



## THE ASSOCIATED GENERAL CONTRACTORS OF AMERICA

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# AGC White Paper On Additional Insured Endorsements

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“Additional insured” endorsements have become one of the hottest topics in construction risk management. The insurance industry has narrowed the standard form of this endorsement three times since 1985 and one of the leading writers on the subject now reports that “several state legislatures are considering limiting coverage for additional insureds even further.”

Following is a quick overview of the reasons why property owners, general contractors and other upstream parties to the construction process seek additional insured endorsements from downstream parties. Also following are:

- an equally quick overview of reasons why downstream parties often oppose these endorsements;
- a summary of the typical responses to the downstream parties’ concerns;
- a few words on the several changes in the standard form of the additional insured endorsement; and
- a note on the new legislation that some states are apparently considering.

Attached is a table comparing the various versions of the standard form of the endorsement. Also attached is a detailed article on the new legislation. The author of the article is Randy Maniloff, a Philadelphia lawyer who frequently represents insurance carriers. AGC of America has reproduced this article with his express permission.

### **Why Upstream Parties Seek AI Endorsements**

Additional insured endorsements give project owners, general contractors and other upstream parties, such as first-tier subcontractors, at least some degree of insurance coverage under the commercial general liability (CGL) policies that downstream parties carry. The upstream parties use that coverage to finance at least a portion of the liability they risk whenever they construct a project, including liability:

- for any damages resulting from defects in the downstream parties’ work;
- for any injuries to those parties’ employees while working on or near the jobsite; and
- for any injuries to anyone else (such as a project owner’s guest) while on or near the jobsite.

Upstream parties, and particularly general contractors, explain that they bear a great and still growing risk of liability for defects in their subcontractors' work. The relatively recent wave of mold litigation is just one piece of the larger problem that upstream parties have to manage. Even when given an additional insured endorsement, general contractors cannot normally recover the costs of correcting defects in their subcontractors' work from the latter's insurance carriers. General contractors normally have to file claims for such costs under their own insurance policies, or depend on their subcontractors to have the financial strength to bear them. As additional insureds, general contractors frequently can, however, file claims under their subcontractors' policies for the cost of repairing any property damage (as defined by the relevant policy) resulting from defects in their subcontractors' work, protecting themselves from the risk that their subcontractors will either refuse or lack the financial strength to pay for at least those repairs.

Upstream parties add that the workers compensation laws generally prevent the men and women working for their subcontractors only from suing their own employers for any bodily injuries that those employees may suffer in the course of their employment. In most states, the law permits such employees to bring "third-party-over actions" against project owners, general contractors and other parties -- other than their employers -- for such injuries.<sup>1</sup> Upstream parties also seek additional insured endorsements from downstream parties to protect themselves from the risk of such "third-party-over actions," explaining that:

- as upstream parties, they risk tort liability for jobsite injuries to construction workers only if and to the extent that they subcontract work to the downstream parties, and do not perform the work with their own employees;
- the downstream parties are primarily responsible for protecting their employees, and should bear the total cost of injuries that their employees suffer, and not simply the portion that their workers compensation premiums cover; and
- jobsite safety will improve if the downstream parties have a financial incentive to protect their employees from all risks of injury, including risks that other parties to the construction process may either create or tolerate.

According to one insurance lawyer, "general contractors contend that most subcontractor employee injuries arise from the means and methods of that trade's jurisdictional work and are not the result of an overt act by the general contractor." This lawyer adds that "[a]s a result, the general contractor does not want its insurance loss record to be tagged with the third-party costs of the claims."<sup>2</sup>

A general contractor similarly writes that "standard construction agreements" merely "require each subcontractor to take control of its work and be responsible for claims that arise out of the performance of that work." He maintains that "additional insured status avoids the more

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<sup>1</sup> For general contractors, the problem is often worse, because they often have a contractual obligation to defend the project owner against the third-party-over actions, and to indemnify the owner for any liability that may result.

<sup>2</sup> All quotations are taken from short essays that were written for a special workshop that the International Risk Management Institute sponsored and held in conjunction with its 24<sup>th</sup> annual Construction Risk Conference in Orlando, Florida on November 8-11, 2004. The title of that workshop was "Allocating Risks in Construction Contracts."

cumbersome process of tendering the claim or action to the subcontractor, who, in turn, must tender it to the insurance carrier and request that coverage be provided to the general contractor. . . .”

