

BREAKOUT SESSION

# Contractual Risk Transfer

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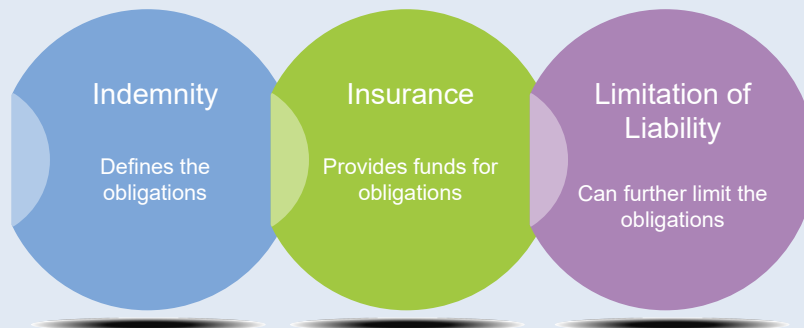
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## The "Basics"



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## TYPES OF INDEMNITY

Type	Indemnitor/ Contractor Negligence	Indemnitee/ Utility Contributory Negligence	Indemnitee/ Utility Sole Negligence	Language "Tells"	Comments
Broad Form	✓	✓	✓	Including caused in whole or in part by Utility	Prohibited by most states
Intermediate Form	✓	✓		Only if caused in whole or in part by Contractor	If Indemnitor's negligence was a contributory cause, Indemnitee's degree of negligence doesn't matter
Comparative Form	✓			But only to the extent caused by the negligent acts of Contractor	Contractor responsible only to the extent a loss arises from its negligence

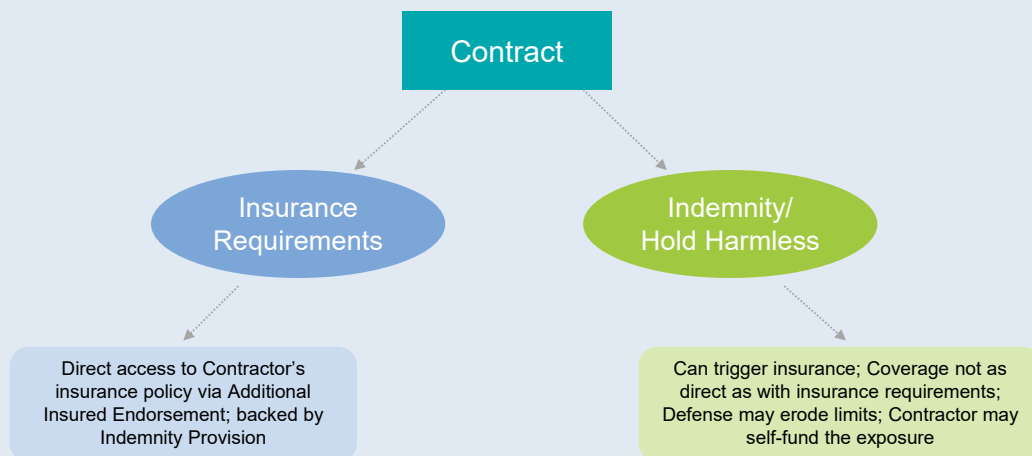
## INDEMNIFICATION CAVEATS & CONSIDERATIONS

- Anti-Indemnity Statutes
  - Statutory limitation on breadth of allowable indemnification
    - Indemnitee's sole negligence
    - Indemnitee's sole or partial negligence
    - Additional Insured "loophole"
  - Typically applies to construction contracts
- Mutual Indemnity
  - Each party agrees to indemnify the other to its own degree of fault
  - Not recommended – Can add complexity in a litigated claim
- Savings Clause
  - To the fullest extent permitted by law

## INDEMNIFICATION CAVEATS & CONSIDERATIONS

- Specific Indemnity Provisions
  - Third Party Bodily Injury & Property Damage
    - Specify includes defense
    - Specify includes claims by Contractor's employees:
      - Wages & benefits
      - Action over / contractor employee injury
  - Environmental Damage
  - Confidentiality / Breach of Confidentiality

