractors and loss prevention measures that are in place on the project. If their risk estimate is low, premiums will be lower.

Builders Risk Insurance: A type of inland marine policy that ensures the structures being built along with all of the materials that are onsite from damages caused by inclement weather, natural disasters, fire, and vandalism. Rather than having each contractor purchase builders risk insurance separately, it is logical to have this included in the insurance package to protect the property.

Completed Operations Coverage: This coverage will protect everyone enrolled in the insurance and it should ideally provide protection through the statute of limitations to make sure that everyone is protected for an extended period of time well past the actual completion date of the project.

Subcontractor Default Insurance: One of the newer types of coverage available with OCIPs, this type of policy is actually pretty similar to Surety Bonds, protecting the sponsor of the project against failures related to the work of the contractor and subcontractors involved. This might be a better option financially than surety bonds in some cases, since contractors working under an OCIP might not put a lot of effort into finding surety bonds at the best possible price.

Professional Liability Insurance: Professional liability insurance purchased within an OCIP can cover engineers, architects, and other professionals associated with the project. Be sure to check if the design professionals involved in the project already have this type of coverage so you are not buying it twice. If there are many professionals of this nature involved in the project, adding professional liability to the coverage might not make sense financially and even when you enroll all the engineers, architects, and other design professionals in the OCIP, the coverage might not be a good enough substitute for the professional liability insurance that they already have in place.

Excess Liability Insurance: Excess liability coverage, also known as Umbrella liability, extends the coverage of an existing General Liability insurance. Excess liability insurance is added to an OCIP to increase limits and cover any possible gaps in the existing coverage. Contractors may also carry excess liability insurance already. In a similar fashion to their CGL policies, contractors may need to modify or eliminate their existing policies to avoid overlap.

III. The Bad

A. Claim 1- Everyone is enrolled, but “nothing” is covered.

Scenario: The project is a 200-unit apartment complex that will take approximately 2 years to complete. The general contractor secures a CCIP wrap policy and is able to get every subcontractor successfully listed as an insured. Because of that, none of the subcontractors seek out and obtain additional insurance coverage. Unfortunately, no one did their homework, and it turns out the CCIP only covers general liability and builders risk coverage.

Problem 1- Once the project is completed, it is discovered that water intrusion is a common problem throughout the complex and causing damage to personal property, lost rent, and relocation expenses. An investigation determines the water intrusion is the result of a design defect, but the CCIP did not include professional liability coverage for the architect. What now?

Problem 2- While the project is ongoing, the framing is winding down and the windows are being installed. The window subcontractor is unloading several windows when an equipment failure results in a catastrophic injury to the framing subcontractor’s employee. Because everyone

relied on the CCIP and no one did their homework, no one secured individual workers compensation coverage. What now?

B. Claim 2- Almost no one is enrolled, but everything is covered

Scenario: The project is a 200-unit apartment complex that will take approximately 2 years to complete. The owner secures an OCIP that includes general liability, builders' risk, workers compensation, completed operations, professional liability, and excess liability coverages, but only has the framing, window, and roofing subcontractors enrolled in the OCIP.

Problem 1- Once the project is completed, it is discovered that water intrusion is a common problem throughout the complex and causing damage to personal property, lost rent, and relocation expenses. An investigation determines the water intrusion is the result of a design defect. The OCIP included professional liability coverage, but the architect was never enrolled in the wrap policy. What now?

Problem 2- While the project is ongoing, the flooring company leaves behind a bucket of flammable materials that a painter mistakenly believes is a general trash bucket. He discards additional materials that cause the contents of the bucket to spontaneously combust, causing a fire that completely destroys 20 units of the complex. Unfortunately, neither the flooring nor the painting subcontractors were ever enrolled in the OCIP. What now?