### **How Downstream Parties View AI Endorsements**

Downstream parties often oppose additional insured endorsements on the grounds that such endorsements are easily abused. They note, for example, that the downstream party’s insurance carrier has a normally indivisible duty to defend the additional insured, and as a result, that carrier may find it necessary to defend every count of a broad multi-count complaint filed against an upstream party even if there is only one count qualifying for coverage under the downstream party’s policy.

Subcontractors also note that construction defects are often difficult to trace, and that several different defects may simultaneously contribute to any property damage that a project suffers. For these reasons, downstream parties maintain that they should have and retain the right to dispute that their negligence caused all or even part of such damage. They consider it simply unfair to require them to give upstream parties the right to go directly to their insurance carriers, without regard to whether, or to what degree, they may be at fault.

These downstream parties add that upstream parties are ultimately liable for any bodily injuries that may result from the construction of a project only if the upstream parties’ negligently caused those injuries. Subcontractors take the position that each of the parties to the construction process should bear the cost of any property damage or bodily injuries that its own negligence may cause, including the cost of insurance coverage for the risk of such damage or injuries.

As one insurance broker has written, the “contractual risk transfer model” that lies at the heart of most of today’s construction contracts “forces responsibility and payment for construction claims to be borne by subcontractors regardless of fault.” He adds that “the primary function of general contractors . . . is the selection, coordination, and supervision of subcontractors, including the scheduling, sequencing, inspection and instructive correction of their work,” and that additional insured endorsements merely “allow[] . . . project leaders to ‘pass the buck’ for their own mistakes to subcontractors.” Further, he complains that “[o]wners and general contractors who can successfully shift the financial consequences of accidental injury losses and defective construction to other parties . . . never face the consequences of their own actions and decisions affecting workplace safety and construction quality.”

Another broker notes that, “[o]ver the years, . . . the interpretations [of the standard form of additional insured endorsement] seemed to stray from the original intent, which was to provide coverage for the additional insured’s vicarious liability for activities or work of the named insured -- not to cover the sole negligence of the additional insured.” An insurance carrier echoes that “[m]any courts have found that [the 1985 version of the standard form] confers additional insured status only for the vicarious liability of the additional insured . . .” but “other courts have construed [that version of the form] more broadly to confer additional insured status for the affirmative negligence of the additional insured.” He adds that “courts have found coverage under [the 1985 version] even though the named insured was not at fault in the

accident.” Further, he notes that additional insured endorsements can dilute the available limits of the named insured’s policy, and [c]reate a conflict of interest if a lawsuit is brought against both the named insured and an additional insured,” requiring the insurance carrier to “appoint separate defense counsel for each party . . . .”

### **How Upstream Parties Respond to the Downstream Parties’ Concerns**

Upstream parties respond that expensive multiparty litigation would be necessary to allocate the responsibility for every construction defect and jobsite injury with the precision that downstream parties prefer. Upstream parties add that the cost of such litigation would offset any savings that downstream parties -- or more precisely, their insurance carriers -- would be likely to realize from taking a different approach. Upstream parties also note that the necessary litigation would long delay any settlements.

One general contractor writes that legal restrictions on additional insured endorsements “result in more cumbersome and expensive litigation, as multiple parties have to participate in the defense of an action that should clearly be allocated to the primarily responsible party,” adding that, “[i]nstead of reducing insurance and litigation costs, such restrictions are most likely to increase those costs . . . .”

In direct response to claims that the insurance industry originally intended additional insured endorsements intended to provide coverage only for vicarious liability, one insurance lawyer suggests that limiting the coverage to vicarious liability would make little sense, as “Section 409 of the Restatement (Second) of Torts severely limits vicarious liability exposure in the construction setting.” He adds that, “[i]f found liable at trial, general contractors are held *directly* negligent for their acts under traditional tort allegations.” He also notes that, “[s]ince the named insured subcontractor is frequently immune from liability due to the . . . state workers compensation statutes, it is unlikely that prior to trial there would ever be a determination as to whether the bodily injury or property damage was caused, in whole or in part, by the named insured.”

