WAIVERS OF SUBROGATION

SHOULD YOU BE WORRIED?

Your bid is accepted, and you want the work, but the owner refuses to negotiate the terms of the contract, which includes a waiver of subrogation provision — so what are the risks if you agree to waive your subrogation rights?

For years construction contracts have contained provisions requiring subcontractors to waive their subrogation rights. In fact, such provisions have now become almost universal. Contractors have generally agreed to waive these rights as a matter of course, and have done so without having to worry about how the waiver may affect their insurance coverage under their liability policies. However, a recent decision of the Pennsylvania Superior Court suggests that contractors need to pay more attention to the subrogation waiver demands being made.

Before we can understand the implications, we must understand the concepts. What is subrogation? Subrogation is an equitable doctrine involving the right of legal substitution. Simply put in English, after an insurer has paid out on a claim, the doctrine of subrogation allows the insurer to attempt to recover the monies paid on the claim from those who are actually liable for the loss. By way of example, your home owner’s insurance carrier has to pay your $10,000 water damage claim caused by leaks from your newly installed roof. Pursuant to the terms of the homeowner’s policy, the insurance carrier has a right to bring a subrogation action, in your name, against the roofer to recover that $10,000.

The goal of subrogation is to place the burden of the loss on the person or business whose negligent actions led to the loss. The insurer essentially steps into the shoes of its insured, and brings claim(s) against negligent third parties to recover the money it paid on the claim. For an insurer, subrogation is the method by which it can seek to recover monies paid on a claim.

What is the practical effect of agreeing to a waiver of subrogation? It bars your insurance carrier from seeking to recover the amounts that it paid on a claim from the person or businesses ultimately responsible for the loss. Up until the

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You just opened today’s mail and discovered a notice that an employee has filed a charge for sexual discrimination against your business with the state civil rights agency. How could this happen? You thought you had protected yourself from such claims by adopting a sexual harassment policy and complaint procedures, and by requiring sexual harassment training. Unfortunately, statistics show that employees today are no more likely to report harassment to their employers than they were fifteen years ago (when few employers had sexual harassment policies or training). 

As a result, an employer’s first notice of a harassment claim often comes through the mail, in the form of a charge of discrimination filed by the employee with the federal and/or state civil rights agency.

These statistics indicate that employers need to do a better job of preventing sexual harassment, and should re-evaluate their existing policies and training. The following provides an overview of issues of which employers should be aware and steps that employers can take to bolster their policies and training:

1. **Review Your Existing Policies.** The law changes over time, and policies prohibiting unlawful harassment and discrimination should be reviewed and updated periodically – about every two years. Also, make sure your policy includes an express non-retaliation provision; the absence of this provision may take away your right to argue that you have an effective policy and claims procedure.

2. **Redistribute Your Policies Each Year.** Even though the policies prohibiting unlawful harassment and discrimination are contained in the company handbook and are given to employees, employers still should distribute the latest versions of the policies each year to all employees. They serve as a reminder to existing employees, and inform new employees who joined after the last distribution.

3. **Active Supervision.** The presence of supervisors and managers serve a deterrent effect. Supervisors and management are most effective, aware and available when they are actively supervising, listening and observing, instead of staying in their offices with the door closed.

4. **Computers in the Workplace.** Instruct employees with computer access about inappropriate use of the computer and other electronic devices. Internet access increases the likelihood that outside individuals will send harass-
Q. I own several rental properties and have been hearing about rental property inspection ordinances ("RPIOs") that are being enacted in municipalities across the country. What are RPIOs and should I be concerned about them?

RPIOs are laws that provide for the periodic registration and inspection of rental properties by municipal codes officials. RPIOs generally require that landlords do the following: 1) register their rental properties with the municipality; 2) submit their properties to inspections by the municipality’s codes enforcement personnel; 3) obtain certificates or licenses in order to operate their rental units; and 4) pay fees to cover the municipality’s costs in administering the RPIOs and the costs of the inspections. For landlords who own many units, these fees can be substantial.

In some cases, the requirements of the RPIOs must be met on an annual basis. In others, landlords are faced with them less frequently, such as bi-annually or only when there is tenant turnover. Many of the RPIOs currently in effect (or proposed) also provide that if a rental property does not pass the inspection, the municipality may terminate the landlord’s right to rent the property until the landlord has remediated all problems. Some of the RPIOs also provide that landlords whose properties have failed the inspections must pay re-inspection fees, which in some cases may be substantial. Nationwide, the courts have upheld RPIOs as being constitutional and legal.