## TRIGGERING INSURANCE



## INDEMNITY VS. INSURANCE

### Additional Insured Protection May be Broader than Indemnity

- Insurance may not be limited by anti-indemnity statutes
- “Step into the shoes of the Named Insured”
- Direct access to the insurer
- Right to immediate defense, and defense typically outside the insurance limits
- Helps prevent subrogation against the Utility

### Indemnity May be Broader than Insurance

- Contractor may still be financially responsible for damages not covered by insurance

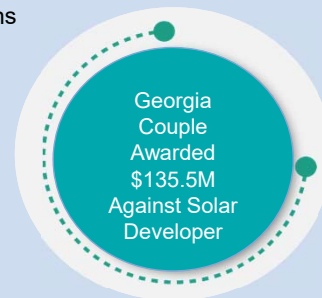
### Avoid Tying Insurance to Indemnity



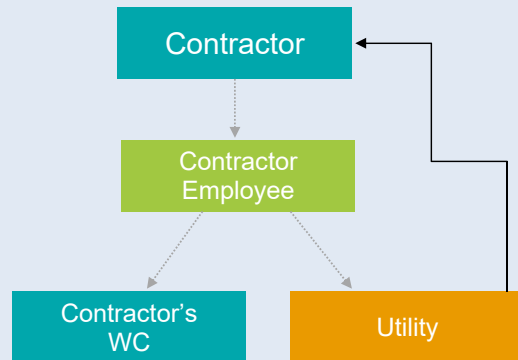
## INSURANCE REQUIREMENTS

Types of Insurance Required	Severability of Interests	Cancellation/Policy Changes
"Minimum" Limits; Follow Form	Waiver of Subrogation	Insurer Security- AM Best Rating
Primary/Non-Contributory	Occurrence/Claims Made Form	Insurance Certificate Requirements
Additional Insured	Deductibles/Retentions Allowed	Affirmative Coverage Requirements

- Insurance does not limit Contractor's other contractual obligations
- Flow down requirement to subcontractors
- Limits may vary greatly depending on risk
- Savings Clause – “To the fullest extent permitted by law”
  - Additional Insured
  - Waiver of Subrogation
  - Punitive Damages



## ACTION OVER CLAIMS



- WC Exclusivity Rule
- Waiver of Subrogation Considerations

## LIMITATION OF LIABILITY

- Limits the Liability of the Contractor to the Utility
  - Third Party Injury
- Common Asks by Contractor
  - Cap to contract amount
  - Cap to amounts paid/amounts received
  - Cap to insurance payments
  - No liability for consequential or indirect damages
  - No liability for business interruption, failure to supply or loss of use
- Emerging Ask
  - Cap for gross negligence for Hail Stow Services
- Utility Required Limitations of Liability



## LIMITATIONS OF LIABILITY

*Suggested Carve-Outs for Utilities*

Indemnity Obligations

Breach of Confidentiality

Insurance Recoverables

Insurance Deductibles

Warranty Obligations

Liquidated Damages

Gross Negligence / Willful Misconduct / Punitive Damages

## DO'S AND DON'TS



- Include a “savings clause”
- Seek the broadest indemnification permitted by your state
- Carefully review Insurance Requirements & Limitations of Liability



- Tie indemnity to insurance
- Allow indemnity to be limited to gross negligence/willful misconduct
- Use mutual indemnity, or only use if necessary

# Challenges to successful contract risk transfer

As told by a non-attorney...

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## CHALLENGES TO SUCCESSFUL CONTRACT RISK TRANSFER

*As told by a non-attorney...*

**An insurance policy is a contract that transfers risk to an insurer.**

### **Coverage Terms and Conditions:**

- Some coverage is conditional: on warranties, on following OEM specifications, on accurate reporting of values, on timely reporting of losses...
- Some coverage is limited: natural catastrophe, extra expense, ingress/egress, and of course, total policy limits!

### **Policy Exclusions:**

- It's equally important to understand what is **not covered** as it is to understand what is covered.
- Exclusions can apply to equipment type, operations, or even the mere existence of something.

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### Underlying coverage is deficient. What about AEGIS or another follow-form excess?

