

# The Perils of Additional Insured Provisions

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### Risk Allocation

- Mechanisms for limiting and allocating liabilities among parties:
  - Indemnities
  - Releases or exculpatory clauses
  - Insurance, including contractual liability coverage and additional insured provisions
  - Damage limitation clauses



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### Risk Allocation

- The purpose is to limit and define risks.
- We do not want to inadvertently create new risks that arise from the contractual risk management provisions themselves.



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### Risk Allocation

- The purpose is to limit and define risks.
- We do not want to inadvertently create new risks that arise from the contractual risk management provisions themselves.



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### Indemnities

- Not favored in the law.
- Special drafting requirements.
  - Express Negligence or Clear and Unequivocal
  - Must be conspicuous in many states.
  - Strictly construed.
- May be prohibited by statute.



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### Indemnities

- Fair Notice Requirements
  - Express Negligence Rule.
    - Indemnity must expressly say that negligence (and strict liability) is covered.
  - Must be conspicuous.



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### Indemnities

- Example of insufficient language
  - “Contractor agrees to ... indemnify owner... from and against any and all claims ... of every kind and character whatsoever ... in connection with loss of life or personal injury ... directly or indirectly arising out of ... the activities of contractor ... *excepting only claims arising out of accidents resulting from the sole negligence of owner.*”



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### Indemnities

- Example: Private Hanger Agreement
  - “Tenant agrees to indemnify ... [owner]... from and against losses of every kind and character ... that arise out of (i) this Agreement ... *[except] losses that arise solely from the negligent acts or omissions of [owner] ....*”



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### Contractual Liability Coverage

- Coverage for a contractually assumed liability.
  - Generally, but not always, coverage for an indemnity obligation.



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### Contractual Liability Coverage

- Policies typically exclude coverage for:
  - Bodily injury or property damage for which the insured is obligated to pay damages by reason of the assumption of liability in a contract ...
  - *Except* liability:
    - Assumed in a contract ... that is an insured contract, or
    - That the insured would have in the absence of the contract.



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### Contractual Liability Coverage

- Under the exception to the exclusion, a party is covered for tort liabilities it has assumed by contract – typically, indemnity obligations:
  - The indemnitor is the covered party.
  - The indemnitee benefits only indirectly because the indemnitor’s solvency is insured.




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### Contractual Liability Coverage

Indemnitee ← Indemnitor  
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 Insurer




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### Additional Insured Provisions



*"And, for insurance purposes, you must buy insurance."*




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### Additional Insured Provisions

- Law favors maintaining financial responsibility via insurance.
- Liberally construed
- No special drafting requirements
- Depending on jurisdiction, may or may not be subject to anti-indemnity statutes





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### Additional Insured Provisions

- *Getty Oil Co. v. INA*, 845 S.W.2d 794 (Tex. 1992).
  - “Prohibited indemnity provisions make the indemnitor liable for the indemnitee’s negligence. Additional insured provisions, on the other hand make the insurance purchaser’s insurers liable for the loss caused by the insured’s negligence. The insurance-purchaser is responsible only for the insurance premiums, presumably far less than the actual loss.”
  - Refused to apply express negligence rule.
  - Refused to apply oil-field anti indemnity statute.





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### Additional Insured Provisions

- “Mid-Continent’s first argument does not require us to determine whether Swift was entitled to indemnity .... Rather, it requires us to answer the different question of whether Swift should be denied coverage as an additional insured under the Policy because the MSA is not an ‘insured contract.’ *The presumptions involved in these different contexts are diametrically opposed.* [U]nder Texas law indemnity agreements are strictly construed in favor of the indemnitor (here, Air Equipment). ... By contrast, insurance policies are strictly construed in favor of coverage (for Swift).”
- *Mid-Continent Cas. Co. v. Swift Energy Co.*, 206 F.3d 487 (5th Cir. 2000)





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### Additional Insured Provisions

- Where a party is an additional insured, the insurance company has a direct obligation to the additional insured.



