

WWM CASE ALERT: MN SUPREME COURT RESTRICTS SCOPE OF AI COVERAGE

ENGINEERING & CONSTRUCTIONS INNOVATIONS V. L.H. BOLDUC & TRAVELERS INDEM. CO. (MINN. JAN. 23, 2013)

CGL insurers will take interest in a recent decision by the Minnesota Supreme Court, in which the Court held that a contractor did not qualify for additional insured (AI) coverage under its subcontractor's policy and the subcontract's indemnity provisions were unenforceable. The decision is noteworthy for two holdings. First, the Court adopted a narrow reading of the scope of an AI endorsement making the contractor an AI for liability "caused by the acts or omissions" of its subcontractor by limiting the AI coverage to claims involving the subcontractor's negligence. Second, the court held that the subcontract's indemnity provision violated Minnesota Statute § 337.01, et seq., because it required the subcontractor to indemnify the contractor for damages not caused by the subcontractor's negligence and, due to the inapplicability of the AI coverage, was not supported by a coextensive insurance agreement.

Engineering & Constructions Innovations, Inc. ("ECI") had a contract to perform work in the installation of an underground sewer pipeline. ECI subcontracted some of its work to L.H. Bolduc Company, Inc. ("Bolduc"). In the subcontract, Bolduc agreed to defend and indemnify ECI to the fullest extent permitted by law and to maintain and provide insurance covering Bolduc's defense and indemnity obligations. Bolduc obtained a CGL policy from Travelers Indemnity Company of Connecticut ("Travelers"). The Traveler's policy had a Blanket AI (Contractors) Endorsement, which provided AI coverage to any party Bolduc agreed to include as an AI in a written contract, but "only to the extent that, the injury or damage is caused by acts or omissions of you [Bolduc] or your subcontractor in the performance of 'your work[.]'" During Bolduc's work on the project, the pipeline sustained damage. ECI spent \$235,339 to repair the pipeline and sought reimbursement from Travelers as an AI. Travelers refused to pay, asserting that Bolduc did not cause the damage and, therefore, the claim did not fall within the AI endorsement language requiring that the damage be "caused by acts or omissions of" Bolduc.

ECI then sued Bolduc and Travelers. Against Bolduc, ECI alleged negligence and breach of contract for failure to perform its work properly and failure to indemnify ECI. ECI alleged breach of contract against Travelers for failure to provide AI coverage. The parties agreed that Bolduc drove a metal sheet into the pipeline, causing the resulting damage, but a jury nonetheless found Bolduc not negligent. After the negligence trial, the parties filed cross-motions for summary judgment on the contract issues.

The trial court granted summary judgment for Travelers, finding that ECI did not qualify for AI coverage. The Minnesota Supreme Court affirmed. The Supreme Court reasoned that, because the jury found Bolduc was not negligent, the damage to the pipe was not "caused" by Bolduc as that word was used in the AI endorsement and, therefore, the AI endorsement did not provide coverage to ECI under the circumstances. The Supreme Court reached this decision even though the AI endorsement did not include the word

“negligence” before the phrase “caused by acts or omissions” and despite the parties’ agreement that Bolduc caused the pipe damage. The Court explained that, even though the concept of negligent fault was not expressed in the AI endorsement, a reading of the policy as a whole led to “only one reasonable interpretation” – the endorsement required negligence by Bolduc. Thus, the court concluded that the AI endorsement could provide coverage to ECI “only in instances of ECI’s vicarious liability for Bolduc’s negligent acts or omissions.” Because the jury previously found Bolduc was not negligent, any liability imposed on ECI would be due to its own direct liability which was expressly excluded by the AI endorsement. Thus, the Court held that the AI coverage did not apply.

The trial court also granted summary judgment for Bolduc, finding the subcontract’s indemnity agreement unenforceable. The Minnesota Supreme Court affirmed. The Supreme Court’s reasoning was, to a significant degree, based on its determination that ECI waived many of its arguments. Thus, on this issue, the Court’s decision may be distinguishable in future cases. But the Court further reasoned that, even if not waived, ECI had no indemnification claim because the jury found Bolduc not negligent. The court explained that under Minnesota Statute § 337.02, an indemnification agreement in a construction contract is unenforceable unless the underlying damage is due to a negligent act or omission of the subcontractor-indemnitor, subject to a “narrow exception” in § 337.05 that saves an otherwise invalid indemnity agreement where the subcontractor-indemnitor agrees to provide insurance coverage for the contractor-indemnitee’s negligence. Because a jury determined that the underlying damage was not due to Bolduc’s negligence, the Court found that any agreement by Bolduc to indemnify ECI for damage caused by anyone else’s negligence would be invalid unless the indemnity agreement was accompanied by a coextensive insurance agreement. The Court reasoned that, because the AI coverage had already been held inapplicable, there was no coextensive insurance agreement. After the determination that there was no coextensive insurance agreement, ECI last sought refuge in a sub-part of § 337.05, which states that a would-be indemnitee has a cause of action against the subcontractor-indemnitor for breach of an agreement to provide insurance. The Supreme Court held that ECI waived its argument that Bolduc breached its agreement to provide insurance for other’s negligence. On this last issue – Bolduc’s failure to provide insurance required by the construction contract – the Court gave no guidance, but rested on its determination that ECI waived the argument.

Overall, the Minnesota Supreme Court’s decision is most noteworthy for its narrow interpretation of the coverage grant in an AI endorsement which imposed a negligence requirement not present in the wording of the endorsement. By doing so, the Court found that damage caused by a subcontractor’s non-negligent acts or omissions does not trigger the AI coverage, regardless of the fact that the AI endorsement does not use the term negligence. The decision is also noteworthy because it shows the Court will invalidate an insured’s indemnity agreement if it does not comply with Minnesota’s statutes regulating indemnity agreements. Minn. Stat. § 337.01, et seq.