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Battle of the Boy Bands: Are Your Construction Contracts and Coverages in Sync or 98 Degrees Off?

It is a new world of construction contracting in light of financial challenges; evolving project delivery methods; material/supply chain issues; pressure to expand your scope of work or to assume new (and unfamiliar) roles on a job; and a host of modern-day issues that plague the construction industry. Ensuring that your contract obligations are harmonious with all necessary insurance coverages is increasingly challenging. We will explore the factors that complicate what coverages are necessary; what happens when you believe you have the appropriate coverages to protect you, but contractual obligations leave you exposed to liability of which you were not aware; and finally, how the various coverages line up and what each policy type actually covers. Communication related to expectations and obligations of the insured, underwriting, claims professionals, brokers and defense counsel is crucial to utilize your construction contracts and insurance coverages as an effective shield and, when necessary, as a sword to transfer risk. How well these players dance together is going to determine success in managing and mitigating risk.

I. BACK TO THE BASICS

In brief, it never hurts to refresh yourself the on the basics of the policy type(s) that are going to determine coverage.

In a commercial liability policy as related to coverages afforded for a construction related claim, there are some key pieces as follows:

Occurrence
Who is an Insured and What Rights Are They Afforded – Named Insured, Additional Insured, Co-Insured?
What is Bodily Injury and Property Damage
Certificates of Insurance

A. Navigating A Liability Policy

1. Additional Insured Endorsements

Blanket additional insured endorsements typically require that two main criteria must be satisfied to trigger coverage: there must be a written contract requiring additional insured coverage, and the loss must be connected to the named insured's acts or omissions. It is common for coverage disputes to arise over whether there is a sufficient contract and if the party seeking AI status has to be a named party to the written contract. (Discussion at length under the portion of outline related to Contractual Risk Allocation). The intent of the parties as to who is supposed to be a named insured is key.

Specific additional insured endorsements have details as to named party, location, etc.

ISO forms in abundance

There are several AI endorsements and 33 ISO form AI endorsements. By sheer volume alone you can understand why there are coverage disputes over the language of the endorsements even if they are standard forms. Four common ISO additional insured endorsements related to commercial general liability policies purchased by contractors are:

1. Additional Insured – Owners, Lessees or Contractors – Scheduled Person or Organization (**CG2010 4/13**)
2. Additional Insured – Owners, Lessees or Contractors – Completed Operations (**CG2037 4/13**)
3. Additional Insured – Owners, Lessees or Contractors – Automatic Status When Required in Construction Agreement with You (**CG2033 4/13**)
4. Additional Insured – Owners, Lessees or Contractors – Automatic Status for Other Parties When Required in Written Construction Agreement (**CG2038 4/13**)

The first two ISO endorsements require specific information regarding the additional insured and the project. The third and fourth ISO endorsements are “blanket” additional insured endorsements and do not require specific information concerning the additional insured or project information be shown on the endorsements. Instead, they require a written contract to be in force which requires the additional insured status.

CG2010 4/13

The CG2010 additional insured endorsement has the following important characteristics:

1. The additional insured (e.g., project owner, general contractor) is not insured for their own sole negligence. The insured/contractor must be liable in whole or in part for a loss before the additional insured can seek coverage under this endorsement.
2. Coverage for the additional insured is for ongoing operations ONLY. In other words, when the contractor’s work is completed on the project, this additional insured endorsement terminates. Any future alleged claims by the additional insured under this endorsement must have resulted from an occurrence when the project was “ongoing” by the insured/contractor.
3. The project must be stated on the endorsement.

4. Coverage under the endorsement is only permitted to the extent that it is allowed by law (which can vary by state).
5. The endorsement does not require that a written contract be in effect which requires this additional insured status.
6. *However*, if there is a contract in existence, then coverage provided by this endorsement will not be broader than what is required by the contract. Additionally, the endorsement will pay the lesser of the amount required in the contract OR the policy limit.

While the coverage appears broad to the additional insured, the endorsement has numerous conditions, limitations and additional exclusions which may lead to contractual disputes and coverage issues if a party agreeing to the endorsement cannot comply with the terms.

CG2037 4/13
This endorsement contains the same limitations and conditions as the CG2010 EXCEPT that this endorsement ensures the additional insured for completed operations of the contractor and not ongoing operations. This endorsement supplements the CG2010.
Therefore, if an additional insured requires additional insured status for the project, the contractor will need BOTH the CG2010 and the CG2037 endorsements in order to comply.

