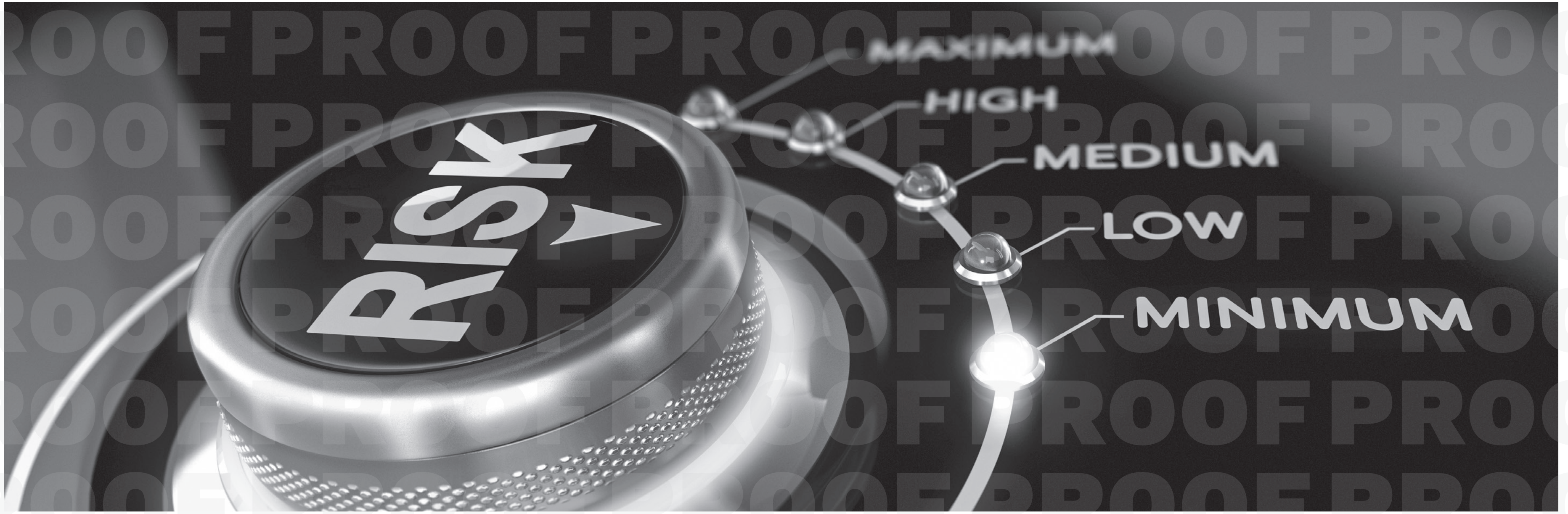
VOLUME 34 NUMBER 4 JANUARY 27, 2020

Missouri Lawyers WEEKLY

www.molawyersweekly.com

PROOF

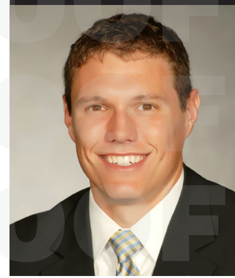


Adventures in Contracting: Is Gross Negligence Covered?

■ Commentary

By Erin Fishman

■ Commentary



By Jason R. Scott

One of the main goals of contracting — whether personally or commercially — is predictability. You want to understand what you are giving up and what you are getting in exchange. For many of our service-based clients, a good portion of that consideration is the allocation of risk, and in particular, which side bears the risk in the event of loss or damage to person or property.

The tools available to help predict and allocate risk contractually range from exculpatory provisions, limitation of damages provisions, waiver of consequential damages provisions, insurance and indemnity allocation provisions, and waivers of subrogation. But many of these tools are ineffective against claims of gross negligence or willful or wanton misconduct. A bit of creative pleading can allow an otherwise-barred claim to move past the pleading stage into discovery, summary judgment and trial, where the bulk of litigation expense lies. This commentary focuses on the one tool that can be effective even against claims of gross negligence: waiver of subrogation provision.

Jurisdictions differ as to whether public policy favors enforcement of waiver of subrogation provisions against gross negligence claims. While the majority of jurisdictions enforce these waivers, a consistent minority do not. Missouri courts and the 8th U.S. Circuit Court of Appeals have not specifically addressed whether a waiver of subrogation precludes a gross-negligence claim, but relevant tort law suggests that Missouri is likely to side with the majority of jurisdictions and enforce these waivers against claims of gross negligence.

The Majority Rule

The majority of courts across the country that have addressed the issue hold that waivers of subrogation extend to claims arising out of alleged gross negligence. Courts in Maine, New York, Nebraska, Vermont, California, Connecticut and Massachusetts, for example, consistently uphold waivers of subrogation in these cases. Most recently, in *United National Insurance Company v. Peninsula Roofing*, the 4th Circuit enforced a waiver of subrogation against a gross-negligence claim. No. 18-1427, 2019 WL 2524253 (4th Cir. 2019). Applying Maryland law, the 4th Circuit distinguished waivers of subrogation from exculpatory clauses, holding that with exculpatory clauses, "the parties expressly . . . agree in advance that the defendant is under no obligation of care for the benefit of the plaintiff, and shall not be liable for the consequences of conduct which would otherwise be negligent." *Id*, at *4, (citing *BJ's Wholesale Club, Inc. v. Rosen*, 435 Md. 714, 80 A.3d 345, 351 (2013). Because they have the effect of "shield[ing]" a party from liability for its reckless or wanton acts, Maryland courts refuse to enforce exculpatory provisions against allegations of gross negligence. *Id.* (citing *Wolf v. Ford*, 333 Md. 525 (1994)). By contrast, waivers of subrogation "specifically contemplate[] that the injured party will be able to recover for its losses" by shifting the risk of loss from the injured party to the party's insurance carrier. *Id.* at *4. Thus, even in the face of gross-negligence claims, the injured party is not left uncompensated for its losses when an insurer is precluded from pursuing a subrogation action. While the insurer will not be reimbursed, the injured party is made whole. As the Supreme Judicial Court of Maine stated in *Reliance National Indemnity*, "there is no risk that an injured party will be left uncompensated, and it is irrelevant to the injured party whether it is compensated by the grossly negligent party or an insurer." 868 A.2d at 226.

