

Workshop W1

Wednesday, October 31, 9:00 a.m. – noon

LESSONS LEARNED ON WRAP-UPS

Presented by



Jason Weintraub
Vice President—General Counsel
DRI Companies

Wrap-ups, both owner controlled and contractor controlled, present challenges for all parties but particularly for the contractors and subcontractors who are required to participate. Many contractors and subcontractors have become comfortable with wrap-ups and don't object to their use as long as their needs and concerns are fairly addressed. This workshop identifies some lessons learned from both the sponsor's and the participating contractors' and subcontractors' perspectives.

- Examines the potential benefits of wrap-ups and when their use may be appropriate.
- Demonstrates the importance of addressing certain coverage and claim issues, such as warranty work, off-site fabrication, and unenrolled subcontractors.
- Identifies common concerns of subcontractors and how to best realize the benefits of a wrap-up.

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Jason Weintraub
Vice President—General Counsel
DRI Companies

Mr. Weintraub is one of the presenters for Workshop W1, “Lessons Learned on Wrap-Ups,” on Wednesday morning. He is vice president and general counsel of the DRI Companies, one of the largest residential and commercial roofing, waterproofing, and alternative energy sub-contractors on the West Coast. Prior to joining DRI, Mr. Weintraub gained extensive experience in complex and class action litigation at the Howard Rice Law Firm and at Horvitz & Levy LLP. Mr. Weintraub has presented at numerous continuing education seminars on such issues as product liability, construction defect law, insurance coverage, unfair competition law, and complex civil litigation. In 2006 and 2007, Mr. Weintraub was selected by his peers as a “Rising Star” lawyer in the *Southern California Super Lawyers Edition Magazine*, published in conjunction with *Law & Politics* and *Los Angeles Magazine*. Articles written by Mr. Weintraub have appeared in *California Litigation* and *Verdict* magazines. Mr. Weintraub received his juris doctor degree from the University of California at Berkeley School of Law (Boalt Hall) and his undergraduate degree in political science from Stanford University.

Notes


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COMMON GROUND: Builders/GCs
& Subs Working Together to Build a
Better WRAP Program

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History of Wrap-Ups



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- 1940s – Introduced on the U.S. defense plants
- 1950s – Applied to other projects (such as Lincoln Tunnel)
- 1990s – Significant increase in popularity on commercial and public works projects
- 2000 – Start of use on residential projects in western United States

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Related Products

- “Rolling Wraps”
 - Specified multiple projects are enrolled in an ongoing insurance program
 - May have aggregate limits for each project or one aggregate for all projects
- Home Builder’s Protective Policy
 - Builder purchases broad insurance coverage for itself and all subcontractors
 - Combines general liability policy with certain warranty obligations to homeowners and HOAs

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Growth of Wrap Programs in Residential Construction



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Contributing Factors

- Increased number of large capital improvement projects during the 1990s economic boom
- Highly competitive construction industry
- Increased risk exposure for multi-family projects prone to litigation
- Insurance became expensive/difficult to procure for subcontractors – many could not insure multi-family projects at all
- Class action lawsuits
- Poor construction quality control

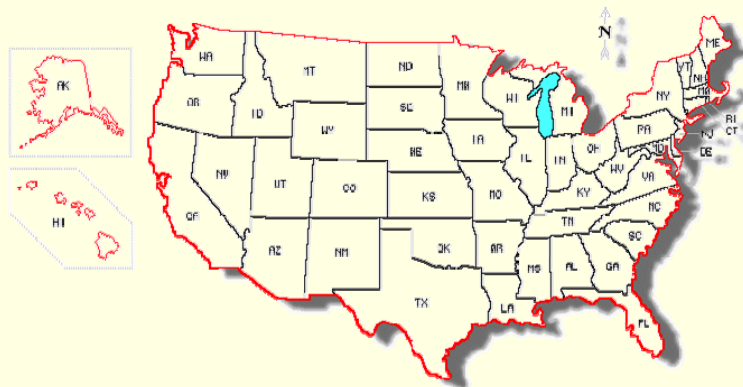
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- Generally used in larger projects (total costs exceeding \$10 million)
- Public works
- Commercial
- Hotels and Resorts
- High-rise and low-rise condominiums
- Mixed-use
- Large residential developments