CG2033 4/13
This additional insured endorsement is a blanket additional insured endorsement and has the following limitations and conditions:

1. The additional insured (e.g., project owner, general contractor) is not insured for their sole negligence. The insured/contractor must be liable in whole or in part for a loss before the additional insured can seek coverage under this endorsement.
2. Coverage for the additional insured is for ongoing operations ONLY. In other words, when the insured/contractor's work is completed on the project, this additional insured endorsement terminates. Any future alleged claims by the additional insured must have resulted from an occurrence when the project was "ongoing" by the insured/contractor.
3. There is automatic additional insured status provided to a party when a written contract requires the additional insured status. The party receiving additional insured status is the named party that contracts with the contractor.
4. Coverage under the endorsement is only permitted to the extent that it is allowed by law (which can vary by state).
5. Coverage provided by this endorsement will not be broader than what is required by the contract. Additionally, the endorsement will pay the lesser of the amount required in the contract OR the policy limit.

While this endorsement provides automatic coverage to additional insureds, there are still numerous conditions, limitations, and exclusions. Additionally, since completed operations are not included in this endorsement, a second endorsement is needed to provide coverage for completed operations for the additional insured.

CG2038 4/13
This endorsement is very similar to CG2033. The primary difference between these two endorsements is that CG2038 applies to a party or parties requiring additional insured status within a construction agreement *that are not the actual contracting party with the contractor*. In other words, the parties are referred to – but not specifically named – in the construction

contract. These "silent" parties are referred to as "upstream parties." As with the CG2033, additional insured coverage for these upstream parties is for ongoing operations only. Therefore, a second endorsement should be included that provides coverage for completed operations if required by the contract.

The key to achieving harmony between the contracts and the AI endorsements is to be aware of the endorsement language that is being bargained for and what limitations, conditions, and additional exclusions the AI endorsement may contain to determine if appropriate coverage is in place.

2. SIR Endorsements and Who Pays It (contracting away this obligation; bankruptcy, drop down issues)

Generally, an insurer owes no obligation to an additional insured to defend or pay damages unless and until the Self-Insured Retention ("SIR") of a policy has been paid. As a result, the additional insured may end up having to bear the entire amount of the SIR or may even be left with no coverage at all from such commercial general liability policy if the SIR was not paid. The misconception that a deductible and SIR are essentially the same thing can be problematic. One key difference is that an insurance policy with a deductible may obligate the insurer to respond to a claim from "dollar one" subject to the insurer's right to later recover the amount of the deductible from the insured. A policy subject to a SIR obligates the insured to satisfy the SIR before the insurer's obligation is triggered. As a result, there is risk to an additional insured if the AI has not considered that the coverage it seeks is subject to the SIR and who has the obligation to pay it. If the actual coverage information is not reviewed prior to a claim arising, and a certificate of insurance is relied upon, it will be too late to address the issue proactively. In the alternative, parties in a construction contract can contractually require another to maintain insurance policies with deductibles and specifically preclude the use of SIR endorsements. Additional costs associated with deductibles and bankruptcy of one of the contracting parties are considerations related to SIRs.

3. Supplemental Payments

When the insured contractually agrees to provide additional insured coverage and fails to do so, coverage disputes are the result. Resolution of this issue may be addressed by supplemental Payments clause in a liability policy Indemnitees (e.g., should be an Additional Insured Status dispute).

4. Key Exclusions

Business Risk Contract Liability Exclusions need to be addressed in the context of contractual obligations and coverage afforded.

B. Professional Liability Policies

Professional liability or professional indemnity policies do not provide additional insured coverage. Coverage disputes arise from the simple fact that parties do not understand how a professional liability policy works. A traditional professional liability policy provides coverage only to the named insured for the negligent performance of professional services. Parties contracting to transfer risk must be wary that indemnification clauses must be drafted carefully to address the obligations of a design professional to defend and/or indemnify another (e.g., split indemnification clauses; design professional performance of services outside scope of "professional services").

II. MANAGING RISK EFFECTIVELY THROUGH INSURANCE

If a party has responsibility for a type of loss on a project, it will want to obtain insurance for that loss to minimize its costs, should the loss be realized. Accordingly, when preparing insurance requirements for construction-related contracts, it is important to identify and address the risk obligations associated with each project discipline and to make sure that the limits are adequate to address possible losses.

Contract insurance requirements for design professionals (e.g., architects, engineers, etc.) should include auto and commercial general liability; workers compensation/employers liability; and, most importantly, professional liability insurance. The limits of design professionals' professional liability coverage are particularly important. Because a professional liability policy typically will cover losses arising on all of a design professional's projects, not just your project, it is important that the aggregate limit be sufficiently high. Indeed, owners often consider requiring excess limits for professional liability coverage or requiring that the coverage be "project specific" either through a separate project policy or sublimits applicable only to the project. For large projects, an owner also may wish to consider obtaining owners protective professional liability insurance coverage, which indemnifies the owner directly for losses arising out of the design professional's professional negligence that exceeds the limits available under the design professional's own professional liability policy.

