

MARSH INSIGHTS: CASUALTY KEEPING PACE WITH CHANGING COLLATERAL REQUIREMENTS: CARRIER DEMANDS, ALTERNATIVES, AND BEST PRACTICE STRATEGIES

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WHY INSURERS REQUIRE COLLATERAL

Under a large-deductible insurance policy, the insurer contractually agrees to pay all claims as they occur, while the policyholder is obligated to reimburse the insurer for all claims that fall under the deductible amount. To secure the policyholder’s liability, the insurer requires the insured to post collateral. This collateral requirement is intended to safeguard the insurer against risk by:

- Protecting against credit losses — carriers are liable through the statutory obligation of the deductible portion of the policy.
- Fulfilling statutory requirements levied upon the insurers by the states.
- Meeting financial rating agencies’ insurer surplus requirements, which is the ratio of total policyholders’ surplus to written premiums.
- Preserving their financial rating.

Recent changes have resulted in more stringent underwriting, increased collateral requirements, and higher costs of collateral. Much of this evolution is due to greater scrutiny of insurers’ financial accountability by rating agencies and regulators.

Insurers’ collateral requirements are also affected by the shrinking amount of available bank credit, client balance sheet strength or weakness, and insurers’ return on capital. Posting collateral has become an increasingly burdensome and expensive requirement for clients with loss-sensitive programs.

DRIVERS OF COLLATERAL AMOUNT

Insurers assess the amount and the price of collateral required on a case-by-case basis, taking into account an individual client’s unique factors, such as parental guarantees, pension obligations, union relationships, and debt maturity. The main drivers of collateral requirements include:



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1. The program structure and duration — retention/deductible level versus historical loss experience.
2. The actuarial loss projections and triangles, including historical policy years' ultimate losses and the traditional payout pattern of prior-year losses.
3. Results of a review of the client's historical, current, and *pro forma* financial statements, as well as the perspective on current trends, liquidity, debt/leverage, coverage ratios, etc. Financial reviews may vary by industry. For example, a client in an industry with a greater useful life of its assets may be viewed more favorably than a client in an industry where assets depreciate or become obsolete at a faster rate.
4. Completeness of underwriting data, including operational changes, losses, financials, potential M&A activity, banking relationships, legacy collateral outstanding, etc.
5. The existence of safety initiatives to prevent losses and protocols to mitigate losses after they occur.
6. Form of collateral — letters of credit (LOCs), trust, cash, surety, credit buydowns, etc.

pyramiding collateral that should be noted include:

- Losses are incurred and developed using client-specific or industry loss development factors (LDFs). LDFs contemplate increases in the original reserves and estimated incurred but not reported (IBNR) losses. This combination of developed old losses and newly occurring losses builds up at a much faster pace than losses are actually paid. Therefore, the collateral required by the insurer will pyramid over time.
- Until the actual paid losses for the cumulative policy years surpass the expected losses for the upcoming policy year combined with the developed outstanding losses for the cumulative policy years, the collateral amount required of a client will grow.
- The potential impact becomes highlighted and burdensome as each new policy year is added to the initial program.

Certain economic/financial improvements can help clients accelerate the reduction of the collateral pyramiding phenomena, including:

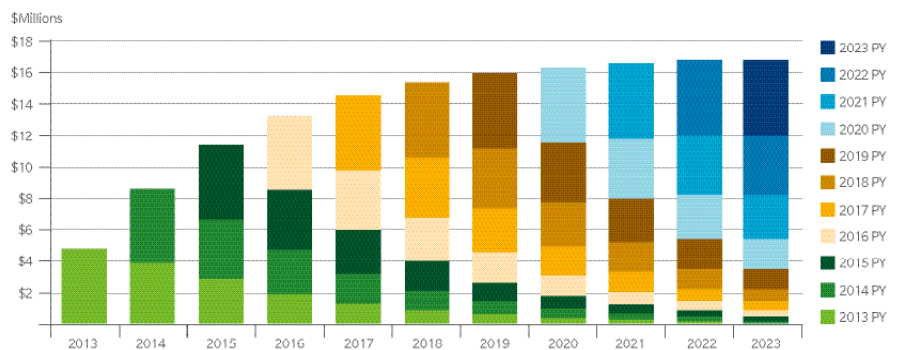
- Balance sheet strengthening: reduction of leverage as the result of improving profit-and-loss (P&L) results.
- Extension of debt maturity: less restriction on immediate cash outlay.
- Improved terms on the debt (rate and covenants).
- Secured debt versus unsecured debt.
- Improvement of cash flow from operations: ability to finance operations without using credit availability.
- The client's particular industry's improved projections/trends; for example, the homebuilding industry and how it was dramatically affected by the economy.