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Problem States

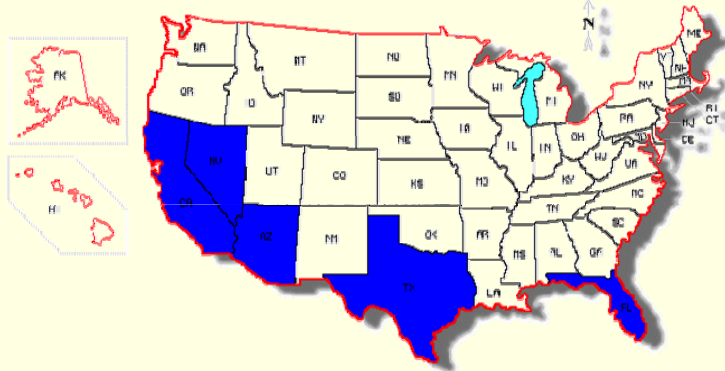


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Problem States

■ Tier 1 States

- Arizona
- California
- Florida
- Nevada
- Texas



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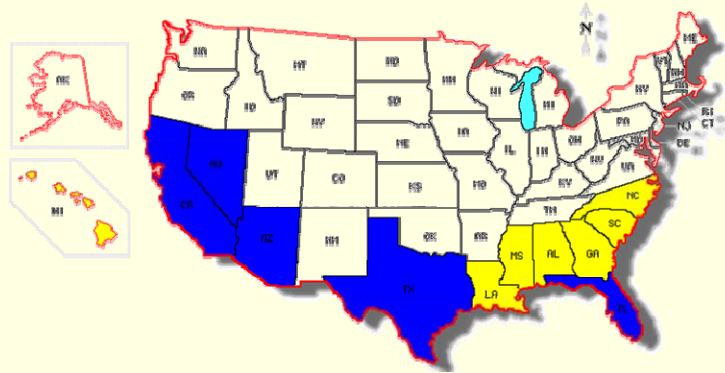
Problem States

■ Tier 1 States

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- Texas

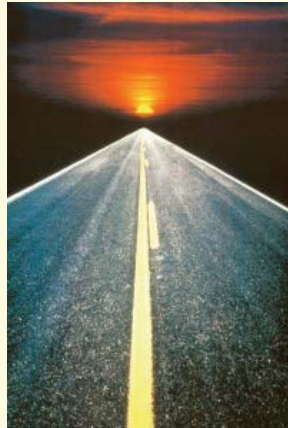
■ Other Problem States

- Alabama
- Georgia
- Hawaii
- Louisiana
- Mississippi
- North/South Carolina



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Stated Goals of Wrap-Ups



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Stated Goals of WRAP Programs

- Save premium dollars due to volume discounts/increased purchasing power of builders
- Reduce defense costs (and, potentially, settlement payments) with a single, unified defense for builder and trades

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Stated Goals of WRAP Programs

- Improve Insurance Coverage for all parties (volume discounts/increased purchasing power)
- Improve Jobsite Safety due to unified loss control program

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The Reality: Many Wraps Make Things Worse

<p>Goal 1 On many projects, trades may have more coverage (higher limits) on their own than under the wrap policies</p>	<p>Goal 2 As currently constructed, many wrap programs will produce <i>more</i>, rather than less, litigation between builders and subs</p>
<p>Goal 3 For many wraps, trades may have had better or equivalent coverage!</p>	<p>Goal 4 More residential wraps should include <i>improve safety</i> Workers' Comp.</p>

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Key Questions for Wraps



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Key Questions on Wrap Projects

- **What is covered?** (*GL, Workers' Comp, Completed Ops, etc.*)
- **What are the policy limits** for each type of coverage?
- **How many projects/units are included?**
- **Where are the covered projects located?**

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Key Questions on Wrap Projects

- **What are the coverage exclusions?**
- **Does completed ops coverage exist** for the statute of limitations “tail”?
- **Are warranty claims and right-to-repair statute claims covered?**

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Key Questions on Wrap Projects

- **How does the subcontractor pay** its portion of the wrap premium?
- **How long is the policy period?** Do limits apply separately per year?
- **Who bears the risk if limits exhaust** prematurely or are unavailable?

