ZURICH
Resilience Solutions

Contractual risk transfer

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1. Introduction

Contractual risk transfer as a risk management tool is unique in that it is interdisciplinary, and proper application requires knowledge of both the law and insurance.

2. Factors affecting risk transfer include:

- Control of the risk - who is in the best position to control the risk?
  Example – a construction contractor, as opposed to an owner might better control jobsite accidents due to contractual management requirements.
- Knowledge of the risk - does one party's knowledge of risk make them more logical to assume risk?
  Example – a demolition contractor using explosives to demolish a building might be the logical choice to assume risk of injuries and damages due to their unique expertise.
- Statutory or common law limitations on risk transfer - may limit risk that can be transferred via contract. One example might be when a statute or common law prohibits one party from assuming another party's sole negligence.
- Custom and practice - generally accepted modes. Example - owner to GC; GC to subcontractor.
- Bargaining position - The bigger the entity the more likely to transfer risk to smaller entity.
  The more competitive the marketplace, the more risk a company is likely to accept in negotiations. Those entities with a reputation for a firm bargaining position may obtain a preferred risk position because of reputation alone.

3. Contractual liability and the CGL policy [1, 2]

Contractual liability is a very important concept in the world of risk management and insurance. Yet, what is meant by contractual liability and how it actually works is not always well understood. This article is intended to clarify the concept of contractual liability with examples of risk transfer by contract as well as providing an explanation, with illustrations, as to how the contractual liability insurance, found in the commercial general liability (CGL) insurance policy, applies.

In general

Outside the context of insurance, contractual liability (or liability because of a contract) has a very broad meaning—a promise that may be enforced by a court. Consider the following simple example. I agree to paint your house for $1,000 and collect $500 prior to the job. After I accept the $500, I obtain a more lucrative offer and never show up to paint your house. You can go to court and claim the $500 you paid me, as I have breached the contract.
Your claim is a contractual liability claim.

Agreement to assume liability

It is common for businesses or organizations to agree, usually in writing, to take on the liability of someone else—liability they would not otherwise have. This form of agreement, where one party takes on or assumes the liability of another by contract, is commonly called a "hold harmless" or "indemnity" agreement.

Hold harmless or indemnity agreement

In an indemnity or hold harmless agreement, one party (the indemnitor) promises to reimburse, and in some cases defend, the other party (the indemnitee) against claims or suits brought against the indemnitee by a third party. The purpose of the hold harmless or indemnity agreement is to transfer the risk of financial loss from one party (the indemnitee) to another party (the indemnitor). This transfer or shifting of financial consequences is often called non-insurance contractual risk transfer and is considered a risk financing technique.

Properly written hold harmless and indemnity agreements override common law and afford an indemnitee the right to collect from the indemnitor, in some cases even if liability arises out of the indemnitee's sole negligence. While each state has its own statutes and case law that may restrict what may or may not be transferred, it is a mistake to conclude that all hold harmless and indemnity agreement are void and against public policy simply because the agreement assumes liability for the sole negligence of another.

One very important aspect of the hold harmless or indemnity agreement is that it does not relieve the indemnitee (the party with the benefit of the promise) from liability to the third party. The indemnitee may be found to be completely liable to the third party for its bodily injury or property damage. The hold harmless gives the indemnitee a legal right to collect from the indemnitor (to the extent included in the contract and allowed by law) for the damages paid to the third party. The purpose of contractual liability insurance is to pay, on behalf of the indemnitor, the damages to the third party.

Where to find hold harmless and indemnity agreements

Businesses or organizations enter into in a wide variety of contracts in which hold harmless or indemnity agreements may be found. One very common contract, in which a hold harmless or indemnity agreement is usually found, is a real estate lease agreement between tenant and landlord. A sample hold harmless and indemnity clause found in a real estate lease is:

The Lessee will save the Lessor harmless and keep it exonerated from all loss, damage, liability or expense occasioned or claimed by reasons of acts or neglects of the Lessee or his employees or visitors or of independent contractors engaged or paid by Lessee whether in the leased premises or elsewhere in the building or its approaches, unless proximately caused by the negligent acts of the Lessor.

As many indemnity or hold harmless clauses may be quite lengthy and difficult to read, it is often a challenge for risk managers to determine with any precision the scope of liability that has been assumed. The following example may prove helpful to explain how the above agreement might work.

