USING OCIPs AND CCIPS TO BRING ORDER TO PROJECT INSURANCE

CMAA Southern California Chapter

October 30, 2014 8:00 a.m.

The Grand Conference Center
4101 E. Willow Street
Long Beach, CA

nossaman.com
Panel

- Greg Kildare
  - Executive Officer Risk Management
  - Los Angeles County MTA (Owner)

- Kevin Peters
  - Senior Vice President
  - Old Republic Construction Program Group (Insurer)

- Jim Holobaugh
  - Senior Vice President
  - Alliant Insurance Services (Broker)

- Tom Long
  - Partner
  - Nossaman LLP (Attorney)
CHARACTERISTICS OF A CONTROLLED INSURANCE PROGRAM ("CIP")

Traditional Insurance Approach
- Multiple Insurers
- Inadequate Limits
- Potential Gaps in Coverage
- Potentially Uninsured Subcontractors
- Cross Litigation Between Contractors
- Indemnity Issues

Wrap-up Approach
- Control
- Cost Reduction
- Higher Coverage Limits
- Consistent Coverage Across Contractors
- Coordinated Claims
- Minimize Cross Litigation/Subrogation
- Allows for a Larger Qualified Contractor Pool
**WRAP UPS**

**Coverages**

- **Excess Liability**
  - $50 - $200 Million Excess
  - Follow Form Excess Liability

- **General Liability**
  - $2 M Combined Single Limit
  - $4 M General Aggregate
  - $4 M Products/Completed Ops Aggregate
  - $2 M Personal/Advertising Injury

- **Employer’s Liability**

- **Workers’ Compensation**

- **Builder’s Risk**

- **Contractor’s Pollution Liability**
  - Pollution Legal Liability
  - $25 Million

- **Owners Protective Professional Indemnity**

**Making it Happen.**

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Proprietary & Confidential
Enrolled vs. Excluded OCIPs and CCIPs

**Included**

- General Contractor
- Eligible subcontractors with on-site labor
- Both prime and lower-tier subcontractors

**Excluded**

- Off-site labor
- Demolition – Structural
- Hazardous materials contractors/transporters
- Architects, engineers, surveyors
- Vendors, suppliers, purchase orders, fabricators, material haulers, truckers
- Others at the discretion of Risk Management
Financial Model

Loss Sensitive Program

Owner Cost without OCIP

Owner Max. Cost with OCIP

Minimum Cost

Fixed Expenses
(Insurance, Excess, Administration)

Loss Ratio

0% 10% 20% 30% 40% 50% 60% 70% 80% 90% 100%

Typical Savings
(0.5% - 1.2%)
of Construction Cost

Cost Avoidance

Claims

Minimum Savings

Savings = Contractor Insurance Costs - OCIP Costs - Losses

MAKING IT HAPPEN.
## WRAP UPS
### Sample Financial Model

**PROJECT(S)**
- **Construction Value**: $350,000,000
- **Payroll**: $70,000,000

**INSURANCE REVENUE/COST AVOIDANCE**

<table>
<thead>
<tr>
<th>Owner Charge or Contractor Credits</th>
<th>PREMIUM</th>
<th>% OF CV</th>
</tr>
</thead>
<tbody>
<tr>
<td>WC/GL/XS</td>
<td>$9,625,000</td>
<td>2.75%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>$9,625,000</td>
<td></td>
</tr>
</tbody>
</table>