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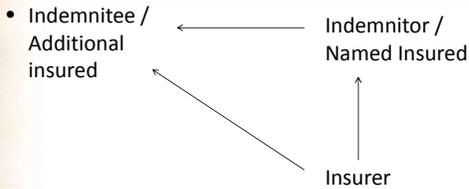
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### Additional Insured Provisions



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### Risks Associated with Various Approaches



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**Indemnities: Risks**

- Risk based on the indemnitor’s financial condition.
  - Indemnitee risks the indemnitor not being able to fund its indemnity obligation.
  - Indemnitor risks directly bearing the loss.
  - Both risks can be mitigated with contractual liability coverage.



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**Indemnities: Risks**

- Failure to understand how the indemnity provision will operate.
  - “B” agrees to indemnify “A” even if “A” is negligent, except if “A” is solely negligent.
    - What if a third party is negligent?
    - What if the indemnitee has joint and several liability with an insolvent third party?
    - What if the indemnitee has its own obligation to indemnify a third party?



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**Additional Insured Clauses**

- May be perceived as less risky for both contracting parties.



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### Additional Insured Clauses

- Contractor may perceive less risk because the insurer, not the contractor, is to bear the liability directly.
  
- Additional insured endorsements may be relatively inexpensive for a company being required to extend its coverage to another company.



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### Additional Insured Clauses

- For a company with a large SIR, being an additional insured on someone else's policy may provide an immediate first-dollar benefit.



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### Additional Insured Clauses

- Additional insured may perceive less risk because:
  - It is relying on the insurer rather than the other contracting party for payment.
  - It is always good to have more insurance, isn't it?



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### Additional Insured Clauses

- The real risks of additional insured clauses are more complicated and difficult to anticipate.
- Often lead to litigation.
- Often misunderstood by both the parties and the courts.
- Have unanticipated pitfalls.



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### Risks for Additional Insureds

- Litigation risk.
- Risk of misunderstanding the scope of coverage.
- Risk of disputes among multiple insurers.



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### Risks for Additional Insureds



"Your health plan covers everything but your deductible is equal to your net worth."



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### Risks for Additional Insureds

- *Phillips Petroleum Co. v. St. Paul Fire & Marine Ins. Co.*, 113 S.W.3d 37 (Tex. App.—Houston [1st Dist.] 2003, pet. denied).
  - Contract required Zachry to carry “Commercial General Liability Insurance on an occurrence form with a combined single limit of \$1,000,000 per occurrence...”, and name Phillips as an additional insured.
  - Zachry obtained a \$1,000,000 CGL policy with a \$1,000,000 deductible.
  - Defense costs eroded limits.




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### Risks for Additional Insureds

- *Phillips Petroleum Co. v. St. Paul Fire & Marine Ins. Co.*, 113 S.W.3d 37 (Tex. App.—Houston [1st Dist.] 2003, pet. denied).
  - “[O]ther than the limits of coverage required, the [contract] does not expressly specify the type of commercial general liability coverage that Zachry was required to purchase.”




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### Risks for Additional Insureds

- *Phillips Petroleum Co. v. St. Paul Fire & Marine Ins. Co.*, 113 S.W.3d 37 (Tex. App.—Houston [1st Dist.] 2003, pet. denied).
- Even if the contract had more clearly specified the type of policy:
  - “[T]he policy’s additional insured endorsement language ... naming Phillips as an additional insured ... ‘as required by contract ...’ is not, as argued by Phillips, ‘an explicit reference clearly indicating the parties’ intention’ to include the terms and provisions of the [contract] as part of the policy.”




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### Risks for Additional Insureds

- How do you verify your coverage as an additional insured?
  - “THIS CERTIFICATE IS ISSUED AS A MATTER OF INFORMATION ONLY AND CONFERS NO RIGHTS UPON THE CERTIFICATE HOLDER. THIS CERTIFICATE DOES NOT AMEND, EXTEND OR ALTER THE COVERAGE AFFORDED BY THE POLICIES BELOW.”



