

Potential Coverage Gap Created by *Kotecki* Waivers

In one of the most important insurance coverage decisions of 2007, the Illinois Supreme Court ruled in *Virginia Surety Co., Inc v. Northern Ins. Co. of New York* that an employer who waives the cap on contribution recognized by *Kotecki v. Cyclops Welding Corp.* may not be covered by a Commercial General Liability (CGL) policy for liabilities associated with that waiver.

In most cases, Illinois law limits an employee's right to recover against an employer for work related injuries to benefits paid under the Workers' Compensation Act. However, the injured employee can (and often does) file a civil lawsuit against other responsible parties, who then, in turn, seek contribution from the employer. This may occur in a situation, for example, when a subcontractor's employee gets injured on a jobsite managed and controlled by a general contractor. In those instances, the law generally caps the employer's liability for the contribution claim at the amount of the employer's workers' compensation liability. That limitation is known as the employer's "*Kotecki*" protection.

However, there is a provision common to many construction contracts which requires subcontractors to indemnify the general contractor for losses arising from personal injuries or property damage. If the indemnification provision is worded correctly (and most are) it can waive the subcontractor's/employer's *Kotecki* protection.

"In most cases, Illinois law limits an employee's right to recover against an employer for work related injuries to benefits paid under the Workers' Compensation Act."

Before *Virginia Surety*, the Illinois courts held that a subcontractor's CGL policy usually provided coverage for losses in excess of the "*Kotecki*" protection. But, business as usual ended when the Illinois Supreme Court held that if the language in the CGL insurance policy, and the indemnification language in the construction contract, resemble those at issue in *Virginia Surety*, a CGL insurer is not required to defend or indemnify an insured who is sued for contribution and who waived its *Kotecki* protection. Additionally, in such situations, CGL insurers may reject targeted tenders of defense and indemnity.

Ultimately, *Virginia Surety* will have a significant impact on both the construction and insurance industries because it will be more difficult to draft construction contracts to circumvent the Court's ruling and in so doing, provide full coverage for construction injury losses. Some may attempt to recast the relationship between contractors and subcontractors in *Kotecki* waiver situations as one of contribution rather than indemnity (i.e. a "contribution" provision in a contract rather than the typical "indemnity" clause), but there is language in *Virginia Surety* that appears to obviate such efforts. In any case,

To the fullest extent permitted by law, the Subcontractor WAIVES ANY RIGHT OF CONTRIBUTION AGAINST AND shall indemnify and hold harmless [General Contractor] from and against claims, damages, losses and expenses arising out of or resulting from performance of the Subcontractor's work under this Subcontract, provided that such claim, damage, loss or expense is attributable to bodily injury, sickness, disease or death which is caused in whole or in part by negligent acts or omissions of the Subcontractor.

Example of a contractual *Kotecki* waiver

subcontractors should be wary of contractually waiving their *Kotecki* protection because they will likely encounter problems finding coverage under their current CGL policies.

Source: *Tribler Orpett & Meyer, P.C.*

This article is intended as an overview and should not be viewed as legal advice. Please consult with your attorney if you have any questions.