Pyramiding of collateral over a 10 year period for a company with an annual loss projection of US\$4.75 million and whose program continues to be written by the same carrier — all financial variables being equal — may see a growth in collateral similar to that illustrated by Figure 1 below.

PYRAMIDING COLLATERAL

An important consideration when selecting retention levels is that each increase in retention level may have a material impact on the collateral requirement. This is also an important consideration when determining whether or not to change carriers. Over time, there is a buildup of collateral that is commonly referred to as pyramiding. Insurers require additional collateral each year a program renews in order to maintain the proper ratio for security purposes. Factors around

Figure 1: Sample Pyramid Structure Over Ten Years



AVAILABILITY OF LETTERS OF CREDIT

Clients can obtain LOCs through their banks/financial institutions or, in some cases, through a third-party trust arrangement. The availability, as well as the cost of an LOC, greatly depends on the financial strength of the borrower and its relationship with its bank.

Some concern is arising regarding the cost and availability of LOCs simply from the amount of capital banks will have to allocate to the LOC obligation. This is due in part to capital requirements embedded in global standards — albeit tailored by country or regions like Eurozone — called Basel III. Basel III rules treat the LOCs as a contingent obligation very similar to a loan. Additionally, there are capital requirements on loans under Basel III. Many newly incepting credit lines — often called revolvers — already charge the same spread for LOCs as for money drawn off the revolver. These new capital requirements are not fully phased in; however, full implementation is scheduled over the next few years. Going forward, these new capital requirements may have a negative impact on both the availability and cost of LOCs.

An interesting development is that those banks that are considered “systemically important financial institutions,” which may be global or national, will have imposed on them capital requirements that will be more stringent. These are some of the largest LOCs-issuing banks in the US, as they are often the agent bank on credit lines. Often, the credit line is backed by a syndicate of banks with an agent essentially fronting the credit line.

The Basel III rules, while not yet fully understood, are not expected to have a positive impact on credit availability and/or its cost.

BANKS

As the result of the current state of the US and worldwide economies — combined with the new regulatory oversight — banks are becoming more restrictive on the total amount of LOCs they extend to their customers, and LOCs can be quite costly. In addition, insurance carriers have limitations or aggregates that restrict the total amount of LOCs they will accept from any one bank or financial institution over multiple insureds, thereby causing additional concerns for those posting collateral. Financial ratings by Moody’s, Fitch, or Standard & Poor’s can affect a carrier’s willingness to accept LOCs from a particular bank; but, in general, carriers will accept banks on the National Association of Insurance Commissioners (NAIC)-approved list. There may be exceptions to the NAIC requirement, but they are rare.

THIRD-PARTY TRUST ARRANGEMENTS

Third-party trust arrangements are viable alternatives to LOCs and are more prevalent than they have been in the past. They are usually only for clients that are experiencing a restriction of credit from their banks or investors and can provide LOC capacity for clients unable to secure their own LOCs. Under this arrangement, the client must provide cash as security to the third party, which in turn will provide the needed LOC to the insurance carrier.

COST OF LETTERS OF CREDIT

Banks and financial institutions are enjoying a period of heavy demand and shorter supply for LOCs, which allows them to price more conservatively. In addition to increased costs for LOCs, some clients (depending on their financial strength) are seeing a requirement to provide cash as collateral to the bank. Insurance carriers, however, have demonstrated an increased

willingness to look at alternative forms of collateral, which has in many cases improved the overall cost and preserved credit lines.

