

INSURANCE RECOVERY ADVISOR

Events Calendar

In each Insurance Recovery Advisor issue, we will let you know about events involving attorneys in our insurance recovery group. Please contact the attorneys involved in the event if you would like more information about the event or the topic.

“Coverage for Green Buildings, Green Insurance, and Green Claims” with Meghan K. Finnerty on March 4-6, 2010 at the ABA Insurance Coverage Litigation Seminar in Tucson, Arizona.

“A Pragmatic Approach for Addressing the Issue of Odorant Fade” with Mark E. Gottlieb and Darin J. McMullen on May 25-26, 2010 at the Natural Gas Odorization Conference in Houston, Texas.

“Insurance Law from A to Z” CLE Seminar with William H. Pillsbury on Friday, July 30, 2010 at the Crowne Plaza Hotel in downtown Philadelphia. ■

“Boss, We have a problem”: Guarding Against the Large Construction Loss

BY: MARK E. GOTTLIEB & DARIN J. MCMULLEN

While the United States economy struggles to recover, new construction will hopefully begin to increase. As new construction projects commence, contractors and sub-contractors should ensure they have adequate insurance coverage in the event of losses arising out of the construction. The first step is analyzing existing insurance policies and prospective coverage needs. However, contractors and subcontractors should also view their business partners and sub-contractors as sources of recovery in the event of a loss that is not covered, or not fully covered, under their own available insurance. Whether through contractual provisions that transfer risk or by requiring that they are named as additional insureds in their business partners’ policies, contractors and owners have the opportunity to obtain this additional layer of potential recovery.

Assess Risk Immediately and Always Assume Your Insurance Will be Inadequate Effective mitigation of construction-related losses requires early consideration of available insurance coverage as well as risk transfer options. Once a project has been awarded and the relevant contract documents are being negotiated, policyholders should look to their existing insurance programs, including their Commercial General Liability (CGL) policies, to determine whether the existing coverage will be sufficient to cover the impending project. To the extent notice of a new construction project is required for coverage or inclusion under an existing policy, such notice should be given promptly in order to avoid any gaps in coverage in the event of a loss occurring early in the project.

Because most CGL policies do not cover the constructed property until construction is completed, Builder’s Risk coverage should be considered. Builder’s Risk coverage, which can be added to multi-peril policies or purchased as a stand-alone policy, is available to contractors, developers and owners. A Builder’s Risk policy will generally provide coverage for the value of the property being constructed prior to owner acceptance, for materials at the job site, as well as for losses due to ordinances or laws.

Partners Can Help Spread the Risk in a Large Loss

Contractors and owners should also, during contract negotiations, build additional risk protection by transferring risk to sub-contractors and other parties involved in the construction project. Contractual indemnity clauses have become commonplace in construction contracts, the scope of the indemnity provision can range from broad indemnification requiring the indemnitor to indemnify the indemnitee for its own negligence, to narrow indemnification provisions which require a comparative fault analysis. A hybrid middle ground exists whereby indemnification will be provided for certain types of “passive” negligence.

Many states, through judicial rulings or legislation, have invalidated the broad “own negligence” indemnification clauses. Consequently, policyholders should have contractual indemnification provisions drafted and reviewed by counsel to ensure that the indemnification provisions in their contracts conform to applicable law. This should be determined at the outset in order to include, when necessary, a narrower indemnification clause. The narrower clause will ensure some measure of risk transfer that otherwise would be nonexistent if an invalid broad form was later invalidated.

Moreover, the requirements sought through these risk-shifting provisions should be kept reasonable in order to increase the likelihood of risk transfer. You may be asked to pay more on the contract in exchange for the transfer of risk. However, the increase in payment under the contract may ultimately pale in comparison to the costs associated with any litigation you would bear if the risk is not transferred in some manner.

Contractors and owners should require that they are named as an additional insured on sub-contractors’ and indemnitors’ CGL policies. Additional insured status provides a safety net to existing contractual indemnification provisions. The scope of coverage, applicable endorsements and exclusions should be analyzed prior to the commencement of work so that you understand what coverages are and are not afforded to you as an additional insured so that you may address any issues or concerns that arise.

In order to maximize the protection afforded as an additional insured, policyholders should request copies of the policies to which they will be named as additional insureds, as well as all endorsements to that policy.

Asking to be named as an additional insured on a policy and receiving certificates of insurance is insufficient. Moreover, policyholders should check the insurance provisions of their own policies to determine if the coverages under their policies are affected by being named as an additional insured.

Faulty Workmanship Claims and the Importance of a Backup Plan

Although no contractor wants to contemplate the possibility of faulty workmanship claims prior to the first day on the job, such claims are a reality and it is once again best to contemplate and prepare for the possibility at the outset of the project. Because the defense and indemnity costs associated with such claims can be costly, the availability of insurance coverage for faulty workmanship claims is critical, particularly because some jurisdictions have ruled that CGL policies do not cover such faulty workmanship claims.

Responding to Losses

It is important to respond to losses promptly and thoroughly in order to maximize the recovery safety nets put in place at the early stages of the process. The diligent policyholder who prepared for claims or losses through early analysis and assessment of existing and available insurance, contractual risk transfer, and additional insured status will be best positioned to look to its sub-contractors for recovery and indemnification following claims or losses arising out of the construction.

Following a loss, provide notice to all potential sources of indemnification or recovery. The timeliness of notice is critical and, depending on your jurisdiction, the failure to give timely notice may result in the forfeiture of millions of dollars in insurance coverage. Consequently, notice should be given broadly and promptly.