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Myth v. Reality: Practical Problems with Wraps



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Administrative Hurdles

- Bidding procedure varies by project
 - Some Builders/GCs charge the same rate the sub pays on their own GL policy
 - Some establish a premium charge that may be even higher
 - Some just ask subs to submit a “net bid” with insurance costs excluded
 - Some do a combination of the above

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Administrative Hurdles

- Using premium credits instead of net bids increases costs for all parties
 - Administrative burden for builder/GC
 - Administrative burden for trades, which leads to increased bids
- Competitive bidding weeds out trades providing false “net” bids

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Coverage Gaps Still Exist For Many Wraps

- Off-site General Liability
- Workers’ Compensation (most wraps)
- Warranty Service
- “Right to Repair” Statute Claims
- Pollution
- Mold
- Subsidence

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GL Coverage Gaps

- Trigger of coverage – Typically “close of escrow”
 - What if a home closes after expiration of the policy period?
- Statute of Limitations/Repose – Does the wrap provide completed operations for the entire statutory period?
 - What about a fraud/PI claim that is not limited by the statute of repose?

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Coverage Gaps: SIR/ Deductibles

- **Typical Minimum**: \$50,000 per occurrence for project-specific wraps; \$250,000 for rolling wraps
- **Typical Maximum**: \$2,000,000 per occurrence or \$25,000,000 aggregate!

PROBLEM: *Does this provide an incentive to treat more claims as warranty issues rather than an insurable “occurrence”?*

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SIR/Deductible Contributions

- How is occurrence defined?
 - Does it match the traditional insurance definition by “including continuous or repeated exposure to substantially the same general harmful conditions?” If not, subs could be required to pay deductibles more often (even on a per-home basis!)

- Amount of Sub’s Contribution
 - Does the builder control this part of the process?
 - How much does the sub have to pay per occurrence?
 - Is the contribution proportional to the sub’s level of fault?

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SIR/Deductible Contributions

- High SIRs/deductibles frustrate goal of single, unified defense
 - The higher the SIR/deductible, the more likely trade contractors are to challenge allocation
 - High SIRs = Increased infighting among defendants!

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Policy Limits for Many Wraps are Insufficient

- Many wraps severely under-funded
- Insurance industry recommends per unit coverage between \$60,000 – \$125,000 per unit constructed, not including defense fees

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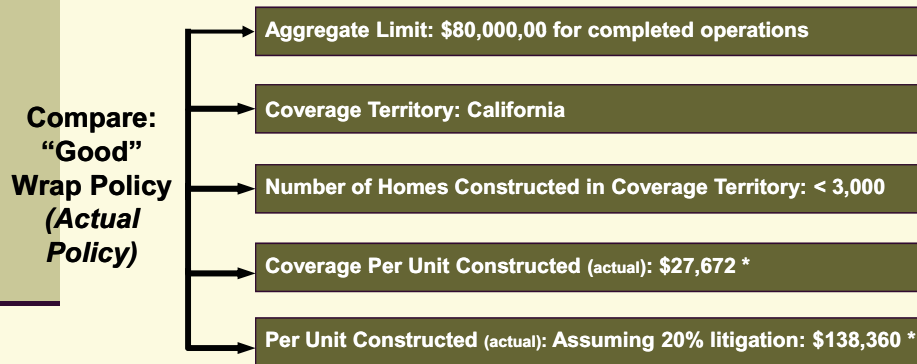
Limits Should Cover all Potential Claims



* defense fees INCLUDED

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Limits Should Cover all Potential Claims



* defense fees EXCLUDED

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Insufficient Policy Limits Prevent Unified Defense

PROBLEM: Who bears risk if limits exhaust prematurely?