ALTERNATIVES TO CUSTOMARY LETTERS OF CREDIT

Carriers have recently become more flexible in accepting alternative forms of collateral to secure deductible responsibilities. These alternatives to the customary LOC come in varying forms and are inconsistently accepted by different carriers writing loss-sensitive casualty programs. Not all forms are universally accepted, and each needs to be negotiated based upon the carrier’s guidelines and the specific financial merits of each client.

The most common alternative forms of collateral are:

- **Trust, or pledge of security.**
- **Cash.**
- **Surety bond.**
- **Credit buydown.**

A **trust, or pledge of security**, arrangement is widely accepted by many carriers; however, the trust usually is in combination with a LOC. Trusts are simply cash or rated securities in the amount of the collateral needed. Not all carriers will accept a trust as a form of collateral; but in those circumstances in which they will, the overall cost for many clients will be less than the cost and constriction of credit imposed when securing a LOC.

Cash is an alternative that far fewer carriers will accept, as cash is not bankruptcy remote for 90 days. This lack of bankruptcy protection exposes the carrier to the potential of the loss of the cash collateral

to the trustee and other creditors. This can occur as a result of other liens the insured/client may have granted against the cash. Cash is a form of collateral that must be negotiated early and structured such that the carrier has minimized its exposure. In the circumstance of bankruptcy, cash can and usually will be considered by the bankruptcy courts as a challengeable asset of the client — therefore accessible by all creditors.

Surety can be an alternative form of collateral but is accepted by only a few carriers. In cases where surety is allowed, most carriers will limit the percentage of the total collateral they will accept as well as the provider of the surety. The standard percentage is no more than 25%, although some will go to 50%; and on a very rare occasion, a carrier may agree to 100% of the collateral in surety. The surety form used is not a customary surety bond, but rather structured to be a “demand instrument,” and must be approved by the carrier accepting the surety.

An increasing number of carriers will provide a **credit buydown** for a portion of the required collateral. A credit buydown is simply a credit charge paid to the insurance carrier in exchange for a reduction in required collateral. The amount of the credit charge varies considerably from one carrier to the next and depends heavily on the client’s financials. In circumstances where a client has a material restriction on its credit position with its lenders, the credit buydown alternative can serve it well.

COLLATERAL NEGOTIATION PROCESS

The process of negotiating collateral encompasses three distinct steps: modeling, financial review, and goal setting/tactical discussion and direction.

MODELING

The negotiation process should always begin with modeling and analysis of the existing collateral position, including:

- Outstanding liabilities, including legacy and incumbent carriers.
- Determination of the appropriate loss development factors.
- Recent or impending state legislation or reforms.
- Current trends.
- TPA reserving practices.
- Existing or planned loss mitigation, such as accelerated claim closure activity, etc.
- Loss projections.
- Collateral ramp-up projection.

FINANCIAL REVIEW

As stated earlier, financial reviews may vary by industry. A thorough client financial review includes:

- Examining pertinent ratios, including liquidity, debt/leverage, coverage ratios, etc.
- Discussing financial objectives specific to collateral — present and future LOC capacity, credit line restriction, and the client’s ability to use credit for operational or growth needs.

- Assessing the internal rate of return on capital versus the cost of a LOC, including any requirement of cash backing of a LOC.
- Evaluating the current forms of collateral and exploring alternatives.

Clients with distressed financials and/or potential bankruptcy will be subject to far more aggressive postures in securing collateral before binding coverage. Insurance carriers do this in order to avoid challenges from the debtor suggesting the collateral was for “antecedent debt,” or already existing obligations. In bankruptcy scenarios, collateral or additional collateral requested for obligations that existed before the bankruptcy filing must have the court’s approval and demonstrate that the carrier’s possession of the collateral provides the debtor with some form of value.

GOAL SETTING/TACTICAL DISCUSSION AND DIRECTION

The first steps in the tactical discussion with a carrier should entail:

- Developing a critical understanding of the existing amount of “unsecured credit” extended by the insurer or deviation from the insurer’s projected collateral need. This includes future paid loss credits, financial strength deviation, or change in operation — for example, discontinued or divested operations and/or change in state venues/improved jurisdiction.
- Selecting the program structure — self-insured retention, deductible, treatment of defense, or nonsubscription that best responds to the coverage requirement and most effectively mitigates the collateral requirement.

