

Repairing the Roof While the Sun is Shining

The Importance of Contract Review and Risk-Shifting Measures



In his first State of the Union Address in 1962, President John F. Kennedy said, “The time to repair the roof is when the sun is shining.”

With this wisdom, President Kennedy was instructing the nation on his belief that in good weather we need to prepare for the rain; or, in good times we need to prepare for the bad times that, inevitably, will come. The same is true with contracts. When drafting and negotiating a contract, it is imperative to formulate terms that will guard against risks, or “bad times,” that may come years after the contract is executed. This article will primarily focus on risk-shifting measures within a contract, like *indemnity*, *insurance coverage*, and *waivers of subrogation*, that will help protect your organization against those risks, or “bad times,” that will come.

While a contract can be as simple as an exchange of promises, most contracts will contain additional terms and conditions. It is within these terms and conditions that the risk-shifting provisions normally fall. To be a valid and enforceable contract, it does not need any risk-shifting provisions. These clauses only add clarity to the agreement between the parties under particular circumstances. Therefore, many contracts do not contain any of the terms discussed in this article. Even if these terms do not fall within a contract, it is advisable to seek professional assistance to assess whether adding such terms may be beneficial.

Indemnification

An indemnification clause is a promise to protect and defend another in the event a particular set of circumstances, as outlined within the clause, that leads to a loss, or potential loss, suffered by another party.

Indemnification provides an avenue to contract your exposure to potential risks to another party. In effect, when, and if, a party agrees to indemnify, defend, and hold you harmless, if a claim arises that fits within the parameters of the subject indemnification clause, you may tender the cost of the defense for such a claim to the other party, and, if a settlement or judgment is reached, the other party will pay your proportional share. There are several ways to draft and phrase an indemnification clause in order to shift risk. However, in any indemnification clause, you should be looking for key components that will ultimately allow your organization to shift your risks to the other party if a claim arises. These components include, (1) which party or parties are required to provide indemnification; (2) what type of claims are covered; (3) does the agreement require the indemnifying party to indemnify and defend; and (4) is the clause one-sided or mutual.

Coverage

When reviewing a contract, it is important to look for language that requires the other party to the contract to purchase and maintain insurance and to name your organization as an additionally insured party. Most insurance policies will provide coverage to a third party if the coverage provider’s insured promises to add that party as an additional insured, but only if the insured is bound to do so by a written contract. The amounts and types of coverage necessary can be different for each specific circumstance. However, when looking through a contract, you should be looking for language that provides your organization with protection outside of your own insurance company. Specifically, the contract language should provide that the other party will purchase and maintain coverage, in an agreeable amount, naming your organization as an “additional insured.” Also, to protect your organization and your coverage provider further, the language should provide that all coverage the other party has agreed to provide will be primary with respect to claims made, and any similar or additional coverage maintained by your organization will be excess to any coverage carried by the other party, including any excess coverage. This way, your organization’s coverage will only be affected and come into play if and when the resources of the other party’s coverage have been fully exhausted.

It is also advisable to include language within the coverage clause that the other party will provide proof of coverage in the form of a “Certificate of Insurance,” naming your organization as an “additional insured.” If possible, the contract should require the contracting party to provide copies of all applicable policies and endorsements. The Certificate should be provided prior to any performance under the contract; however, if it is not given to your organization before work under the contract is performed, the language in the

contract should provide that your organization has not waived its right to such protection. Moreover, if the other party ultimately fails to procure the agreed upon coverage, the clause should provide that your organization will be entitled to pursue a claim against the other party, including a claim for all attorneys’ fees and costs associated with such a claim.

Finally, documented on the Certificate of Insurance should be the relevant policy period for which the coverage will be effective. Typically, the policy period covers a 12 month period of time. Therefore, depending on the term of the particular contract, your organization may need to request subsequent Certificates of Insurance evidencing coverage for the appropriate time period. Moreover, at the time the contract is executed, your organization should make certain the original Certificate of Insurance provides for coverage during the agreed upon time period in the contract, and for a reasonable time period thereafter. Your organization needs to be aware of any lapses in coverage.