- Many form subcontracts require sub to indemnify builder if wrap limits are "inapplicable, exhausted or unavailable"
- Many subs are negotiating this indemnity obligation out of their subcontracts

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Insufficient Policy Limits Prevent Unified Defense

- In many jurisdictions, subs cannot economically insure any project with a wrap
- Subs cannot measure the risk of inadequate wrap insurance
- Even with anti-indemnity laws, subs typically asked to defend lawsuits up-front

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Insufficient Policy Limits Threatens Coverage

PROBLEM: Minimal wrap coverage puts pressure on tendering claims to wrap carrier

- ***RESULT:*** Warranty Provisions in subcontracts now more broad:
 - Right to Repair Claims
 - Longer Warranty Periods
 - Strict “your work” Exclusions

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Importance of Adequate Limits

- Some states limit wrap-up insurance use by setting a minimum project cost and requiring a prior approval from the state insurance regulator (Oregon and Michigan)

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Lawsuits: “All in One Basket” Exposure

- Conflict of interest issues
 - Who controls the lawsuit for all parties?
 - Is there any obligation to inform trades of the lawsuit or its progression?
 - Do trades have any influence over litigation and/or settlement strategy?
 - Will the conflict waiver in the subcontract agreement be enforced years later?
 - How can a single attorney and a single expert represent the potentially conflicting interests of over 40 companies?

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Lawsuits: “All in One Basket” Exposure

- Potentially higher settlement payments for subs
 - Can builder demand payment for warranty repairs, uninsured items, and additional SIRs?

- Potential to circumvent anti-indemnity laws
 - How can subs ensure they only pay for their fault when the subs cannot influence the process?

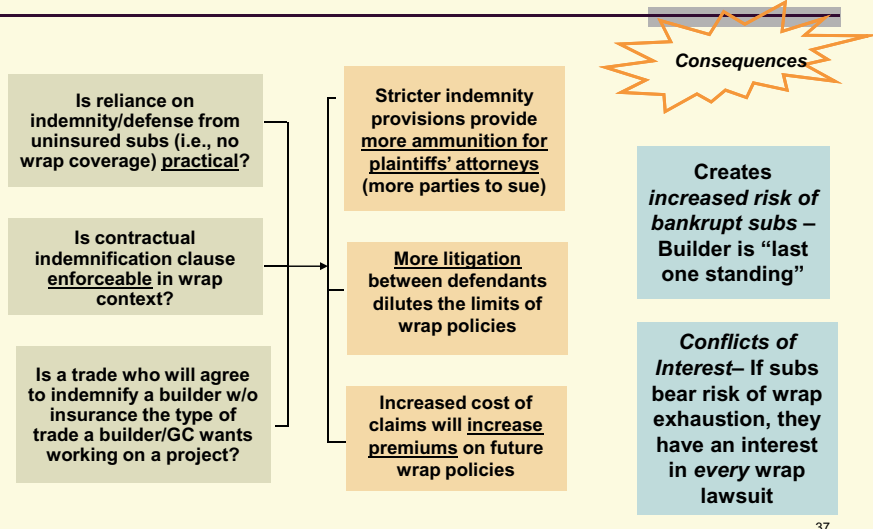
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Making the Myth a Reality: New Risk Model



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Wraps Challenge Risk Transfer Model



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Inadequate Wraps Destroy Unified Defense



RESULT: *More Litigation between Builders and Subs!*

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Caselaw Undermines Risk Transfer Model

- *Stevenson v. HH & N/Turner*, 2002 U.S. Dist. LEXIS 26831 (E.D. Mich.)
- Sub's employee injured on project covered by OCIP - sued manager for tort liability
- OCIP included CGL and work comp. coverage

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Caselaw Undermines Risk Transfer Model

- **HOLDING:** Policy underlying work comp. and OCIPs barred tort liability – *purpose of OCIP is to reduce cost of insurance and allow coordinated risk management and safety program for all insureds.*

LESSON: Courts may bar suits between parties on Wrap projects

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Caselaw Undermines Risk Transfer Model

- *Affiliated FM Ins. Co. v. Patriot Fire Protection, Inc.*, 2004 WL 418102 (Wash.App. Div. 1) (*unpublished*)
- Sub enrolled in OCIP installed defective fire sprinkler system
- OCIP carrier paid owner for damage and sued sub for subrogation
- Sub argued that merely by purchasing OCIP, the owner impliedly waived subrogation rights