In many cases, a meeting between the insured and the carrier's credit officer may be advantageous. In these scenarios, it is extremely important to prepare the risk manager and/or treasury personnel for the discussion, including preparing for any and all questions the insurer's credit officer may ask. At this time, it is also important to discuss the realistic mobility of the client's program from one carrier to another — for example, the impact on legacy and overall collateral. Insurers are not inclined to extend any unsecured credit/deviation to past clients in the same manner as they do for existing clients. In certain circumstances, this provides the opportunity for the client to consider a loss portfolio transfer or closeout of older policy years.

CONCLUSION

Collateral remains a challenge for many clients. With early and proper preparation, open and frequent dialogue, thorough modeling and analysis, and the exploration of all alternatives, insured companies can be best positioned to work to mitigate the amount of collateral required and free up credit to reinvest in their businesses.

Marsh's Casualty Practice formed the Collateral Solutions Group (CSG) to help clients negotiate favorable collateral outcomes by bringing together world-class experts to focus on a combination of advanced analytics, program design, and intimate knowledge of carriers' credit appetite and flexibility.

CSG helps companies to:

- Understand why insurers require collateral.
- Conduct extensive loss analysis and prepare for financial discussions with insurers.
- Assess what alternative collateral options are currently available in the market and which may be appropriate to meet their needs.
- Access appropriate insurers to begin collateral discussions.
- Reduce costs and free up capital for other corporate purposes.

Further, capitalizing on our deep and established relationships with leading carriers and their credit officers, along with our deep analytic capabilities, the CSG is able to bring a multidimensional analysis and evaluation to each client's unique situation.

Our collateral experts are available to facilitate a discussion with you on these topics, explore ways to minimize collateral, and investigate potential collateral alternatives. The goal is singular: Deliver the best for our clients.

OKLAHOMA AND BEYOND: SUMMARY OF SIGNIFICANT STATE WORKERS' COMPENSATION REFORMS PASSED IN 2013



The cost of providing workers' compensation insurance is one of the top issues for companies of all sizes and across industries. Because it is regulated at the state level, companies need to stay abreast of issues in any state in which they do business. To date in 2013, nine states have seen significant workers' compensation reform bills signed into law. Highlights from the legislation in each of those states follows.

OKLAHOMA

Oklahoma's recent workers' compensation reforms have received widespread attention due to the inclusion of an opt-out provision, known as the "Oklahoma Option." The law takes effect on February 14, 2014, and only applies to injuries occurring on or after January 01, 2014. Under this option, employers in Oklahoma can replace traditional workers' compensation coverage with an alternative benefit program that meets statutory requirements. Before Oklahoma's law passed, opting-out was only available in Texas and, to a limited extent, in Wyoming.

The Oklahoma Option is different than opting out in Texas. Employers must replace their workers' compensation with a defined

benefit plan that replicates the indemnity benefits available in the traditional system. The cost savings come from employer control of the medical, which ensures the employees receive appropriate care and that return to work is timely. Oklahoma employers who elect the option also retain exclusive remedy, with only a narrow exception for intentional acts.

Another significant element of the Oklahoma reforms was a switch from a courts-based to an administrative-based system. This should reduce litigation expenses and expedite dispute resolution. Overall, the reforms in Oklahoma are viewed as being favorable to employers.

DELAWARE

Recently passed reforms in Delaware were designed to control medical costs and encourage return-to-work efforts. Medical cost savings are expected to be achieved through a two-year suspension of the annual inflation increase on medical fees, new cost-control provisions on prescription medications, and changes to the fee schedule.

Other changes included more emphasis on return-to-work programs, with related efforts being considered in calculating the workplace credit safety program. These changes are expected to lower employer workers' compensation costs in Delaware.

FLORIDA

In Florida, the use of physician-dispensed medication has been a significant workers' compensation issue. New legislation creates a maximum reimbursement rate for physician-dispensed medication at 112.5% of the average wholesale price, plus an \$8 dispensing fee. Although the bill is expected to produce cost savings for employers in Florida, the fee schedule amount for physician-dispensed medications is still significantly higher than the same medications at retail pharmacies. Despite savings, this will continue to be a cost driver.

