



NEW TEXAS CLIENT ALERT– December 20, 2011

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“Insured Contracts,” “Additional Insured” Provisions, OCIPS and Consolidated Insurance Programs in Texas—New 5th Circuit Case and Big Changes Coming Effective 1/1/2012

Standard liability insurance policies (*i.e.*, CGL, Commercial Auto) not only typically cover the insured’s direct liability to plaintiff but, in several areas, also potentially cover the insured’s obligation, if any, to contractually indemnify others for the other’s liability to the plaintiff. Typically, in standard ISO policy forms, this is accomplished by carving out an “insured contract” exception to certain exclusions that otherwise might apply (*i.e.*, the CGL policy’s “contractual liability” and “employee injury” exclusions). “Insured Contract,” in turn, is then typically defined to generally encompass written contracts under which the insured has assumed the tort liability of another.

At the same time, particularly in the construction context, the insurance policy may extend “additional insured” coverage to upstream hiring contractors or the owner under an “additional insured” endorsement “as required by contract” or “as required by an ‘insured contract.’” But what if there is a contractual indemnity provision in the relevant contract but it is unenforceable for some reason (*i.e.*, it fails to comply with the Texas “express negligence” doctrine)?

In *Gilbane Building Co. v. Admiral Ins. Co.*, 2011 WL 6153370 (5th Cir. 12/12/11), the Federal 5th Circuit held that, under Texas law, even an unenforceable contractual indemnity provision can trigger the “insured contract” provisions of the insurance policy. The court held, therefore, that even if the contractual indemnity provision contained in the subcontract between the injured Plaintiff’s employer/sub and the general contractor was unenforceable under the “express negligence” doctrine, the general contractor still potentially qualified as an “additional insured” on the subcontractor’s policy. While the A/I endorsement only extended A/I status as required by a written contract that qualified as an “insured contract,” the fact that the indemnity provision purported to require the subcontractor to assume the tort liability of the general was sufficient, even if it was unenforceable.

Legislative Change Effective 1/1/12. However, due to a bill signed into law in the 2011 Legislative Special Session, **for construction contracts entered into after 1/1/12**, many contractual indemnity and additional insured risk transfer schemes that previously were used among contractors and owners will now be ineffective notwithstanding the *Gilbane* decision. Under newly added Chapter 151 of the Texas Insurance Code, any provision in a construction contract or agreement collateral thereto is void and unenforceable to the extent that it requires an indemnitor (*i.e.*, typically a sub) to indemnify or defend another party (*i.e.*, typically a GC or owner) against a liability claim caused by the negligence or other fault of the indemnitee, its employees, agents, or subs. The prohibition does not apply if the fault lies with the indemnitor or indemnitor’s employees, agents or subs. And, under Section 151.004, additional insured provisions contained in the insurance policy are, likewise, void and unenforceable to the same extent. **In short, if the statute applies, upstream contractors and owners will no longer be able to use the traditional risk transfer mechanisms of contractual indemnity provisions and additional insured endorsements to shift responsibility for their own fault to downstream contractors and subs or their carriers.**



The new statute, however, carves out several exceptions:

OCIPS/Consolidated Insurance Programs. The new statute encourages the use of “owner controlled” or “owner sponsored” consolidated insurance programs (also known as “wrap ups” or “OCIPS”) whereby multiple contractors and subs are all listed as *named insureds* on a single CGL or workers comp policy insuring a single or multiple projects. Such “consolidated insurance programs,” as defined in the statute, are exempt from the prohibitions. Under Section 151.051, any CGL coverage in any such program must extend completed operations coverage for at least three years.

Claims by an Employee of the Indemnitor or its Subs/Agents. The prohibition against indemnity and additional insured coverage does not apply if the injured plaintiff is an employee of the indemnitor (*i.e.*, typically the named insured on the policy) or an agent or subcontractor working under and for the indemnitor. In those limited circumstances, the statute does not apply and the risk transfer will be effective.

Single Family Home, Townhomes, Duplex Construction. Section 151.105 provides, among several other exceptions, that the new prohibitions also do not apply to contracts for the construction of a single family house, townhouse, duplex or land development directly related thereto.

Practical Pointers—Insurance carriers that insure construction risks must factor this new statute into their overall marketing and underwriting strategies. Likewise, builders, developers and contractors, as well as their insurance brokers and agents, need to be aware of and educated about these new restrictions. No longer can insurers of Texas construction risks or their policyholders assume that even the most carefully drafted and documented contractual indemnity and “additional insured” risk transfer and insurance mechanisms will insulate a contractor, developer or owner, or their own insurance policies from having to respond to claims alleging negligence against them. OCIPS and other forms of consolidated insurance programs will now become even more attractive than before for Texas projects. Claims handlers presented with demands for A/I coverage or defense will also need to determine if the statute applies or not. A revised definition of “insured contract” will likely be promulgated by ISO for use in Texas along with revised A/I endorsement language to take the statute into account.

If you wish to discuss any insurance-related issues or needs, please feel free to contact Schubert & Evans, P.C. at 214.744.4400 or visit our website at www.schubertevans.com.