An illustration of the workings of a hold harmless or indemnity agreement

A tenant (Lessee) in a multi-tenanted professional office building hires an electrician (an independent contractor) to rewire a portion of the tenant's (Lessee's) office. About a year after the rewiring is finished, another tenant receives a severe electrical shock when plugging in an appliance, resulting in serious injuries to the tenant.

The injured tenant sues the landlord (Lessor) demanding compensation for her injuries, alleging that the landlord breached its duty to properly wire the building. The investigation strongly suggests that the injury of the tenant was caused, at least in part, by the electrician's wiring job. Nonetheless, the landlord (Lessor) is found to have responsibility for the injuries and is ordered to pay the injured tenant $150,000 in compensatory damages.

As the tenant (the Lessee) has agreed to indemnify the landlord (Lessor) for the acts of the tenant's (Lessee's) independent contractors, the tenant (Lessee) is obligated by the lease's hold harmless clause to pay the $150,000, either as payment to the landlord or directly to the injured tenant. In this situation, the tenant (Lessee) would not normally have had any liability to the injured tenant. His liability arises solely from the agreement, as part of the lease, to take on the liability of the landlord. The tenant's contractual liability insurance would pay on his behalf the $150,000 damages owed.

While the electrician may ultimately have to pay $150,000 (or a lesser amount) via a subrogation action, the landlord (Lessor) does not have to wait for the result of further litigation or be concerned with proving fault on the electrician's behalf in order to recover the $150,000 (the tenant assumed liability for the acts of his independent contractors, regardless of negligence). Even if the Landlord could prove fault on the electrician's behalf, it may only be partial fault, and may result in the landlord collecting less than the $150,000 in damages.

In short, the landlord has transferred the financial risk of having tenants in his or her building back to each tenant via the hold harmless and indemnity agreement inserted in the lease.

Contractual liability insurance and the commercial general liability policy

Contractual liability insurance has been automatically provided within the commercial general liability (CGL) policy since 1986. The mechanics of how coverage is actually provided does merit some explanation. The first mention of "Contractual Liability" in the 2001 CGL policy is as the title of exclusion. Coverage is eliminated by this exclusion for assumption of liability in a contract or agreement. There are, however, two important exceptions:

- Liability of the insured that would be imposed without the contract or agreement

or

- Liability assumed in a contract or agreement that is an "insured contract."

The term "insured contract" is defined later in the policy and is critical to understanding the coverage provided. More on "insured contract" later.

Breach of contract claims

On occasion, a policyholder will seek coverage under the CGL policy for a breach of contract claim. In other words, the damages being demanded do not arise from liability assumed in a hold harmless or indemnity agreement, but are due to failure to meet an agreed upon obligation. Avoiding coverage for breach of contract claims is the very reason the CGL first excludes all contractual coverage, then grants limited contractual liability coverage by an exception to the exclusion. Here is an example of what is intended to be excluded:

A contractor agrees in a construction contract to insure a building that is being built for the owner. Unfortunately, the contractor forgets to place the insurance on the building, which a tornado destroys shortly before its completion. The owner seeks payment from the contractor for the value of the building, asserting a breach of contract action for failing to purchase insurance. The contractor then makes claim under the contractual liability coverage of his CGL policy for the value of the building.

Assumption of liability by contract or agreement

What is actually meant by "liability assumed by contract" has been the topic of a considerable amount of litigation, with varied outcomes. An Alaska case—Olympic, Inc. v Providence Washington Insurance Co., 648 P2d 1008 (Alaska 1982), as quoted in Gibbs M. Smith v United States Fidelity & Guaranty Co., 949 P2d 337 (Utah 1997)—provides this explanation, which reinforces the concept that coverage is not for breach of contract:

Liability assumed by the insured under contract refers to liability incurred when one promises to indemnify or hold harmless another, and does not refer to liability that results from breach of contract.

The court went on to explain the differences in the nature of the obligations:

Liability ordinarily occurs only after breach of contract. However, in the case of indemnification or hold harmless agreements, assumption of another's liability constitutes performance of the contract.

Assuming a duty versus assuming a liability

Assuming the liability of another (agreeing to be responsible for some else's legal obligation to pay damages to third parties) is sometimes confused with assuming a duty to others (an obligation to act or not to act that would not exist but for an agreement). For example, I may enter into a maintenance contract whereby I agree to regularly service the machinery on your premises, creating a duty that I would not otherwise have had. But I carelessly fail to service a machine that later malfunctions, injuring your employee. It is subsequently found that my failure to service the machine caused the malfunction and employee's injury. The employee brings suit against me for their injuries.