Recent rulings by the First District Court of Appeals have also affected the workers' compensation arena in Florida as two separate rulings found sections of the statutes unconstitutional. The decision with the greatest potential impact is *Bradley Westphal v. City of St. Petersburg* (No. 1D12-3563, February 2013), which eliminated the 104-week cap on temporary total disability (TTD) benefits. This decision is now under appellate review, and is not final.

The savings produced via the fee schedule for physician-dispensed medications will lower employer costs. However, the court's decision in *Westphal* may end up outweighing the savings.

GEORGIA

Legislation passed in Georgia means that, effective July 1, 2013, medical benefits for non-catastrophic cases will be capped at 400 weeks from the date of accident. Previously, injured workers were entitled to lifetime medical benefits for all claims. Other changes involve requirements related to an injured worker's efforts to return to work when a modified-duty position is offered, and an increase in the maximum rates for TPD and TTD benefits. The net impact of the changes is likely to be a slight reduction in workers' compensation costs.

INDIANA

Recent Indiana legislation establishes a hospital fee schedule at 200% of Medicare rates, and caps the prices of repackaged drugs and surgical implants. The fee schedule takes effect on July 1, 2014.

The law also included indemnity benefit increases including:

- Increasing the maximum average weekly wage (AWW) by 20%.
- Graduated percentage increases for degrees of permanent partial impairment/disablement over a three-year period, beginning on July 1, 2014.

The expectation is that this legislation will produce a small degree of savings for employers.

MINNESOTA

Minnesota joined most other states in amending their statutes to allow for mental-mental injuries, which are psychiatric disorders without physical injuries. Other changes include a cap on job

development benefits, a restructuring of how attorney fees are paid, an increase in cost of living adjustments (COLA) for permanently disabled workers, and an increase in the maximum indemnity rate. Additionally, rulemaking authority is now in place to include narcotic contracts as a factor in determining if long-term opioid or other scheduled medication use is compensated.

A slight overall increase in claim costs is expected as the result of the legislation.

MISSOURI

Missouri's reforms focused on addressing the insolvent Second Injury Fund and returning occupational disease claims to the workers' compensation system. The state's Second Injury Fund was heavily used by injured workers to supplement permanent partial disability (PPD) awards. The fund became insolvent when prior reforms capped assessments supporting it while not reducing the claims that were covered by it. Under the new reforms, which become effective January 1, 2014, PPD claims will be excluded from the Second Injury Fund and access to the fund will be limited to permanent total disability (PTD) claims where the total disability was caused by a combination of a work injury and a pre-existing disability. In addition, employer assessments to cover the funds' liabilities will be increased by no more than 3% of net premiums. These increased assessments expire December 2021.

The new law also:

- Indicates that occupational diseases are exclusively covered under the workers' compensation statutes, with some exceptions.
- Takes away employers subrogation rights on toxic exposure cases, which is a potentially significant issue that could result in increased filings of such claims.
- Establishes a mesothelioma fund (Meso Fund) that employers can opt into. If an employer does not opt into the fund, then their liability for a mesothelioma claim is not subject to the workers' compensation exclusive remedy, and action may be pursued in the civil courts.

Between the increased assessments, expanded benefits for toxic exposure, and the loss of subrogation on toxic exposure cases, it is expected that this legislation will increase costs for employers in Missouri.

NEW YORK

Governor Cuomo has said that the workers' compensation reform legislation he recently signed into law will reduce employer costs by about \$800 million annually. These savings are mostly projected from the streamlining of the assessment collection process and the elimination of the 25-A Fund and the assessments associated with it. New York's workers' compensation assessments are the highest in the nation, so any relief in this area would be welcomed by employers. However, the process for streamlining the assessments is not known, so it is unclear if the assessments will be significantly lowered. Also, since 25-A liabilities are being shifted from the Fund to employers, there is no savings from elimination of the Fund.

The minimum weekly indemnity benefit was increased from \$100 to \$150. This will have a negative impact on employers that use part-time workers earning near the minimum wage.

Until more details on the assessments emerge, it is difficult to determine whether or not this legislation will actually reduce employer costs.

