



## Expert Commentary

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# Commercial Umbrellas and the Demand for Primary and Noncontributory

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The demand for primary and noncontributory has become a very common insurance requirement. Found in many business relationships—such as construction, real estate, and equipment leasing—the trend is to mandate not only additional insured status but also insist on coverage for the additional insured as "primary

and noncontributory."

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 Liability Insurance

Such insurance requirements often expect "primary and noncontributory" to apply to all liability policies on which the additional insured has been added—including any and all excess or umbrella policies. Because substantial confusion still surrounds not only the meaning but also the effect of these terms, revisiting intent in the context of its usage may be valuable.

## Primary Means First

The term "primary" is concerned with *the order* in which liability insurance policies respond when more than one liability policy *covers the same insured for the same claim*. In the context of "primary and noncontributory," primary typically means that the liability policy on which the additional insured has been added will respond first—before the liability policy the additional insured has purchased in its own name (as a named insured). In this context, however, *primary does not necessarily mean first dollar*.

Consider an umbrella policy—which by definition is not a primary policy—and the insurance requirement that the *total limit* of the insurance available to the additional insured is to be "primary and noncontributory." Often, these requirements allow the named insured to use any combination of commercial general liability (CGL) and umbrella insurance to provide the required limits for the additional insured (for example, the required limits may be \$5 million).

## Primary Does Not Mean First Dollar

Does the additional insured truly expect the umbrella, which the additional insured has permitted to fill out the \$5 million limit, to respond first dollar? Very likely not—otherwise, the additional insured would have required a \$5 million CGL policy and prohibited using an umbrella policy. A more reasonable interpretation of this requirement is that the umbrella would respond *excess* of the named insured's CGL policy—and, therefore, not first dollar. In this instance, primary means first—*first* in relation to the CGL policy purchased by the additional insured as a named insured.

And herein lies the crux of the problem. Most umbrella policies' other insurance condition simply states the umbrella policy will be excess of virtually any other liability policy, regardless of the other liability policy's other insurance condition. The only exception to this excess condition is if the other liability policy is written specifically to be excess of the umbrella—commonly referred to as a second layer or excess umbrella (for more on a typical umbrella other insurance condition, see "Commercial Umbrella—A Few Things To Consider," January 2016). More on the commercial umbrella problem below.

## Contribution

Contribution is an insurer's right to recovery after paying more than its share of a loss—but it is not subrogation (for more on primary and noncontributory, see also "Primary and Noncontributory," March 2012). The distinction between subrogation and contribution is not merely a technical nuance but an important practical difference. For example, at least one commentator has opined that a waiver of subrogation effectively prevents the insurer from seeking contribution. Such a notion seems to confuse the derivation of the insurer's rights. In fact, the conflation of contribution and subrogation is important enough in the context of determining the order of coverage between primary and excess policies that at least one court saw fit to describe the differences between subrogation and contribution.

It is also difficult to think of two legal concepts that have caused more confusion and headache for both courts and litigants than have contribution and subrogation. The right of subrogation is **purely derivative**. An insurer entitled to subrogation is in the same position as an assignee of the insured's claim, and succeeds only to the rights of the insured. Equitable contribution is entirely different. It is the right to recover, not from the party *primarily* liable for the loss, but from a *co-obligor who shares* such liability with the party seeking contribution. In the insurance context, the right to contribution arises when several insurers are obligated to indemnify or defend the same loss or claim, and one insurer has paid more than its share of the loss or defended the action without any participation by the others. Where multiple insurance carriers insure the same insured and cover the same risk, each insurer has **independent standing** to assert a cause of action against its coinsurers for equitable contribution when it has undertaken the defense or indemnification of the common insured.

[Emphasis in bold added.]

