

Construction Contracts for Subcontractors— Are You Covered?

BY RON THOMPSON

When you clearly understand what you're being asked to sign, you may want to go for better terms.

YOU HAVE PROBABLY been there a 1,000 times. You have bid a job, fairly certain you will get the job and then the old, dreaded 40-page “Subcontractors Agreement” comes flying in from your customer. “Sign and send back” is the request. Digging through the Killer Subcontractors Agreement can be onerous, written in nearly incomprehensible terms, then you come to the “Indemnity” section and the indemnification clause creates a fairly straightforward obligation: the subcontractor (you) will defend and pay damages if the general contractor, owner and architect are sued for injury arising out of the subcontractors’ (your) work.

At this point, it is important to know about risk transfer. Contractual risk transfer is generally achieved through two types of provisions. The contract may include an “indemnification” clause, an “additional insured” clause (sometimes part of a broader “insurance” clause), or both. These provisions create unique obligations for the subcontractor (you) and should be carefully reviewed because they could possibly create additional exposures that may not be covered in your general liability policy.

Coverage Issues on Subcontractor’s General Liability Policy

By signing the Killer Subcontractors Agreement in its original form without negotiating more favorable terms, you may be exposing your company to additional unwanted exposure and potential uncovered claims. In the indemnity section, the contract usually states that you (the subcontractor) will hold harmless the general contractor, owner and architect for all claims, damages, etc., for all liability *arising out of* the subcontractor’s (your) work, in essence requiring you to handle, indemnify and defend claims caused by the general contractor’s negligence, even in the absence of fault on the part of the subcontractor (you). The general contractor or owner may have had faulty general supervision, failed to provide a safe place to work or failure to take reasonable precautions and adopt proper safeguards to protect workers from injuries, for which you the sub-

contractor had no fault. But the definition of all liability arising out of your work could potentially drag you (the subcontractor) in to defend and indemnify the GC and owner.

Here is the coverage problem. Many court decisions have applied coverage even when the result of subcontractor’s (your) negligence was absent because of the broad interpretation by the courts of “liability arising out” definition of subcontractors work, found in the construction agreement. In 2004, insurance carriers changed the wording in the additional insured endorsements on your general liability policy to the injury or damage must be “caused, in whole or in part” by subcontractor’s acts or omissions. The revised wording is more restricted and narrows the definition of what your liability coverage offers.

Your coverage now specifically states that in order to indemnify the GC, owner and architect, the injury or damage must be directly caused by you in whole or in part. The “liability arising out of” language is gone due to its broader application and coverage for additional insureds. This is good, you think?

Why Is This Bad for Subcontractors?

If the Subcontractors Agreement mandates that your policy grants the GC, owner and architect additional insured status for injuries and claims “arising out of” subcontractor’s work, and your general liability policy restricts coverage to claims to only “caused in whole or in part,” there is a disconnect where the contract you signed doesn’t match your insurance coverage in your liability policy. The contract language is much broader than what your liability policy covers.

When this happens and you are tendered a claim or lawsuit by the GC, owner or architect, and the dreaded coverage disclaimer letter arrives in the mail from carrier stating “no coverage,” you may be stuck with an uncovered claim and possible breach of contract exposure, which usually isn’t covered by the policy either. The contract you signed states “arising out of or connected to” your work, but your insurance policy states coverages for claims “caused in whole or in part” by your work.

Conclusion

It is important, therefore, to be diligent in reviewing your construction agreements and make certain your attorney and/or insurance advisor reviews the coverages in your general liability policy and that they are sufficient to address the exposures that you have agreed to in your construction contract. Parties to construction contracts (especially subcontractors) must use great care to determine that proper coverage is in place to avoid a potential coverage disaster. Don’t just sign the contract and send it back without thoroughly reviewing and negotiating more favorable terms. **MSC**

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