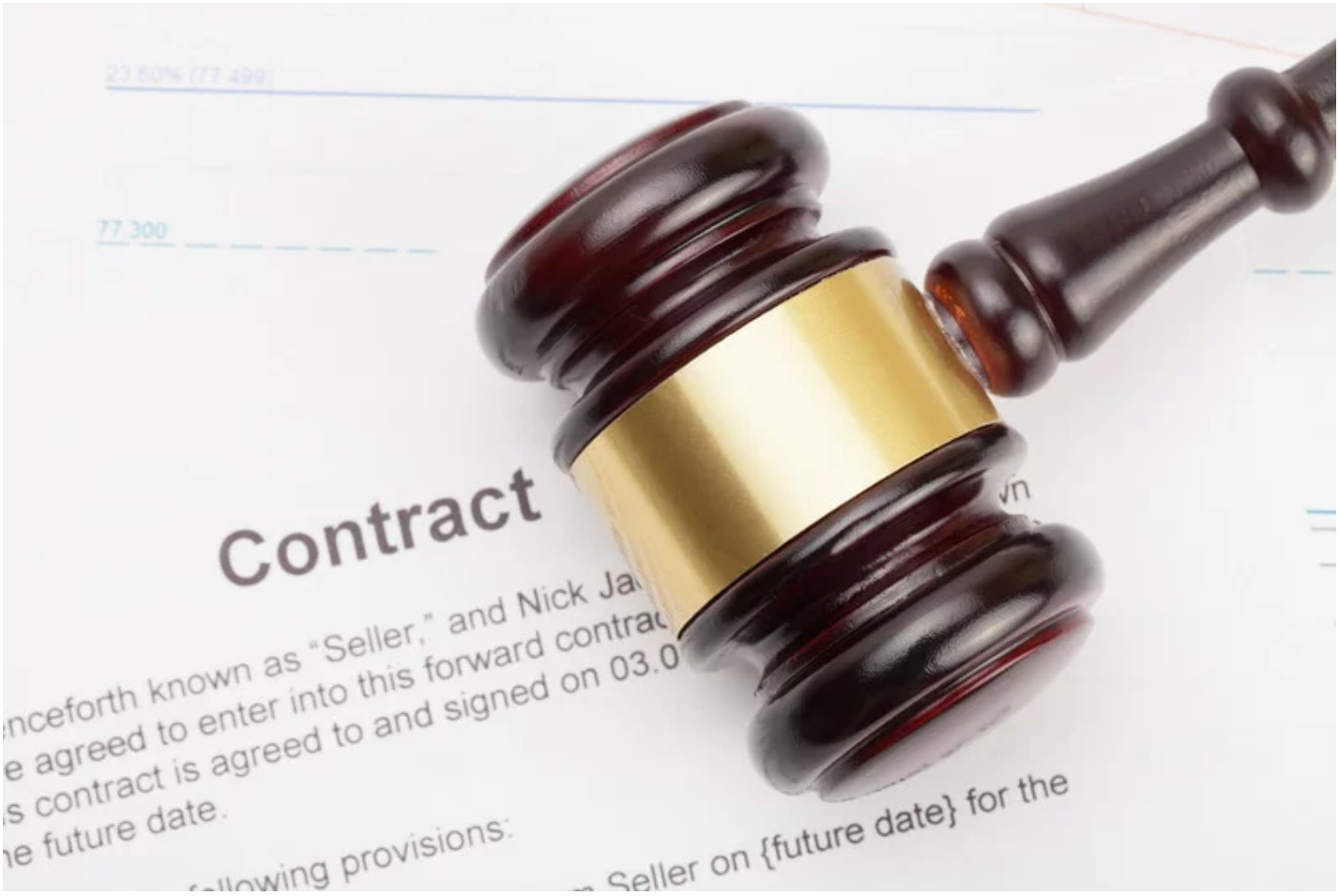
Expert Commentary

Whose Contract Is It Anyway: Gilbane Decision Requires Contractual Privity



As previously addressed in "Whose Contract Is It Anyway: Addressing the Contractual Privity Problem," additional insured coverage under Insurance Services Office, Inc. (ISO), standard blanket additional insured endorsements is often conditioned, in part, on the existence of a written contract requiring additional insured coverage.

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Additional Insured Issues

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However, across the country, disputes have arisen as to the necessary scope of that written contract and whether certain language requires that there be a direct contract between the named insured (i.e., "you") and each additional insured (i.e., "such person or organization"). This can become problematic in effectuating the intended risk transfer.[1] In these situations, courts are split on whether direct contractual privity is required to satisfy certain additional insured endorsements.

New York's high court recently weighed in on this issue in the highly anticipated *Gilbane Bldg. Co./TDX Constr. Corp. v. St. Paul Fire & Marine Ins. Co.,* 2018 NY Slip Op 02117, decided on March 27, 2018. Ultimately, the court held that a direct contractual relationship was required when interpreting manuscript language modeled after the ISO blanket additional insured endorsement.

Strong additional insured contractual requirements and endorsement review have always been critical in the New York market, and this decision serves as a stark reminder of that fact. As is often the case for insurance coverage litigation, New York also serves as a potential bellwether for the rest of the country, and owners/contractors operating in multiple jurisdictions should likewise take note.