Contractors performing work on the project should be required to carry automobile liability, commercial general liability (CGL) and workers compensation/employers liability policies, as well as an excess liability policy providing coverage over the automobile and CGL policies' limits. For those contractors and subcontractors performing any design-build functions, professional liability coverage also should be required. To prevent coverage gaps, contractors' and subcontractors' insurance requirements should include pollution liability coverage. If the owner will procure the property or builder's risk coverage, as discussed below, contractors and subcontractors should consider the need for an "installation floater" or similar coverage to protect their equipment and supplies on-site, off-site, and in transit.

While the liability coverage referenced above covers most project accidents resulting in (i) bodily injury and (ii) damage to property other than what is being constructed, in most cases it does not cover damage to the structure being built or the materials being used. This damage, however, can be covered by obtaining a "builder's risk" policy. While it is sometimes possible to cover damage to construction projects under an owner's existing property policy, there are coverage limitations in standard property insurance forms that make procurement of a builder's

risk policy desirable in most cases. If a builder's risk policy is procured, consideration should be given to whether the owner or the contractor obtains it. This determination is best made on a project-by-project basis, taking into consideration such factors as the type of project (e.g., new construction or renovation of an existing structure), type of contract (cost plus or stipulated sum), financing/lender's requirements (owner may want to "bundle" soft cost and loss of income coverage with the builder's risk policy to avoid claim delays and argument among insurers over coverage), the presence of a master property program (owner or contractor), location of project, the parties' relative economic leverage to negotiate the most favorable premium and coverage, the contractor's level of sophistication, and the owner's desire to participate in project-specific risk management. That being said, it is more common for owners than contractors to purchase builder's risk insurance, which covers the interests of all of the other parties having an interest in the project.

A. Additional Insured Status and Reliance on Certificates of Insurance

A party seeking Additional Insured ("AI") status under the policies of another should require status as an Additional Insured for itself and, by name, any other entities that should also be afforded AI status (e.g., general contractor, construction manager and owner/developer entities). Further, there should be an express request for no limitations on the AI status (to be afforded the same rights under all applicable policies as the Named Insured) and, to the extent it is possible, seek specific AI endorsements, to fit the needs of the AI and ensure the proper coverages are available. The liability coverages afforded should be primary over all other available coverages to the AI entities. The AI entities should seek follow form excess policies (no limiting language in the excess policies for AI coverage) as an additional security to ensure that all policies under which AI status is afforded are primary and exhausted prior to any other policies, available to the AI, come into play (vertical exhaustion) (e.g., Iacovino coverage issues).

B. Sufficient Proof of Insurance v. What You are Able to Obtain

As we know, Certificates of Insurance ("COI") are simply proof that an entity has certain insurance coverages. The COI alone and/or the language written on the face of the COI are not, as a general rule, able to be used to legally enforce an insurer to provide the specific type of coverage demanded by an AI. In other words, a COI is nothing more that paper generated to show that a specific type of policy with certain limits exists. The terms, conditions, exclusions, and the type of AL endorsement of a policy is not evident from this "proof of insurance." The issues surrounding what is sufficient proof to ensure the coverages bargained for are actually available is ongoing. In a perfect world, before a project commences, the entities in contractual privity would exchange all contract documents and policies under which coverage may be afforded. Realistically, there is a resistance to providing policies, in their entirety to someone who should be afforded AI status (e.g., global v. project specific policies). It is a matter of negotiation and at the very least, the party who has AI status should be requesting COI, declarations page, schedule of forms/endorsements, AI endorsement, SIR endorsement as a preliminary request. If there are red flags in the schedule of forms, then you should be allowed to view the forms at issue.

C. Addressing Potential Coverage Gaps - Multi-use projects, wrap programs (those excluded), coverages over time (e.g., policy types, retroactive/tail coverage)

The subject of potential coverage gaps in the context of coverages for a construction project is one that is an endless minefield for brokers, attorneys, claims and underwriting professionals. The issues that the insurance industry is dealing with today are very different from a decade ago and carriers, brokers, defense attorneys have had to adapt to effectively deal with unchartered territory in the construction arena such as various project delivery methods (design/build), new/novel project types (cannabis production facilities; modular building), specialized projects (multi-use with different insurance programs on one project), global development/projects that involve foreign laws, insurance considerations.

D. Waivers of Subrogation

A waiver of subrogation clause in a contract is intended to prevent an insurer from suing a third party to recover damages the insurer paid on a claim. Waivers of subrogation can impact insurance coverage.

Waivers of subrogation are used in liability insurance to reinforce a transfer of risk from one party to another in a contract. If a party assumed liability on behalf of another, it could use a waiver of subrogation to protect itself against subrogation lawsuits by the other party's liability insurer.

This can protect the business in cases when the partner's employees or clients file insurance claims for bodily injury or property damage that occur on the business's premises, as a result of the partner working with the business, or due to negligence on the part of the business.

Most general liability policies contain a condition that prohibits you from waiving your rights of subrogation after a loss has occurred. They are typically silent on waivers executed before a loss occurs.

