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The policy giveth and the policy taketh away: Do you know your insurance policy's coverage exclusions?

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If you own a construction business, a Commercial General Liability (CGL) policy is a crucial part of protecting your business from various losses. Generally, a CGL policy provides a business with insurance coverage for bodily injury and property damage caused by the business's operations, products, or injuries that occur on its premises.

While a CGL policy's name implies that it provides very broad (or "general") coverage, it does not cover all risks a business may face. Often, particularly when written with an "Excess" or "Surplus Lines" insurer, a CGL policy can potentially include significant and surprising exclusions and coverage limitations.

These exclusions can be based on specific types of projects, products, or services; acts committed by certain individuals; and may limit your CGL based on geographic considerations.

The Policy Giveth: Start with the Insuring Agreement

While your CGL policy typically covers bodily injury and property damage to others, it is not an "all-risk" policy, nor is it a performance bond. Your CGL policy is not designed to insure you against claims for breach of contract or poor workmanship.

To determine what the CGL policy covers, look to the beginning of the policy—the insuring agreement. Coverage can never be broader than what the insuring agreement provides, but as discussed below, it can (and frequently is) narrower. A proper analysis of what an insurance policy covers, therefore, starts by looking at what the policy gives. Jumping straight into the policy's exclusions can lead to coverage misinterpretations because exclusions (and exceptions to the exclusions) can be read to imply things are covered that fall outside of the insuring agreement.

Below is a brief overview of potential CGL policy exclusions of which you may not be aware, and which could significantly alter the coverage you thought you purchased to protect your business. While this is hardly an exhaustive list, what follows are examples of several exclusions that may be included in your CGL policy and which you need to consider.

The Policy Taketh Away: Key Exclusions and Endorsements

Some basics before we consider several notable exclusions: first, an exclusion is language in an insurance policy that sets forth a loss the policy does not cover, even though the insuring agreement seems to suggest there would be coverage.

The law in Massachusetts, and in most jurisdictions, requires that exclusions be written clearly and unambiguously. Ambiguity in an insurance policy is interpreted against the drafter of the policy (the insurance company) but what may seem ambiguous to a lay person may not necessarily be considered ambiguous legally speaking, so it is important that if you have questions, you ask your insurance agent, an attorney, or the insurance carrier directly.

Typically, where there is a reasonable difference of opinion about the meaning of an exclusion, or

an insurance policy generally, courts will resolve the dispute in favor of the policyholder. Further, courts will usually adopt the narrowest interpretation of policy language.

Where should you look to find the exclusions to your specific CGL policy? The first place is, naturally, the exclusions section of the policy. Additionally, certain policy “endorsements” can modify the CGL policy—and not necessarily by increasing coverage. An insurance endorsement or rider is an amendment to the existing insurance contract that changes the terms of the policy. Your insurance carrier may issue an endorsement at the time you purchase your policy, mid-term, or upon renewal. It is critical that you have all the exclusions and endorsements to fully understand your coverage.

Your CGL policy’s Declarations Page summarizes the information essential to your insurance coverage and may reflect certain insurance policy forms and endorsements. If you do not have all the corresponding forms and endorsements referenced on your Dec Page, you should obtain them so that you have your complete CGL policy and understand the entirety of the policy, including applicable exclusions and endorsements that modify or eliminate coverage. Your insurance agent or the carrier itself can provide you with the “complete” policy forms.

“Your Work” Exclusion

A critical exclusion that contractors must understand is the “Your Work” Exclusion. A typical “Your Work” exclusion states:

This insurance does not apply to property damage to work performed by or on behalf of the Named Insured arising out of the work or any portion thereof, or out of materials, parts, or equipment furnished in connection therewith.

An example of how this exclusion would apply can be seen in a typical construction project where the contractor performing the work does so defectively and is sued by the owner for the costs of repairing the defectively performed work. The cost of repairing or replacing the poorly executed work would be excluded by the CGL policy pursuant to the Your Work exclusion (and possibly other exclusions). The CGL policy’s “Your Work” exclusion means that there would be no insurance for such a claim (usually brought as a breach of contract, negligence, or breach of warranty claim). Accordingly, your business would likely be responsible for paying for those damages out of pocket.