IV. The Ugly: How it is Going.

A. Defense Counsel

1. Conflicts

If there is professional liability coverage in place, there will be tension between the OCIP or CCIP insurer and the professional liability insurer. First, is who will defend the insured and controls the defense. In a perfect world the professional liability and OCIP or CCIP insurer would agree to defend the case with the same counsel. The obvious advantage for the insurers is sharing in the cost of the defense – a defense which is often costly. Plus, with one firm defending the insured, it will preserve the policy limit of the professional liability policy if claims expenses are within limits. However, in most cases this does not happen since the two insurers have divergent interests and different panel counsel firms. The professional liability insurer will defend the case by arguing the design was not the legal cause of the damages. In contrast, the OCIP or CCIP insurer will focus on the construction methods and means and argue that defective construction was not the legal cause of the alleged damages. Although the law requiring independent counsel and who controls the defense may differ from state to state, this divergence of issues over whether the cause of the loss is predicated upon the insured's professional or construction activities should not create a conflict since both the professional liability and OCIP or CCIP insurer as well as the counsel they retain, have a common interest to defeat the claim and whether one

or two lawyers are retained by the insurers, that lawyer(s) should and typically do follow their ethical obligations.

In large exposure cases, defense counsel may need to be careful in several respects. First, defense should consider the insured's available insurance. For example, if the available OCIP or CCIP coverage is \$25 million and the available professional liability coverage is \$5 million, and the potential damages are \$15 million, shaping the defense strategy to minimize the potential professional liability exposure may be appropriate. Second, if defense expenses are within the policy limit of the professional liability policy, then defense counsel may have an obligation to try and settle the claim, in whole or in part, before the limit of the professional liability policy is significantly eroded. Third, defense counsel should consider if either the OCIP or CCIP or professional liability policy has a large deductible or SIR. The failure of defense counsel or the insurer to take these factors into consideration may lead to extra-contractual and/or legal malpractice claims.

Counsel for either (or both) the OCIP and CCIP or professional liability carrier may consider asking for an itemized verdict or intervening to ask for an itemized verdict. In certain circumstances this may be required, although not preferable since a lawyer for the insurer will not be present to advocate for the insurer's position (e.g., that the loss was caused by professional as opposed construction methods and means) during the trial, unless the court allows the intervenor to participate in the trial.

The policyholder's coverage counsel also plays an important role in helping to settle the claim where more than one policy is potentially triggered. Determining the cause(s) of the loss and then making demands upon the carriers is a key role. For example, if the dewatering design is deficient in one area of a project and the failure to properly install the dewatering system in another area of the project caused the project to flood and resulting in property damage and construction delays convincing one or both insurers to settle may require the hiring of a forensic engineer to apportion the loss. The need for a forensic engineer may equally apply to the carrier's coverage counsel. Without this evidence in hand, the insured may have difficulty convincing either (or both) the OCIP or CCIP and professional liability carrier to pay as the insurers may argue that the primary cause of the loss was not covered by their respective policy.

2. Joint Defense Agreements

When there is no need for infighting or finger-pointing among the enrolled parties, Joint Defense Agreements should always be considered early in the claims process. There are many benefits to JDA's, including shared litigation expenses on experts and discovery as well as the promotion of a unified defense against third-party claims. It may also be beneficial to include a JDA provision in the wraps policy language requiring the enrollees to agree to be represented by the same defense counsel where the enrollee's defense interests are aligned.

B. Coverage Issues

1. Gaps

OCIPs and CCIPs may also leave gaps in coverage. For example, OCIPs and CCIPs may cease to respond once a project reaches substantial completion leaving the OCIP and CCIP participants without completed operations coverage for some period of time after the date of project completion. In addition, OCIPs and CCIPs only insure "property damage" and may contain business risk exclusions which can preclude coverage for damage to the insured's own work. Thus, if each enrolled contractor and subcontractor is a named insured, then any property damage to the insured's work may be excluded from coverage, unless the policy is modified to treat each insured separately. Finally, Commercial General Liability policies typically contain exclusions precluding coverage if there is and OCIP or CCIP in place, or a waiver of the right to sue another participating contractor which may preclude an action by the sponsor of the OCIP or CCIP against the responsible subcontractor(s).