Depending on the terms of a liability policy, an insured may breach the insurance agreement terms if the insured agrees to a waiver and does not discuss doing so with the liability insurer beforehand. A party negotiating a contract who seeks a waiver may demand that you add a waiver of subrogation endorsement to your liability policy. This ensures that the insurer is aware of the waiver (sometimes for additional premium for the endorsement). Coverage issues arise when the insured agrees to a waiver, but the insurer is not aware, and the policy is clear that it prohibits such a waiver.

There are two basic types of waiver endorsements used on liability policies: scheduled and blanket.

- A **scheduled endorsement** states that the insurer will not sue the party listed in the endorsement if you have waived your rights of subrogation against him or her.
- A **blanket endorsement** affords broader coverage and typically states that if you have agreed in a contract to waive your rights to sue someone, the insurer will not sue that party.

Key Takeaways related to waivers of subrogation are as follows:

- A waiver of subrogation prevents an insurance company from suing a third party to recover damages they paid on an insurance claim.
- Subrogation is the legal right of an insurance carrier to sue a negligent third party that caused an insurance loss that the carrier had to pay.
- If you sign a waiver of subrogation and your insurance company pays out a claim to you, the insurance company cannot recover that money from the third party that was at fault in the claim.
- Waivers of subrogation often are used in general liability, commercial auto, workers' compensation, and commercial property insurance.

III. Allocating Risk Effectively Through Contracts

A. Allocating Risk to the Person in the Best Position to Control the Risk (e.g., crap usually flows downward)

A fundamental risk management concept is that owners and contractors should anticipate potential project risks and determine whether it is more advantageous to accept responsibility for each risk or to allocate responsibility for that risk to another party. From a risk management perspective, it is important to assign a project risk to the party best able to control and manage it. For example, a project owner will want to allocate the risk that someone is hurt by construction operations to the contractor, who is in the best position to provide a safe work site. A contractor will want to allocate the risk of design errors to the owner, who often holds the contract with the architect and therefore is in a better position to address and minimize these losses.

B. Contractual Privity and Third-Party Beneficiary outside Contractual Privity

As we briefly touched on earlier, blanket additional insured endorsements typically require that two main criteria must be satisfied to trigger coverage: there must be a written contract requiring additional insured coverage, and the loss must be connected to the named insured's acts or omissions. Disputes arise as to whether the named insured and the intended additional insured must be parties to the contract (i.e., whether the parties must be in direct contractual privity to trigger the blanket additional insured endorsement).

In the construction industry, upstream parties (owners / general contractors) transfer risk downstream to subcontractors via contractual risk transfer and additional insured requirements (e.g., contract between GC and owner obligates the GC and subcontractors to name the owner, and frequently the “owner’s representatives”, design professionals, as additional insureds on their general liability policies). Even if the GC, in turn, requires the subcontractors to name the owner et al. as additional insureds and the subcontractors procure policies containing blanket additional insured endorsements, it is not always clear that the subcontractor's insurer will be obligated to provide additional insured coverage to the owner et al. due to the absence of a direct contract between those parties.

Courts across the country are split as to whether direct contractual privity is required to satisfy certain additional insured endorsements as follows:

Contractual Privity Is Not Required

The following cases from Connecticut, Maine, and Texas held that contractual privity is not required to satisfy certain additional insured endorsements.

Connecticut: The Federal District Court for the District of Connecticut held that direct contractual privity is not required in *First Mercury Ins. Co. v. Shawmut Woodworking & Supply, Inc.,* 48 F. Supp. 3d 158, 160-175 (D. Conn. 2014) (*aff'd,* 2016 U.S. App. LEXIS 16152 (2d Cir. Aug. 29, 2016)), which concerned coverage for bodily injury claims arising out of a construction project at a Yale facility.[1]

Maine: The Federal District Court for the District of Maine also found that direct contractual privity is not required in *Pro Con, Inc. v. Interstate Fire & Cas. Co.,* 794 F. Supp. 2d 242 (D. Me. 2011). [2]

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[1] The general contractor, Shawmut Woodworking, hired steel fabrication subcontractor Shepard Steel, which hired sub-subcontractor Fast Trek Steel to perform erection work. Three employees of Fast Trek were killed when a steel web structure collapsed during installation. The estates of the employees filed suit against Shawmut and Shepard.

Shawmut and Shepard both tendered additional insured claims to Fast Trek's commercial general liability (CGL) insurer, First Mercury Insurance. The First Mercury policy contained an additional insured endorsement that conveyed additional insured status to "any person or organization for whom you are performing operations when you and such person or organization have agreed in writing in a contract or agreement that such person or organization be added as an additional insured on your policy...."

