

**INSURANCE 101 FOR CONSTRUCTION LAWYERS –
PART I: FUNDAMENTALS OF LIABILITY COVERAGE
FOR CONTRACTORS**

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This article provides an overview of some of the fundamental issues regarding general liability insurance for construction contractors. These include the purpose of liability insurance, tendering claims, and potential insurance traps for construction attorneys.

The next issue of this newsletter will include a discussion of additional, more complex, insurance coverage issues such as strategies for defeating some of the coverage arguments raised by carriers, various types of coverage found in additional insured endorsements, decisional treatment of Oregon’s anti-indemnity statute, and recent case law in the insurance arena.

I. GENERAL LIABILITY INSURANCE FOR CONTRACTORS

General liability insurance provides an insured with protection against two types of potential loss resulting from a lawsuit. First, it covers damages awarded to a third party (the plaintiff) because of injury or damage for which the insured is legally responsible. Second, it covers the cost of defending the insured against

the claims alleged in the suit. Defense costs, which include attorney fees, consultant fees, and other legal expenses, can add up quickly even when plaintiffs’ claims are meritless. The indemnity (payment of damages on the insured’s behalf) and defense (payment of legal expenses) duties constitute an insurer’s primary obligations under a general liability insurance policy.

While insurance exists for various types of loss a contractor may experience, general liability insurance only insures against the potential loss arising from claims against the insured. General liability insurance does not protect a contractor from, for example, damage to its own property, or damage to or loss of its equipment. The following chart summarizes some types of loss that generally are not covered by general liability insurance, and references the type of policy that would provide the necessary coverage:

Nature of Liability / Damage / Loss	Appropriate Insurance Policy
Bodily injury, property damage, and cleanup costs due to pollution	Environmental Liability / Pollution Insurance
Claims against an organization arising from mistakes by directors and officers of a corporation	Directors and Officers Liability Insurance
Damage to an insured’s equipment or tools	Inland Marine Insurance; Contractors Equipment Floater
Loss caused by dishonest or fraudulent acts of an employee	Commercial Crime Insurance
Damage to property during the course of construction	Builder’s Risk Insurance

II. TENDERING CLAIMS TO GENERAL LIABILITY INSURERS

A. Deciding Whether to Tender to The Insurer

When a claim is made or a suit is filed against a contractor, the contractor and its counsel need to decide whether to tender the claim to its liability insurers. In order to trigger coverage under a general liability policy, the insurance company must first receive notice of the claim. This process is called tendering the claim.

While a contractor may not initially know whether a particular policy provides coverage for a lawsuit, it should strongly consider tendering the claim to its insurer as soon as possible. When considering whether to tender, contractors may need to find out if the tender may, regardless of the insurer's ultimate response, increase the contractor's future premiums or make it difficult for the contractor to find coverage with the same or another insurance carrier in the future. Nonrenewal of a policy can be a particular problem in the construction field where coverage for certain trades and projects has narrowed with the increase in construction defect litigation. In addition, contractors may not wish to tender to certain carriers where coverage may be needed for payment of other claims.

Where possible, contractors should consult their risk managers, brokers, or attorneys to discuss the possible impact of a tender on their insurance programs. Unless, however, a contractor has made an informed decision with sound professional advice to not tender, the best advice is to tender a claim, and to tender it as soon as possible.

B. The Mechanics of Tendering a Claim

The initial tender can impact the handling and outcome of a claim. After locating its insurance policies (a task made unnecessarily difficult by document retention policies that do not specifically require permanent retention of all insurance policies, however old) and deciding whether to tender the claim, a contractor will need to decide:

1. Whether to make a "short form" or a "long form" tender;
2. Who should make the tender; and
3. When to make the tender.

A short form tender simply notifies the insurance company of the case, usually by attaching a copy of the complaint or other form of written demand to a short letter tendering the defense and requesting indemnity. An "additional insured" party to the insurance contract should enclose with the tender letter all certificate and endorsements in its possession evidencing its additional insured status (as well as a copy of the construction contract creating the additional insured requirement when the additional insured endorsement provides blanket or automatic coverage based on the construction contract). A short form tender is appropriate where coverage is relatively clear or as a precursor to a long form tender, enabling the contractor to establish an earlier date of tender and, therefore, an earlier date for potential reimbursement of defense costs from the insurer.