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### Risks for Additional Insureds



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### Risks for Additional Insureds

- Disputes among multiple insurers.
  - *Evanston Ins. Co. v. ATOFINA Petrochemicals, Inc.*, 256 S.W.3d 660 (Tex. 2008).
  - An additional insured's own insurance may refuse to pay on the basis that the additional insurance should be primary.
  - This leaves the additional insured footing the bill until the insurance dispute is resolved.



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### Risks in Extending Coverage

- The insurance and the underlying contract must be consistent with each other.



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### Risks in Extending Coverage

- Risk of breach.
- Risk of depleting coverage.
- Risk of losing coverage.



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### Risks in Extending Coverage

- Risk of breach.
  - If the coverage provided is not at least as broad as the coverage required by the contract, the party extending coverage could be liable for what the insurance should have covered.
  - May also be liable for attorneys' fees.
  - Unlike an indemnity obligation, breach of contract is unlikely to be covered by insurance.



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### Risks in Extending Coverage

- Risk of breach.
  - *Getty Oil Co. v. INA*, 845 S.W.2d 794 (Tex. 1992).
  - “All insurance coverages carried by Seller, whether or not required hereby, shall extend to and protect [Getty] ... to the full amount of such coverages...”.
  - Court construed this as an additional insured requirement.




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### Scope of Coverage

- What is the role of the underlying contract on the scope of coverage afforded to an additional insured?
  - Insurers argue that the scope of coverage is restricted by the underlying contract; typically, by the indemnity provisions in the underlying contract.
  - Insureds argue that the underlying contract does not restrict coverage.




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### Scope of Coverage

- Why would the parties go out of their way to restrict a party’s indemnity obligation and then “undo” those limitations through a broad additional insured provision?
  - Possibly because people are more comfortable shifting liability to their insurer than taking it on directly through indemnity agreements.
  - “[I]ndemnity provisions make the indemnitor ... liable for the indemnitee’s ... negligence. Additional insured provisions ... make the insurance-purchaser’s insurers ... liable for the loss caused by the insured’s ... negligence. The insurance-purchaser is responsible only for paying the insurance premiums....”




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### Scope of Coverage

- *Getty Oil Co. v. INA*, 845 S.W.2d 794 (Tex. 1992)
  - “The indemnity provision in paragraphs 3-4 of [the contract] is supported by an insurance provision separate from and additional to the additional insured provision in paragraphs 1-2. ... Thus, the additional insured provision of the contract does not support the indemnity agreement, but rather is a separate obligation.”




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### Scope of Coverage

- Courts started to look to see if the indemnity provision was supported by its own separate insurance provision and, if not, they concluded that the additional insured provision merely supported the indemnity.
  - *E.g., BP Chemicals v First State Insurance Co.*, 226 F.3d 420 (6th Cir. 2000).




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### Scope of Coverage

- This was clarified in *Evanston v. Atofina*.
  - “ATOFINA does not seek indemnity from Triple S; it claims instead that it is entitled to indemnification from Evanston by virtue of its status as an additional insured on the umbrella policy Evanston issued.... *Instead of looking ... to the indemnity agreement in the service contract to determine the scope of any coverage, we base our decision on the terms of the umbrella insurance policy itself.*”




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### Scope of Coverage

- But some confusion remains.
  - “[W]e have also noted that *where an additional insured provision is separate from and additional to an indemnity provision, the scope of the insurance requirement is not limited by the indemnity clause.*”
  - *Evanston v. Atofina*, (citing *Getty v. INA* in a footnote).



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### Scope of Coverage

- The Rule:
  - Look to the Policy to determine the scope of coverage.
  - If the Policy language incorporates limitations from the underlying contract, then look to the underlying contract.



