

Risk Monitor



When Does Your Insurance Company Have to Defend You in Court?

Commercial general liability insurance pays for lawsuit settlements or court judgments that an organization would otherwise have to pay for certain types of harm others suffer. These include bodily injuries, property damage, advertising injuries, and personal injuries such as violations of privacy. Another benefit of this insurance, however, can be just as valuable or even more so: coverage for the cost of legal defense.

The standard CGL insurance policy gives the insurance company "the right and duty to defend the insured" against any suit seeking damages. Conversely, the company has no duty to defend the insured against a suit seeking damages for an incident the policy does not cover. The company's duty to defend ends when it has paid out the policy's maximum limit of insurance for settlements or judgments. Most policies provide coverage for defense costs in addition to the amounts available for payment of damages.

Because the company does not have to defend a claim it believes the policy does not cover, disputes about whether a duty exists can arise between the company and the insured organization. Courts in most states have given the policy a broad interpretation and favored the insured. For example, New York's highest court has said that "an insurer will be called upon to provide a defense whenever the allegations of the complaint suggest ... a reasonable possibility of coverage." However, courts have put limits on the duty. A Texas court in 1997 ruled that a court may not "read facts into the pleadings, look outside the pleadings, or imagine factual scenarios that might trigger coverage." Also, an insurance company's defense of a claim does not

necessarily mean that the policy covers the claim. Another Texas decision in the same year held that the company's duty to pay for the damages is governed by the facts of the case, not just the possibility of coverage.

Suppose the insured is a construction firm. An employee, frustrated by a particular task, throws a wrench, striking and injuring another contractor's employee on the job site. The injured employee sues the contractor and the worker. The CGL policy does not cover injuries expected or intended by the insured. If a

court decides the employee expected the wrench to injure someone else, the policy will not cover the settlement. However, it is possible that the employee expected or intended no such thing. Because the possibility of coverage exists, the insurance company will have to defend the firm and the employee against the lawsuit.

Now assume the insured is a restaurant. A group has dinner after spending the afternoon tailgating at a football game. One person, already intoxicated from the tailgating, has six beers with dinner and leaves the restaurant very intoxicated. He makes a wrong turn, walks into busy traffic, and suffers serious injuries when a car strikes him. He sues the restaurant for his injuries. The CGL policy does not cover injuries for which the insured is liable by reason of contributing to a person's intoxication if the insured is in the business of selling alcoholic beverages. Because there appears to be no possibility that the restaurant's policy will cover this claim, the insurance company has no duty to provide defense.



continued on page 2

Welcome to The Chadler Group's Newsletter!

It is with great satisfaction that we bring our newsletter to you. In this issue and the coming quarterly newsletters, we will discuss pertinent insurance topics which affect your business and personal insurance needs. We hope you find this information both informative and useful in your overall risk management practices.



The Chadler Group, Inc.
PO Box 11115
330 Passaic Ave, Ste. 200
Fairfield, NJ 07004

Phone: (800) 706-2478
Fax: (973) 227-4026



Keep an Eye on Your Employees...Legally

Inherent in the employer-employee relationship is the understanding that the employer should supervise an employee's work activities. Effective supervision ensures that the necessary work is being performed at the time it's needed, resulting in an efficient and profitable operation for the employer. Also, a minority of workers, if left unsupervised, may do or say things that can hurt a business's reputation, reveal trade secrets, or even incur legal liability. While this has always been so to some extent, the rapid changes in communications technology over the past two decades have heightened concerns about it. An employee can hurt a business by saying something inappropriate on the phone, sending an offensive e-mail, visiting web sites that are inappropriate for work, or in a variety of other ways. As a result, employers are using new technology tools to monitor their employees' activities.

Some employers frequently monitor employees' phone conversations. Federal and state law generally allows this for quality control purposes when an employee is on the phone with a client. While some states require advance notification of monitoring to the parties to a call, federal law allows monitoring of business calls with no prior notice. A federal court decision does require employers to stop listening when it becomes apparent that a call is personal in nature, but an employer might monitor all calls made from phones designated as "business use only." It is also legal for employers to obtain lists showing phone numbers dialed from a particular extension and the duration of each call. While the law does not require notifying employees in advance, employers may wish to do so to head off problems.

