Insurance Company Waived Claim to Recover $7,990,000 from Owner's Contractor

by

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The Western District of Missouri recently denied the subrogation claim of an owner's insurance company for $7,990,000 against one of the owner's contractors. The court decided that the owner waived its claim by virtue of contracts it had with other contractors. The case is *RLI Insurance Company v. Southern Union Co. d/b/a Missouri Gas Energy*, 341 S.W.3d 821 (W.D. Mo. 2011).

The contracts that contained the waiver were industry standard form contracts prepared by the American Institute of Architects (AIA). The contract between the parties to this dispute, however, did not have any such waiver provision and it did not incorporate any of the contracts that contained the waiver provision.

The lawsuit was between the owner (Triumph Foods LLC) and Triumph's contractor, MGE. Triumph assigned its claim on appeal to RLI, Triumph's builder's risk insurer.

The Western District found that MGE was a third-party beneficiary to the contracts that contained the waiver. Thus, MGE was covered even though it was not a direct party to the contract.

A third-party beneficiary is one for whose benefit a promise is made in a contract but who is not directly a party to that contract. A third-party beneficiary can in fact enjoy the rights and privileges provided in a contract that it did not sign. This holds true even though the third-party beneficiary is not specifically identified by name in the contract.

The construction involved a hog processing plant in St. Joseph, Missouri that Triumph owned. A natural gas explosion destroyed part of the plant during construction.

Triumph separately contracted with MGE to transport natural gas to the plant during initial construction. Triumph alleged that MGE caused the explosion.

RLI paid to Triumph $7,990,000 to reconstruct the plant as a result of the gas explosion. RLI sought to recover this payment from MGE on a claim of subrogation.

Subrogation occurs when the insurance company (after paying a claim) files its own claim in the name of its insured (in this case Triumph) to recover for payments it made under the insurance policy.

Triumph used AIA's A101/CMa form of contract to enter into several separate contracts with contractors for various portions of construction work at the plant. Each AIA contract incorporated a separate set of general conditions. The general conditions contained a waiver of subrogation provision in Paragraph 11.3.7, which provided that the owner and contractor waived all rights against each other as well as the owner's other contractors for damages caused by fire or other perils to the extent covered by property insurance.

Paragraph 6.1.1 of the general conditions addressed the owner's right to perform construction with its own forces or to award contracts to others without using a construction manager. In this case, Triumph separately contracted with MGE.

The MGE contract did not use the AIA contract or the general conditions and did not provide for a construction manager. The MGE contract did not contain a waiver of subrogation provision or even mention subrogation. The MGE contract, however, did include an integration clause which is commonly found in construction contracts. This clause is designed to prevent one party to the contract from claiming an agreement with the other party that is at variance with the written contract.

The trial court entered summary judgment in favor of MGE, finding that Triumph could not maintain through its insurance company a subrogation claim against MGE.

On appeal RLI argued that the MGE contract exclusively defined the relationship between MGE and Triumph. This contract did not include a waiver of subrogation and thus, according to RLI, there was no prohibition from pursuing a subrogation claim.

The Western District noted that generally speaking, a written contract, especially one containing an integration clause, is the "final memorial of the parties' agreement." It further reasoned, however, that by virtue of the AIA contracts, MGE was a third party beneficiary to those contracts.

While MGE had a separate contract with Triumph, Triumph's contracts with the other contractors precluded a subrogation action against any contractor. Since MGE was a contractor, this waiver included MGE.

The contract between Triumph and MGE did not expressly negate MGE's rights as a third party beneficiary. Thus, the subrogation claims against MGE had been waived by virtue of the AIA contracts.

The Western District concluded that MGE fell into the identifiable class of "Owner's Other Contractors and own forces" and thus MGE was an intended third-party beneficiary of the waiver of subrogation provision. Accordingly, MGE could enforce these terms against Triumph pursuant to a contract in which MGE was not specifically one of the parties.

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