**CCIP PROGRAM COSTS**

<table>
<thead>
<tr>
<th>Costs</th>
<th>Minimum</th>
<th>Loss Aggregate</th>
<th>Maximum</th>
</tr>
</thead>
<tbody>
<tr>
<td>Combined WC/GL/Excess/Administration</td>
<td>$3,325,000</td>
<td>$4,900,000</td>
<td>$8,225,000</td>
</tr>
<tr>
<td>Excess Premium</td>
<td>$1,200,000</td>
<td>$1,200,000</td>
<td></td>
</tr>
<tr>
<td><strong>Total CCIP Program Costs</strong></td>
<td>$4,525,000</td>
<td>$4,900,000</td>
<td>$9,425,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>LOSSES</th>
<th>PROGRAM COSTS PLUS LOSSES</th>
<th>INSURANCE CREDITS</th>
<th>PROGRAM SAVINGS</th>
<th>% OF CV</th>
</tr>
</thead>
<tbody>
<tr>
<td>0%</td>
<td>$</td>
<td>$4,525,000</td>
<td>$9,625,000</td>
<td>$5,100,000</td>
</tr>
<tr>
<td>10%</td>
<td>$490,000</td>
<td>$5,015,000</td>
<td>$9,625,000</td>
<td>$4,610,000</td>
</tr>
<tr>
<td>20%</td>
<td>$980,000</td>
<td>$5,505,000</td>
<td>$9,625,000</td>
<td>$4,120,000</td>
</tr>
<tr>
<td>30%</td>
<td>$1,470,000</td>
<td>$5,995,000</td>
<td>$9,625,000</td>
<td>$3,630,000</td>
</tr>
<tr>
<td>40%</td>
<td>$1,960,000</td>
<td>$6,485,000</td>
<td>$9,625,000</td>
<td>$3,140,000</td>
</tr>
<tr>
<td>50%</td>
<td>$2,450,000</td>
<td>$6,975,000</td>
<td>$9,625,000</td>
<td>$2,650,000</td>
</tr>
<tr>
<td>60%</td>
<td>$2,940,000</td>
<td>$7,465,000</td>
<td>$9,625,000</td>
<td>$2,160,000</td>
</tr>
<tr>
<td>70%</td>
<td>$3,430,000</td>
<td>$7,955,000</td>
<td>$9,625,000</td>
<td>$1,670,000</td>
</tr>
<tr>
<td>80%</td>
<td>$3,920,000</td>
<td>$8,445,000</td>
<td>$9,625,000</td>
<td>$1,180,000</td>
</tr>
<tr>
<td>90%</td>
<td>$4,410,000</td>
<td>$8,935,000</td>
<td>$9,625,000</td>
<td>$690,000</td>
</tr>
<tr>
<td>100%</td>
<td>$4,900,000</td>
<td>$9,425,000</td>
<td>$9,625,000</td>
<td>$200,000</td>
</tr>
</tbody>
</table>
Identifying Insurance Costs

- **Net Bid**
  - Subcontractor Bids Without Insurance (Bid Accepted)
  - Savings Estimated

- **Insurance Add Alternate**
  - Insurance Cost Identified & Reviewed (Bid Adjusted)
  - Savings Identified Up-Front (Not adjusted by project end)

- **Bid Credit Tracking**
  - Subcontractor Bids With Insurance Included (Bid Adjusted)
  - All Insurance Costs Identified and Removed
Identifying Insurance Costs

Ensure proper bidding
- Insurance Cost Worksheet
- Contract language
- Education

Large Deductibles
RFP Credit Approach - Example

<table>
<thead>
<tr>
<th>Fees</th>
<th>Fee Percentage</th>
<th>Fee in $</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(Fee as % of the Const. Cost Budget)</td>
<td></td>
</tr>
<tr>
<td>Design Fees</td>
<td>7.53%</td>
<td>$3,012,000</td>
</tr>
<tr>
<td>Site Management Fee</td>
<td>4.27%</td>
<td>$1,708,000</td>
</tr>
<tr>
<td>Design Builder Bonds</td>
<td>.72%</td>
<td>$288,000</td>
</tr>
<tr>
<td>Subcontractor Bonds</td>
<td>.30%</td>
<td>$120,000</td>
</tr>
<tr>
<td>Overhead and Profit</td>
<td>3.70%</td>
<td>$1,480,000</td>
</tr>
<tr>
<td>Total Fee</td>
<td>16.52%</td>
<td>$6,608,000</td>
</tr>
<tr>
<td>OCIP Credit (GC &amp; Subs)*</td>
<td>-2.50% *</td>
<td>-$1,000,000</td>
</tr>
<tr>
<td>Basis of Award</td>
<td>14.02%</td>
<td>$5,608,000</td>
</tr>
</tbody>
</table>

*Insurance costs are subtracted from total fee for the purpose of proposal scoring only. Proposed OCIP deduct is actually debited from direct construction costs.
OCIP Insurance Manual

- All subcontractors should receive an Insurance Manual when bidding and with their contract agreement
- Functions as a “user-guide” and outlines the wrap-up administrative process
- Explains requirements and responsibilities
- Details off-site insurance required of subcontractors
- Includes project roles and contacts
- Describes coverages provided
- Describes claims procedures and points of contact
OCIP Administration Flowchart

**Contract Signed with Subcontractor**
- Subcontractor supplied with OCIP Manual
- Contractor Notifies Broker via Notice of Award (NOA)

**Broker Adds contractor to RMIS system**
- Broker sends Login information to contractor

**Contractor Enrolls Online**
- Any additional Subcontractors identified during enrollment process

**Contract Closeout**
- Completion of work
- Notification via NOC or online entry

**Contractor Ongoing Duties**
- Online monthly payroll reporting directly to Broker
- Offsite Certificates updates

**Enrollment Completed**
- COVERAGE STARTS
- Policy number issued by Carrier
- Welcome packet and COI issued by Broker

**Project Closed**
- Individual Subcontractor WC policies Terminated
- Start of 10-year tail
COMPARING CIPS WITH TRADITIONAL INSURANCE

OCIPs AND CCIPs
- Common limits and scope.
- Common defense, lower litigation costs.
- Added burden of administration.