Courts have also recognized an employer's right to monitor use of its e-mail system. A federal court held that a private sector employee did not have a reasonable expectation of privacy in e-mail messages where he described management in profane and derogatory language. Another court ruled against a CIA employee who violated agency Internet use policy by downloading pornographic material. The federal Electronic Communications Privacy Act of 1986 permits employers to monitor employee e-mail in the ordinary course of business, when the employee consents to monitoring, or when messages are stored on a computer located on an in-house network. Employers may even monitor an employee's keystrokes on a computer to see what and how much text the employee is producing.

Oregon-based law firm DuVal Business Law recommends that employers take the following steps to avoid legal problems arising out of e-mail monitoring:

- Working with legal counsel, develop a comprehensive e-mail and Internet use policy for employees.
- The policy should make it clear that employee communications over the employer's network are not private and that the employer will monitor them for legitimate business reasons.
- The policy should state the workplace's rules for Internet use, including types of sites employees may not visit and types of files they may not download. It should also state the penalties for breaking the rules.
- Finally, the policy should state how long the employer will store electronic files and how it will delete them.

DuVal also recommends either having employees sign a copy of the policy before they may receive access to the system or posting the rules on the login screen they see at the start of each day.

Even with these precautions, employee lawsuits for invasion of privacy are still possible. Employers should consider buying employment practices liability insurance to cover them for the cost of defending these suits and the cost of any court-ordered judgments. With this coverage and common sense policies in place, employers can take advantage of Internet technology while not placing themselves at undue risk.



continued from page 1...When Does Your Insurance Company Have to Defend You in Court?

The cost of defending a lawsuit can often exceed the cost of the settlement. All businesses should discuss their liability coverage with their insurance agents to ensure that they have the protection they need if they get sued. The agent can identify

coverage gaps and recommend solutions. They may involve additional premiums; better that a business pays more for insurance than endure bankruptcy due to uncovered legal costs.

Manage Risk with Hold Harmless Agreements and Contractual Liability Insurance

Lawsuits are a common occurrence in our litigious society. An effective way to limit your liability is to specify your responsibility in a contractual relationship. Risk can be transferred contractually by including “hold harmless” clauses in agreements.

In a hold harmless agreement, one party agrees to protect or “indemnify” another from claims brought by a third party for financial loss or damage. A good example is a general contractor who hires a subcontractor to complete a job for a third party. To protect himself, the general contractor may require the subcontractor to sign a hold harmless agreement. The agreement would indemnify the general contractor if any problems arose from the subcontractor’s work.

Read...Before You Sign on the Dotted Line

In a hold harmless agreement, the indemnitor (the party that has assumed the liability) is responsible for all financial loss. Some hold harmless clauses are very broad. Surprisingly, they may include liability even if the indemnified company was solely responsible for the damage. On the other hand, a contractual liability insurance policy can protect the indemnitor, but may not cover all aspects of liability.

In our example above, the hold harmless agreement gives the general contractor the right to collect for damages paid to the third party to the extent enforceable under the law. However, the indemnified party should exercise caution. The ability to uphold indemnification agreements differs from state to state because state laws vary as to what risks may be transferred. Also, some courts have ruled indemnification clauses unenforceable if they were not clear and precise.



Protect Your Assets

With a general liability policy, contractual liability insurance is automatically provided. The coverage is created to pay to a third party damages assumed as part of an “insured contract.” However, the definition of an insured contract is limited, and coverage is written as an exception to an exclusion. That means the policy excludes coverage except for specific circumstances. Additional policies, such as professional liability insurance, may be required to cover exposures that are not covered under general liability policies.

Usually, general liability insurance covers only bodily injury or property damage. But, once again, these are subject to exclusions, conditions and limitations, and the injury or damage must have occurred after entering into the contract.

Furthermore, the liability must be one that would be imposed without the contract or one that is assumed in a hold harmless or indemnity agreement that falls within the definition of insured contract under the policy. General liability policies do not cover breach of contract.

Before signing any contract, it is wise to talk to an attorney, so that you do not assume liability that is not covered under your general liability insurance policy. Take time to carefully read your insurance policy endorsements, and don’t be afraid to ask your insurance agent to explain anything you do not understand. Your agent will help you determine the type of coverage your business needs to protect your assets.

continued from page 4...Understanding Waivers of Subrogation

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.

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.

continued on page 3



The Chadler Group, Inc.
PO Box 11115
330 Passaic Ave, Ste. 200
Fairfield, NJ 07004

Phone: (800) 706-2478
Fax: (973) 227-4026

Risk Monitor