Q. How do I know if my properties are subject to RPIOs, and what should I do if they are?

Currently, dozens of municipalities in Pennsylvania have RPIOs already in effect and more are currently considering enacting them. Pennsylvania is not alone in this; municipalities in other states also either have or are in the process of enacting RPIOs. Landlords should check with their municipal officials to determine if their properties are subject to RPIOs.

It is likely that most landlords will be affected by RPIOs at some point in the future. While there is probably no way to avoid this challenge altogether, there are several things landlords can do to ease the pain:

Make sure properties are up to code Code violations could result in lost rental income and additional costs for re-inspections.

Maintain good relationships with codes inspectors Landlords who have good working relationships with the codes personnel may avoid problems, even in the face of minor code violations, while those who do not get along with the inspectors can likely expect no accommodations or courtesies. Use common sense in your interaction with the inspectors and be respectful, polite, and professional.

Amend leases Under most scenarios, it is the tenant who refuses entry to an inspector. However, it is the landlord who may pay the price if an inspector must take legal action to obtain an order or a warrant to gain entry. Leases should provide that the landlord, or his designees, may enter the property at any reasonable time, with notice to the tenant, for the purpose of conducting inspections. If the tenant refuses entry to an inspector, the landlord will then have the ability to grant access to the inspector.

Work with municipal officials If landlords find that the municipalities in which they own properties are considering enacting RPIOs, landlords can offer to assist the municipalities in drafting them. This is not an uncommon practice; in many instances, residents of municipalities who will be affected by proposed legislation participate in the drafting of it. By doing this, landlords can make known to the municipal officials the issues that are important to landlords, and may be able to make sure that the RPIO is narrowly tailored so that it addresses the municipality’s legitimate concerns while at the same time being the least offensive to landlords’ rights to own rental properties and their goals of maximizing the return on their investment.

-- Steven M. Williams, Esquire
recent court decision, this waiver had no practical impact on your insurance coverage, other than to possibly affect your future premiums in the event that your insurer pays a claim and then was unable to bring a subrogation action to recover the monies paid on the claim. This was because Pennsylvania courts had long held that Pennsylvania residents were permitted to waive their insurer’s right to subrogate without first giving the insurer notice that they intend to do so. Even without notice, the insured’s actions in waiving its right to subrogate were binding upon its insurer.

Yet, a recent decision may change the way insurers do business in Pennsylvania. In Universal Underwriters Ins. Co. v. A. Richard Kacin, Inc., the Superior Court of Pennsylvania reaffirmed that an insured can waive its insurer’s right of subrogation without first notifying its insurer. However, in its opinion, the court advised insurers doing business in Pennsylvania that they too can take steps to protect their interests in such a situation. In its opinion, the court implied that insurance carriers doing business in Pennsylvania should respond to the risk of an insured waiving its right to subrogation by “inserting an exclusion into their policies that permits the insurer to deny coverage if an insured waives the insurer’s subrogation rights...”

What does the court’s decision mean in the long term? Insurance carriers looking to recover the costs of claims through subrogation actions will take a cue from the court and seek to revise their insurance policies to include a provision that permits the insurer to deny coverage if an insured waives the insurer’s subrogation rights. Accordingly, it is important that you talk to your insurance broker and review your insurance policies to make sure that you are permitted to waive your carrier’s right to subrogate without jeopardizing your coverage.

-- Alexander F. Barth, Esquire

WHAT’S NEW AT THE FIRM?

Cohen Seglias would like to welcome Nella Bloom to its Business Practice Group. Prior to joining the firm, Nella served as the judicial law clerk for the Honorable Howland W. Abramson of the Court of Common Pleas of Philadelphia County. Welcome Nella!

Cohen Seglias has recently launched a series of new seminars to help its clients with their business and legal needs. In October 2007, the Construction Group and the Business Practice Group gave the first of several seminars on indemnity and insurance. Ed Seglias, Jonathan Cass and Alexander Barth spoke to a group of business owners at the Marriott Hotel in Conshohocken, Pennsylvania about negotiating indemnity agreements; the pitfalls of waiving the immunities provided by the Worker’s Compensation Act; and identifying important insurance coverage issues in construction contracts. Additional seminars on insurance and indemnity issues will be provided throughout 2008. In February 2008, the Labor and Employment Group will begin a series on sexual harassment in the workplace. The seminars will provide valuable information to management regarding how to deal with this difficult issue. Please contact our Marketing Director, Aria Vaida, if you are interested in attending any of the seminars offered by Cohen Seglias.