Some insurers have mistakenly denied CGL claims such as these, contending the claim is a breach of contract claim and thus excluded by the contractual liability exclusion of the CGL. A more careful analysis of this type of claim will reveal that it is in actuality a tort-based claim—specifically negligence. I breached a duty (to maintain the machinery), such breach being the proximate cause of the injury to the employee. The duty was assumed or created by the contract; no assumption of liability via a hold harmless or indemnity agreement was involved. The damages claimed were not by the other party to the contract and were not the cost to fulfill the contract, but rather damages resulting from injuries to an unrelated party, the injured employee.

This issue was addressed in Olympic, in which the Alaskan court held that:

Legally obligated to pay as damages … refers to liability imposed by law for torts and not to damages for breach of contract … the only exception to this general rule arises when the contract breach itself results in injury to persons or property. (Emphasis added.)

Coverage by exception—the "insured contract"

The exception to the contractual liability exclusion does provide broad contractual liability coverage for liability assumed in a contract as long as:

- The bodily injury or property damage occurs after entering into the contract, and
- The liability is assumed in a hold harmless or indemnity agreement that falls within the definition of "insured contract."

The contractual liability coverage provided for "insured contracts" is "blanket" in that the insured does not need to list or designate the covered contracts (as was required under the 1973 Contractual Liability Coverage Part), nor is a separate premium charge made for contractual liability coverage. Contractual liability coverage in the CGL is also "broad form," as it applies even if an insured assumes liability for the sole negligence of the indemnitee.

"Insured contract" is defined, and the definition begins by listing five types of contracts that are common to many businesses and organizations:

- 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

Coverage for the above five contracts was automatically included in the 1973 CGL policy (and prior editions) as "incidental contracts." When the CGL was overhauled and simplified in 1986, the listing of these "incidental contracts" remained to clarify that coverage was still intended to apply to liability assumed in these contracts.

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. Tort liability means liability imposed other than by contract. Put another way, coverage applies only to a particular type of assumed liability—that which arises from a breach of duty and that exists independent of any contractual relationship the indemnitee may have with the injured party. [Barry R. Ostranger and Thomas R. Newman, Handbook on Insurance Coverage Disputes 7.01 (8th Ed. 1995).]

What is not an "insured contract"

"Insured contract" does not include an agreement to indemnify:

- A railroad for construction or demolition operations within 50 feet of railroad property and affecting any railroad bridge or trestle, tracks, roadbeds, tunnel, underpass or crossing.
- An architect, engineer or surveyor for their professional services.
- Others for professional services if assumed by an insured who is an architect, engineer or surveyor.

Railroad protective liability and professional liability coverage is needed if an insured has exposures falling within the exclusions.

4. Methods of protection

Insurance carriers offer several types of products of protection, but a contractor should never use those products to guarantee 100% protection.

Types of insurance coverage:

- CG – Commercial General Liability Coverage
  - Provides broad standardized coverage for both property damage and personal injury claims – third party coverage
- OCP – Owners and Contractors Protective Liability Insurance
  - Provides separate limits and generally insurance specifications in contract require contractor to provide this coverage to the Owner
- Automobile liability coverage
  - Provides protection from liability arising out of use, maintenance or operation of covered vehicle
- Excess coverage
  - Provides coverage over and above primary general liability coverage
- Workers' compensation insurance
  - Provides coverage for injuries to employees during the scope of their employment
- Builders risk coverage
  - Coverage for direct property damage to property under construction – first party coverage Indemnification
- Contractual indemnification
- Common law indemnification
- Contribution among joint tortfeasors
- Understanding the policy
- First party vs. third party coverage - the differences between property and casualty coverages
  - First party covers yourself (the contractor).
  - Third party covers anyone else (liability).
  - Property coverage only relates to first party exposures – damage to a contractor's property.
- The party who had been wronged or injured is called the "third party".
- Liability can manifest itself as injury, damage or loss of use.

Hold harmless agreements

In an indemnity or hold harmless agreement, one party (the indemnitor) promises to reimburse, and in some cases defend, the other party (the indemnitee) against claims or suits brought against the indemnitee by a third party. The purpose of the hold harmless or indemnity agreement is to transfer the risk of financial loss from one party (the indemnitee) to another party (the indemnitor). This transfer or shifting of financial consequences is often called non-insurance contractual risk transfer and is considered a risk financing technique.

A hold harmless agreement is a written contract between two parties that states that one party will assume the risk of legal liability for the other party. Rather than seeking to bar a lawsuit, a hold harmless agreement obligates one party to pay any costs the other incurs as a result of a claim or lawsuit.