### **Overview of the Standard Form of Additional Insured Endorsement**

The Insurance Services Office (ISO) is a group that the insurance industry founded and continues to fund for the purpose of developing standard forms of insurance. While many (particularly regional) insurance carriers do not use all of these forms, many carriers do use them, and many others are influenced by their terms and conditions.

Presentations on the standard forms the additional insured endorsement inevitably begin with the version that ISO adopted in 1985. As the attached table reveals, that version is broad, granting an additional insured coverage for both property damage resulting from construction defects and third-party-over actions. The later versions of the form are, however, narrower. In an effort to cut off coverage for completed operations, and in turn, construction defects, ISO revised the form in 1997 and again in 2001. The 1997 version of the form limits coverage to “ongoing operations,” and the 2001 version further provides that it “does not apply” to events that occur

after the named insured has completed its work, or the relevant portion of the project has been put to its intended use.

In 2004, in an effort to limit coverage for third-party-over actions (in not only the construction but also other industries) ISO went further. It revised the standard form to provide an additional insured with coverage “only with respect to” property damage or personal injury that the named insured also causes, at least in part. In other words, the latest version of the form eliminates coverage for the upstream party’s sole negligence, and it continues to provide coverage only if the name insured contributed to the damage or injury.

The practical effects of these changes are more difficult to assess. While the revisions to the form influence the insurance carriers, some continue to offer the older versions of the form, or several versions of it. Insurance brokers report that owners continue to demand, and on occasion, some large general contractors can still get the 1985 version of the form. General contractors are, however, finding it more and more difficult to get that version, and subcontractors are finding it impossible to do so.

### **More Recent Developments**

In the attached article (published in May of 2005), Randy Maniloff reported that subcontractors had started urging state legislators to go even further than the insurance industry. Specifically, he reported that subcontractors were seeking legislation that forbid additional insured endorsements to provide coverage for the additional insured’s negligence even if and when the named insured contributed to the property damage or personal injury. He explained that “bills ha[d] been introduced in Arizona (SB 13230, California (AB 573), Colorado (SB 05-142), Illinois (HB 0704) and Texas (SB No. 445) that would preclude an insurer from providing defense and indemnity to an additional insured for its own negligence, even when the additional insured is not solely negligent.”

### **Conclusion**

With the assistance of the insurance professionals and construction lawyers active in their areas, chapters and members should be able to assess the potential effects of any legislation that their particular states are considering. In addition to the legislation that the attached article addresses, and perhaps as an alternative, some states have also considered, and in some cases, enacted statutes requiring project owners and subsequent purchasers to give construction contractors an opportunity to inspect and cure any alleged defects, before resorting to litigation. Some states have also expanded the definition of an “employer” for workers compensation purposes to include the project owners, general contractors and other upstream parties for whom subcontractors typically work.