TRADITIONAL INSURANCE
- Orphan shares and gaps.
- Separate defense and finger pointing.
- Lower administration burden.
OCIPs AND CCIPs

- Project specific limits.
- Coverage term to match project term.
- Control over coverage scope.

TRADITIONAL INSURANCE

- Limits for some lines shared with other projects.
- Annual renewals.
- Less control over coverage scope.
COMPARING CIPS WITH TRADITIONAL INSURANCE (contd.)

OCIPs AND CCIPs

- Lower costs if better claim experience though centralized risk management and a loss sensitive premium (retro).

TRADITIONAL INSURANCE

- More predictability of costs. Losses on others’ history.
COMPARING CIPS WITH TRADITIONAL INSURANCE (contd.)

OCIPs AND CCIPs

- Enrollment of subs means more control, easier small sub participation.
- Greater insurer insolvency risk. Compensate with drop down and participation.

TRADITIONAL INSURANCE

- Less control, harder for subs to meet requirements.
- Insolvency risk is diffuse.
COMPARING CIPS WITH TRADITIONAL INSURANCE (contd.)

OCIPs AND CCIPs

- Builder’s risk coverage requires a formal enrollment process.

TRADITIONAL INSURANCE

- Builder’s risk coverage is automatic to all with an interest in the property.
OCIPs AND CCIPs

- Professional liability coverage often limited to bodily injury and property damage. Consider an owner’s professional protective insurance (OPPI) policy.

TRADITIONAL INSURANCE

- Professional liability coverage is broader—extending to economic and other consequential damages.
OCIPs vs. CCIPs
Considerations

**OCIPs**
- Owner receives maximum financial benefit
- Owner posts collateral and pays premiums
- Same coverage terms
- Dedicated program limits
- Owner controls claims for completed operations period

**CCIPs**
- GC receives maximum financial benefit
- Contractor posts collateral and pays premiums
- Same coverage terms
- Limits can be dedicated or shared depending on program structure
- General contractor controls claims for completed operations period
OCIPs vs. CCIPs
Considerations

**OCIPs**
- Broker provides claims advocacy
- Owner sets contractor insurance requirements and assembles underwriting data
- Owner monitors program progress
- Broker administers program
- Owner can include multiple projects in its OCIP program through a “rolling” OCIP

**CCIPs**
- GC manages contractor insurance requirements and program administration
- Broker administers the program
- Other projects cannot be included in the same program unless the same GC is utilized
OCIPs vs. CCIPs

Considerations

**OCIPs**
- Startup costs can be significant
- Claim resolution can be difficult in the public sector context
- Can accommodate multiple prime contractors at multiple jobsites
- Difficult to access contractor’s cost of risk during selection

**CCIPs**
- Better alignment of incentives for loss control
- Premiums tend to be a bit cheaper.
- Large contractors already have rolling programs (no startup costs)
- Need one prime contractor
- Pricing is a signal of lost control in bid
Limited Indemnity for Construction Defects

- Broad Indemnities and the *Crawford* Surprise [44 Cal. 4th 541 (2008)].
  - Old Rule allowed standard indemnities by which GCs and owners could be indemnified by others for their own negligence.
  - *Crawford* Must a subcontractor who was found not to have done anything wrong indemnify a GC for costs of defense?
  - Yes! The California Supreme Court arguably made subs the insurers of GCs and GCs the insurers of owners.
Limited Indemnity for Construction Defects (contd.)

- Legislative action. Civil Code section 2782 et. seq. AB 2738 restrictions protected subcontractors. SB 474 went further to protect all “promisors.”

- Indemnities from all parties to a construction contract now arguably limited to their own negligence only. “Active negligence” of GCs and public agencies and “sole negligence” of private owners may not be indemnified.
Limited Indemnity for Construction Defects (contd.)

- The new indemnity limitations apply to “construction defects” but not “design defects.”

- Only “wrap-up” insurance is clearly excluded from all of the indemnity limitations.
Other Practical Considerations

- How does the owner assure compliance with contract insurance requirements without control of and review of the CCIP policy?

- How do you fit the scope of the CIP (project coverage) with other insurance?
  - How do you address off site manufacturing risks?
  - Transportation risks? Staging risks?
Other Practical Considerations

- How do you assure the hoped for savings in any CIP?
  - Is the bid specified with and without the CIP?
  - Do you have to audit the rating base on other contractor coverage to see the premium savings?
Other Practical Considerations

- Rolling wrap ups? What are they? Have you used them and what are their advantages and disadvantages?

- How is warranty period work covered? Sometime a CIP will exclude it from ongoing operations and yet it may not be part of completed operations.