**Contractual Indemnity:** If the primary policy does not provide contractual liability coverage - i.e., coverage for the policyholder's contractual indemnity obligation to a third party (which exists by virtue of the "insured contract" exception to the "contractual liability" exclusion), then the follow-form coverage on the excess won't cover it either.

**Additional Insured Status:** The AEGIS form has ITS OWN "additional insured status" provisions, which, it appears, can operate independently of the primary.



## CHALLENGES TO SUCCESSFUL CONTRACT RISK TRANSFER

*As told by a non-attorney...*

### Case Study & Case Law – AI and Indemnity

**The Contract:** Vessel charter - The contracting parties (Halliburton chartered a vessel from McCalls Boat Rentals) agreed to indemnify each other for job-related liabilities and to back up the cross-indemnity provisions with insurance.

**The Contract Requirements:** While the cross-indemnity provisions were effectively identical, the parties agreed to treat the insurance provisions backing up their indemnities quite differently.

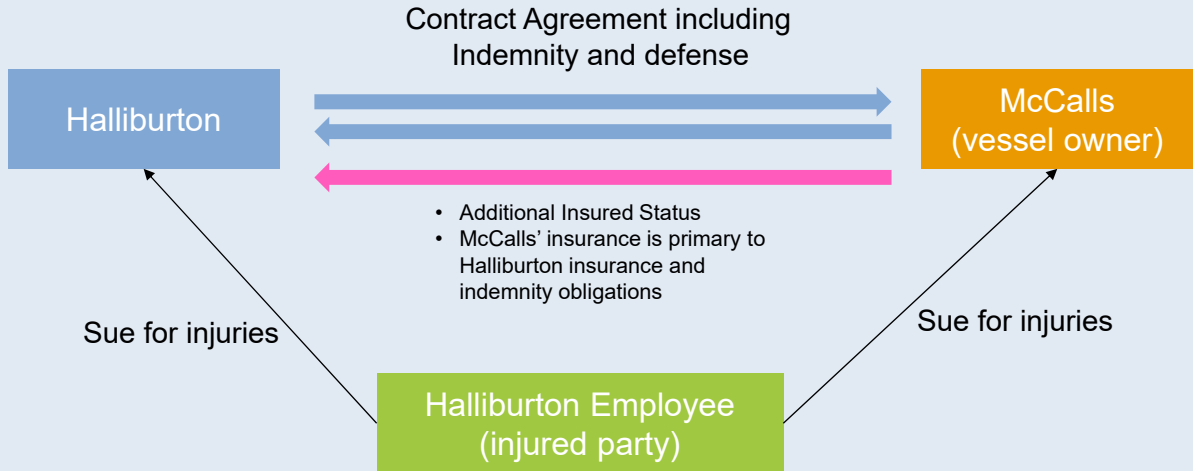
**The Facts:** Halliburton was required to insure the liabilities it assumed under contract with a CGL policy with suitable maritime endorsements. McCalls agreed to maintain P&I and CGL coverage and shall name Halliburton as AI. **All McCalls insurance required by the contract are primary as respects AI, irrespective of any excess or other insurance.**





## CHALLENGES TO SUCCESSFUL CONTRACT RISK TRANSFER

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## CHALLENGES TO SUCCESSFUL CONTRACT RISK TRANSFER

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### Case Study & Case Law – AI overturns Indemnity

**The Issue:** Underlying contract can overturn a carefully negotiated indemnity with a sloppy AI provision.

**Case and Result:** *Tullier v. Halliburton Geophysical Servs. (appellant) v. McCalls Boat Rentals, Inc. (appellee)* - The appeal court found that as appellee agreed to provide additional assured coverage for appellant under the terms of the agreement, **it had to exhaust that coverage before seeking indemnification from appellant.**

**The Facts:** Halliburton employee was injured in galley of McCalls' vessel and filed suit against both parties. Under the terms of the charter agreement, they agreed to indemnify and defend each other from claims brought by indemnitor's employees. In addition, McCalls agreed to provide AI status to Halliburton. The appeals court found that a party, such as appellee, who entered into a contractual indemnity provision, but who names the indemnitor, appellant, as an additional assured under its liability policies, had to first exhaust the insurance it agreed to obtain before seeking contractual indemnity. The court ruled this way because the agreement required appellee to provide coverage on a primary basis to appellant.