Although most policyholders will think to provide notice to their own insurance companies, it is equally important to provide prompt notice of the loss to the insurance companies of your sub-contractors, as well as the parties with whom you have contracted for indemnification. Even if a sub-contractor’s involvement or scope of work does not immediately appear to be directly involved in the loss, you should nevertheless provide notice of the claim or loss to that party as well as its insurance companies, particularly if you are named as an additional insured.

Conclusion

Policyholders involved in the construction industry are at constant risk of losses and claims arising out of their work. Construction-related losses and claims can have significant price tags associated with the costs of defense as well as indemnification and potential damages. However, through thorough analysis and negotiation, contractors, sub-contractors, developers and owners can secure a number of potential insurance coverage and contractual indemnification sources prior to the start of a construction project in order to minimize the exposure in the event of such losses. ■

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I didn't know I had insurance coverage for that!

BY: MICHAEL CONLEY & MEGHAN K. FINNERTY

While every business person knows that their property insurance policy covers risks such as fire and their auto insurance policy covers vehicle accidents, your basic insurance program often provides coverage for a whole host of losses that may not be so widely known. Here are some examples of losses that would be covered under most business package insurance programs.

1. If an employee takes cash, the theft from the company would be covered under a Crime Coverage policy, but did you know that other types of employee thefts, such as overstatement of hours in order to obtain overtime or inflating sales or production numbers to obtain a bonus, are also covered losses? Any time the company loses money because of the misconduct of an employee, the Crime Coverage should be reviewed to determine if the loss is covered by insurance.

“Policyholders must keep in mind that the purpose of insurance is to transfer risk from their business to the insurance company – that is why you pay all of those premium dollars. As such, for any loss by the company or claim against the company, the first question should always be – is this covered by my insurance?”

2. If your business is shut down because of a fire, you would immediately know that your insurance policy would cover the loss of income, but did you know that if your business is affected by damage to a third-party's business that attracts customers to your business, you may also have coverage? The most common example of this is if a flagship store at a mall is damaged or destroyed, the other businesses in the mall may have coverage for their resulting loss of income.

3. If a natural disaster damages your property you would know that you have coverage for the interruption of your business, but did you know that if circumstances prevent ingress or egress to your property, or if access to your property is interrupted by order of civil authority, even if your property is not damaged you may still have coverage? One example of this would be wild fires that cause roads to be closed. Even if your property is not damaged and your business could remain open, if the customers cannot get to you, you should have coverage.

4. While most people know that a discrimination claim by an employee would be covered by the company's Employment Practices Liability Insurance, did you know that an allegation in a suit that the company breached a written employment contract also may entitle the company to at least having the insurance company pay the defense costs for that suit? Even if there is no written contract, as long as the claim or suit alleges a written contract, the insurance company's defense obligation is triggered.

5. If a claim is made against your company because of the actions of one of your vendors or a sub-contractor, if you requested the vendor or sub-contractor to name you as an additional insured, did you know you can treat the vendor's or sub-contractor's insurance company as your own? Being named an additional insured creates essentially the same right as a named insured, including the right to sue the insurance company for bad faith if the insurance company fails to act appropriately.

6. If you have Boiler and Machinery coverage, you probably are aware that a breakdown of your mechanical or electrical systems are covered, but did you know that, under most Boiler and Machinery coverage, damage to computers caused by electrical equipment breakdown would be covered. As an example, if the electrical equipment in your office caused a surge that destroyed your servers and other computers, not only would the repair to the electrical equipment be covered but also

“I didn't know” continues on page 4

the costs to repair or replace the server and other computers.

These are just a few examples of claims that you might not initially think would be covered by insurance. Policyholders must always keep in mind that the purpose of insurance is to transfer risk from their business to the insurance company - that is why you pay all of these premium dollars. As such, for any loss by the company or claim against the company, the first question should always be - is this covered by my insurance? ■

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INSURANCE LAW UPDATE

BY: WILLIAM H. PILLSBURY

In *D.R. Horton-Texas, Ltd. v. Markel International Insurance Company, Ltd.*, the Texas Supreme Court concluded that an insurance company may have a duty to indemnify even if the duty to defend never arises. In this case, D.R. Horton-Texas was a contractor who was sued for construction defects. The complaint did not mention the subcontractor who was negligent and was the policyholder. The trial court and court of appeals concluded that, because the complaint failed to mention the policyholder the duty to defend was not triggered and, as such, the duty to indemnify did not arise. The Texas Supreme Court overturned and concluded that the duty to indemnify was not contingent upon the duty to defend.

In *Allstate Insurance Company v. Leong*, the District of Hawaii limited the definition of "pollution exclusion." In this case, a homeowner sought coverage for damage to a neighbor's retaining wall caused by the release from the sewer line. Allstate sought a declaratory judgment that it did not have a duty to defend arguing the damage was excluded under a pollution exclusion which excluded property damage consisting of or caused by "waste materials or other irritants, contaminants, or pollutants." The District of Hawaii found in favor of the policyholder because, amongst other reasons, the damage could have been caused by water pressure not just "waste material." ■

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The Insurance Recovery Advisor is a quarterly newsletter at Offit Kurman. This newsletter is provided to inform its readers of insurance coverage issues that may affect them or their business. The articles in the Insurance Recovery Advisor do not constitute legal advice or opinion. If you require more information, legal advice or an opinion regarding a specific situation, please do not hesitate to contact Michael Conley at 267.338.1317, the authors, or the editorial board.

Our insurance coverage attorneys assist businesses and individuals in identifying insurance available to pay a claim and recovering what they are owed from their insurance companies. Offit Kurman attorneys provide a realistic claim analysis, then work to develop a cost effective recovery strategy and beneficial resolution. Should negotiations break down, our team of seasoned litigators has the experience and expertise necessary to successfully see the matter through trial.

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