Commercial Insurance Update

Topics Concerning Buyers of Commercial Insurance

MSP C 02/2009 – "The Obligation to Defend Your Client" February, 2009

Commercial Insurance Update Newsletter

The 'Obligation to Defend' Your Client...

and Why You Should Avoid It at All Costs!

Implications of a Recent California Supreme Court Decision

By Jeffrey W. Cavignac, CPCU, ARM, RPLU, CRIS

On July 21, 2008 the California Supreme Court issued its verdict in a landmark case which deals with a subcontractors 'duty to defend.'

The case in question is known as Crawford v. Weather Shield Manufacturing, Inc. Crawford, a developer, contracted with Weather Shield to provide windows on a project. In the contract between the two parties, Weather Shield was obligated to not only indemnify and hold Crawford harmless, but also to '*defend any suit or action brought against Crawford founded upon the claim of such damage…*'

Several years after the project was completed some homeowners filed suit against Crawford alleging, among other things, that the windows were defective. Crawford incurred legal fees to defend the claim and ultimately settled with the homeowners and the cross-defendant subcontractors except for Weather Shield (and one other party). Crawford then brought an indemnity action against Weather Shield attempting to recover what it paid for indemnity as well as its legal costs in the homeowner litigation.

The lower court ruled that even though Weather Shield was found ***not negligent***, the firm still had an obligation to pay Crawford's legal fees. The rationale was that the 'obligation to defend' was a separate issue from the 'obligation to indemnify.' The decision was upheld by the California Supreme Court.

In a nutshell, even though Weather Shield was determined to be not at fault, it was still

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responsible for legal costs of the indemnitee (developer Crawford) legal fees in the homeowner litigation.

This is problematic for any contractor, subcontractor, consultant or anyone else who agrees to 'defend' an upstream party. Not only is it not fair, it may not be covered by Commercial General Liability (CGL) policies, and it is not covered by a Professional Liability policy.

If a favorable Additional Insured endorsement names the upstream party on the downstream parties' CGL policy and if the claim is tendered correctly, the downstream parties' insurer may have a defense obligation if any of the claims against the upstream party are potentially covered by the downstream parties' CGL policy.

The problem is that many different Additional Insured (AI) forms are currently in use. Many insurance companies have drafted their own AI endorsements and many of these are tied to either the partial or sole negligence of the named insured. In a situation like the Crawford case, these AI endorsements would not have covered Crawford (the additional insured) for its defense costs because the 'named insured' (Weather Shield) was determined not to be negligent.

A second way that defense costs might be afforded or reimbursed to an upstream party is through the Contractual Liability coverage built in to most CGL policies. Note, however, that this would only cover the named insured for its contractual assumption of liability.

In other words, if the downstream party were contractually obligated to indemnify the upstream party for its defense costs and assuming no other provisions of the policy excluded coverage, then the downstream parties' insurer would cover the named insured for its obligation. This would in all likelihood reduce the downstream parties' liability limits. More importantly, however, is that many insurers are modifying the contractual liability coverage by requiring that the named insured be at least partially negligent.

From the insurance industry's perspective the Crawford ruling is potentially very costly. Insurance companies never intended to provide coverage when their insureds didn't do anything wrong. Because of this you can expect to see specific exclusions for the duty to defend in the absence of negligence of the 'named insured.'

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As mentioned above, while this may be covered under a commercial general liability policy, it is ***not*** covered under most professional liability policy forms. Whereas a general liability policy's contractual liability coverage allows the insured to assume the tort liability of a third party, the contractual liability coverage under most professional liability forms is not nearly as broad. Contractual coverage under most professional liability forms is limited to liability that the design professional would have had in the absence of the contract.

In other words, a design professional can agree to hold harmless, indemnify and defend a third party for the consequences of the design professional's negligence, but anything that goes beyond that negligence (such as the obligation to defend the client in the absence of negligence) would ***not*** be covered.

So What Is a Downstream Party to Do?

- Whenever possible, avoid contractual indemnity provisions.
- If you must agree to contractual indemnity, seek to make it reciprocal. If that is not an option, make certain the contractual language expresses that your obligation to indemnify must be caused by your negligence.
- **Avoid Accepting Defense Duties in an Indemnity Provision**

  If you cannot have the 'obligation to defend' deleted, then seek to tie it to a negligence standard. Consider the following example:

  'Contractor agrees, to the fullest extent permitted by law, to defend, indemnify and hold Client harmless against damages, liabilities and costs caused by the negligent acts, errors or omissions of Contractor in the performance of professional services under this Agreement, but only to the extent that Contractor is responsible for such damages, liabilities and costs on a comparative basis of fault between the Contractor and the Client after adjudication in a Court of Competent Jurisdiction. Contractor shall not be obligated to defend or indemnify Client for the Client's own negligence or for the negligence of others.'

  Alternatively you can use the indemnity provision in the AIA 2007 A201. Section 3.18.1 obligates the Contractor to *'indemnify and hold harmless the Owner… but only to the extent caused by the negligent acts or omissions of the Contractor….'*

Conclusion

From a risk management perspective, the indemnification agreement is a critically important element in any contract. The Crawford case has illustrated the dangers in a poorly worded indemnity agreement.

The good news is that many of your clients will understand that it doesn't make sense for you to assume obligations that are not backed up by your insurance program or that are inherently unfair, and they will agree to the modifications outlined above. After all, if the shoe were on the other foot, would your client assume responsibility for another's defense costs when it didn't do anything wrong?