OCIPs and CCIPs do not preclude all coverage litigation. As noted above, CCIPs and OCIPs only cover property damage. Under Florida and most state laws, the insured's own defective work is not property damage. Only damage caused by defective work is property damage. *Auto-Owners Ins. Co. v. Pozzi Window Co.*, 984 So. 2d 1241 (Fla. 2008); *Amerisure Mut. Ins. Co. v. Auchter Co.*, 673 F.3d 1294 (11th Cir. 2012) (finding "there is no coverage '[i]f there is no damage beyond the faulty workmanship,' i.e., unless the faulty workmanship has damaged some 'otherwise non defective' component of the project.... In other words, 'unless the[e] defective component results in physical injury to some other tangible property, i.e., other than to the component itself, there is no coverage.") and *Trovillion Const. & Development, Inc. v. Mid-Continent Cas. Co.*, 2014 WL 201678 at *7 (M.D. Fla. Jan. 17, 2014) (applying the standard from *Auchter* and finding the cost of repairing the subcontractor's defective work not covered, as distinguished from a claim for repairing structural damage to the completed project caused by the subcontractor's defective work).

Business risk exclusions may also limit coverage, even where there is property damage. *Vinings Ins. Co. v. Byrdson Services, LLC*, 2016 WL 3584715, at *6 (E.D. Tex. June 17, 2016) ("The unambiguous language of the exclusion states that there is no coverage under the Policies for 'any claim or 'suit' for the cost of ... removal, loss of use... or otherwise making good any faulty, defective, or poor workmanship' in Byrdson's work for which it may be liable."); *VRV Dev. L.P. v. Mid-Continent Cas. Co.*, 630 F.3d 451, 455 n.5 (5th Cir. 2011); *Bradfield v. Mid-Continent Cas. Co.*, 143 F. Supp. 3d 1215, 1252 (M.D. Fla. 2015) and *Builders Mut. Ins. Co. v. Wingard Properties, Inc.*, 2010 WL 3069544, *3 (D. S.C. July 1, 2010).

2. Priority

Whether you have an applicable OCIP or CCIP, there is a likely scenario in which the subcontractor(s) at the heart of a claim against the wrap policy may also have overlapping coverage from their own individual insurance carrier. In these situations, a determination regarding which coverage is primary and which is excess will need to be made in order to analyze the coverages'

priority for purposes of indemnity, settlement, and/or satisfaction of a judgment. To make this determination, you must analyze the language of each policy.

In many states, "where there are multiple policies covering the same risk, and each generally purports to be excess to the other, the excess coverage clauses are held to cancel out each other and each insurer contributes in proportion to its limit amount of insurance." *Muss Dev., LLC v. Nationwide Ins. Co.*, No. 13 CV 4848 RJD MDG, 2015 WL 6160240, at *9 (E.D.N.Y. Oct. 20, 2015) (quoting *Murnane Bldg. Contractors, Inc. v. Zurich Am. Ins. Co.*, 107 A.D.3d 674, 676, 966 N.Y.S.2d 486, 488 (2d Dep't 2013)); *see also Couch on Insurance (Third Ed.)*, Chapter 219, Part IV(A)(3) § 219:47 (collecting cases). "This rule is inapplicable," however, "where it clearly distorts[s] the plain meaning of the terms of the policies of insurance." *Muss Dev., LLC*, 2015 WL at *9 (quoting *Murnane*, 107 A.D.3d at 676, 966 N.Y.S.2d at 488); *Couch on Insurance (Third Ed.)* at § 219:47.

Another consideration for analysis of priority is the supporting documents and/or communications regarding the purpose and intent of wrap coverage. In the event the excess clauses in the respective policies facially conflict with one another, a court may be free to consider extrinsic evidence and/or contemporaneous documents to resolve the conflict between the provisions. *Zurich Am. Ins. Co. v. Acadia Ins. Co.*, 243 F. Supp. 3d 1201, 1208 (D. Colo. 2017).

3. Exclusions

Because OCIPs and CCIPs are not a typical General Liability Placement they lend themselves to being somewhat unique. Especially in the GL only marketplace which is dominated by Excess and Surplus Lines carriers that are not as regulated by the department of insurance as the admitted carriers are. This means they have greater flexibility in implementing various exclusions and modifications of coverage. This is another reason to evaluate the technical abilities of the brokers placing the CIP. The relationships they have with the marketplace will give them better success in negotiating the removal and modifications of some of these exclusions. For example, one of the benefits and key features of the Wrap is the extended completed operations endorsement which extends the products and completed operations aggregate through the Statute of Repose.

C. Resolution

Revisiting our Scenarios and Problems in "The Bad" with what we have learned to navigate the issues presented by these hypotheticals and illustrate the ways in which general contractors and owners can avoid these types of issues when crafting the proper wraps coverage for their specific project.