Attachments

## Evolution of the Standard Form of Additional Insured Endorsement 1985-2004

CG 20 10 11 85	CG 20 10 03 97	CG 20 10 10 01	CG 20 37 10 01	CG 20 10 07 04	CG 20 37 7 04
<ul style="list-style-type: none"> <li>● 1985 version of the additional insured endorsement</li> <li>● Provides the “additional” insured with coverage for liability arising out of the “named” insured’s work for the “additional” insured</li> <li>● Provides coverage not only while the “named” insured’s work is in progress but for the “named” insured’s completed operations.</li> <li>● Meets a contractual that project owners frequently impose on their general contractors – namely, that the general contractor provide the project owner with additional insured coverage for claims against the project owner arising out of the completed work</li> <li>● Regularly used until three years ago</li> </ul>	<ul style="list-style-type: none"> <li>● 1997 version of the additional insured endorsement</li> <li>● Provides the “additional” insured with coverage only for liability arising out of the “named insured’s” ongoing operations</li> <li>● Intended to limit the term of the “additional” insured’s insurance coverage to the time period during which the “named” insured is actually performing operations</li> <li>● Intended to deny coverage for completed operations</li> </ul>	<ul style="list-style-type: none"> <li>● 2001 version of the additional insured endorsement</li> <li>● Provides the “additional” insured with coverage only for liability arising out of the “named” insured’s ongoing operations</li> <li>● Expressly excludes injuries or damages suffered after (1) the “named” insured’s work at the site of the covered operations has been completed, or (2) the relevant portion of “named” insured’s work has been put to its intended use</li> <li>● Intended to limit the term of the “additional” insured’s insurance coverage to the time period during which the “named” insured is actually performing operations</li> <li>● Intended to deny coverage for completed operations</li> <li>● Adopted in conjunction with CG 20 37 10 01, a new standard form endorsement that will, if used in conjunction with this form, provide coverage similar to the CG 20 10 11 85</li> </ul>	<ul style="list-style-type: none"> <li>● New standard form of endorsement for completed operations, adopted in 2001</li> <li>● Provides “additional” insured with coverage for the “products-completed operations hazard” arising out of the “named” insured’s work</li> <li>● Only applies to completed operations</li> <li>● No coverage for premises or operations</li> <li>● When used in conjunction with CG 20 10 10 01, provides coverage similar to CG 20 10 11 85</li> </ul>	<ul style="list-style-type: none"> <li>● 2004 version of the additional insured endorsement</li> <li>● Provides the “additional” insured with coverage only for liability caused in whole or in part by the acts or omissions of either (1) the “named” insured or (2) someone acting on behalf of the “named” insured</li> <li>● Also limits coverage to ongoing operations for the “additional” insured</li> <li>● Express excludes injuries or damages suffered after (1) the “named” insured’s work at the site of the covered operations has been completed, or (2) the relevant portion of “named” insured’s work has been put to its intended use</li> <li>● Intended to limit the coverage provided to the “additional” insured to liability caused at least in part by the “named” insured’s ongoing operations</li> <li>● Intended to eliminate coverage for the “additional” insured’s sole negligence</li> </ul>	<ul style="list-style-type: none"> <li>● 2004 version of the completed operations endorsement</li> <li>● Provides the “additional” insured with coverage for the “products-completed operations hazard” caused in whole or in part by the acts or omissions of either (1) the “named” insured or (2) someone acting on behalf of the “named” insured</li> <li>● Intended to limit the coverage provided to the “additional” insured to liability caused at least in part by the “named” insured’s completed operations</li> <li>● Not Intended to provide coverage for the “additional” insured’s sole negligence</li> <li>● When used in conjunction with CG 20 10 07 04, meets typical contract requirements to provide additional insured coverage for both ongoing and completed operations.</li> </ul>

\* *Note:* Where the two parties are the project owner and the general contractor, the owner would be the “additional” insured and the general contractor would be the “named” insured. Where the two parties are the general contractor and one of its subcontractors, the “additional” insured would be general contractor and the “named” insured would be the subcontractor

## ADDITIONAL INSURED'S COVERAGE AND LEGISLATIVE CHANGES ON THE HORIZON

### TAKING ISO'S 07 04 ADDITIONAL INSURED REVISIONS A STEP FURTHER

**Summary:** The Insurance Services Office (ISO) has published revised additional insured endorsements for the purpose of negating coverage for an additional insured for its sole negligence. Now, some states are following up on this effort with legislation. This article notes and analyzes the attempts by some states to restrict coverage for additional insureds under general liability policies. The article is written by Mr. Randy J. Maniloff.

Randy J. Maniloff is an attorney at White and Williams, LLP in Philadelphia. He concentrates his practice in the representation of insurers in coverage disputes over primary and excess policy obligations for various types of claims, including construction defect, mold, general liability (products/premises), environmental property damage, asbestos/silica and other toxic torts, director's & officer's liability, professional liability/medical malpractice, media liability, first-party property, homeowners, community associations, public official's liability, school board liability, police liability and computer technology liability. The author expresses his gratitude to Frank Keres of Construction Risk Associates, Inc., Brookfield, Wisconsin, for his invaluable assistance with the preparation of this article. The views expressed herein are solely those of the author and are not necessarily those of his firm, its clients, Construction Risk Associates or Mr. Keres.