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### Scope of Coverage

- The Hard Part:
  - Deciding whether the Policy language is sufficient to incorporate limitations from the underlying contract.
  - Ambiguous language is construed in favor of the insured.



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### Scope of Coverage

- “Texas law has long provided 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.”
- *Urrutia v. Decker*, 992 S.W.2d 440, 442 (Tex.1999).





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### Scope of Coverage

- Sufficient Language
- *Urrutia v. Decker*:
  - “WHO IS AN INSURED... is amended to include the following:
    - C. Both lessees and rentees of covered autos ..., *but only to the extent and for the limits of liability agreed to under contractual agreement with the named insured.*





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### Scope of Coverage

- Sufficient Language
- *Becker v. Tidewater*:
  - “In no event shall Insurance coverage be afforded hereunder to such other assureds to any greater extent than that which the Named Insured [Tidewater] is expressly obligated by contract to provide.”





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### Scope of Coverage

- Sufficient Language
- *Aubris Resources v. St. Paul Fire and Marine:*
  - Policy: “Any person ... that you agree ... to add as an additional protected person under this agreement is also a protected person for the following *if that written contract for insurance specifically requires such coverages for that person...*”.





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### Scope of Coverage

- Sufficient Language
- *Aubris Resources v. St. Paul Fire and Marine:*
  - Underlying contract: “United ... shall be named as additional insureds in each of Contractor's policies ... however, *such extension of coverage shall not apply with respect to any obligations for which UNITED has specifically agreed to indemnify Contractor.*”





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### Scope of Coverage

- Sufficient Language
- *Aubris Resources v. St. Paul Fire and Marine:*
  - Court found coverage because, while there was a general indemnity from United to the Contractor, there was no *specific* indemnity related to the underlying litigation at issue.
  - Because the contract was incorporated into the policy, the court construed ambiguities in favor of coverage.





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### Scope of Coverage

- Insufficient Language
- *Evanston v. Atofina:*
  - A person or organization *for whom you have agreed to provide insurance as is afforded by this policy*; but that person or organization is an insured only with respect to operations performed by you or on your behalf, or facilities owned or used by you.




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### Scope of Coverage

- Insufficient Language
- *Saavedra v. Murphy Oil United States:*
  - “[A]dditional insureds are covered under this policy as required by written contract, but only with respect to operations performed by or for the named insured [Lou-Con].”
  - *See also, Phillips Petroleum Co. v. St. Paul Fire & Marine.*




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### Scope of Coverage

Case 2:10-md-02179-CJB-SS Document 4588 Filed 11/15/11 Page 1 of 42

UNITED STATES DISTRICT COURT  
EASTERN DISTRICT OF LOUISIANA

In re: Oil Spill by the Oil Rig	•	MDL No. 2179
“Deepwater Horizon” in the Gulf	•	
of Mexico, on April 20, 2010	•	SECTION: 4(i)
This Document Applies to:	•	JUDGE BARBER
11-274 c/w 11-275	•	MAGISTRATE JUDGE SHUSHAN
	•	

.....

ORDER AND REASONS  
[As to the Insurance Actions]

Before the Court are the Motion for Judgment on the Pleadings in the Insurance Actions (Rec. Doc. 3211) filed by BP Exploration & Production, Inc. and its related entities (collectively,



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### Scope of Coverage

- The contract required BP to be named as an additional insured: “in each of [Transocean’s] policies, except Workers’ Compensation for liabilities assumed by Transocean under the terms of this Contract.”



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### Scope of Coverage

- The policies defined Insured to include:
  - Any person or entity to whom the “Insured” is obligated by any oral or written “Insured Contract” ... to provide insurance such as is afforded by this Policy....
- And they defined “Insured Contract” as:
  - [a]ny written or oral contract ... entered into by the “Insured” ... under which the Insured assumes the tort liability of another party ...