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## CHALLENGES TO SUCCESSFUL CONTRACT RISK TRANSFER

*As told by a non-attorney...*

### Case Study & Case Law – AI and Indemnity

**The Contract:** Drilling Contract – Drilling rig owner agrees to provide AI status under its policies to oil field developer to the extent of coverage provided by rig owner’s policies.

**The Facts:** Texas law affirms that a separate contract can be incorporated into an insurance policy by an explicit reference clearly indicating the parties’ intention to include that contract as part of their agreement.

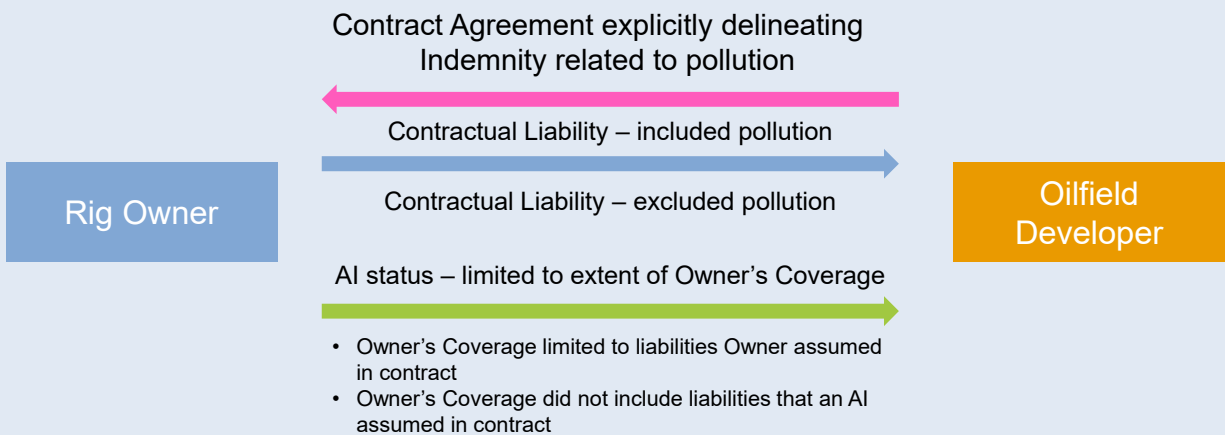
An insurance policy may incorporate an external limit on additional-insured coverage. By tying additional-insured coverage to the terms of an underlying agreement, the parties procure only the coverage the insured is contractually obligated to provide, thereby minimizing the insurer’s exposure under the policy and the named insured’s premiums.

The contractual duties to indemnify and to maintain insurance may be separate and independent. Consequently, a statute invalidating an indemnification clause does not relieve a party of a separate duty to obtain insurance.



## CHALLENGES TO SUCCESSFUL CONTRACT RISK TRANSFER

*As told by a non-attorney...*



## CHALLENGES TO SUCCESSFUL CONTRACT RISK TRANSFER

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### Case Study & Case Law – AI does not overturn Indemnity

**The Issue:** Underlying contract tie insurance coverage to a carefully structured indemnity obligation.

**Case and Result:** *In re Deepwater Horizon: BP (oil field developer) v. Transocean (rig owner)* - The issue presented concerns only the extent of insurance coverage afforded to BP, as an AI under primary and excess insurance policies procured by Transocean. The court found that BP's status as an AI was limited to the liabilities Transocean assumed in the drilling contract; BP was not entitled to coverage under the Transocean insurance policies for damages arising from subsurface pollution because BP, not Transocean, assumed liability for such claims in the drilling contract.

**The Facts:** The contracting parties had the wherewithal to negotiate and agree to detailed insurance and indemnity requirements in the subject drilling contract. Because Texas law allows insurance policies to contemplate applicable contract terms and requirements when they are deliberately and explicitly tied to the applicable policies, coverage extended to the Additional Insured can limited to the extent of liabilities assumed by the indemnitor in the contract.