A "long form" tender provides the insurer with an analysis of why coverage exists under the policy terms for the claim. Contractors may want to supplement their initial tender with a long form tender when coverage is not obvious for a variety of reasons, including the following: (1) situations where the area of coverage is uncharted or controversial and the contractor wants the insurer to know that it is sophisticated and aggressive; (2) when the contractor suspects that a blanket denial will come from the carrier and wishes to speed up the pace of the anticipated coverage dispute. Long form tenders do run the risk, however, of educating insurance adjusters to coverage defenses that otherwise may have not been reserved by the insurer. Thus, if time permits, it may be best to provide the contractor's coverage analysis to the insurer only in response to the specific points of denial raised by the insurer.

Contractors generally should not leave this crucial tendering task to a risk manager or broker unless a short form tender is all that the contractor intends to send. Where the tendering task is

delegated to a risk manager or broker, the contractor should follow up to ensure timely tender, to confirm tender under all potentially relevant policies, and to make sure it has adequate documentation of the tenders. Long form tenders usually include an analysis of the triggering events and the law, and typically have more effect when sent by counsel. Moreover, coverage for contractors often requires creative and unconventional approaches, which risk managers and brokers may not be trained to consider. There may be reasons, however, to send a long-form tender over the signature of the risk manager or broker, such as not wishing to convey an overly-aggressive tone by revealing the retention of coverage counsel.

Tenders should be made to the contractor's general liability insurers for the relevant time period (in a construction defect case this would span from start of construction to the present), as well as to other sources, depending on the type of claim and the position of the insured. Some examples include tendering to a homeowners association's carrier (on behalf of a developer) and tendering to another contractor's carrier (as an additional insured).

Up-to-date contact information for admitted carriers can be located with the Oregon Insurance Division's insurance company search engine (<http://www4.cbs.state.or.us/ex/ins/inslic/company/index.cfm>). Contact information for non-admitted carriers, also called surplus lines carriers, may be found on the Surplus Line Association of Oregon's website (www.slaor.org/Insurance.aspx). Policy forms may also contain contact information for tendering claims, though the contact information contained in older policies may no longer be accurate.

In addition to forwarding a copy of a complaint to the insurer upon receipt, the following are examples of claims that should be tendered as soon as possible:

1. Notice of defect letter sent pursuant to ORS 701.565;

2. Secondary notice of defect letter sent pursuant to ORS 701.570; and

3. Written demands from owners relating to construction defects not affected by ORS 701.565 and 701.570.

Some policies are written on a "claims made and reported" basis. These policies are triggered only if the claim is made against and reported by the insured to its carrier within the policy period. Failure to tender on time can forfeit coverage under such policies. Most other policies contain provisions requiring notice "as soon as practicable" (for example) or requiring the insurer's consent before incurring any expenses, and insurers will argue that they are not required to reimburse attorney fees incurred prior to notice to the insurer. Again, sooner is better.

III. COMMON INSURANCE TRAPS AND PITFALLS FOR CONSTRUCTION ATTORNEYS

Construction attorneys often take on multiple roles, each of which requires the attorney to address a variety of issues. Some of the roles may include drafting construction contracts, dealing with construction financing or liens, advising clients on insurance coverage, defending an insured against lawsuits, and tendering claims to insurance companies. With such varied responsibilities, the nuances of the insurance process can become traps for construction attorneys. Some of these potential problems are briefly discussed below.

A. Insurance Coverage Requirements in Construction Contracts

Insurance coverage problems often begin with construction contracts that do not include basic requirements for insurance coverage. To adequately protect a contractor every construction contract should contain minimum requirements for insurance coverage. Contractors should discuss with their attorneys what insurance requirements to include. Points to consider include the following:

1. Required limits;

2. Coverage for completed operations⁸;
3. Length of coverage after final payment and completed operations;
4. Nature and form of coverage for additional insureds;
5. Coverage for contractual liability; and
6. Whether the insurance provided by the contractor is to be considered primary and non-contributory.