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### Scope of Coverage

- The issue was the extent of “additional insured” coverage, if any, to which BP is entitled by virtue of the insurance contracts procured by Transocean as the named insured.
  - Narrow coverage: Only to the extent Transocean is obligated to indemnify BP.
  - Broad coverage: Not limited by the Drilling Contract and interpreted solely in reference to the terms of the Insurance Policies.



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### Scope of Coverage

- BP’s argument.
- The missing comma: “in each of [Transocean’s] policies, except Workers’ Compensation for liabilities assumed by Transocean under the terms of this Contract.”
  - Let’s eat, Grandma.
  - Let’s eat Grandma.





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### Scope of Coverage

- Insurer’s argument:
  - “The Insurers start from the premise that the Court must look beyond the face of the Policies. The Court cannot ignore the underlying Drilling Contract. To do so would absurdly posit that TransOcean would apportion liabilities between itself and BP in the Drilling Contract, and then contradictorily afford BP boundless ‘additional insured’ protection for liabilities that BP specifically assumed in that same drilling contract.”





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### Scope of Coverage

- District Court’s analysis:
  - When the *ATOFINA* court proceeded to follow its own mandate of looking to the terms of the policy, it was face to face with a policy that made *absolutely no reference to the service contract in determining the scope of available insurance coverage, which is diametrically opposed to the Policies at issue in the present case.* The Policies issued to Transocean all refer to an “Insured Contract” under which Transocean assumes the tort liability of another entity.





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### Scope of Coverage

- District Court’s analysis:
  - The court felt that the policy’s reference to the underlying indemnity agreement was sufficient to use it to limit coverage.
  - “It is true that indemnity and insurance are two different things, involving contracts with different parties. But contrary to BP’s assertion, this statement is not an assertion that where, as in this case, the insurance policy references the underlying indemnity agreement, the court must ignore the indemnity agreement and – with tunnel vision – look solely at the insurance policy.”





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### Scope of Coverage

- Fifth Circuit reversed, and gave BP access to Transocean’s full \$750 million insurance stack.
- Relied heavily on *Evanston v ATOFINA*:
  - “This case law makes clear to us that *only the umbrella policy itself may establish limits upon the extent to which an additional insured is covered* in situations such as the one before us. ... [T]he policy itself does not contain any limitation on additional insured coverage nor incorporate any limits from the underlying Drilling Contract.”





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### Scope of Coverage

- On rehearing, the Fifth Circuit vacated its own decision and certified two questions to the Texas Supreme Court:





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### Scope of Coverage

- “Whether *Evanston* ... compels a finding that BP is covered for the damages at issue because the language of the umbrella policies alone determines the extent of BP’s coverage as an additional insured if, and so long as, the additional insured and indemnity provisions of the Drilling Contract are ‘separate and independent’?”




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### Scope of Coverage

- “Whether the doctrine of *contra proferentem* applies to the interpretation of the insurance coverage provision of the Drilling Contract under the *ATOFINA* case ... given the facts of this case?”




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### Risk of Losing Coverage

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF TEXAS  
HOUSTON DIVISION

ACE AMERICAN INSURANCE §  
COMPANY §  
§  
Plaintiff, §  
v. § Civil Action No. \_\_\_\_\_  
§  
M-L L.L.C. §  
Defendant. §

ACE AMERICAN INSURANCE COMPANY’S ORIGINAL  
COMPLAINT FOR DECLARATORY JUDGMENT

TO THE HONORABLE UNITED STATES DISTRICT JUDGE:

This Complaint for Declaratory Judgment is filed by ACE American Insurance Company (“ACE”) against M-L L.L.C. (“M-L”) pursuant to the Declaratory Judgment Act, 28 U.S.C. § 2201 and Rule 57 of the Federal Rules of Civil Procedure to determine an actual case or




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### Risk of Losing Coverage

- ACE's pleadings:
- BP is an additional insured under the ACE Policy issued to MI.
- The Policy contains an exclusion --
  - This insurance does not apply to: "Bodily injury" or "property damage" arising out of the ... use ... of any watercraft owned or operated by or rented or loaned to *any insured*.
- BP was leasing and using the *Deepwater Horizon* ... at the time of the Deepwater Horizon Incident.
- The Watercraft Exclusion operates to exclude coverage for *all insureds* under the ACE Policy including the Named Insured, MI.



