

Understanding Waivers of Subrogation

Suppose an air conditioning contractor, while installing a system for a new industrial building, has an accident. Another contractor's employee on the job site suffers injuries when the AC contractor's scaffolding collapses and falls on top of him. The injured worker sues the AC contractor and the project owner. The project's contract included a requirement that the contractor assume the owner's liability for any accidents arising out of the contractor's work. Consequently, the contractor's general liability insurance company pays the injured worker for both the contractor and owner's shares of the damages. The insurance company, however, has determined that the owner was twenty percent responsible for the accident. It files a claim with the owner demanding some of its money back.

The insurance company's action is entirely legal. Many project owners and general contractors, wanting to avoid this situation, insist that their subcontractors agree to a waiver of subrogation.

Subrogation is a legal principle in which a person who has paid another's expenses or debt assumes the other's rights to recover from the person responsible for the expenses or debt. For example, if someone hits your car in a parking lot and causes significant damage, your insurance company will pay you for the damage (assuming you bought collision insurance,) then recover the amount of its payment (subrogate) from the other driver (or, more commonly, from the driver's insurance company.) Subrogation holds ultimately responsible the person who should pay for the damage.

Owners and general contractors want to transfer their liability to subcontractors, to the extent that they can. Therefore, contracts often include a waiver of subrogation agreement. In such an agreement, the subcontractor promises not to pursue recovery from the other party. That agreement might bind the subcontractor's insurance company, depending on the type of policy and its terms.

A standard commercial general liability policy forbids the policyholder from doing anything to impair the insurance company's rights after the loss occurs. This implies that a waiver of subrogation agreed to before a loss binds the company. Also, the sub's policy may protect the other party if it names him as an additional insured. Under common law, an insurance company may not subrogate against its own insured. To remove any doubt, the sub should ask the company to add an endorsement applying a waiver of subrogation to the person or organization named in it. Insurance companies vary on the amount of premium they charge for this; some make no charge at all.

The standard business auto insurance policy has language similar to the general liability policy. Unlike GL insurance, there is no standard waiver of subrogation endorsement for auto insurance. Some insurance companies may offer their own versions of such an endorsement. Again, premium charges will vary.

Workers' compensation policies require an endorsement whenever a waiver of subrogation is desired. This endorsement may apply on a blanket basis to all parties with whom the insured has written contracts requiring waivers. Alternatively, it can apply only to the party listed on its schedule. The insurance company may charge up to two percent of the policy premium for blanket coverage or two to five percent of the project's premium for individual coverage.

Commercial property and inland marine insurance policies vary as to whether they permit waivers of subrogation even before a loss.

In all cases, a contractor or building tenant who is required by contract to provide such a waiver should check the relevant insurance policies. Policy changes should be requested if it is unclear whether they permit pre-loss waivers. The firm should consult with an insurance agent on all insurance-related contractual matters to ensure that the proper coverage is in place.