TENNESSEE

The recent workers' compensation legislation in Tennessee was designed to make the state more attractive for businesses. Most employers are likely to see lower costs as the result of the reforms. Tennessee's reform moved its dispute resolution process from a court-based system to an administrative system, leaving Alabama as the only state that still uses the trial courts for all workers' compensation litigation. This may reduce employer costs associated with litigation and provide more timely resolution of disputes. Other changes in Tennessee involved:

- Strict statutory construction of the Workers' Compensation Act.
- Calculation of permanent partial disability.
- Burden of proof on causation.
- Creation of a medical advisory committee to develop treatment guidelines for common workers' compensation injuries.

OTHER STATES

Some states were still considering workers' compensation legislation as of this writing. Marsh's Casualty Practice and Marsh's Workers' Compensation COE plans to keep clients informed of significant developments in all states. For more information about workers' compensation issues, please contact your Marsh representative or the COE at wccoe@marsh.com.

This article is adapted from a Marsh Risk Management Research report. For more details on each state listed above, please visit <http://usa.marsh.com/NewsInsights/MarshRiskManagementResearch/ID/32241/Oklahoma-and-Beyond-Significant-State-Workers-Compensation-Reforms-in-2013.aspx>.

ADDITIONAL INSURED: THE IMPORTANCE OF INDEMNITY AND INSURANCE PROVISIONS IN CONTRACTS AND POLICY LANGUAGE

By John Denton, US Excess Casualty Claims Leader



Indemnification and insurance provisions are common features of many types of commercial contracts, including construction, engineering, oil and gas, and product distribution. Many of these contracts and insurance policies have three separate components: (1) an indemnification provision, (2) an insurance provision, and (3) an additional insured provision, that reflect the parties' efforts to contractually allocate risk and to use insurance as a backstop. Much has been written about indemnification provisions, including as to how they are interpreted and restrictions on covering a party for its sole negligence. Thus, this article will focus on the contractual insurance and additional insured provisions that may be used as a backstop.

SCOPE OF ADDITIONAL INSURED COVERAGE: CONTRACTUAL PROVISIONS AND LANGUAGE OF INSURANCE POLICY

Contractual insurance provisions and additional insured language are often viewed as intertwined with indemnification provisions in a contract. In other words, parties may intend that the additional insured's right to coverage applies to the other party's indemnification obligations but does not cover any liability of the

additional insured that is beyond the scope of any contractual indemnification provision. For example, many jurisdictions prohibit indemnification of the indemnitee's sole negligence, and the parties may assume that the additional insured's rights extend only to liability arising out of the indemnitor's negligence and not to the indemnitee's negligence or even sole negligence. If the parties intend for the indemnitee's rights as an additional insured to be limited to the indemnitor's obligation to indemnify, it is important for the parties to pay careful attention to both the insurance provisions of the contract as well as any additional insured provisions or endorsements. While the parties may assume that both merely backstop the indemnification provision, cases in several different jurisdictions — including recent cases in Texas involving the oil and gas industry — demonstrate the potential that insurance provisions in a contract and additional insured provisions in a policy may be interpreted to provide the additional insured with coverage for all of its liability, including liability beyond any contractual indemnification obligation and potentially extending to the sole negligence of the indemnitee.

IMPORTANCE OF INSURANCE PROVISIONS IN CONTRACTS

Initially, if the parties' intention is that the additional insured is entitled to coverage for only the indemnitor's indemnification obligation, this intention should be explicitly stated in the contract's insurance provision so that the court does not extend the additional insured's right to coverage beyond its right to indemnification under the contract, including the sole negligence of the indemnitee.

For example, in *Shell Oil Co. v. Nat. Union Fire Ins. Co. of Pittsburgh, PA*, 44 Cal.App.4th 1633 (2nd Dist. 1966), the insured entered into a contract to perform engineering work on a refinery owned by Shell and agreed in the contract to indemnify Shell excepting liability resulting from Shell's sole negligence. Although the insurance provision obligated the contractor to obtain "Comprehensive General Liability Insurance, including product/completed operations coverage and contractual liability coverage **for [contractor's] obligations hereunder to defend and/or indemnify Shell...**" the contract also provided, "To the fullest extent

permitted by law, all insurance policies maintained by [contractor] ... shall include Shell and any parties in joint operation with Shell as additional insureds ...” As a result, the court held that Shell was entitled to coverage as an additional insured for its sole negligence, stating, “There is no textual or practical reason to perceive the broad, plain language of these insurance provisions of the contract as requiring coverage only for [contractor’s] indemnity obligations.”

