WHAT IS SUBROGATION, AND HOW DOES IT AFFECT YOU?

Introduction to Subrogation

Subrogation refers to when an insurance company that has paid a claim obtains the right to “step into the shoes” of its insured for the purpose of pursuing reimbursement from the party that should have responsibility for paying the claim. For example, if you are in an automobile accident that is not your fault, your insurer will pay to have your vehicle repaired. Your insurer becomes “subrogated” to your rights and can pursue a claim against the other driver to recoup the money it paid to you. The insurance company takes all your rights exactly as they are. In other words, the insurance company can have no greater rights than you, and the opposing party can assert all the same defenses against as it could have asserted against you, such as contributory fault on your part.

A waiver of subrogation places the risk of any covered loss with the insurance company providing coverage, regardless of fault, thereby eliminating lawsuits over covered claims. Because a subrogated party cannot have any greater rights than the party whose rights it obtained, a waiver of subrogation is binding on your insurer and prevents it from recouping any losses from the responsible party.

Most construction contracts include waiver of subrogation provisions requiring the parties—or only the roofing contractor—to waive the right to pursue damages against the other if the loss is covered by insurance. Most waiver of subrogation provisions, including The American Institute of Architects (AIA) provision, limit the waiver to losses covered by property insurance, but some go much further.
AIA Approach to Waivers of Subrogation

The most common waiver of subrogation clause is the one contained in AIA’s A201 General Conditions, which provide, in pertinent part:

The Owner and Contractor waive all rights against (1) each other and any of their Subcontractors, Sub-subcontractors, Agents and Employees, each of the other, and (2) the Architect, Architect's Consultants, Separate Contractors described in article 6 [separate contractors hired by Owner], if any, and any of their Subcontractors, Sub-subcontractors, Agents and Employees, for damages caused by fire or other causes of loss to the extent covered by property insurance obtained pursuant to this paragraph 11.4 or other property insurance applicable to the Work, except such rights as they have to proceeds of such insurance held by the Owner as fiduciary… .

Under this provision, the parties waive all rights against each other for damages caused by fire or other causes of loss to the extent covered by property insurance. This provision, which has been consistently enforced by the courts, applies to builder’s risk coverage purchased by the owner and any property coverage the contractor may have that pays for a loss.

General Contractor or Owner-drafted Contract Approach to Waivers of Subrogation

General contractors and owners frequently seek to reach beyond the AIA provision by requiring waivers of subrogation on all policies provided by a roofing contractor through use of a broad waiver of subrogation clause, such as: “Except where prohibited by law, the insurance carriers for each coverage set forth herein shall waive all rights of subrogation that the insurer may have against Contractor, Owner, and the indemnified parties.”

Waiving subrogation for damages covered by insurance policies can be risky, and it is recommended you do not agree to do so without consulting your insurance agent and attorney. Of particular concern are waivers of subrogation in workers’ compensation and commercial general liability (CGL) policies.
Waivers of Subrogation Pertaining to Worker’s Compensation

In situations where compensation is payable under a worker’s compensation policy and the insurer already has paid benefits, the insurer typically is granted a subrogation lien against any subsequent, duplicate recovery by the employee for benefits or expenses paid for by the insurer. Although it may be the intent of the general contractor, a waiver of subrogation generally does not prevent an injured employee from filing suit against the general contractor because the employee initiating the claim is not bound by the waiver. However, a waiver of subrogation may bar the insurer from initiating a subrogation action or enforcing its lien on a third-party claim. Therefore, the waiver may allow a double recovery to the injured employee, who gets to keep the full recovery obtained from the general contractor despite having already been paid for medical costs and other benefits received through the worker’s compensation claim.

Although the party requiring waiver receives little benefit, such waivers may have a significant effect on you if, after paying an additional premium to add the waiver of subrogation to a policy, you face the threat of a further premium increase because of your insurer’s lack of recovery on the worker’s compensation lien.

Waivers of Subrogation Pertaining to CGL

A CGL policy protects against liability claims for bodily injury and property damage. A waiver of subrogation comes into play when bodily injury or property damage covered by your insurance was caused by or contributed to the upstream party’s fault. Although that party is responsible, at least in part, if subrogation has been waived your insurer may be required to pay 100 percent of the loss because it has lost the ability to recoup losses from the responsible party.
Many CGL policies available to roofing contractors include a blanket waiver of subrogation provision agreeing to waive subrogation whenever it is required by written contract before the loss occurs. Even if your CGL policy includes a blanket waiver of subrogation, it is still advisable to attempt to negotiate that waiver of subrogation out of your contract. You should not simply assume a waiver of subrogation is a harmless allocation of risk among insurance companies. Instead, an insurer saddled with exposure and losses because of loss of subrogation rights will typically mitigate that risk by, among other things, raising premiums.

**Harmonize Your Contract and Insurance Policy BEFORE Signing the Contract**

Before executing a contract with a waiver of subrogation clause, ensure the clause does not violate the terms of your policy. CGL policies often specify the insured must not do anything to impair the insurer’s rights of recovery. If the policy does not include a blanket waiver of subrogation provision, waiving subrogation without the insurer’s consent would certainly violate the requirement not to impair the insurer’s rights. The key is knowing and understanding what your policy allows and ensuring your contract is consistent with the terms and conditions of the applicable insurance policies. If you waive subrogation rights but fail to get your insurer’s consent, you may have materially breached the construction contract and given your insurer an excuse to deny coverage, saddling yourself with a loss that should have been covered by insurance. Similarly, failure to obtain waivers of subrogation from insurers where required may entitle the other party to terminate the contract if the breach is not remedied.