Many contracts increasingly include hold harmless agreements. To protect your company, carefully read the language in the agreement and make certain that you are not assuming a disproportionate share of the risk. If you must assume risk, assume it for those things over which you have control. Properly drafted by an attorney, a "hold-harmless" agreement may be better than a standard indemnification clause. A hold harmless agreement may obligate the party to pay expenses as they arise rather than requiring indemnification or reimbursing the other party for expenses incurred. Furthermore, the courts presume that the agreement applies to all costs for which the other party is liable including the legal costs of responding to and defending against a claim. Costs would also include the payment of any damages awarded to the claimant.

Properly written hold harmless and indemnity agreements override common law and afford an indemnitee the right to collect from the indemnitor, in some cases even if liability arises out of the indemnitee's sole negligence. While each state has its own statutes and case law that may restrict what may or may not be transferred, it is a mistake to conclude that all hold harmless and indemnity agreement are void and against public policy simply because the agreement assumes liability for the sole negligence of another.

An important aspect of the hold harmless or indemnity agreement is that it does not relieve the indemnitee (the party with the benefit of the promise) from liability to the third party. The indemnitee may be found to be completely liable to the third party for its bodily injury or property damage. The hold harmless gives the indemnitee a legal right to collect from the indemnitor (to the extent included in the contract and allowed by law) for the damages paid to the third party. The purpose of contractual liability insurance is to pay, on behalf of the indemnitor, the damages to the third party.

Because a hold harmless agreement does not foreclose a lawsuit, the ability of the executing party to pay expenses that do arise limits its practical value. A hold harmless agreement from an entity with no assets and no insurance is nearly worthless. For this reason, most hold harmless agreements require proof of insurance coverage. The entity promising to pay must provide proof that it has insurance to cover any claims that may arise. For complete protection, the insurance policy must include coverage for liability assumed under contract. A certificate of insurance verifies that the entity carries insurance with the specified limit and offers possible assurance of payment.

Waivers

Although an individual's behavior (for example, engaging in an obviously hazardous activity such as skydiving) occasionally implies a waiver or release, the term refers to an express or written agreement customarily. Liability waivers are valid only if the person enters into the agreement knowingly, voluntarily and the person waiving certain rights receives something in exchange. Few attempted waivers satisfy these standards. Courts often find that arrangements are not voluntary when they are between an individual and an organization because of unequal bargaining power. Courts often invalidate waivers on the grounds that a participant did not fully appreciate the rights being waived or that the waiver did not specifically indicate that it covered liability for negligence.

Despite their legal vulnerability, if properly drafted and executed, waivers may help block liability. Moreover, an individual who has signed a waiver may be less likely to initiate a lawsuit than someone who has not. A waiver may also assist an organization in asserting the legal defense of "assumption of the risk." This defense asserts that the individual proceeded with the activity despite being aware of the risks, and therefore should not be permitted to receive damages.

The validity of a waiver may depend on when the person executed it. Those executed before any actual damages occur are more tenuous than those executed after an injury has occurred (commonly referred to as "releases"). Waivers written before any damages actually occur generally seek to establish that the individual recognizes the risks involved in a forthcoming activity and voluntarily consents to accept the consequences of those risks in exchange for the opportunity to participate. The circumstances of each case determine whether a court will enforce such a "before the fact" waiver. If the individual has no practical choice but to sign the waiver, it is unlikely that the court will uphold it.

Waivers executed after an injury are on much more solid legal ground because the value of the exchange is less speculative. Claimants often execute such a waiver in conjunction with a settlement arrangement. In either event, consult legal counsel when drafting such agreements. The laws governing waivers varies widely from state to state and some states prohibit their use in certain situations.

Additional insured endorsements

Additional insured endorsements are important contractual risk transfer tools. These endorsements modify the policy's coverage by including the named endorsement holder as an insured. A hold harmless agreement is a separate agreement between the parties, while an additional insured endorsement is a modification of an existing contract between the insurance company, or risk pool, and the insured person or organization.

Disclaimers

A "disclaimer" is an express disavowal, repudiation, or limitation of liability by one party to a transaction. Disclaimers differ from waivers in that they are unilateral; the injured party does not explicitly agree to the liability limitation. As such, they are of limited legal value. Their principal functions are to refute assertions about extra duties that a program has taken upon itself and to apprise potential claimants of relevant program limitations. In this sense, a disclaimer is roughly equivalent to an advisory or warning of risks that an individual may choose to accept or avoid. Regardless of legal effect, disclaimers, like waivers, may deter claims.