First Mercury denied coverage to Shawmut on the basis that it was not an additional insured because it had no direct contractual relationship with Fast Trek. Shawmut argued that a direct contractual requirement with Fast Trek was not required and that, together, the Shawmut-Shepard contract and the Shepard-Fast Trek contract triggered the additional insured endorsement.

The court held that, for purposes of the First Mercury endorsement, the agreement to provide additional insured coverage can be memorialized in separate contracts without direct contractual privity. The court noted that nothing in the endorsement's language required direct contractual privity, and the court declined to read in additional terms, such as "direct" contract or have agreed "with each other."

In 2016, the Second Circuit Court of Appeals affirmed the district court's ruling, reinforcing the idea that the additional insured endorsement did not require the parties to enter into a "single" contract "with each other." The Second Circuit also noted that, if First Mercury intended for the additional insured endorsement to apply only to parties in direct contractual privity, it could have added in language specifying the need for a single, direct contract or agreement.

[2] In that case, Pro Con was serving as general contractor for construction of a hockey rink at Bowdoin College. Pro Con hired steel subcontractor Canatal Industries and required Canatal to name both Pro Con and Bowdoin College as additional insureds on Canatal's liability policies. Canatal hired sub-subcontractor CCS Constructors to provide structural steel work and required CCS to name Pro Con, Bowdoin, and Canatal as additional insureds on CCS's liability policies.

To fulfill its contractual obligations, CCS purchased a CGL policy from Interstate Fire and Casualty. The Interstate policy contained a blanket additional insured endorsement that provided coverage to "[a]ny person or organization for whom you are performing operations when you and such person or organization have agreed in writing in a contract or agreement that such person or organization be added

Texas: *Millis Dev. & Constr. v. American First Lloyd's Ins. Co.,* 809 F. Supp. 2d 616, 618–636 (S.D. Tex. 2011).[3]

The courts in the referenced cases held similarly that additional insured coverage can be memorialized in separate contracts without direct contractual privity. The courts noted that nothing in the endorsement's language required direct contractual privity, and the court declined to read in additional terms, such as "direct" contract or have agreed "with each other." The courts emphasized that if the intent of the endorsements was to be applied only to parties in direct contractual privity, language expressing that intent should be found in the endorsement.

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as an additional insured on your policy." A CCS employee was injured while working on the project and sued Pro Con for his injuries. Pro Con sought coverage under the Interstate policy, but Interstate rejected the tender, and a declaratory judgment action followed.

In determining whether Pro Con qualified as an additional insured under the blanket endorsement, the district court emphasized the importance of reading what the endorsement actually said, instead of reading what it could have said. The endorsement did not include the phrase "with you" or "with each other" after the phrase "agreed in writing in a contract or agreement"; it simply stated that there must be a written contract.

The court held that CCS had agreed in writing to add Pro Con as an additional insured, thereby satisfying the blanket additional insured endorsement. The fact that CCS had agreed to do so in a written contract with Canatal as opposed to Pro Con was immaterial. The court also pointed out that a certificate of insurance produced in connection with CCS's work on the project stated that Pro Con was an additional insured on the policy, which was consistent with the court's determination that Pro Con qualified as an additional insured.

[3] A similar decision was reached by the Federal District Court for the Southern District of Texas in *Millis Dev. & Constr., Inc. v. American First Lloyd's Ins. Co.,* 809 F. Supp. 2d 616, 618–636 (S.D. Tex. 2011). In that case, which concerned a construction project at the Cross Creek Ranch Visitors and Recreation Center, general contractor Millis Development and Construction hired subcontractor Texas Mechanical Contractors (TMC), which hired sub-subcontractor Dynamic Air Balancing. The contract between Millis and TMC required that TMC obtain a CGL policy and make Millis and the project developer, Trendmaker Homes, additional insureds on that policy. An employee of Dynamic was injured while performing work on the project and sued Trendmaker and Millis for his injuries.

Trendmaker and Millis sought additional insured coverage from TMC's CGL insurer, America First. The America First policy contained a provision that conveyed coverage to "any person or organization when you and such a person or organization have agreed in writing in a contract, agreement, or permit that such person or organization be added as an additional insured on your policy." America First confirmed that Millis qualified as an additional insured on the policy but denied coverage for Trendmaker on the basis that it did not have a contract with the named insured, TMC.

Like the decisions by courts in Connecticut and Maine, the Southern District of Texas determined that a direct contract between the named insured and the additional insured is not necessarily required by the plain language of the policy. First, the court noted that the additional insured endorsement did not include the words "direct" or "between" in reference to the written contract or the words "with each other" or "together" after the phrase "have agreed." The endorsement also did not require that both the named insured and additional insured have signed the written contract, only that they both agreed, which they did in separate contracts. Accordingly, the court held that Trendmaker qualified as an additional insured on the America First policy.

Contractual Privity Is Required

Unlike courts in Connecticut, Maine, and Texas, courts in New York, Illinois, and Louisiana have held that privity is required where certain additional insured endorsements are involved.