#### Topics covered:

**The additional insured debate: extent of coverage**

**The Oregon example**

**The effect of expanded anti-indemnity statutes**

**Conclusion**

#### The Additional Insured Debate: Extent of Coverage

Additional insured claims are like fingerprints—no two are identical. At least it seems that way when you consider the variation in facts, contractual provisions creating the additional insured obligations, and language of the coverage grants. But despite their unique qualities, many additional insured claims still manage to have one thing in common: the additional insured frequently secures broader coverage than was intended by the insurer.

In a typical claim scenario, without regard for potential additional insured rights, coverage is afforded if a loss satisfies the policy's insuring agreement and conditions and does not come within the terms of an exclusion. Additional insured claims demand all that, as well as, in most cases, the putative additional insured must also establish that its claim satisfies a certain causation requirement between the named insured's actions and the additional insured's liability. Some courts' interpretations of this causation element have left insurers

shaking their heads in disbelief over the circumstances in which they have been obligated to provide coverage to additional insureds. See *Ohio Casualty Insurance Co. v. PetsMart, Inc.*, 2003 U.S. Dist. LEXIS 22782 (N.D. Ill.) (Based on the court's interpretation of the causation element in a vendor's endorsement—"bodily injury" arising out of "your products"—PetsMart, a retailer of a cat scratching pole, was entitled to coverage as an additional insured under the manufacturer's policy, for a claim for bodily injury caused when one of the poles fell from a store shelf.)

Last year, in an effort to stem the tide of unintended additional insured coverage, Insurance Services Office introduced changes to its various additional insured endorsements (effective July 2004 and containing a 07 04 form number suffix). At the heart of these changes was the preclusion of coverage for an additional insured's sole negligence—something that many courts around the country, based on the language of certain previous ISO endorsements, have not hesitated to provide. ISO set out to eliminate coverage for an additional insured's sole neg-

ligence by amending its endorsements to specify that coverage is only available for their vicarious or contributory negligence. (Incidentally, for an in-depth discussion of ISO's 07 04 amendments to its additional insured endorsements, see "Additional Insured Endorsements: ISO's Revisions", Casualty & Surety, Public Liability section; M.23 pages.)

Despite ISO's clearly expressed intention to limit the extent of coverage available for an additional insured, its amendments are not designed to preclude coverage for an additional insured's own negligence; unless it rises to the level of *sole* negligence.

Now comes word that several state legislatures are considering limiting coverage for additional insureds even further than accomplished by ISO's recent amendments. Putting aside various nuances in legislative provisions, bills have recently been introduced in Arizona (SB 1323), California (AB 573), Colorado (SB 05-142), Illinois (HB 0704) and Texas (SB No. 445) that would preclude an insurer from providing defense and indemnity to an additional insured for its own negligence, even when the additional insured is not solely negligent. In addition, bills have recently been introduced in Kentucky (05 RS HB 449/GA), Indiana (House Bill 1035), and Hawaii (SB 1853) that would introduce or expand the scope of anti-indemnity statutes, but which either expressly exclude their applicability to insurance or are silent on the issue.

As an example, consider Illinois HB 0704, introduced in the 94th General Assembly on February 1, 2005, which provides as follows (the proposed amendment to 740 ILCS 35/1 is indicated by the underlined text):

Sec. 1. With respect to contracts or agreements, either public or private, for the construction, alteration, repair or maintenance of a building, structure, highway bridge, viaducts or other work dealing with construction, or for any moving, demolition or excavation connected therewith, every covenant, promise or agreement to indemnify or hold harmless another person from that person's own negligence and any covenant, promise, or agreement to procure an insurance policy to indemnify or hold harmless another person from that person's own negligence is void as against public policy and wholly unenforceable.

(Note that on March 10, 2005, as this article was in the final stages of preparation for publication,

Judiciary I, Civil Law Committee of the Illinois House amended HB 0704 by deleting the proposed amendment and re-referred the bill to the Rules Committee. Given the fluid nature of the legislative process, it is suggested that the status of this bill should be monitored by those with an interest in the outcome.)