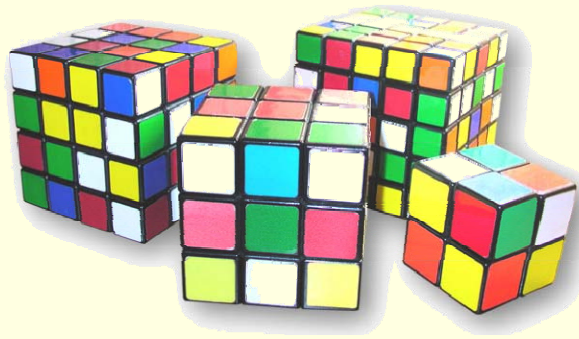
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Caselaw Undermines Risk Transfer Model

- HOLDING: OCIP carrier could *NOT* subrogate against party for whose benefit insurance was written – even though that party’s negligence may have caused loss.

LESSON: *In most states an insurer cannot subrogate against an insured.*

Solutions: Building Better Wraps



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How to Build a Better Wrap: Coverage

Purchase real insurance with minimal exclusions – good subs will pay for this

Ensure per-project coverage limits adequate based on litigation history

Keep SIRs low/non-existent to avoid infighting among defendants over claims (loss runs weed out poor quality subs)

Allow subs to submit bids “net of insurance” to avoid increased administrative costs

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How to Build a Better Wrap: Coverage

■ Specific Coverage to Include:

- All jobsite incidents (i.e. workers' comp.)
- Warranty claims after 1st Year
- Mold allegations
- Subsidence/soil issues
- All defect allegations



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How to Build a Better Wrap: Defense

- Avoid Contractual Risk Transfer for Wrap claims (equitable indemnity remains)
- Keep required SIR/Deductible Contributions Low
- Focus defense efforts on securing coverage from wrap carrier and battling plaintiffs' case

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How to Build a Better Wrap: Risk Management

- Practical Solutions for **Planning** (Residential)
 - **Reduce** the Number of Plan Versions
 - **Improve** Plan Accuracy
 - **Reduce** the Number of Products
 - **Minimize** the Number of Options
 - **Eliminate** Unnecessary Design Complexity
 - **Reduce** the Number of Subcontractors Bidding

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How to Build a Better Wrap: Risk Management

Practical Solutions for **Jobsite Safety**

- Pre-hire check of subcontractor's safety records
- Consistent enforcement of safety rules on site
- Ensure (budget for) adequate fall protection and other safety measures

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How to Build a Better Wrap: Risk Management

Practical Solutions for Quality

- Implement a Constructability Review Team:
 - ✓ Builder
 - ✓ Architect
 - ✓ Engineer
 - ✓ Trade Contractors

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How to Build a Better Wrap: Risk Management

- Practical Solutions for Quality
 - Hire the best
 - Continuous training
 - Meaningful supervision
 - Maintain your standards
 - Work with the best
 - Make customer service a top priority

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How to Build a Better Wrap: Risk Management

- Practical Solutions for **Claims**
 - Prevent Defects in Planning & Production
 - Resolve Issues at Customer Service Level
 - Handle Right-to-Repair Statute Claims “in house”
 - Don't tender to your carrier
 - Don't turn it over to outside counsel
 - Make a reasonable settlement offer
 - Meet all statutorily imposed deadlines

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Benefits to Builders of Building a Better Wrap

- Reduced litigation expenses: true “unified defense”
- Eliminates “bankrupt” sub problem because wrap program provides sole (and sufficient!) remedy
- Can weed out/quantify poorly performing subs during bidding process based on loss histories



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All Parties Win if Wraps Achieve Their True Purpose

- **Improved financial security for builders:** Claims funded by legitimate insurance, not by questionable indemnity agreements
- **Reduced admin & construction costs:** No premium deductions or increased bids from subs to cover risk of inadequate insurance
- **Reduced litigation between subs and builders:** No more fights regarding who is “responsible” for claims
- **Increases participation from quality trade contractors** who will remain viable partners throughout statute of repose period



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All Parties Win if Wraps Achieve Their True Purpose

HISTORY PROVIDES THE ANSWER:

Wrap insurance was conceived over 30 years ago on large commercial projects to take advantage of great buying power to purchase incredibly broad coverage with high limits. This practice benefited the owner and all contractors.

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The Goal

To Go From This



To This



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