Other contractual provisions, such as indemnity requirements, also have bearing on coverage and should be reviewed. Advice from counsel may vary according to the trade and bargaining position of each contractor, but contractors should continually evaluate and update the insurance language in their contracts to provide the best protection from claims arising out of their projects. Without the proper contractual language regarding insurance requirements, the extent of insurance money available to settle claims or pay judgments may be diminished, increasing the exposure for all of the contractors.

B. Contractual Requirements for Additional Insured Coverage

Many construction contracts require additional insured coverage for entities such as developers and general contractors. Too many times, however, these developers and general contractors who are contractually entitled to additional insured coverage under subcontractors' policies fail to follow through and collect the required certificates of insurance evidencing this additional insured coverage.

In addition to requiring all subcontractors to provide *certificates* of additional insured status, the contract documents should specifically require

⁸ Note that Section 19 of House Bill 2654, effective January 1, 2008, imposes on contractors the obligation of obtaining coverage for liability of products and completed operations. *See also*, OAR 812-003-0200(e). A step forward, this new requirement is only effective at the time of each contractor's CCB license renewal, meaning that a contractor with a December renewal can perform construction without having to comply with Section 19 for most of 2008.

– and the developer and general contractor should enforce compliance with this obligation – that the subcontractors provide copies of the additional insured *endorsements*. In addition, developers and general contractors should take care to ensure that the endorsements provided by the subcontractors either specifically name the necessary parties as additional insureds or that the language of the endorsement automatically makes the necessary parties additional insureds by virtue of the requirements of the construction contracts (the former is preferable).

At the same time, counsel for subcontractors should confirm that the subcontractors comply with any contractual obligations to procure additional insured coverage for developers or general contractors. Otherwise, a denial by the insurance company of an additional insured's tender leaves the subcontractor susceptible to a breach of contract claim for failure to procure the insurance required by the construction contract, which may be asserted in yet another lawsuit.

Too often insurance companies deny additional insured tenders from developers and general contractors for the specific reason that they have no record of ever having issued any additional insured endorsements. Copies of the endorsements foreclose this argument, forcing insurers to take the additional insured claims more seriously.

Do not overlook the possibility of additional insured coverage under policies issued to other entities. Although the additional insured will not typically have possession of the actual policy, the applicability of this coverage (and, at least, the ability to tender) can be gleaned from the certificate and endorsement forms.

C. Timing and Scope of Tenders

As noted above, late tenders create unnecessary problems with insurers, from limitations on recovery of pre-tender defense costs to complete denials of coverage. In addition, tenders that do not apprise the insurer of all claims against the insured – or that tender on behalf of one entity and not on behalf of another related

entity – give insurance companies reason to deny claims that may otherwise be covered. Ensure that tenders are timely. Ensure that tenders request both a defense against and indemnity for all claims asserted. Finally, ensure that tenders are made on behalf of all entities – and individuals – that are implicated by the claims.

D. Following Up on Factually-Based Denials

Under Oregon law defense obligations are triggered by the allegations in the complaint – regardless of their truth or merit – and nothing else. Some insurance adjusters deny claims based on information not contained in the complaint. Carriers have been known, for example, to deny claims for a defense where the construction was “obviously” still in progress at the expiration of the policy. The denial letter from the adjuster will indicate that because the project was not a “completed operation” no coverage exists under the policy.

While an insurer may – or may not – have a valid point on indemnity, if the basis for the denial comes from information gleaned from sources outside the complaint the insurer still has a defense obligation. If the first letter back from the carrier contains a denial based on information gleaned outside the complaint, a polite response through a letter discussing Oregon law on the topic (perhaps citing *Ledford v. Gutoski*, 319 Or 397, 399-400 (1994)) and pointing out the lack of relevant allegations supporting the denial in the complaint may go a long way toward procuring a defense for the contractor.

IV. CONCLUSION

The involvement of insurance coverage in construction litigation is often essential to satisfactory resolution of claims against contractors. Construction attorneys can help their clients achieve that satisfactory resolution with careful planning and detailed attention to insurance coverage from the contracting process to the assertion of arguments in favor of indemnity.

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