New York: In New York, trial level courts have inconsistently decided the issue of whether direct contractual privity is required for certain additional insured endorsements. However, a recent decision from the Appellate Division of the New York State Court confirms that New York courts tend to interpret additional insured endorsements to require direct contractual privity. *Gilbane Bldg. Co./TDX Constr. Corp. v. St. Paul Fire & Marine Ins. Co.,* 2016 N.Y. App. Div. LEXIS 5930 (N.Y. App. Div. 1st Dep't Sept. 15, 2016).[4]

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[4] In *Gilbane,* the Dormitory Authority of the State of New York (DASNY) hired Gilbane Building/TDX Construction, a Joint Venture (JV), as construction manager and Samson Construction as prime contractor. During the course of the construction project, Samson's excavation and foundation work caused adjacent buildings to sink. DASNY filed suit against Samson and the project's architect, and the architect brought a claim against Gilbane/TDX JV.

Per the construction management contract between DASNY and Gilbane/TDX JV, any prime contractor was required to name the construction manager as an additional insured. Accordingly, Gilbane/TDX JV sought additional insured coverage from Samson's insurer, Liberty Mutual. Samson's Liberty policy contained an endorsement that provided additional insured status to "any person or organization with whom you have agreed to add as an additional insured by written contract…."

Liberty filed summary judgment, seeking a declaration that it had no duty to defend Gilbane/TDX JV because it did not have a direct contract with the named insured, Samson. At the trial level, the court denied summary judgment, finding that the endorsement required only a written contract to which Samson was a party (i.e., the contract between DASNY and Samson) and, because that contract obligated Samson to name the construction manager as an additional insured, Gilbane/TDX JV was entitled to additional insured coverage under the Liberty policy.

On appeal, the New York Appellate Division, First Department, reversed the trial court's holding, relying on two New York cases: *AB Green Gansevoort, LLC v. Peter Scalamandre & Sons, Inc.*, 102 A.D.3d 425, 961 N.Y.S.2d 3 (N.Y. App. Div. 1st Dep't 2013), and *Linarello v. City Univ. of N.Y.*, 6 A.D.3d 192, 774 N.Y.S.2d 517 (N.Y. App. Div. 1st Dep't 2004). Both of those cases involved endorsements that conveyed additional insured coverage "when you and such … organization have agreed in writing in a contract or agreement that such … organization be added as an additional insured on your policy." In both cases, the First Department found that direct contractual privity was required. Although the language in the Liberty policy differed from that in *AB Green Gansevoort* and *Linarello*, the First Department found those cases controlling and held that the Liberty policy also required direct contractual privity.

In a lengthy dissent, Judge Kahn opined that *AB Green Gansevoort* and *Linarello* were indeed distinguishable because they involved "when you and such person" language as opposed to the "with whom" language found in the Liberty policy. Furthermore, Judge Kahn pointed out the poor syntax of the Liberty endorsement, where the word "whom" is the object of both preposition "with" and infinitive "to add." Judge Kahn opined that, to correct the syntax, the endorsement should be read without the unnecessary "with," which would cause the endorsement to provide coverage for "any person or organization whom you have agreed to add as an additional insured by written contract…." Finally, Judge Kahn stated that the Liberty endorsement was ambiguous due to the poor syntax and as illustrated by the fact that certain New York trial and district courts interpreting similar language have held that no contractual privity is required.

Illinois: The Illinois Appellate Court has also held that certain additional insured endorsements require direct contractual privity. In *Westfield Ins. Co. v. FCL Builders, Inc.*, 407 Ill. App. 3d 730 (Ill. App. Ct. 1st Dist. 2011).[5]

Louisiana: The same reasoning held true in a case before the Federal District Court for the Eastern District of Louisiana in *Venable v. Hilcorp Energy Co.*, 2010 U.S. Dist. LEXIS 42629 (E.D. La. Apr. 29, 2010).[6]

Contractual Privity Key Takeaways

The key take away is that the contract documents and additional insured endorsements of the applicable policies, when seeking risk transfer, should be reviewed and both the contract and

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[5] FCL Builders was acting as general contractor on a construction project. FCL subcontracted steel fabrication and erection work to Suburban Ironworks, which in turn subcontracted steel erection work to JAK Ironworks. The contract between FCL and Suburban required Suburban to obtain CGL insurance that would provide coverage for FCL and to require any subcontractors Suburban hired to do the same. When Suburban hired JAK, it incorporated the terms of the FCL-Suburban contract into the Suburban-JAK contract. Therefore, JAK was also obligated to procure insurance and include FCL as an insured. JAK did so by purchasing a CGL policy from Westfield Insurance.
During the course of the construction project, an employee of JAK was severely injured when he fell off a steel beam. The worker sued FCL and Suburban, which tendered the lawsuit to Westfield for defense as additional insureds. The Westfield policy included as an additional insured "any person or organization for whom you are performing operations when you and such a person or organization have agreed in writing in a contract or agreement that such person or organization be added as an additional insured on your policy." However, Westfield denied FCL's tender, claiming that it was not an additional insured, and a declaratory judgment action followed.