## CHALLENGES TO SUCCESSFUL CONTRACT RISK TRANSFER

*As told by a non-attorney...*

When do we discover problems?

- Potential claim...
  - and you're seeing applicable contract(s) for the first time
- Successfully closed an acquisition...
  - and now you begin contract review
- Successfully complete a financing arrangement...
  - and now you have to certify compliance
- Successfully execute a contract...
  - and now you review the insurance requirements
- Start negotiating a contract...
  - and the insurance requirements are blank



# How can risk management play a role?

## UNS ENERGY'S APPROACH

Enhance communication channels between Procurement, Legal and Risk Management

Establish a procedure/ guidelines to streamline the contract process

Educate others on risk transfer techniques

### Insurance Playbook Objectives:

Streamline insurance exception requests

Review service categories & recommended insurance limits and provisions

Establish a contract / insurance guide for Procurement, Legal and Risk Management

Provide examples of insurance application through real-life scenarios

## SNAPSHOT OF THE PLAYBOOK (SERVICE CATEGORIES)

Service	General Liability/ Excess Liability	Auto Liability	Workers' Compensation & Employers Liability	Pollution Liability/ Environmental Impairment Liability	Cyber Liability	Professional Liability	Property/ Builders Risk	Additional Coverage Considerations
Additional Insured	Yes	Yes	No	No	No	No	No	
Loss Payee							Yes	
	Per Occurrence/ General Aggregate & Completed Ops Aggregate	Each Accident	WC Benefits/ EL Limits for BI by Accident & Disease	Each Claim / General Aggregate	Each Claim / General Aggregate	Each Claim / General Aggregate	Yes/No	
Residential and commercial energy efficiency program implementers								
ELECTRICAL GENERAL & LOW VOLTAGE	\$2,000,000 / \$4,000,000	\$1,000,000	Statutory / \$1,000,000					CGL Additional Insured Ongoing and Completed Operations
ELEVATOR	\$5,000,000 / \$10,000,000	\$1,000,000	Statutory / \$1,000,000					
EMBROIDERY LAUNDERING	\$2,000,000 / \$4,000,000	\$1,000,000	Statutory / \$1,000,000					
ENGINEERING CIVIL	\$2,000,000 / \$4,000,000	\$1,000,000	Statutory / \$1,000,000			\$2,000,000 / \$4,000,000		For large projects over \$100k, or projects involving Power Plants or road design, consult with Risk Management
ENGINEERING ELECTRICAL	\$2,000,000 / \$4,000,000	\$1,000,000	Statutory / \$1,000,000			\$2,000,000 / \$4,000,000		
ENVIRONMENTAL								
Transportation, storage, processing, and/or disposal of non-hazardous wastewater & Transportation of non-hazardous waste	\$1,000,000 / \$2,000,000	\$1,000,000	Statutory / \$1,000,000	\$1,000,000 / \$1,000,000				1. Ensure Auto Liability includes coverage for pollution. 2. If vendor is storing waste, include CGL Additional Insured Ongoing and Completed Operations
Transportation, storage, recycling, processing, or incineration of used oil including non-de Minimis oily wastewater Disposal of non-hazardous waste	\$2,000,000 / \$4,000,000	\$1,000,000	Statutory / \$1,000,000	\$2,000,000 / \$2,000,000				1. Ensure Auto Liability includes coverage for pollution. 2. If vendor is storing waste, include CGL Additional Insured Ongoing and Completed Operations
Transportation, treatment, storage, or disposal of hazardous waste, PCB, and/or asbestos	\$5,000,000 / \$10,000,000	\$1,000,000	Statutory / \$1,000,000	\$5,000,000 / \$5,000,000				1. Ensure Auto Liability includes coverage for pollution. 2. If vendor is storing waste, include CGL Additional Insured Ongoing and Completed Operations