While the information contained in this document may be helpful as you look at the potential use of risk transfer tools such as waivers and hold harmless agreements in your organization, do not regard this document as a substitute for the advice of legal counsel. If you are considering the use of contractual risk transfer mechanisms, consult an experienced attorney for advice on your particular circumstances.

5. Insurance certificates and contracts

Insurance certificates

Certificate of insurance controls

A certificate is not a contract between the holder and the insurer. It only provides information to an interested third party that insurance is in force at the time of issuance.

Certificate issues:

- Cancellation
- Types of coverage
- Deductibles/SIR
- Disclaimers on form

Receiving certificate of insurance alone is not enough to afford protection - you must have policy and endorsements to guarantee coverage before work starts.

It is imperative that, like the contract, the contractor has an effective program in place to monitor the receipt of the certificate of insurance prior to the contractor being allowed on the jobsite. It is also important for the contractor to realize that the certificate offers no binder of coverage. The certificate cannot amend the insurance contract and therefore, is informational only. However, this certificate does indicate that the contractors' insurance agent or broker has issued the form to you for informational purposes to show you the coverage in effect.

Insurance certificate management

- Establish an organized system to monitor compliance with insurance requirements and serve as a permanent record
- Verify certificates are received, properly filled out and signed
- If requirements are not met, request a new certificate
- Ensure there is an acceptable certificate on file prior to work commencing. If this is not possible, at a minimum, provide contract language allowing payment to be withheld until an acceptable certificate is received
- Review certificates periodically to ensure they are still current

Contracts

A contract is an agreement that outlines a promise or set of promises for compensation. The law may give remedy for failure to complete a contract and recognizes the promise (s) outlined as a duty to perform. In order to enforce a contract, a binding contract has to exist between parties. These three requirements are an offer, acceptance and compliance with terms of the offer, some type of consideration or payment.

There are three (3) basic construction contract types:

1. Fixed price (sometimes called stipulated sum or lump sum)
2. Unit price (sometimes also called unit rate)
3. Cost type (sometimes called cost plus or cost plus a fee)

Fixed price contracts

Fixed price contracts are used when the scope of work is well-defined. The scope of work consists of the following documents: design drawings and technical specifications, all relevant building codes and safety standards, a project schedule, a construction schedule, duties and responsibilities of the owner or the owner's agent, i.e., a construction manager, identification and coordination of other owner-contractors, if any, owner-furnished items, if any, status and responsibilities for all required permits, status of owner's funding, etc. This is the traditional form of construction contracting as practiced by most public entities.

Unit price or unit rate contracts

Unit price contracts are used when the units of work are well-defined but the quantities of the units are uncertain. The number of units may vary, but the definition of what constitutes a unit does not vary.

Unit rate contracts are sometimes called force account contracts (denoting the work force and the principal of on-account or credit) and consist of a set of "all-inclusive" fixed labor and equipment hourly unit rates for straight-time, over-time and premium-time by labor classification; "all-inclusive" hourly, daily, weekly and monthly equipment by equipment description; and various third-party mark-up percentages that are added to the cost of material purchases or subcontracted services ---these typically run between 5% to 15% of the delivered cost of the material or service. "All inclusive" rates mean that the rates include all of the contractor's profit, insurance and overhead. Labor rates include all payroll taxes and insurance, employee benefits, and small tools and minor equipment. Equipment rates include fuel, oil and grease, cutting edges, tire repair and equipment maintenance. Fixed rates mean that the rates are fixed for a given length of time, usually, a year. Daily timesheets for labor and equipment are completed daily by the contractor and signed by the owner or the owner's representative, i.e., the construction manager. Material receiving documentation is attached to the purchase invoice for the goods or service and the applicable markup is added. Signed timesheets for labor and equipment are extended by the applicable unit rate and this establishes the cost to the owner.

Cost type contracts

Cost type contracts are generally used when the scope of the work is not well-defined or very complex (for instance when building something that has never been constructed before) or when the project schedule is tight. Cost type contracts are used on "fast track" projects where the design is being completed as the construction and procurement is taking place.

Cost type contracts have lengthy sections that define precisely what is an allowable cost.
The term "cost of the work" generally means all of the cost elements that go into constructing the actual structure or building. The term "general conditions" generally means the cost elements that go into running the construction project, the cost of the contractor's staff supervision, cost of the construction trailers, copy machines, telephones, computers, construction equipment, temporary facilities, utilities, etc.
The term "fee" generally means the contractor's profit and home office overhead.