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### Risk of Losing Coverage

- Be wary of any exclusion that excludes coverage based on the acts of "any insured."



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### Anti-Indemnity Statutes

- Over 40 states have Anti-Indemnity Statutes
  - They apply to various industries, including construction and transportation that can involve the aviation industry.
  - Some prohibit additional insured provisions.
  - Some do not.



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### Anti-Indemnity Statutes

- Section 151.001 et seq of the Insurance Code.
- Applies to “new or renewed” consolidated insurance programs for construction projects that begin on or after January 1, 2012.



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### Anti-Indemnity Statutes

- Enormous potential impact.
- Many additional insured cases arise in the construction context.
- Statute is broad.



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### Anti-Indemnity Statutes

- Section 151.001 et seq of the Insurance Code.
- A “construction contract” is:
  - “a contract, subcontract, or agreement, or a performance bond assuring the performance of any of the foregoing, entered into or made by an owner, architect, engineer, contractor, construction manager, subcontractor, supplier, or material or equipment lessor for the design, construction, alteration, renovation, remodeling, repair, or maintenance of ... a building ... or other improvement to or on public or private real property ....”



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### Anti-Indemnity Statutes

- So, if you have a contract that relates to building an airport or supplying steel for a building or even painting a hanger or repairing a jetway, this statute applies.





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### Anti-Indemnity Statutes

- “Agreement Void and Unenforceable:
  - “[A] provision in a construction contract, or in an agreement collateral to or affecting a construction contract, is **void and unenforceable** as against public policy **to the extent it requires an indemnitor to indemnify**, hold harmless, or defend a party, including a third party, **against a claim caused by the negligence or fault**, the breach or violation of a statute, ordinance, governmental regulation, standard, or rule, or the breach of contract **of the indemnitee**, its agent or employee, **or any third party under the control or supervision of the indemnitee other than the indemnitor or its agent, employee, or subcontractor of any tier.**” Section 151.102





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### Anti-Indemnity Statutes

- “Agreement Void and Unenforceable:
  - So, if you are the indemnitor, and you are under the control of the indemnitee, you can indemnify for your own negligence and the negligence of your subcontractors. Section 151.102
  - You can also indemnify for injuries to your own employees and your subcontractors’ employees. Section 151.103.





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### Anti-Indemnity Statutes

- “Unenforceable Additional Insurance Provision”:
  - “[A] provision in a construction contract **that requires the purchase of additional insured coverage**, or any coverage endorsement, or provision within an insurance policy providing additional insured coverage, is **void and unenforceable** to the extent that it required or provides coverage the scope of which is prohibited under this subchapter for an agreement to indemnify, hold harmless or defend.” Section 151.104(a).
  - “This section **does not apply to** a provision in an insurance policy, issued under a **consolidated insurance program** to the extent that the provision or endorsement lists, adds or deletes named insureds to the policy.” Section 151.104(b).




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### Anti-Indemnity Statutes

- Section 151.001 et seq of the Insurance Code.
- A “consolidated insurance program” is:
  - “a program under which a principal provides general liability insurance coverage, workers’ compensation coverage, or both that are incorporated into an insurance program for a single construction project or multiple construction projects.”




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### Anti-Indemnity Statutes

- “A consolidated insurance program that provides general liability insurance coverage, must provide completed operations insurance coverage for a policy period of not less than three years.” Section 151.051




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## Summary

- Know what is in your contracts.
- Make sure your policies are consistent with your contracts.
- Make sure you understand the language in your policies and contracts. Seemingly minor differences in language can have major impacts on how they are applied.
- Be aware of individual state's laws and how they impact your agreements.



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## The End

Please don't hesitate to contact me with questions.

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