The Illinois Appellate Court found that direct contractual privity between the named insured and additional insured was required, stating that "[t]he policy explicitly and unambiguously requires a direct, written agreement to that effect in order to cover anyone other than JAK under the policy." The court emphasized that the endorsement provided coverage "when you *and such a person or organization*" enter into a contract, not when you and "any" person enter into a contract. Because there was no such agreement directly between JAK and FCL, FCL could not qualify as an additional insured on the Westfield policy.

[6] The *Venable* matter concerned injuries sustained by a worker on a drilling barge owned by Hilcorp Energy. Hilcorp hired Greene's Energy Group to perform work on the barge, and an employee of Greene's suffered a heart attack while working aboard the barge. Hilcorp had separately hired HTK Consultants to work on the project, which hired Heard Consulting. The worker sued a number of entities involved in the project, including HTK and Heard, which sought coverage from Greene's general liability insurer Nautilus Insurance.
The Nautilus policy contained an additional insured endorsement that stated, "where required by written contract, a person, firm or organization is included as Additional Insured but only in respect of liability for Bodily Injury … arising out of operation performed by or on behalf of the named Insured under written contract with such additional insured…." Nautilus argued that HTK and Heard were not additional insureds on the policy because they did not have a direct contract with Greene's, and the court agreed. The court stated that the additional insured endorsement, "while not a paragon of clarity, does require that a party have contracted directly with the Named Insured in order to attain additional insured status." Because neither HTK nor Heard entered into a direct contract with Greene's, they could not be additional insureds on the Nautilus Policy.

the policy should expressly provide for AI coverage even for parties not in direct contractual privity (if the contract does provide this intent/language and the policy does not, there may be resistance by the insurer, even if the party seeking AI status may still be a contractual indemnitee).

If the ultimate goal is to ensure coverage where the parties are trying to do the right thing and provide coverage for defense and indemnity of another, all parties involved are detrimentally affected if there is a dispute over the contractual privity requirement issue is related to AI coverage: (1) the owner is denied additional insured coverage on the subcontractor's policy, (2) the general contractor is likely obligated to provide additional insured coverage for the owner and can no longer pass that obligation downstream to the subcontractor, and (3) the subcontractor is exposed to a potential claim for breach of contract for failure to procure additional insured coverage for the owner et al.

C. Indemnification and Insurance Provisions in a Contract

An indemnity provision generally is a section in a contract that requires one party to pay for losses incurred by the other party (and, often, to defend the other party against claims for such losses) as a result of claims made by third parties. Following up on the risk allocation example set forth above, a construction contract indemnity provision often requires the contractor to indemnify and defend the owner from and against claims for bodily injury and property damage that arise from the negligence of the contractor or one of its subcontractors while performing the work. Another indemnity clause may require the owner to indemnify and defend the contractor from and against claims based on the existence of hazardous materials on the project site over which the contractor has no control.

Contractual indemnity provisions included in contracts are only as good as the indemnitor's ability to honor them. The indemnitor must have the financial ability to satisfy its indemnification obligations. Accordingly, when transferring risk through an indemnity provision, it is important to ensure that the transferee (or the indemnitor) has or is able to procure the proper insurance coverage sufficient to pay for the assumed indemnity obligations. One caveat to this general principle is that some risks allocated in an indemnity provision, such as liability arising out of an indemnitor's intentional misconduct, are not insurable (e.g., public policy considerations). The lack of insurability for such conduct, however, does not necessarily constitute a valid argument for not requiring the indemnity—the party best able to control the loss should be the one indemnifying the other party from and against that loss, regardless of whether insurance is available to back up the contractual obligation assumed to defend/indemnify.

Interpretation and enforcement of indemnification clauses is another issue and very jurisdictionally specific. (Anti-Indemnity statutes, jurisdictional nuances). Jurisdictions are split as to whether to hold the contracting party who agrees to defend/indemnify but, for whatever reason, there is no insurance coverage to provide for the obligation. (e.g., PA / NJ courts

difference in treatment of breach of contract for failure to provide proper insurance coverage for contractual defense and indemnification obligations).

