RBJ RBJ.NET ROCHESTER BUSINESS JOURNAL
Part of the BridgeTower Media network
NOVEMBER 1, 2021

Insurance and Injury Corner: Issues in settling an owner's claims against a contractor's insurer


Jared K. Cook

When a contractor's alleged negligence injures a third party who sues the owner, the owner may be able to sue the contractor for common law or contractual indemnification. And in many cases, depending on the contract, the owner may also have a right to obtain insurance coverage for the loss directly from the contractor's insurer under additional insured or "insured contract" coverage from the contractor's commercial general liability policy of insurance.

Of practical note, settling the underlying claim may not extinguish the right of the owner, or its insurer, to seek reimbursement from the contractor's insurer. This is something to consider if the other parties and insurers in negotiations are seeking finality.

Absent a contractual agreement requiring more, a contractor's insurer is liable to only cover the contractor's losses. To the extent that those losses include the contractor's liability to indemnify the owner's liability to a third party, the contractor's insurer may be indirectly responsible for the owner's liability, but only to the extent that that liability can be passed on to the contractor. Under these circumstances, the contractor's insurer is not directly liable to cover damages of the owner.

However, counsel should obtain all policies to determine if coverage exists, including "insured contract" coverage.

Some contracts for construction, landscaping, snow removal, or similar services include a provision requiring the contractor to obtain insurance for the owner, often as an additional insured. Likewise, many commercial policies contain a provision that extends additional insured coverage not only to named additional insureds, but also to any party that the policyholder is required by a contract to add to the policy as an additional insured (even if the policyholder does not formally do so). In such cases, the owner may have, in addition to possible indemnification claims against the owner, a claim against the contractor for failure to procure insurance, or if the contractor did procure insurance and the contractor's insurer denied coverage, it may also have a direct claim against the contractor's insurer for coverage as an additional insured.

If an injured third party sues the owner and the owner sues the contractor for indemnification, the contractor's insurer may pick up and control the owner's defense. Ultimately, the insurer may decide to settle the claims. Obtaining the policies is important, because in settlement, as part of the tripartite relationship, the contractor's insurer may seek releases to include it. And this may present a conflict if the insurer did not cover all the owner's damages, because settling the owner's claims against the contractor may not preclude the owner from bringing a later claim for coverage against the contractor's insurer directly seeking additional insured coverage.

If this issue arises, defense counsel should refer any insurers to their own coverage counsel given their ethical obligations to the client, because the owner's claims against the contractor are legally distinct from the owner's claim against the contractor's insurer. And because they are legally distinct, when the claims against the contractor are dismissed, claim preclusion will not apply to the owner's (or its insurer's) claim against the contractor's insurer for reimbursement.

In New York, claim preclusion requires (1) a final judgment on the merits, (2) identical parties (or parties in privity with the original parties), and (3) an identical cause of action. [1] Each of these elements will be problematic without a release of the owner's insurance claims.

First, although a stipulation of dismissal is not actually an adjudication of the merits, it is considered a final judgment on the merits for purposes of claim preclusion, but unlike a final judgment, which will typically preclude not only claims actually asserted, but also claims that could have been asserted, but were not, a stipulated dismissal is narrowly construed to only preclude those claims that were actually asserted.[2] Therefore, the stipulated dismissal of the owner's claims against the contractor should not preclude the owner's unasserted claims against the insurer for direct coverage.

Second, because the contractor's insurer is a legally distinct party from the contractor, the identical parties requirement will not be satisfied. Although it is true that the contractor's insurer is in privity with the contractor for certain purposes, it will not be in privity with the contractor for purposes of the owner's claim against the insurer for coverage, because that claim is a direct claim against the insurer itself and the contractor should never be held liable for such a claim (as opposed to a direct indemnification claim). In addition, if the owner has asserted a claim against the contractor for failure to procure insurance naming the owner, then there will be a conflict of interest between the contractor and the contractor's insurer with respect to that claim — a finding that the insurer owed coverage would exonerate the contractor of any alleged failure to procure insurance naming the owner, and a finding that the contractor failed to procure coverage may relieve the insurer of any liability to cover the owner as an additional insured depending upon the policy language. This conflict of interest would destroy privity.

Finally, because the owner's claim against the insurer for coverage is legally distinct from its claims against the contractor, the identical claims requirement should also not be satisfied. The claim against the insurer for coverage will depend on the terms of the policy and what coverage the insurer agreed to provide, regardless of the contractor's fault or lack of fault, while the claims against the contractor depend on the owner's contract with the contractor and the contractor's fault, and may have nothing to do with coverage conferred by the insurance policy.

Therefore, when an insurer defending a contractor agrees to settle an owner's claims against the contractor, even if the owner has not also asserted claims against the insurer, the insurer should obtain its own counsel to potentially include its representation reviewing the contract to see if there is a provision requiring the contractor to procure insurance coverage for the owner. If there is such a provision, the insurer should either take such claims into account in the settlement and determine if it may obtain a release of such claims (consistent with its obligations to its insureds), or it should be aware that such coverage claims may be litigated later.

Jared K. Cook is an associate with Vahey Law Offices, PLLC, a litigation firm. Mr. Cook focuses his practice in the areas of employment litigation, commercial litigation, federal practice, appeals, and professional ethics. He can be reached at jcook@vaheylaw.com.