Finally, our annual toy drive is under way and we ask for your help. We are currently collecting new, unwrapped toys that will be donated to the Support Center for Child Advocates in Philadelphia and the Allegheny County Department of Human Services, Office of Children, Youth and Families in Pittsburgh. Collectively, these organizations have more than 700 children in their care. With your help, we hope to make this holiday season a joyous one for each and every child.

For more details, please contact Robbie Bloom or Aria Vaida at (215) 564-1700 or Lisa Wampler at (412) 434-5530.

-- Edward T. DeLisle, Esquire
Have you ever been on a project where either you or another contractor encountered a hidden condition such as solid rock or an underground spring? If you have, then you know that these unforeseen site conditions can cause huge expenses and delays. Who should bear the unexpected costs associated with unforeseen site conditions – the contractor or the owner?

The answer to this question is usually found in specific terms of the contract. However, conflicting provisions found in many construction contracts can make finding such an answer difficult. Construction contracts often contain provisions that are commonly referred to as “site investigation” clauses, which require contractors to examine the site before submitting a bid, and often state that the submission of a bid is proof that the contractor has made such an examination. Additionally, these provisions generally provide that any subsurface information provided by the owner is for ‘information only’ and that the contractor cannot rely on this information. On the other hand, many of these same construction contracts also include “differing site conditions” clauses, which generally require that an equitable adjustment to the contract be made in the event that a contractor encounters conditions that are either different than those indicated in the contract documents or different from those conditions ordinarily encountered or inherent in the work.

The interpretation of these competing provisions was recently at the center of a dispute before the Pennsylvania Commonwealth Court. In the matter of Department of General Services v. Pittsburgh Building Company, PBC was seeking to recover damages it had incurred after encountering unforeseen conditions on a project. During its cut and fill operations, PBC discovered soil containing excessive moisture. DGS, therefore, suspended the project, waiting for warmer weather to allow the soil to be air dried to meet the specifications. When PBC re-commenced excavation operations, attempts to aerate the soil failed to achieve compaction requirements despite the warmer weather. It was unable to either aerate the soil or use soil from other areas of the site. As a result, PBC was forced to import soil despite DGS’s representation in the specifications that all soils on site were appropriate for fill. Eventually, PBC completed its work using acceptable fill imported from offsite. In total, the unforeseen soil conditions delayed the project approximately eleven months.

When PBC made a claim for the extra costs it incurred as a result of the delay, DGS took the position that it would grant PBC an extension of time, but disclaimed any responsibility for additional costs resulting from the delay. In the court battle that followed, DGS argued that the contract documents did not make any affirmative representations to PBC, and that the general conditions contained a “site investigation” clause which placed all risks in excavating on the contractor and, the contractor was not to rely on any subsurface information obtained from DGS. PBC, on the other hand, relied on the “differing site conditions clause” in the general conditions, which provided that the contract sum would be equitably adjusted should unusual hidden conditions be encountered.

In finding in favor of PBC, the court relied on three different legal theories. The first two theories involved DGS’s failure to disclose an internal memorandum which indicated that the site would be unsuitable for earthwork in winter and early spring. More significantly in the third theory, the court found that, taken together, the “site investigations” and “differing site conditions” clauses of the contract were ambiguous. Relying on a fundamental tenet of contract law which provides that ambiguities in a contract must be construed against the drafter of the contract, DGS in this case, the court ruled in favor of PBC and found that PBC was entitled to an equitable adjustment to the contract.

While the Commonwealth Court’s decision will not stop owners from relying on “site investigation” clauses, it certainly will make it more difficult for them to prevail on such arguments. Moreover, this case highlights the importance of understanding each provision of your contract and their implications.

-- Robert G. Ruggieri, Esquire
Welcome to the Fall 2007 Edition of Construction In Brief. During the past year, we have seen many changes in construction law. In this edition, we continue to analyze these changes in articles addressing recent court decisions regarding waiver of subrogation clauses and unforeseen site conditions. In addition, we discuss rental property inspection ordinances which many municipalities have recently enacted or are currently considering.

As always, we welcome you to submit suggestions for future articles that may be of interest to you, either by regular mail or e-mail at: jtreiman@cohenseglias.com. Remember, if you have a specific legal concern, we recommend that you consult with counsel so that you may receive the best advice. See you next issue.

-- Janet L. Treiman, Esquire
Editor, Construction In Brief

Watch for upcoming “Client Alerts” regarding the scheduling of a public hearing for the proposed new prompt payment ordinance for projects for the City of Philadelphia.

Questions regarding a specific legal matter? We recommend that you speak with a CohenSeglias attorney:

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Words From Our Editor

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• What’s New at the Firm
• and more!

CLIENT ALERT

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