

Third-Party-Over Liability

Work Comp Suits Keep Going and Going and...Going

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A major exposure for any contractor is the potential liability for employees who are injured at work.

An employer's primary protection from this exposure is the "exclusive remedy" rule, a major component of every state's workers' compensation statute. Under "exclusive remedy," if the employer has workers' compensation coverage, an injured employee's sole remedy against the employer is the right to workers' compensation benefits. These statutes maintain that the employer is legally responsible for work-related injuries regardless of employee fault. In return, the employer's liability is capped at the statutory benefits.

That's not the end of the story

Employers, especially contractors, may be exposed to suits against third parties by employees who are injured on the job. These suits are typically called third-party-over claims and are filed by employees seeking additional reparation beyond workers' compensation. This type of suit is usually brought against a project owner by the general contractor's employee under the theory of "failure to provide a safe worksite." It may also occur against the owner and/or the general contractor (GC) when the employee works for a subcontractor (SC). In the following examples, it is assumed that the employee works for the GC. (The same scenarios apply to

subcontractors, but it is likely that this type of suit will filter down to the SC from two levels above—from the owner to the GC and then to the SC.)

The owner sends this type of suit "downstream" to the GC via the GC's obligation to indemnify the owner, which falls under the indemnity clause in the construction contract. (Some indemnity clauses contain specific language that addresses this type of law suit. For example, read the last paragraph of clause 3.18 of the AIA A201.) The owner may also make a claim directly upon the GC's general liability insurance if the owner is included as an additional insured on the GC's general liability policy, a typical insurance requirement in construction contracts.

Historical approaches by owners

For this type of suit, owners have traditionally sought protection and indemnification from GCs through the auspices of the legal system. As suits progress through the courts of various states, a variety of theories and rulings have resulted. Again, the scenarios assume that the injured employee works for the GC (with the same being true for the SC).

Contribution—some owners have sought "contribution" from the GC. For example, assume an employee of the GC is injured on the job. The employee sues the project owner



for failure to maintain a safe worksite and the owner seeks contribution from the GC. Typically, a third party (the owner) is not allowed contribution from the injured employee's employer (the GC) due to the exclusive remedy rule effective in most states. The vast majority of cases have denied any recovery by the owner, holding that, as the employer, the GC was immune from suit for contribution.

There is one exception to this ruling. In 1991, a third party in Illinois was allowed contribution from the employer up to the amount of the compensation benefits paid to the injured employee (*Kotecki v. Cyclops Welding Corporation*). If you work in Illinois, you may have added exposure due to this ruling. You may also need to add certain endorsements to your general liability and/or employer's liability policy(ies) to properly address this exposure.

Implied Indemnity—where no written indemnity clause exists or is considered to be unenforceable, owners may seek indemnity under this theory, which holds that a party may be able to recover from a third party when one party owes a legal duty to the third party. Historically, courts have not found an implied duty of indemnity to exist in the typical construction scenario and, therefore, often stipulate that an owner is not entitled to indemnification from a GC under this theory.

Express or Contractual Indemnity—most construction agreements contain indemnity provisions whereby the GC agrees to indemnify the owner for liabilities arising out of the performance of the construction agreement. Presuming the indemnity clause is enforceable, most states allow the owner to be indemnified by the GC for the owner's liability to the injured employee in excess of the workers' compensation benefits paid by the GC.

What happened to “exclusive remedy?”

What is the justification in allowing third-party-over claims? While these claims aren't really an exception to the exclusive remedy rule, a third-party-over action filed against a GC by an owner in the construction process certainly circumvents the exclusive remedy provision.

The difference in the courts' view is that the tender of a third-party-over action from an owner to the GC is a legitimate transfer of risk. The courts apparently believe that in the construction process it is the GC, SC or sub-SC that maintains the primary responsibility for the safety of employees on the jobsite. Thus, absent any serious misconduct on the part of the owner or other upstream indemnitee, the liability should find its way to the party that has the greatest opportunity

to avoid jobsite accidents—the employer. There are times when transferring liability back to the employer may not be proper (e.g., a hidden defect that is discovered in the owner's premises or a GC who orders an SC's employee to perform an unsafe task).

Protection for a GC or SC

Contractual Liability Coverage—Review and understand the indemnity clauses contained in the construction contracts you sign. Most will be written broadly enough to include an obligation on your part to indemnify an owner or GC for a third-party-over claim. To properly insure your potential liability to these parties, be sure that you have the broadest contractual liability coverage available and that you and your agent discuss any restrictions under this coverage. You do not want to unknowingly assume liability outside of your contractual coverage.

Most liability policies provide standardized wording for contractual liability coverage as drafted by the Insurance Services Office. However, there are other forms in use which are more restrictive, and some insurance companies routinely use endorsements that change the standard wording and, thereby, restrict coverage.

Additional Insured Coverage for the Owner—Many construction contracts require the GC to include the owner on the GC's general liability policy (or the SC to include the GC and owner). Be sure to read the insurance requirements thoroughly and comply with these requirements. Also, be sure that your insurance matches the additional insured requirements as required by the contract. Do not give the owner or GC broader coverage than required, but be certain that your insurance is as comprehensive as needed.

As with contractual coverage, some insurers “push back” on additional insured coverage forms and restrict offerings. Be sure that you understand any meaningful restrictions in the additional insured endorsements used by your insurance company. Watch out, too, for owners who require specific additional insured endorsement forms. These owners may be asking for endorsements that are no longer written by insurance companies.

Third-party-over claims can make a work comp claim feel like it's never going to end. Protection from this type of suit can be the difference between staying in business and losing your business. It's critical that you understand the contracts you sign and your insurance coverages.