Another example of proposed legislation that would preclude an insurer from providing defense and indemnity to an additional insured for its own negligence is Arizona SB 1323, introduced on January 27, 2005. This legislation, for purposes of coverage for an additional insured (but not a named insured), would amend §32-1159 of the Arizona Revised Statutes as follows (note that the italicized text is to be deleted and the capitalized text is to be added):

A. A covenant, clause, or understanding in, collateral to or affecting a construction contract or architect-engineer professional service contract that purports to INSURE, TO indemnify, to hold harmless or to defend the promisee from or against liability for loss or damage resulting from the *sole* negligence of the promisee or the promisee's agents, employees or *indemnitee* INDEMNITEES is against the public policy of this state and is void.

A succinct explanation of the rationale for this proposed legislation comes from American Subcontractors Association, Inc. (ASA), which, according to its website, is a membership trade association of 5,500 subcontractors, specialty trade contractors and suppliers in the construction industry. The following is from an ASA news release from January 2005.

Most states have so-called "anti-indemnity statutes" that regulate the use of hold harmless terms by general contractors in written subcontract agreements, but almost no states put similar restrictions on the use of additional insured contractual requirements. In other words, anti-indemnity statutes in most states have a loophole, permitting upper-tier contractors to use additional insured arrangements to achieve the very same ends that are forbidden in use of hold harmless clauses. Courts in most states have permitted the loophole even though anti-indemnity legislation is designed to protect the public from the dangers and consequences of unsafe, or poor quality, construction. Anti-indemnity legislation such as

Oregon's forces project leaders to use their own resources and insurance, rather than that of their subcontractors', when workers are injured, or building occupants are harmed, as a result of their own poor decision-making or poor oversight.

ASA has much to gain from the passage of Illinois HB 0704, and other similar legislation, as its members are the ones frequently obligated to procure additional insured coverage for the benefit of sometimes negligent general contractors. Subcontractors no doubt view it as unfair that their policies' experience is negatively affected by the actions of negligent parties, whose own policies may sit on the sidelines, unimpaired, when the time comes to compensate an insured party.

According to ASA, the issue goes beyond mere unfairness: it is one of avoiding a moral hazard, the chance that the existence of insurance will increase the likelihood of the insured event; this is from a brief—*Amicus Curiae* American Subcontractors Association at 12, *Walsh Construction Company v. Mutual of Enumclaw*, 338 Ore. 1 (2005), quoting *Hall v. Life Insurance Company of North America*, 317 F.3d 773, 775 (7th Cir. 2003). ASA goes on to argue the following: "In the ordinary insurance relationship, the insured is also deterred from engaging in risky activity by the notion that an accident or occurrence will result in the insurer raising its premiums"; however, "the additional insured is insulated against this prospect by the fact that it is not responsible for premium payments to the insurer and is unaffected by the raising of premiums"; *Id.* at 11, citing Mehta, "Additional Insured Status in Construction Contracts and Moral Hazard," 3 *Conn. Ins. L.J.* 169, 186-187 (1996), quoted in *National Union Fire Ins. Co. v. Nationwide Ins. Co.*, 82 Cal.Rptr.2d 16, 22 (Cal. App. 4 Dist. 1999). ASA believes that if additional insureds do not have a financial motivation to exercise a high standard of care, third parties will be exposed to an increased likelihood of harm; *Id.* at 13-14, citing Mehta at 187.

Insurers also stand to benefit from anti-indemnity legislation that is expanded to include the procurement of insurance for an indemnitee's own negligence. Of course, for insurers, the benefit is more difficult to measure. After all, when an insurer is relieved of an obligation to provide coverage for an additional insured for its own negligence, the additional insured will simply seek coverage under its own policy, on which it is a named insured. Thus, unless an insurer issues policies to *only* subcontractors or general contractors, the expansion of

anti-indemnity legislation to include additional insured obligations will likely be a win some/lose some situation.

### The Oregon Example

While ASA notes that almost no state anti-indemnity statutes apply to additional insured obligations, an exception is Oregon, which has had such legislation since 1995. Other exceptions are Montana and New Mexico, which, since 2003, have applied their anti-indemnity statutes to additional insured requirements in construction contracts; *Id.* at 9 (see MCA §28-2-2111 and N.M. Stat. Ann. §56-7-1).