## PLAYBOOK OUTCOMES



Enhanced relationships with key stakeholders



Established a best practice through a streamlined process



Broadened understanding of insurance for other departments



Increases Risk Management's participation with key business transactions

## RECOMMENDATIONS ON INITIATING A PROCESS



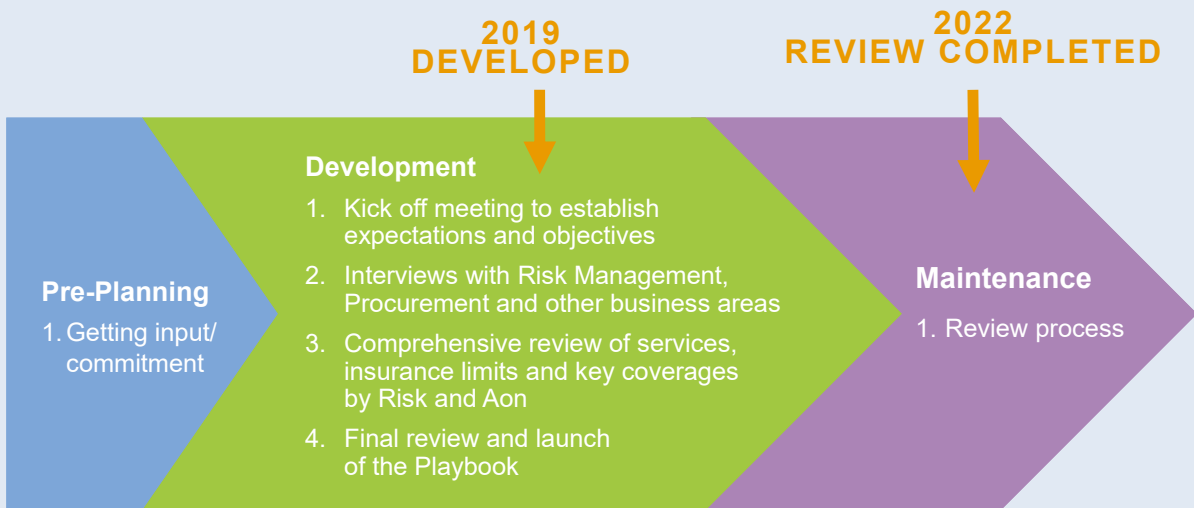
- Map out a plan
- Engage stakeholders early on and get buy in up front
- Have a shared goal/ purpose
- Maintain flexibility
- Build in back up positions
- Make continuous improvements/ updates
- Communicate and educate

## KEY TAKEAWAYS

- Establish solid relationships with key stakeholders among the organization involved in contracts (i.e., Procurement & Legal)
- Develop ways to streamline the contract review process
  - Templates, processes/guidelines
- Stay current on emerging risks, trends, court decisions, etc. and keep your processes and recommendations in line with industry best practices
- Continue to communicate and educate with your teams internally and externally

# Appendix

## PLAYBOOK DEVELOPMENT PROCESS



## EXCEPTION REVIEW FORM

### Scope of Services

#### Briefly Describe

For Master Service Agreements/Master Scopes of Work: Is there a potential to use this vendor in the future? If so, what types of services would be considered?

Where are the services being rendered? (Onsite, Offsite, Tucson Power Plant, etc.)

If onsite, will they be escorted?

If offsite, are the services being provided in a remote location or a more densely populated location?

How often will this service be used (Daily, Monthly, Annually, or as needed)?

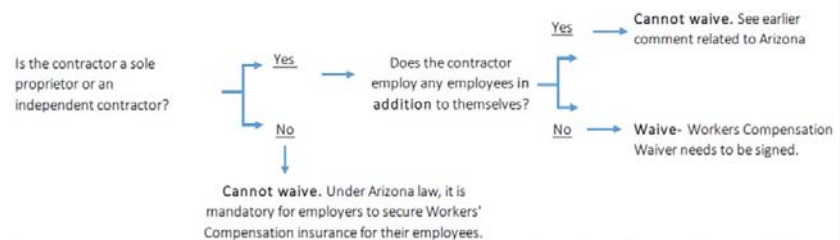
For IT counterparties: Will they have access to our systems? If so, will they have access to any PII or CIP?

## DEVELOPING FALL BACK POSITIONS

### Example 1: Automobile Liability



### Example 2: Workers' Compensation







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