# Waiving Goodbye To Subrogation Claims

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The project caught fire at 80 percent completion. The owner's fire insurance carrier paid to have the project restored. The insurer then turned to the architect and contractors for reimbursement, alleging that design or construction errors caused the fire. The fire insurance carrier's claim is called subrogation, allowing an insurer paying a claim to step into the shoes of the party on whose behalf the claim is paid. Many standard form agreements, however, expressly waive subrogation rights. What does this mean and why is it important?

***What is Subrogation?*** You may be familiar with subrogation in the automobile insurance context. You look to your own insurance coverage, leaving the insurer to pursue the guilty party. Imagine if you were forced to litigate who caused the accident before you could get your car fixed. The same concern exists in construction. The industry long ago recognized the disruption caused by finger-pointing and litigation over construction-phase failures. Standard form agreements were developed to include a risk allocation mechanism that would enable parties to look to their own insurers for certain claims, without litigating fault or cause. There would be no arguments over fault, no litigation and no disruption of the project.

***How Subrogation Claims Are Waived.*** Buried deep within the boilerplate of the AIA B141 and A201 are provisions that provide a/e's with an impenetrable shield against certain types of claims. The A201 General Conditions provides for the owner's insurance coverage and for a waiver of subrogation rights (AIA A201, ¶11.4.7, 1997 ed.). The B141 contains a similar waiver "to the extent damages are covered by property insurance during construction." (AIA B141, ¶1.3.7.4, 1997 ed.).

To be covered by the waiver, the damage must occur "during construction" and the claim must be "covered by property insurance." What about damage to existing buildings not under construction? Or damage to previously completed work? Are subcontractors covered by the waiver? What if the owner fails to procure a separate builder's risk policy and instead relies on existing coverage? The nature of construction failures and the creativity of insurance lawyers have lead to a continuous analysis of these issues. Overall, however, these waiver provisions have been upheld as valid and enforceable components of an accepted risk-shifting mechanism.

The Illinois Appellate Court recently upheld such a waiver on behalf of an architect for a claim arising out of a fire after substantial completion but before final payment of the contractor. The Village of Bartlett planned to expand its Village Hall. The project included an emergency backup generator, powered by natural gas. The generator was located in the building's mechanical equipment room, with a metal, double-jacketed flue extending up and out the roof of the building. The flue had an extremely high operating temperature, and was to be supported by bolts to the masonry block. Instead of bolting the flue to the masonry, it was alleged that a subcontractor bolted the flue to the roof's wood trusses. Oops.

The building was substantially complete and was partially occupied while punch list work proceeded. In January of 1994, an ice storm knocked out power to the building, the generator kicked on and restored power. The flue pipe heated itself and the roof trusses to the point of conflagration. The Village's fire insurance carrier (not the builder's risk carrier) paid to restore the roof and even moved the generator to an outside shed, later demanding reimbursement from the architect and contractors.

The architect's attorney pointed to the waivers of subrogation in the AIA contracts. The insurer argued that it was not the builder's risk carrier for the project, that the Village lacked authority to waive the insurer's rights, and that the fire did not occur "during construction." The Illinois Appellate Court rejected these arguments, affirming the dismissal of the fire insurance carrier's lawsuit. The architect saved its deductible and the insurer was stuck with the claim.

***Adding a Belt to the Suspenders*.** As a legal matter, an insurer cannot seek subrogation from its own insured. Prudent a/e's require that the project's insurance policies name the a/e as an additional insured, at least on the general contractor's general liability policy. The builder's risk or "all risk" policy is frequently forgotten, however. Requiring that the builder's risk policy name the a/e as an additional insured provides a second shield to fend off subrogation claims because the a/e becomes an insured under the policy.

Waivers of subrogation are yet another reason to use standard form agreements, at least as a starting point for your agreements. The standard forms contain provisions that have been legally tested and apply to circumstances not typically anticipated. In any event, waivers of subrogation are important tools for risk allocation and should be included with your agreements and general conditions whenever possible.

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