Not long ago, the Supreme Court of Oregon had occasion to address, and uphold, the applicability of Oregon's anti-indemnity statute to additional insured obligations. On January 27, 2005, the Supreme Court of Oregon issued its opinion in *Walsh Construction Company v. Mutual of Enumclaw*, *supra*, addressing the availability of coverage for an additional insured under the following circumstances. Walsh Construction, a general contractor, entered into a subcontract with Ron Rust Drywall, Inc. to perform work on a Walsh project. Rust was obligated to name Walsh Construction as an additional insured on Rust's liability policy. Rust's policy, issued by Mutual of Enumclaw, contained a blanket additional insured endorsement that automatically afforded the coverage required.

A Rust employee was injured on the job and made a claim against Walsh. Walsh did not contend that Rust was in any way responsible for the employee's injury. Walsh tendered the claim to Enumclaw. The insurer refused it, on the basis that the additional insured provision violated ORS 30.140, which provided as follows:

- (1) Except to the extent provided under subsection (2) of this section, any provision in a construction agreement that requires a person or that person's surety or insurer to indemnify another against liability for damage arising out of death or bodily injury to persons or damage to property caused in whole or in part by the negligence of the indemnitee is void.
- (2) This section does not affect any provision in a construction agreement that requires a person or that person's surety or insurer to indemnify another against liability for damage arising out of death or bodily injury to persons or damage to property

ty to the extent that the death or bodily injury to persons or damage to property arises out of the fault of the indemnitor, or the fault of the indemnitor's agents, representatives, or subcontractors.

Enumclaw argued that, because the additional insured provision violated the statute, Walsh was not a legally cognizable additional insured, and, therefore, not entitled to defense or indemnity. Walsh countered by arguing that its subcontract with Rust did not require either Rust or its insurer to indemnify Walsh. Instead, in Walsh's view, the subcontract required only that Rust procure insurance for Walsh's benefit. Walsh further argued that the term *indemnity* connotes unlimited liability exposure, whereas insurance limits the insurer's liability to the amount of coverage purchased. If you are not convinced by that distinction, get in line. Neither were the trial court, Court of Appeals or Oregon Supreme Court.

The Supreme Court adopted a substantial excerpt of the Court of Appeals' decision, including the following conclusion:

"In sum, the text of ORS 30.140, and its historic evolution, strongly suggests that the statute prohibits not only direct indemnity arrangements between parties to construction agreements but also additional insurance arrangements by which one party is obligated to procure insurance for losses arising in whole or in part from the other's fault."

The Oregon Supreme Court held that the textual and contextual analysis of the statutory wording went even further than strongly suggesting its meaning, but, instead, demonstrated the legislature's intent conclusively.

Another illustration of Oregon's expanded anti-indemnity statute at work, this time in the context of an additional insured claim for construction defect, is *MW Builders, Inc. v. SAFECO Insurance Company*, 2004 U.S. Dist. LEXIS 18866. In *MW Builders*, the U.S. District Court for the District of Oregon addressed the extent of coverage for MW Builders as an additional insured under SAFECO policies issued to Portland Plastering. MW Builders subcontracted with Portland Plastering to install an exterior insulation and finishing system (EIFS) on a hotel that MW Builders was constructing. After the hotel was completed, its owner became aware of substantial water intrusion and damage to the building, caused by defects in the EIFS material.

The hotel owner filed for arbitration against MW Builders, who tendered the defense and sought indemnity from Portland Plastering and its insurer, SAFECO. SAFECO declined to defend or provide indemnity on behalf of MW Builders. MW Builders settled the claim with the hotel owner for \$2,000,000 and pursued its own arbitration claim against Portland Plastering. An arbitrator determined that the fault of Portland Plastering caused 31 percent of the damage sustained by the hotel.

Relying on ORS §30.140 and the Oregon Court of Appeals' decision in *Walsb*, SAFECO argued that the agreement to procure insurance in Portland Plastering's subcontract with MW Builders, and any insurance issued pursuant to that agreement, were unenforceable. Conversely, MW Builders argued that *Walsb* was distinguishable because the subcontract did not require Portland Plastering to obtain insurance for MW Builders' own fault or negligence and because MW Builders was not seeking damages arising from its own fault or negligence. The court agreed:

"MW Builders is not precluded, under Oregon law, from arguing that it was entitled to coverage, as an additional insured, under Portland Plastering's policy for covered damages arising from the fault or negligence of Portland Plastering. Conversely, of course, MW Builders may not recover under the SAFECO CGL policies for any damages that resulted from its own fault or negligence."

