

It is a fact of life in the construction business. Almost all [construction contractors](#)

, from the general contractor all the way to the

[landscape contractor](#)

will occasionally have to hire an uninsured subcontractor.

There are hidden costs to this arrangement but knowing them in advance can help you prepare for the costs and minimize the damages to your insurance program.

It's helpful to understand, from the beginning, that insurance companies don't like for their clients to hire uninsured subcontractors. The reason is that they feel that your control over a subcontractor is much reduced and therefore losses are more likely.

If they are uninsured, then the exposure for those losses is pushed on to your insurance company.

And that makes you a less attractive risk for your insurance company.

So hiring uninsured subs causes two big problems that can generate increased insurance costs for you. Both are things you can prepare for if you do your homework in advance. And by taking the steps I will outline below, you can possibly reduce the cost to zero for each of these problems.

And remember, if you use a subcontractor that is insured, be sure to take the appropriate steps to obtain a valid certificate of insurance.

To read more about what you need to know about insurance certificates, please [click here](#)

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The first problem that uninsured subs will cause for you is increased insurance premiums on your [general liability insurance policy](#) and your [workers compensation insurance policy](#). This is a stealth increase because if you don't take steps in advance to protect yourself, then by the time you find out how much your subcontractor costs you, the sub may be long gone and your chances of wringing it out of him or her will be nil.

If you are unable to produce a

[valid certificate of insurance](#)

on a subcontractor, then when your policy is audited by the insurance company

at the end of the policy term, they will include as payroll, the full amount of cost that you paid to the uninsured subcontractor.

You can defend against this problem by withholding from the amount you pay the uninsured subcontractor an amount equal to or greater than the amount you will be charged by the insurance company at audit. To understand how much to charge, you should contact your agent and find out the rate per \$1000 of payroll for the subcontractor's classification on both [workers compensation](#)

and

[general liability insurance](#)

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I would suggest that you add an amount over the rates you face to cover your administrative expenses of handling this transaction.

The second problem caused by uninsured contractors has to do with the insurance company's reaction to finding out you have used them. As I mentioned earlier, insurance companies do not like for their clients to utilize uninsured contractors but their appetite for them will vary.

Check with your agent first and find out just what percent of payroll or gross sales paid out to uninsured subs will be tolerated by your insurance company.

Some may not tolerate any and still others may be willing to let you go as high as 50%.

It is important to know in advance how high you can go so that you don't break your insurance company's rules unknowingly. If they find out on audit that you have been using more uninsured subs than their underwriting guides allow, they may cancel your policy or take away discounts that will result in much higher rates for you. In this case it is better to ask permission first then to ask for forgiveness later.

Remember, when you deal with an uninsured subcontractor you are now allowing them to use your insurance for their risks. Over the long term this is not advisable because they could cause a loss that is so catastrophic it might destroy your ability to get insurance at all, or it may create a high experience modification factor on your workers compensation policy that might cost you a lot of money for the next 3 years. It is always best to deal with subcontractors that have their own insurance.

[Clinard Insurance Group, in Winston Salem, NC](#) specializes in [helping small contractors](#) of all types all across North Carolina.

If you would like a second opinion on your business insurance or if you need help with your [general liability policy](#) or your [North Carolina workers compensation policy](#)

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