

Client Alert

A report
for clients
and friends
of the firm June 2005

Second Circuit Finds Insurance Waivers of Subrogation Enforceable Against Claims of Gross Negligence

Last week, in an important public policy decision, *St. Paul Fire & Marine Ins. Co. v. Universal Builders Supply, Inc.*, ___ F.3d ___, 2005 WL 1220473 (2d Cir. May 24, 2005), the Second Circuit held that waivers of subrogation in an insurance contract bar an insurance company from asserting claims of gross negligence in order to recover amounts paid under that contract. The Circuit rejected the argument that waivers of subrogation were analogous to unlawful exculpatory clauses in contracts that would leave an injured party without recovery for its damages. Rather, the Court held that waivers of subrogation do not violate any public policy, even where gross negligence is alleged.

Background Facts

The case stems from a 1998 incident at the construction site of Four Times Square (now known as the Conde Nast Building) in New York City, a property owned by the Durst Organization. Proskauer Rose LLP represented Universal Builders Supply, Inc., the contractor responsible for constructing and erecting the scaffolding and hoist tower at the site.

After the temporary scaffold/hoist structure at the construction site collapsed on July 21, 1998, St. Paul paid approximately \$19 million to Durst to satisfy claims for property loss filed under a builder's risk policy it had issued to Durst. St. Paul, as subrogee of Durst, then brought this action against Universal Builders to recover for the amounts St. Paul had paid to Durst. St. Paul's complaint alleged that our client, Universal Builders, was liable on various grounds,

including gross negligence, in connection with the construction, installation, and maintenance of the scaffolding.

The Second Circuit Opinion

Three federal district courts had previously supported the position urged by St. Paul - that New York public policy forbids a party to escape liability, through contractual exculpatory clauses, for damages caused by gross negligence. The Second Circuit, however, affirmed a decision by the Honorable Kimba Wood of the Southern District of New York in favor of Universal Builders. The Court held that the public policy of the state of New York does not prohibit waivers of subrogation with respect to gross negligence claims where the parties to a construction contract have agreed to insure such losses as part of their risk allocation agreement and where the injured party is not deprived of compensation for its loss.

Although the New York Court of Appeals had not addressed the precise question at issue, the Circuit, citing New York Court of Appeals decisions, noted that a party may obtain insurance as a protection against its own gross negligence. Moreover, the Second Circuit distinguished between the exculpatory clauses relied upon by St. Paul and indemnity contracts that simply shift the source of compensation without restricting the injured party's ability to recover. The Circuit ruled that the insurance contract and waiver of subrogation in this case, which simply required one of the parties to obtain insurance for all of the parties involved in the construction project, thereby shifting the risk of damage to the insurance company, fell into the latter category and were not contrary to public policy.

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