Risk assignment/risk-sharing

The general rule is: all risks are rightfully the owner's unless transferred or assumed by another party for fair compensation.

The basic principles of risk assignment are:

- Which party can best foresee the risk?
- Which party can best control the risk?
- Which party can best bear the risk?
- Which party benefits or suffers if the risk materializes?

The owner holds the key to risk assignment through its selection of contract compensation type.

There are two (2) extremes:

1. All risk on the owner (owner pays low $'s, owner self-insures) – cost-type contracts
2. All risk on the contractor (owner pays high $'s, contractor acts as insurer of owner) – fixed price contracts.

In negotiating a construction contract, each party attempts to minimize its own risk. Contractors understand that assuming risk is part of the business of construction contracting. However, the contractor will always insist on fair compensation for assuming risk.

"Tough" owners generally pay a higher price to build the same facility over the long run as word gets out around the construction community that this owner transfers risk unfairly, e.g., is slow to pay, denies legitimate change orders, denies legitimate time extensions, over-inspects the work, etc. This will be in the form of higher bid prices and numerous inflated claims for additional compensation – the "tough" owner pays twice.

The following is a commonly used risk assignment basis as written into the most widely used construction contracts in North America, i.e., American Institute of Architects, Association of General Contractors, etc.

Type of risk	Best party to assume risk	Remarks
Site access	owner	
Subsurface conditions	contractor	except for "unforeseen conditions"
Weather	contractor	except for extremely unusual weather
Acts of god	owner	
Quantity variations	contractor	up to +/- 15% to 25% (typically)
Capability	each party assumes own risk	
Defective design	architect/engineer	
Subcontractor default	contractor	
Defective work	contractor	except for design defects
Accident	contractor	contractor buys insurance, owner pays indirectly
Managerial competence	each party assumes own risk	
Financial failure	each party assumes own risk	
Inflation	contractor	typically only for 12 to 18 month duration
Economic disaster	owner	
Funding	owner	
Labor, materials, equipment	contractor	
Acceleration	owner	
Suspension	owner	
Environmental	owner	
Compliance with regulations	contractor	
Public disorder, war	owner	
Union strife	contractor	

Even though the law may not require a particular contract be in writing, the bottom line is that there is not a problem with not having a written contract, unless either party has a problem. Unfortunately in today's litigiousness society, written contracts are a key practice.

6. Controls

It is important to have an orderly, efficient contract administration program for the control of contractual risk transfer. This administration relies exclusively on the cooperation and communication of the various departments entering into contractual agreements and the administrator of the contract. This includes everyone who drafts contracts as well as those who accept contracts.

From the beginning, the general objective should be to give clear instructions to all personnel regarding the grave consequences of accepting risk hidden in innocuous, "plain vanilla" contracts and the need to submit all contracts to the responsible party for review and evaluation.

Is there a program in place to control receipt of signed contract?

Realistically, not all contracts are signed prior to a subcontractor entering the jobsite due to negotiations of terms. However, the lack of a signed contract can have a dramatic impact on the transfer of risk. This could very well spark long and expensive legal wrangling that could ultimately impact the price and program design of insurance coverage. The most effective control is the receipt of the signed contract before work commences but if that is not possible, then the inclusion of your hold harmless agreement and insurance requirements, along with identifying a specific, limited scope of work, on a letter of intent will at the least assist in stating the expectations prior to commencement of work. If you are not using letters of intent in this fashion, you could be impacting your risk transfer plan.

Are the duties and responsibilities clearly defined in regards to safety?

Anyone accepting risk transfer through contract should be sure that their duties are clearly defined and that the duties meet generally accepted safety standards. Remember you may be accepting risk of others in the contract and want to be sure that safety standards will allow you to control risk of loss. The idea of transferring risk in construction contracts follows the premise that the subcontractor has the most control over their work area and should accept liability for that work area. By following that logic, the impact of controls, contract design, safety programs, pre-qualification of subcontractors and loss history gains critical importance.

Risk acceptance

Some of the factors that should be considered when making decisions on accepting risks are:

- Pre-qualification of subcontractors
- Contract design
- Contractor experience
- Controls
- Contractor safety program
- Contractor loss history

7. Conclusion

Risk management theory suggests the use of four major tools in controlling risks: avoidance, modification, retention, and transfer (sharing). The transfer options include both the purchase of insurance and the contractual transfer of risk to another party. For companies seeking to minimize potential liability, they should consider risk transfer as a useful risk management tool.

8. References

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