Insurance Coverage & Construction

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Catastrophic Construction Accidents:
General Contractors Working in New Jersey Can Recover Consequential Damages From Subcontractors’ General Liability Insurance Policies

INTRODUCTION

General contractors across the nation are particularly vulnerable to damages because of property damage flowing from accidents caused by their subcontractors’ work. In order to insulate against any adverse financial impacts from potential on-site disasters, subcontractors pay substantial premiums to insurance companies for Comprehensive General Liability (“CGL”) insurance policies. CGL policies are designed to shield the contractors and subcontractors from sums that the insured becomes legally obligated to pay as damages because of bodily injury or property damage. When purchasing insurance, subcontractors are typically obligated to and do list their general contractors as an “additional insured” on the insurance policy. Once disaster strikes, however, general contractors are faced with, and at times stymied by, several unanticipated roadblocks, including:

1) Unanticipated consequential costs, such as paying deductibles, replacing damaged construction materials, paying significant sums to reconstruct the project on an accelerated schedule in order to avoid liquidated delay damages (e.g., increased number of crews at premium labor costs and lower labor efficiency, overtime, etc.), additional project management costs and extended general conditions to cope with the accident;

2) Unanticipated defense costs resulting from insurance companies’ neglecting their “duty to defend” the insured contractor against bodily injury and/or property damage claims; and

3) An unanticipated struggle to obtain any insurance coverage because of the insurance companies’ narrow interpretation of the CGL policy.

Depending on the size of the project and accident, a general contractor easily can be blind-sided by the aforementioned cost burdens, which may seriously undermine expected profits.

Most general contractors working in the State of New Jersey are unaware of the extent of their insurance coverage. Recently, Kirkpatrick & Lockhart, LLP (“K&L”) successfully challenged several national insurance companies that denied insurance coverage (i.e., defense and indemnity) to a general contractor operating in New Jersey who was sued over a major project collapse. What was the result? Through complex litigation and creative arguments, coupled with existing case law, K&L successfully obtained “duty to defend” costs and consequential damages totaling over $1,000,000 for a general contractor. The following case study is based on this recent ruling and is provided to allow other contractors working in New Jersey to draw relevant information from the case.

CASE STUDY

In 1995, a local New Jersey county hired a Design/Builder (“DB”) to design, construct and operate a county-owned material processing and recovery facility in New Jersey. DB, in turn, retained the services of a general contractor (“GC”) to provide engineering services and to serve as the general contractor for the project. A subcontractor (“Sub #1”) was hired to conduct roofing and major steel erection for the entire proposed project. Sub #1, in turn, retained the services of a structural steel subcontractor (“Sub #2”) to fabricate and erect the steel framing for the entire structure, including steel joists, joist girders, girts, metal decking and shear connectors. On March 7, 1996, a large portion of the erected steel structure collapsed. The collapse caused serious bodily injury and ultimately death to one
employee and massive property damage to the structure. Sub #2 was found to be the sole cause of the accident because it negligently removed temporary braces before permanent braces were in place. GC and Sub #1 asserted substantial claims for damages flowing from the collapse.

The insurance company in this case denied all of GC’s insurance coverage claims made as an additional insured under Sub #2’s CGL policy. The insurance company set forth two main arguments in support of its insurance coverage denial. First, the insurance company argued that none of GC’s damages included actual “property damage” as defined by the CGL policies; rather, the claims were for uncovered consequential damages. Second, even if the claims constituted “property damage,” the business risk exclusions contained in the insurance policy precluded such insurance coverage. GC successfully argued to the court that it was an “additional insured,” that there was a covered occurrence, that the negligent actions of Sub #2’s steel work caused property damage, and that no “business risk” exclusions barred insurance coverage.

The successful legal approach employed was both grounded in the insurance policy precluded such insurance coverage. GC successfully argued to the court that it was an “additional insured,” that there was a covered occurrence, that the negligent actions of Sub #2’s steel work caused property damage, and that no “business risk” exclusions barred insurance coverage. GC recovered consequential damages exceeding $1 million. GC also recovered its defense costs, which were substantial.

Overall, by successfully arguing various legal issues and for a narrow interpretation of the business risk exclusion provisions in insurance policy, GC recovered insurance coverage for the consequential damage flowing from Sub #2’s negligence. All of the GC’s damages were recovered.

Conclusion
The number of significant construction projects in the State of New Jersey involving construction managers and general contractors continue to rise. With this rise comes an equal and proportionate amount of corresponding risk. The recent construction boom in New Jersey and across the country leads to one unfortunate, yet inevitable conclusion—there will be project accidents that could cause catastrophic damage. Construction disasters, such as the above-mentioned case study, illustrate the fact that general contractors and construction managers must know their legal rights, must know the extent of their insurance coverage (including under their subcontractor’s CGL policies), and most importantly, must never concede the insurance coverage to which they are entitled.

Under current New Jersey law, contractors have strong arguments that they can recover damages that flow from the negligent work of their subcontractors if such work has caused property damage. General contractors in New Jersey should be armed with the following information: (1) insurance companies selling CGL policies will construe those policies as narrowly as possible; (2) contractors will incur a multitude of unanticipated consequential and economic costs associated with on-site catastrophic events; (3) recent legal actions in New Jersey have construed insurance coverage in certain scenarios to include consequential damages; and (4) contractors should persist in attempts to recover such damages. Such vigilance will continue to solidify the contractor-friendly environment in New Jersey.

The Insurance Coverage practice group at Kirkpatrick & Lockhart LLP is one of the nation’s largest policyholder-oriented practices. Its attorneys have authored Policyholder’s Guide to the Law of Insurance Coverage and edited the Journal of Insurance Coverage.

FOR ADDITIONAL INFORMATION about these issues, please consult the authors or any of Kirkpatrick & Lockhart’s office contacts listed below:

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