The Facts and Decision in *Gilbane*

Despite conflicting authority nationally, and conflicting opinions between the New York trial court and the Appellate Division, the New York Court of Appeals found that the language of the blanket additional insured endorsement at issue—*"with whom you have agreed"*—was "facially clear" and did not confer additional insured status unless an organization has a direct written contract with the named insured policyholder.

As background, in *Gilbane Bldg. Co./TDX Constr. Corp.*, the Dormitory Authority of the State of New York (DASNY) hired Gilbane Building/TDX Construction, a joint venture ("Gilbane/TDX JV"), as construction manager and Samson Construction as prime contractor. During the course of the construction project, Samson's excavation and foundation work caused adjacent buildings to sink. DASNY filed suit against Samson and the project's architect for the damage, and the architect brought a claim against Gilbane/TDX JV.

Per the construction management contract between DASNY and Gilbane/TDX JV, any prime contractor was required to name the construction manager as an additional insured. Accordingly, Gilbane/TDX JV sought additional insured coverage from Samson's insurer, Liberty Mutual. Samson's Liberty policy contained a blanket additional insured endorsement that provided:

> WHO IS AN INSURED (Section II) is amended to include as an insured any person or organization with whom you have agreed to add as an additional insured by written contract but only with respect to liability arising out of your operations or premises owned by or rented to you.

Liberty filed a motion for summary judgment, seeking a declaration that it had no duty to defend Gilbane/TDX JV because it did not have a direct contract with the named insured, Samson.

The New York trial court denied Liberty's motion for summary judgment, finding that the endorsement required only a written contract to which Samson was a party (i.e., the contract between DASNY and Samson) and, because that contract obligated Samson to name the construction manager as an additional insured, Gilbane/TDX JV was entitled to additional insured coverage under the Liberty policy. Specifically, the trial court held that the endorsement "requires only a written contract to which Samson is a party. It does not require that Liberty be a party to such a contract. Thus, there is no merit to Liberty's argument that plaintiff cannot be additional insureds because they are not in privity with Liberty."

Both the New York State Supreme Court, Appellate Division (intermediate court), and the New York Court of Appeals (high court) disagreed. The New York Court of Appeals' majority opinion focused on the "reasonable expectations" of the insured and found that the language in the endorsement was not ambiguous, meaning that it was not reasonably susceptible to more than one interpretation. Specifically, the court focused on the word "with" in the phrase "with whom," and concluded that, when read by the average insured, the phrase "can only mean that the written contract must be 'with' the additional insured." Notably, the majority evaluated the language in relative isolation and without specific consideration given to the expectations of construction professionals in the construction industry.[2]

The New York Court of Appeals' dissenting opinion objected to the majority's narrow view of the language based upon the single word "with" and asserted that "the majority focuses on a single word in the blanket additional insured endorsement at issue while ignoring others, thereby finding clarity where none exists." The dissenting opinion found that the blanket additional insured provision was susceptible to "more than one reasonable interpretation" because the language could also be read to simply require a "written contract" under which a party is promised additional insured coverage.[3] Moreover, the dissenting opinion addressed the significance and purpose of blanket additional insured endorsements in the construction industry and the negative impact that the majority's decision could have on an industry that is so reliant on transferring risk to those parties that are closest to that risk.

How To Be Prepared Post-*Gilbane*

Importantly, in this author's view, this decision does not reflect an upstream versus downstream issue; it's purely a coverage question. In the construction setting, it is the common expectation of all parties that downstream insurance will be available to upstream parties for appropriate risks. Outcomes like this are unexpected and can frustrate those risk transfer goals. There are a few fundamental solutions for avoiding this outcome and establishing appropriate downstream risk transfer in similar scenarios. First, know which additional insured endorsements do not require contractual privity—CG 20 38 04 13 is a prime example—and make sure the relevant contract expectations are explicit. Second, conduct a careful review of additional insured endorsements, and learn to spot troublesome language. When you see "with whom" in the contractual requirements of an additional insured endorsement, think about this ruling, and recognize the exposure that not all upstream parties may be afforded the intended risk transfer. Allocating resources to this kind of meticulous contract review is always a struggle, but sometimes there's simply no substitute for diligence.

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[1] Frequently, these disputes involve language that conveys additional insured status to "any person or organization for whom you are performing operations when you and such person or organization have agreed in writing in a contract or agreement that such person or organization be added as an additional insured on your policy...." See ISO form CG 20 33 07 04.

[2] Amicus curiae Turner Construction Company explained that "a critically important component of risk transfer in the construction industry is additional insured coverage afforded to organizations that are upstream and do not have immediate control over the work being performed on the project.... Downstream subcontractors, at every tier, are typically required to provide this coverage for all upstream parties." Brief for Turner Construction Company as amicus curiae, p. 8, *Gilbane Bldg. Co./TDX Constr. Corp.,* 2018 NY Slip Op 02117. As a result, Turner argued, blanket additional insured endorsements "are intended to streamline the complexities of risk transfer in the construction industry and prevent common administrative oversights, such as, failing to properly identify an additional insured, or identifying the incorrect additional insured." *Id*. at p. 6.

[3] "[I]t is reasonable for the average insured to expect that the phrase 'by written contract' modifies only the immediately preceding infinitive 'to add,' such that the phrase prescribes only that the agreement by which the named insured commits to extend coverage to the purported additional insured must be evidenced in a contract reduced to writing." *Gilbane Bldg. Co./TDX Constr. Corp.*, 2018 NY Slip Op 02117 (Stein, J., dissenting) at 4.

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