What if, however, the contractor’s defective work not only needs to be replaced, but caused an accident that injured the owner or damaged the owner’s car? In those situations, the CGL policy would likely provide insurance and an attorney to handle the litigation for personal injury and property damage (subject to the CGL policy’s other limitations and exclusions). The cost of repairing or replacing the defective work itself would likely not be covered because of the “Your Work” Exclusion.

Subcontractor Exception to the “Your Work” Exclusion

An important caveat to the “Your Work” exclusion is the subcontractor exception to the exclusion. Where the Your Work exclusion takes coverage away to repair defective work, if a general

contractor's subcontractor performed the defective work, and the owner sues the general contractor for the costs of repairing such defective work, the general contractor's policy may nevertheless provide insurance to repair the defective work pursuant to the Subcontractor Exception to the Your Work Exclusion. The exception usually states: "This exclusion does not apply if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor."

Questions about how the policy defines a "subcontractor" are critical to determining whether there will be insurance coverage, but this exclusion and its exception are frequently the subject of insurance coverage disputes and construction litigation.

"Injury to Independent Contractors (Subcontractors)" Exclusion

Many unsuspecting general contractors have discovered after a loss that the CGL policy they purchased, assuming it covered them for accidents to non-employees on a project, includes a potentially devastating "Injury to Independent Contractors" or "Injury to Subcontractor's Employee" Exclusion. As discussed above, a CGL policy typically covers eligible bodily injury claims brought by anyone other than an insured's employees. That said, certain construction insurers (usually in the excess/surplus lines marketplace) may seek to exclude coverage for employees of subcontractors or independent contractors.

This is often attempted by adding an exclusion for "Injury to Contractors or Subcontractors and Their Workers," or an exclusion to that effect. While an injured employee of a subcontractor or independent contractor should theoretically be covered by that subcontractor's workers' compensation policy, that does not stop the worker from bringing a bodily injury suit against other parties involved in the construction project. Accordingly, it is critical that this exclusion be removed, when possible, to avoid uncovered claims associated with jobsite accidents. If it cannot be removed, then you must take the appropriate steps to ensure via your subcontract and additional insured status that you have coverage for these types of losses.

"Designated States" and "Designated Work" Exclusions

Another type of policy exclusion may exclude coverage for damages arising out of work performed in certain geographic areas or of certain categories of work. For example, a "Designated States" exclusion may exclude or limit coverage for work performed in certain states or jurisdictions. Many insurers have added Designated States exclusions to exclude work performed in New York, a state known for local laws and statutes unfavorable to contractors and their insurance carriers.

Similarly, a "Designated Work" exclusion may eliminate coverage for damages arising out of certain types of work performed by the insured. Some Designated Work exclusions eliminate insurance coverage from CGL policies for claims arising out of work performed on residential or so-called "habitational" projects. Insurance underwriters understand that these types of projects result in claims with a higher frequency and value and have sought to include residential exclusions as a result.

The specific language of the policy is key here to determine whether a residential or habitational exclusion applies to single-family homes only, or to a broader array of projects, including

condominiums, apartments, tract housing, hotels, dorms, and assisted living facilities. On the other hand, commercial contractors can access lower rates by allowing insurers to exclude residential work (or certain types of residential work) – so it is not always damaging to have an exclusion of this nature on one’s policy, provided that the appropriate contractual and insurance risk management tools are used to obtain coverage and protection through a subcontractor’s CGL policy and via the subcontract itself.

Closing Thoughts

In 1736, Benjamin Franklin coined the phrase “an ounce of prevention is worth a pound of cure” to remind the citizens of Philadelphia to remain vigilant about fire awareness and prevention. Close to 300 years later, the saying applies to reviewing your CGL policy, its exclusions, and endorsements—before a loss. Make reviewing your business’s CGL policy a priority as you head into 2022 and beyond.

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