The 4th Circuit in *National Insurance Company* recognized that enforcing subrogation waivers against claims of gross negligence promotes important public policy. Waivers of subrogation provide certainty, deter litigation and allow injured parties quick resolution of claims. *See id.* ("Making subrogation waivers . . . unenforceable against claims of gross negligence would undercut one of the well-recognized purposes of such waivers: to reduce litigation over insured losses sustained during construction projects.") Put another way, a subrogation waiver "substitutes the protection of insurance for the uncertain and expensive protection of liability litigation." *TX. C.C. Inc. v. Wilson/Barnes Gen. Contractors Inc.*, 233 S.W.3d 562, 567-68 (Tex. App. 2007). Such efficiencies are particularly important in construction contracts where litigation can cause significant delay in project completion. Furthermore, sophisticated commercial parties should be free to allocate risk to insurance companies, which are paid large sums of money to assume that risk. Without waivers of subrogation, a subrogated insurer receives a windfall because it was paid premiums but did not truly have to cover the loss. Courts following the majority rule support similar policy considerations. *See St. Paul Fire & Marine Ins. Co.*, 317 F.Supp.2d at 341; *see also Reliance National Indem.*, 868 A.2d at 226. These jurisdictions also acknowledge how easily an insurance company could vitiate the subrogation waiver simply by alleging gross negligence. *See Behr*, 787 A.2d at 504.

The Minority Rule

A few jurisdictions have negated waivers of subrogation against allegations of gross negligence. Most recently, the Michigan Court of Appeals held that while "a waiver of subrogation clause bars [] claims . . . [other than] gross negligence . . . a party may not, by contract, protect itself from liability for gross negligence or willful or wanton misconduct." *Lexington Ins. Co. v. Alan Grp.*, 2016 WL 4203610 at *3 (Mich. Ct. App. Aug. 9, 2016) (unpublished). Similarly, courts in Georgia, Kansas and Indiana have held that waivers of subrogation are unenforceable against gross-negligence claims. These jurisdictions equate waivers of subrogation with exculpatory clauses and characterize both as provisions which permit a party to excuse its own liability for intentional harms and gross negligence.

Missouri

The 8th Circuit and Missouri courts have declined to address the validity of subrogation waivers against claims of gross negligence. However, a review of relevant case law discussing the ability to contract for insurance to cover gross negligence or willful or wanton misconduct provides some indication of how Missouri courts will treat this issue.

First, while Missouri courts have not yet ruled on whether individuals are permitted to insure against their own grossly negligent conduct, in limited circumstances, individuals may obtain insurance coverage for willful acts, at least where no personal injuries are involved. *See, e.g., Colson v. Lloyd's of London*, 435 S.W.2d 42, 47 (Mo. Ct. App. 1968); *Mo. Public Entity Risk Mgmt. Fund v. Investors Ins. Co. of Am.*, 451 F.3d 925, 929 (8th Cir. 2006) (applying Missouri law). Also, Missouri courts do not recognize "gross negligence" separate and apart from ordinary negligence. *See Milligan v. Chesterfield Village GP LLC*, 239 S.W.3d 613, 618 n.5 (Mo. Ct. App. 2007) (noting that [Missouri's] general tort law does not recognize degrees of negligence). These two well-established Missouri principles suggest that grossly negligent conduct is likely insurable. If willful conduct receives insurance, less culpable negligent conduct may merit protection as well.

Additionally, contracting parties in Missouri are free to negotiate the terms of insurance contracts. As long as the terms do not violate public policy, "an insured and an insurer are free to define and limit coverage by their agreement." *Buehne v. State Far Mut. Auto. Ins. Co.*, 232 S.W.3d 603, 606 (Mo. Ct. App. 2007); *see also Ullrich v. Owners Insurance Company*, 2013 WL 2111667 (W.D. Mo). In that light, Missouri courts honor waivers of subrogation. *See Netherlands Ins. Co. v Cellar Advisors LLC.*, 2019 WL 296536, at *4 (E.D. Mo. 2019) ("Under Missouri law, 'contract provisions waiving subrogation rights are valid and enforceable.'") (quoting *Messner v. Am. Union Ins. Co.*, 119 S.W.3d 644,649 (Mo. Ct. App. 2003). Similar to other jurisdictions that favor subrogation waivers, Missouri courts endorse the public policies achieved by such waivers. *See RLI Ins. Co. v. Southern Union Co.*, 341 S.W.3d 821, 830-31 (noting that a waiver of subrogation is a mechanism for reducing litigation). Importantly, no Missouri case explicitly characterizes a subrogation waiver as an exculpatory clause.

This distinction, coupled with Missouri's refusal to recognize gross negligence as separate from ordinary negligence and the state's willingness to permit individuals to obtain insurance coverage for willful acts, heavily suggests that Missouri will enforce waivers of subrogation against claims of gross negligence.

Jason R. Scott is a partner at Shook, Hardy & Bacon. He advises clients nationally on risk-mitigation techniques to avoid or minimize litigation.

Erin Fishman is an associate at Shook, Hardy & Bacon. She defends Fortune 500 companies sued for product and premises liability.

Reprinted with permission from Missouri Lawyers Media, 319 North Fourth Street, Fifth Floor, St. Louis, MO 63102. © 2019