Some clients may not be as reasonable. In those situations where despite your best efforts (and the efforts of your risk manager/insurance broker and attorney) your client remains unyielding, you will have a difficult decision to make.

Disclaimer: *This article is written from an insurance perspective and is meant to be used for informational purposes only. It is not the intent of this article to provide legal advice, or advice for any specific fact, situation or circumstance. Contact legal counsel for specific advice.*

Articles courtesy of Cavignac & Associates Employee Benefits Department

LIVE WELL, WORK WELL

Ignorance Is Toxic!

Poison Prevention Week is March 15-21. Are you familiar with how to protect yourself and your family from hazardous substances?

According to **poisonprevention.org**, the Poison Control Center receives over 2 million reports of poisonings each year, and more than 90% of these happen in the household. Children under age 6 fall victim to the most non-fatal poisonings.

Follow these tips so that you and your family avoid falling victim to poison ingestion.

- **Lock up all medicines and chemicals —** This is the easiest way to prevent little ones from getting into trouble.
- **Never leave loose pills out —** Even if you leave the room for a few seconds (for example, to get a glass of water), a child or pet will have more than enough time to ingest potentially fatal materials.
- **Be mindful of children/pets who visit your home —** You may not have children or pets of your own, but you likely receive visitors. Therefore, it is wise to put away anything hazardous that might look tempting to small children or animals.
- **Never use cups or soft drink bottles for paint thinner, gasoline, or other household chemicals** Children– or even adults – can mistake these for actual drinks and ingest them.
- **Never refer to medicine as "candy" when administering it to a child —** The child may remember this at a later date and be tempted to take medicine on his/her own.
- **Always read the labels of potentially hazardous products —** This is the best way to avoid adverse effects.
- **Leave the light on when taking medication —** Adults have been poisoned when they do not properly read the label of a medication, or confuse it with another one.
- **Pay attention to tamper-proof and/or child-resistant packaging —** If a product looks like it has been corrupted, do not risk using it.
- **Never create your own cleaning solutions —** A poison control center will not be able to give you proper instruction regarding ingestion.
- **Keep children out of the way when using pesticides —** Make sure their toys are removed from the area before applying, and never leave pesticides unattended while in use.

For additional, non-urgent information, visit www.poisonprevention.org or the Soap and Detergent Association (SDA) at www.cleaning101.com.

Poison Hotlines

► 24 hours a day / 7 days a week ◄

HUMANS — Call (800) 222-1222 to reach the Poison Control Center

ANIMALS — Call (888) 426-4435

POST THESE NUMBERS by your home phone or program into your cell phone in case of emergency!

LIVE WELL, WORK WELL.

Energy Drinks: Help or Harm?

In recent years, the younger generation has taken to gulping down an energy drink rather than old-fashioned coffee. However, several studies on energy drinks have shown that strong doses of caffeine increase the risk of hypertension, heart palpitations, headaches, insomnia, and can incite irritability and anxiety.

In addition, energy drinks do not sufficiently hydrate, and contain excessive amounts of sugar and especially caffeine. This is because the Food and Drug Administration (FDA) has guidelines for the caffeine content in soft drinks (17 milligrams in 12 ounces), but none for energy drinks. However, the American Beverage Association asserts that most 16-ounce energy drinks contain about half the caffeine found in a typical 16-ounce cup of coffeehouse coffee.

Experts also warn against consuming energy drinks mixed with alcohol. One such reason is because the caffeine content may fool an inebriated person into believing he/she is sober. The effects of alcohol are reduced when combined with an energy drink. Thus, a person may drink even more.

The Bottom Line

While it is generally safe to indulge in an extra boost of caffeine once in awhile, be mindful of certain side effects. When choosing an energy drink, opt for the sugar-free kind.

Finally, if you choose to mix an energy drink with alcohol, make sure you have a designated driver.

COBRA Alert!

The American Recovery and Reinvestment Act of 2009 (ARRA), effectively "restarted" the clock for former employees and their dependents who became COBRA eligible between **September 1, 2008** and **December 31, 2008**, but did **not** elect coverage when it was made available to them.

ARRA mandates that **by April 17, 2009** employers **MUST** notify these eligible former employees and their eligible dependents of their right to elect COBRA now, and of their right to a subsidy of their COBRA premium.

The Society of Human Resource Management provided its members with a summary of how employers will be affected and what they need to do. This summary was written by the law firm of Butzel Long. Click the link below to access:

COBRA Summary

Please contact **Linda O'Hara**, Account Manager of our Employee Benefits Team, if you have questions.

Need Chocolate? Walk It Off!

According to a recent study by the University of Exeter in Great Britain, walking for just 15 minutes can reduce chocolate cravings. Many studies have been done on how exercise reduces the need for a cigarette, but this is the first that linked exercise with chocolate.

In the study, not only were the cravings reduced during the walk, but for 10 minutes afterwards as well!

Simply must have chocolate?

It's not necessarily a bad thing to indulge your cravings. However, only eat sweets in moderation, and choose **dark** chocolate whenever possible. It contains antioxidants, and studies suggest it may even lead to lower cholesterol and lower blood pressure.

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"Neighbors helping neighbors in San Diego"

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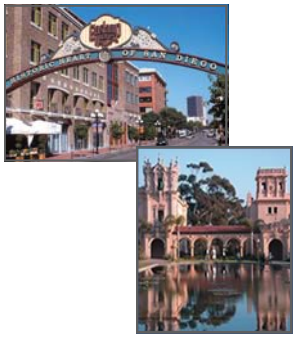

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