D. Hold Harmless v. Limitation of Liability clauses and the Effect of Anti-Indemnity Laws

Hold harmless indemnification clauses are enforceable but are generally strictly construed. Language required for enforceability is very jurisdiction specific; the language must be express and unambiguous on its face; it cannot be overreaching or against public policy; and many courts will not enforce a hold harmless clause in favor of a party seeking to be indemnified for its own negligence, with exceptions. Certain states require magic language (e.g., PA); certain states require that the indemnification language in a contract be bolded, set apart and/or jumping off the page to be enforced (e.g., TX); and then there are several states that have Anti-indemnity statues which preclude indemnification in varying circumstances and as to certain entities involved in a construction project. It is imperative to know your anti-indemnity laws and the common law of different jurisdictions where it will affect risk allocation and coverage defenses.

Generally, anti-indemnification statutes limit the enforceability of indemnification requirements, in construction contracts, by requiring each party to take responsibility for their own negligence. The states that have anti-indemnity statutes vary regarding which form of indemnity agreements are prohibited. The three forms of indemnity agreements are:

Limited: Subcontractor is only responsible for its own negligence, and only if solely at fault. The owner or general contractor receives no indemnification if they are even partially at fault. All states allow limited indemnity agreements.

Intermediate: Subcontractor is responsible for its own negligence, as well as partial negligence. If the owner or general contractor is solely at fault, there is no indemnification from the subcontractor. Contracts using intermediate indemnity often include the phrase "caused *in part* by," which establishes that the negligence can be partially contributed by each party involved.

Broad: Subcontractor is required to indemnify the owner or general contractor, regardless of who is at fault. This means the subcontractor must indemnify the general contractor for the subcontractor's sole negligence, the owner or general contractor's sole negligence, or any combination of negligence between the two parties. Broad indemnity is the most favorable for owners and general contractors and puts the greatest indemnification requirement on the subcontractors. Contracts using broad indemnity include the phrase "caused *in whole* or in part by…indemnified parties." The inclusion of "in whole" establishes the sole negligence indemnification requirement and including "indemnified parties" specifies that the sole negligence can be caused by parties other than the subcontractor or indemnitor.

In general, broad indemnity agreements favor owners and general contractors, whereas limited indemnity agreements provide protection for subcontractors.

Limitation of liability clauses are different from hold harmless clauses because they are generally more likely to be enforced by a court if they are if they are express/unambiguous, reasonable and/or reasonably related to the portion of the work or services performed on a project (e.g., fee/compensation, insurance limits). Hold harmless and limitation of liability clauses in a contract are not mutually exclusive and a way to shield a party from excessive exposure and/or limited coverage due to gaps/oversight on procurement of coverages.

E. Obligation to Defend v. Indemnify and the Obligation of Insured v. Insurer to Defend and/or indemnify.

Jurisdictions vary in their treatment of the trigger to defend but the obligation to defend is generally broader that the obligation to indemnify. We have previously discussed at length the coverage issues that can arise if an insured agrees to defend and indemnify another party, providing the party contractual indemnitee status, but this does not automatically provide the party seeking defense and indemnity the status of an AI. The resulting exposure to the insured by failing to work with its insurer to properly set up coverages for the insured's obligations may result in significant exposure and, coverage disputes between insured and insurer (e.g., declaratory judgment and bad faith allegations). On the flip side, if the insured seeks defense and indemnity from another party but fails to do its due diligence in ensuring that there is insurance coverage (as well as the proper language to be afforded AI status), the insured's carrier is then in a position, along with the insured, to pursue defense/indemnity from an entity that may not be financially sound and its insurer(s) who are resisting tender, potentially creating significant additional litigation costs (not necessarily recoverable in certain jurisdictions).

F. Consistency of Contractual Obligations and Coverages and Key Information Needed to Ensure Contracts and Coverages are Consistent.

Claims professionals, brokers and defense counsel should work in harmony with their respective clients/insureds to address the need for consistency of contracts and coverages so that claims are addressed efficiently and cost effectively.

There are several caveats in the shared goal to do so:

(1) Cookie Cutter Contracts Do Not Fit All Projects – standard form contracts are problematic as they do not necessarily consider the nuances of jurisdictional / legal limitations; address specific insurance program issues and/or project delivery details which may alter the types of coverages and contract language required to properly allocate risk.

(2) Global v. Project Specific policy issues – this is not a basis for not providing or giving key policy information as there are ways to protect information that is not relevant AND at some point (litigation) this is discoverable.

(3) Resistance to the Request for Contract Documents and Policy Information – This is an ongoing reality but if an insured has an opportunity to request the contract documents and make policy information a requirement, at the inception of a project, before entering into contracts, it should be done (e.g., COVID examples; contract language related to the right to view the contract documents; getting contracts post litigation).

(4) Vetting business partners and their insurers – litigious, financial status, if unknown to you it is even more important to get airtight contract language and ensure policy language that follows the contractual obligations the business partner assumes toward you.

(5) Regular review/update of contract language / policies – this is always important to the insurer and the insured, but construction projects are fluid and costs/delay are the primary concern, so this risk management tool is severely underutilized; pandemic lessons – new and novel claims related to insufficient contract language and increased coverage issues.