Insurance Coverage That Does Not Cover

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At the beginning of a construction project, once the construction contracts are negotiated and executed, everyone is focused on beginning the physical construction. However, once the physical construction work begins, some of those carefully drafted and negotiated clauses of the construction contract get overlooked and often times the construction management team does not follow up to ensure that the contractors and subcontractors are procuring the proper insurance to adequately protect the upstream contractors and owner in the event of a third-party personal injury or damage to property.

Often forgotten by contractors in the haste of getting the job started is the fact that insurance policies are also a negotiated contract between the insurer and the insured. The terms of that insurance contract may, and frequently, does not follow the requirements of the construction contract. As recent case law reaffirms, the insurance contract trumps the construction contract when there are questions whether the insurance company is required to provide additional insured defense and indemnification to the contractor and owner.

In a recent decision, in reviewing a subcontractor's insurance policy, the court found that an exclusion in the insurance policy prevented the upstream contractor from receiving the contractually agreed additional insured coverage and indemnity when an employee of its subcontractor was allegedly injured on the project.

In a declaratory action commenced by the subcontractor's insurance company to determine that it was not obligated to indemnify and defend the contractor, the insurance company claimed that two provisions in the insurance contract excluded coverage for the alleged injury. First, the insurance policy only listed five types of covered construction activities and the alleged injury was not the result of any of the activities listed in the policy. Secondly, the policy excluded injuries to persons who were employees of the contractor or any of the contractor's subcontractors and sub-subcontractors.

The subcontractor's insurance company claimed that, in issuing the insurance policy to the subcontractor, it only agreed to provide coverage for five types of construction work: "Carpentry-Dwelling," "Carpentry-interior," "Dry Wall or Wallboard Installation," "Painting-interior-buildings or structures-Painting and Decorating," and "Tile, Stone, Marble, Mosaic or Terazzo Work-interior construction." The court in reviewing the underlying personal injury complaint determined from the allegations that the injury occurred while the subcontractor's employee was performing heating, ventilation and air conditioning (HVAC) work. The court held that the allegations of the underlying complaint made clear that the work the individual was performing at the time of the accident fell outside of the five classifications enumerated in the insurance policy and, therefore, the subcontractor's insurance company had no duty to defend or indemnify the contractor in the underlying action.

The contractor attempted to argue that the insurance policy's declaration of covered activities should not be read so narrowly and that the underlying personal injury complaint's reference to "renovation" or "construction work" should bring the injured employee's activities under the ambit of the policy because it is possible that the employee's renovation or construction work was reasonably related to or was in support of the contractor's covered work. The court dismissed this argument because the policy declarations did not include "general contracting" and the court found the contractor's interpretation to be too broad and would trigger a duty to defend whenever a complaint stated that a worker was injured while performing a specific task that, although not covered by the specific policy classifications, involved "construction."

The court, in reaching this decision, cited to the general rule that in determining whether the underlying complaint can be read as even potentially bringing the claim within the coverage of a policy, a court should not attempt to impose the duty to defend on an insurer through a strained, implausible reading of the complaint that is tortured and unreasonable. Here the court determined that there was no reasonable possibility that the HVAC work was performed in furtherance of the covered activities. Because the court determined that the work activities were not covered by the policy, it did not analyze the insurance carrier's second argument that there was an exclusion in the policy that there was no coverage for injuries to a subcontractor's employees.

Commentary

The reality of this case is that the contractor is now left without insurance coverage (defense and indemnity) that it was contractually entitled to receive. The additional insured coverage of insurance defense and indemnity was likely negotiated and required under the subcontract agreement. However, because of the exclusion in the subcontractor's insurance policy, the contractor is left to defend and pay any judgment obtained by the subcontractor's injured employee out-of-pocket. Depending on the severity of the injury, this absence of insurance coverage can put a contractor out of business because it may not be able to pay the legal fees and judgment.

This case outlines the dilemma that a contractor finds itself in when it does not review its subcontractor's policy before the subcontractor begins work on a project. In the most basic terms a subcontractor's insurance policy should never have an exclusion or absence of coverage for the specific work activities that the subcontractor is being hired to perform. A careful reading of the subcontractor's exclusions or declarations would have uncovered the fact that an HVAC subcontractor was not insured to perform HVAC work. The all too common course of conduct of merely obtaining the single page Acord certificate is not enough to adequately protect a contractor. None of the policy exclusions or endorsements are listed on the Acord certificate and, the Acord certificate does not even prove that insurance was actually procured by the subcontractor.

There should never be a situation where a contractor or a subcontractor should be left without insurance coverage. Before any subcontractor steps foot on the job site

the contractor should require its subcontractors to provide copies of the insurance policies or, at the very least, obtain copies of the policy declarations and exclusions. Those documents should be reviewed by the contractor, its insurance broker and attorney to confirm that the contractually required insurance is actually procured. If it is found that the subcontractor's insurance is inadequate, the subcontractor should not be permitted to enter the job site and commence work. A little diligence in the beginning of the job can go a long way to prevent an uninsured loss.