Notwithstanding the Oregon Supreme Court's decision in *Walsb* and the Oregon District Court's decision in *MW Builders*, the jury is still out on who will get the last word on Oregon's anti-indemnity statute. The 73rd Oregon Legislative Assembly has introduced Senate Bill 154, which, if enacted, would have the effect of overruling the court's decision in *Walsb*. Among other amendments related to the same purpose, the Senate Bill would add the following provision to ORS 30.140:

(3) This section does not affect any provision in a construction agreement that requires a party to acquire insurance coverage for liability attributable to death, personal injury or property damage arising out of the construction and to name another party to the contract as an additional insured.

One thing's for certain—the beavers are busy.

### **The Effect of Expanded Anti-Indemnity Statutes**

Given the unique features of additional insured claims, where even the slightest nuance can be outcome-determinative, and paucity of case law addressing anti-indemnity statutes that apply to additional insured obligations (none interpreting the Montana and New Mexico statutes could be located), it is difficult to predict how such statutes may affect additional insured tenders. Nonetheless, some general observations can be made.

First, additional insureds whose claims are governed by anti-indemnity statutes may be forced to turn to their own liability policies to seek coverage (subject to all terms, conditions and exclusions) for the proportionate share of a loss that is attributable to their own negligence. No longer will the additional insured's principal insurer likely be able to rely on its other insurance clause to reject any request for contribution on behalf of the additional insured. This is often-times the case now, given that, since the July 1998 version of the CGL forms, ISO's CGL forms (form CG 00 01 and form CG 00 02) contain the following provision in its other insurance clause:

This insurance is excess over any other primary insurance available to you covering liability for damages arising out of the premises or operations for which you have been added as an additional insured by attachment of an endorsement.

Thus, in a state that expands its anti-indemnity statute to include additional insured obligations, even a defendant that secures a complete defense as an additional insured, based on a broad duty to defend standard (assuming it was determined not to be superseded by the statute), may still be required to seek coverage from its own insurer for the share of indemnity, and reimbursement of defense costs paid by the additional insurer, that is attributable to the additional insured's own negligence. As an example, California's proposed legislation (AB 573) includes the following addition to Section 2782(b) of the Civil Code: "An indemnitee who has been afforded a defense by an indemnitor shall reimburse that indemnitor a percentage of costs and fees actually incurred by the indemnitor

in that defense, equal to that indemnitee's percentage of comparative negligence or comparative willful misconduct."

Expanded anti-indemnity statutes will also likely create some challenging issues if an additional insured secures a defense, but there are allegations that it was partially negligent, and, hence, not entitled to indemnity for its own negligence. This is likely to raise some complex questions between the additional insured, the insurer providing the defense, and the additional insured's principal insurer over who controls the defense.

What's more, while it's easy for legislation to talk about parties' shares of negligence, most cases seeking damages for bodily injury and property damage are settled without the benefit of a finding of fact on this issue. Neat and tidy cases like *MW Builders*, which had an arbitrator determine that one party caused 31 percent of the damage at issue, are the exception and not the rule. If an insurer is now prohibited from providing coverage to an additional insured for its own negligence, it is likely to make it more difficult to settle cases, since an agreement among the defendants concerning relative shares of fault will be required.

Another impact of the legislation is likely to be choice of law disputes. Given the significant difference in the amount of coverage that would be available to an additional insured, depending upon whether its claim is governed by an anti-indemnity statute, disputes over choice of law seem inevitable when there are geographic contacts that can potentially support the application of more than one state's law.

### **Conclusion**

ISO took a big step in July 2004 when it set out to adopt a fault-based additional insured standard in an effort to negate coverage for an additional insured for its sole negligence. Several state legislatures are now considering taking fault-based additional insured coverage an even bigger step further, by eliminating defense and indemnity for an additional insured's own negligence, even if it does not rise to the level of sole negligence.