A similar case is *Hartford Acc. and Ind. Co. v. U.S. Natural Resources, Inc.*, 897 F.Supp. 466 (D. Or. 1995), in which the insured entered into a contract with the additional insured for installation of certain machinery being built for the additional insured. In the contract, the insured agreed to indemnify the additional insured, excluding liability arising out of the additional insured’s sole negligence, and to procure certain insurance. The insurance obtained by the additional insured contained a broad form comprehensive general liability endorsement that included as an “insured” any organization to which the “name insured” was obligated to provide insurance pursuant to a written contract. After an employee of the insured was injured, the insured asserted that the additional insured was not entitled to coverage inasmuch as the indemnification provision did not entitle the additional insured to indemnification for its own negligence. The court, however, rejected the argument that the indemnity provision limited the additional insured’s right to coverage, holding that “Nothing in the language of the insurance clause or any other provision of the ... contract ties the insurance requirements to the indemnity clause...” Therefore, if the parties to a contract desire to limit the additional insured’s coverage to an obligation to indemnify, the insurance provision should be linked to the indemnity provision and should specifically state that the additional insured’s rights to coverage are limited to any obligation of the other party to indemnify it under the contract.

ADDITIONAL INSURED PROVISIONS/ ENDORSEMENTS MAY OVERRIDE CONTRACTUAL INSURANCE LIMITATIONS

Even if the insurance provision is explicitly limited to any obligation to indemnify, the additional insured may be held to have unlimited rights to coverage beyond any indemnity obligation if the additional insured provision in the policy or endorsement does not limit the additional insured’s rights to coverage. An example of this can be observed in the recent Texas case: *In Re Deepwater Horizon*, 710 F.3d 338 (5th Cir. 2013). In *Deepwater Horizon*, the insured, the owner of an off-shore drilling unit, entered into a drilling contract with an oil company in which the insured agreed to maintain certain insurance and to name the oil company “as additional insureds in each of [the insured’s] policies, except Workers’ Compensation **for liabilities**

assumed by [the insured] under the terms of this Contract.” After an explosion aboard the drilling unit, the oil company sought coverage as an additional insured under the insured’s liability insurance policies, and the insurers filed a declaratory judgment action seeking a declaration that they had no obligation to the oil company. Although the policy limited the insured’s obligation to name the oil company as an additional insured to “liabilities assumed by [the insured],” the oil company argued that “the insurance policies alone — and not the indemnities detailed in the Drilling Contract — govern the scope of [the oil company’s] coverage rights as an ‘additional insured.’” While the lower court held that the contract “required [the insured] to name [the oil company] as an insured only for liabilities [the insured] explicitly assumed under the contract,” the Fifth Circuit Court of Appeals reversed, finding that “[even] if the [insurance] clause is construed as the insurer’s desire, that is, even if it is understood to mean that [the oil company] is an additional insured under [the insured’s] policies only for liabilities [the insured] specifically assumed in the Drilling Contract ... [the] clause was insufficient to limit coverage.” In holding that the oil company was an additional insured without limitation to any indemnity obligation of the insured, the Fifth Circuit held that “we are bound to look only to the policy itself to determine whether [the additional insured] is covered in the current case.” See also *Evanston Ins. Co. v. Atofina Petrochemicals, Inc.*, 256 S.W. 3d 660 (Tx. 2008). As a result, if the intent of the parties is to limit the additional insured’s rights to coverage for the indemnity obligations in the contract, the insured should ensure that the policy limits the additional insured’s rights, rather than leaving the additional insured’s rights undefined and giving it the right — at least under Texas law — to recover for liability outside the insured’s indemnity obligation, including, potentially, the additional insured’s sole negligence.