Waiver of Subrogation

A waiver of subrogation clause may protect you if the other party to a contract agrees to maintain insurance coverage; however, it can hinder your organization, and your insurance provider, if your organization has agreed to maintain insurance for the benefit of the other party. In practice, once a loss occurs, if one party has agreed to maintain insurance to protect the other party, the insurance company will be forced to cover the loss, even if it was caused by the negligence of the other party. If the contract also contains a waiver of subrogation clause, the insurance company will have no recourse to recoup these funds from the at-fault party. However, without the waiver of subrogation clause, the insurance company would be free to pursue a claim against the at-fault party.

Continued on page 25

“When drafting and negotiating a contract, it is imperative to formulate terms that will guard against risks, or ‘bad times,’ that may come years after the contract is executed.”

Repairing the Roof continued from page 23.

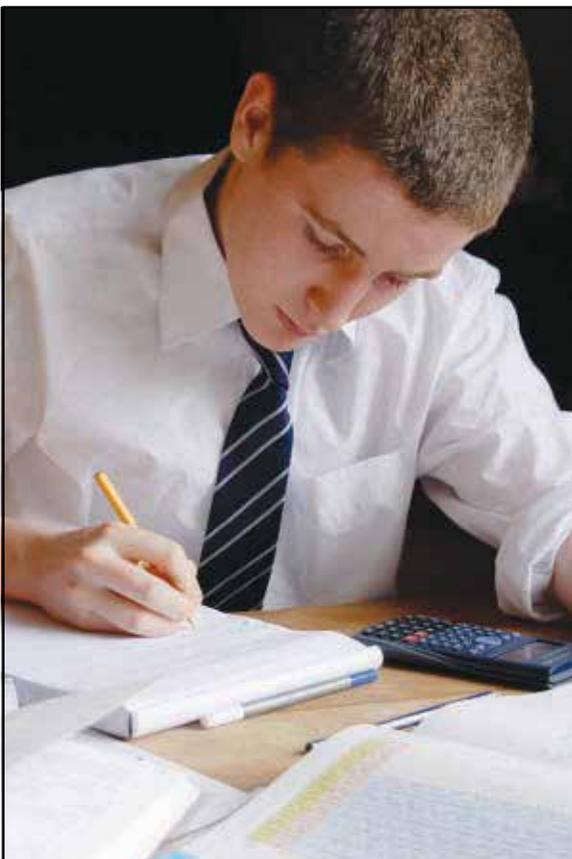
Therefore, when your organization agrees to maintain insurance coverage for both your organization and the other party, it will be important to look for a term within the contract that would waive your organization's ability, through its coverage provider, to pursue a subrogation claim against the other party. Of course, the converse is true, as well. If another party has agreed to maintain insurance for your organization, then a waiver of subrogation clause is recommended to protect your organization against a potential subrogation action by the other party's insurance company.

It is highly recommended that all contracts be reviewed by an attorney and/or insurance professional before agreeing to the terms, including any and all risk-shifting

terms. By carefully drafting and negotiating a contract before execution, during the "good times" while the sun is still out, you can best protect your organization from the rain during the "bad times" that will inevitably come.

Members of Christian Brothers Risk Pooling Trust have free access to risk evaluation of contracts and agreements by a contractual risk transfer analyst. Contact your account manager for more information. ☀

P. Patrick Cella is an attorney specializing in contract formation, policy implementation and complex civil litigation. He is a member of the law firm Kopon Airdo, LLC, which is the national coordinating council for Christian Brothers Risk Management Services.



Protect Your School and Students

Christian Brothers Services Tuition Refund Program

protects schools from the financial consequences of a student's forced or voluntary withdrawal prior to completion of the term or school year. This program pays benefits to the school, subject to the terms, conditions and

limitations of the Plan and provides substantial assistance in allowing the school to either cancel the parent's unpaid tuition obligation or refund the unused portion of tuition.

For more information on the
Tuition Refund Program
contact us at:
tuitionrefund@cbservices.org