CONCLUSION

Indemnification and insurance provisions have been, and will continue to be, important tools in managing risks in contracts involving services and products. Where one party agrees to indemnify the other, the parties may intend that the indemnitee’s right to insurance coverage only extend to the other party’s obligation to indemnify it under the contract. If that is the parties’ intention, it is important that the insured consult legal counsel and determine to what extent the insurance provision and the insurance policy need to specify that the additional insured’s rights extend no further than any indemnify obligation in the contract. It is important to note that such limitations in the contract should serve to limit only the additional insured’s rights and not any rights the insured may have under the policy for its own liability.

WHAT'S NEW FOR SUMMER: MARSH CASUALTY PRACTICE

Marsh's Casualty Practice experts regularly monitor and analyze the wide range of issues affecting the casualty marketplace. Some of our upcoming events and recent initiatives include:

MARSH IN THE MARKETPLACE

- On July 17, **Tracey Ant** and **Chui Yuen** took part in a webcast in Marsh's *The New Reality of Risk*® series — "Insurance Market Update: Midyear 2013."

To listen to a replay of the webcast, please click [here](#).

- **Mark Walls**, workers' compensation market research leader, will be speaking at the following conferences:
 - **Workers' Compensation Institute:** Mark will join a panel of industry bloggers in the session, "Around the Country and Around the Block: The 'Ultimate Bloggers' Perspectives on Hot Topics & Trends." The panel will discuss current issues in workers' compensation. The conference is scheduled for August 18-21 in Orlando, Florida. For more information, please click here: <http://www.wci360.com/conference>.
 - **University Risk Management and Insurance Association (URMIA) Annual Conference:** Mark will moderate the panel, "Enhancing Your Risk Management Program with a Cost Allocation System." The panel of higher education risk managers will discuss the merits of a cost-allocation system and how to implement one. Mark will also lead a second panel, "Workers' Compensation Issues and Answers: The Sequel," at which higher education risk managers will discuss the unique workers' compensation exposures faced by colleges and universities. The conference takes place October 13-16, in Phoenix, Arizona. Please click here for more information: <https://urmia.site-ym.com/page/2013Conference>.
- On June 10, Marsh's Casualty Practice published a paper about the **2013 changes to the Insurance Services Office (ISO) general liability endorsements**. This paper followed an earlier paper and webcast explaining the changes to the main policy. The papers and replay of the webcast are available at: <http://usa.marsh.com/NewsInsights/ThoughtLeadership/Articles/ID/31462/2013-Changes-to-ISO-Endorsements.aspx>.
- **Mark Walls** authored an article for *Claims Journal* magazine: "Will Competition Drive Improvement in Workers' Comp?" <http://www.claimsjournal.com/magazines/idea-exchange/2013/06/24/231505.htm>.

PRACTICE INITIATIVES

- In July, the Work Comp Analysis Group (WCAG) on LinkedIn, founded and managed by **Mark Walls**, reached the milestone of 20,000 members. Launched in late 2008, the WCAG is the largest online discussion group dedicated exclusively to workers' compensation issues and is viewed as a leading industry networking and informational resource. Members discuss emerging workers' compensation trends, issues, and regulatory and legal developments. In addition to online discussions, the WCAG has an industry jobs board, a Twitter feed, and a resource center that features more than 40 industry blog feeds and links to the rules and statutes for all 50 states. Search "Work Comp Analysis Group" on LinkedIn.com to join.
- Our proprietary excess liability policy form, **Marsh XSellence**, has reached total capacity of \$420 million with the support of 14 global insurers in the US, London, and Bermuda — with additional capacity expected. Using Marsh's longstanding and deep claims advocacy experience and global presence, we designed Marsh XSellence with the intent to mitigate ambiguities in excess follow form policies by eliminating conflicting terms and conditions. Marsh XSellence is a significant advancement in our industry's quest to achieve consistency of coverage throughout the excess casualty tower. For more information, please contact your Marsh casualty team, or email questions@marsh.com.

Marsh is one of the Marsh & McLennan Companies, together with Guy Carpenter, Mercer, and Oliver Wyman.

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This information is provided as forward-looking commentary as to Marsh’s views regarding likely future insurance market conditions and incorporates both qualitative and quantitative assessments of the US casualty market. Actual results may vary from these predictions.