*Fireman's Fund Ins. Co. v. Maryland Cas. Co.*, 65 Cal. App. 4th 1279 (Cal. App. 1st Dist. July 31, 1998), pages 1291-1292

The key takeaway is that contribution is an insurer's *independent* right to seek recovery when it has paid more than its share of a loss and that the right of subrogation is *derived solely from the insured's right*. While there are similarities, contribution is entirely different from subrogation because each right originates from a different source. What should be evident is that an insurer's agreement to give up its right of subrogation has no effect on that insurer's independent right of contribution—and, therefore, the waiver of subrogation is not the equivalent of "noncontributory."

## The Commercial Umbrella Problem

### Not Follow Form

The too often held but mistaken belief that all umbrella policies are "follow form" and thus follow the "primary and noncontributory" wording of an underlying CGL policy fails to recognize the fundamental nature of the "primary and noncontributory" issue. Even umbrella policies that are actually "follow form" do

not follow the other insurance condition of the underlying policies—to do so would reduce the "follow form" umbrella to primary (first dollar) insurance.

For example, the most recent Insurance Services Office, Inc. (ISO), "Commercial Excess Liability Coverage Form" CX 00 01, April 2013 edition, insuring agreement clearly limits the "follow form":

The insurance provided under this Coverage Part will follow the same provisions, exclusions and limitations that are contained in the applicable "controlling underlying insurance", *unless otherwise directed by this insurance. To the extent such provisions differ or conflict, the provisions of this Coverage Part will apply.* [Emphasis added.]

Specifically, as respects the other insurance condition, the above ISO form includes a "stand alone" other insurance condition that does not follow the underlying insurance:

#### 8. Other Insurance

a. This insurance is excess over, and shall not contribute with any of the other insurance, whether primary, excess, contingent or on any other basis. This condition will not apply to insurance specifically written as excess over this Coverage Part.<sup>1</sup>

## Failure To Comply

The named insured's umbrella, which has included the additional insured, will usually respond *after* the CGL purchased by the additional insured<sup>2</sup> (i.e., the CGL policy on which the additional insured is the named insured). This is not the order of coverage contemplated by "primary and noncontributory." The order of coverage agreed upon is for the named insured's umbrella to respond *before* the CGL policy purchased in the name of the additional insured. In this instance, that order of coverage has not been met. As a general matter, agreeing to provide "primary and noncontributory" coverage to include an umbrella policy may result in failure to comply with the insurance requirements.

## Failure To Comply—Illustration

The tenant has agreed with the landlord to include the landlord as an additional insured on the tenant's liability policy with no less than a \$5 million limit. The landlord allows the tenant to provide the \$5 million of liability coverage in any combination of CGL and umbrella coverage. The tenant also agrees coverage for the landlord as an additional insured will be on a primary and noncontributory basis for the full limit of \$5 million.

The tenant purchases a \$1 million each occurrence CGL policy and a \$4 million umbrella policy—both policies include the landlord as an additional insured. The landlord also has its own CGL policy on which the landlord is a named insured with a \$1 million each occurrence limit and its own umbrella on which the landlord is a named insured with a \$5 million limit. The umbrella purchased by the tenant includes the usual

other insurance condition—the tenant's umbrella will be excess of all liability insurance available to any insured unless the liability insurance has been specifically obtained to be excess of the tenant's \$4 million umbrella.

A serious bodily injury claim occurs at the tenant's premises—triggering coverage for the landlord as an additional insured. The tenant's CGL provides coverage for the landlord as an additional insured—but the damages awarded exceed \$1 million—damages actually awarded are \$2.5 million. After the tenant's CGL insurer pays \$1 million of damages on behalf of the landlord, the tenant's umbrella insurer refuses to pay any damages on behalf of the landlord until the landlord's CGL has paid its \$1 million limit. This refusal by the tenant's umbrella insurer to respond next is based on the wording of the umbrella policy's other insurance condition—the tenant's umbrella insurer is excess to any other liability insurance—including the CGL policy on which the landlord is a named insured. The trouble begins.

After the landlord's CGL insurer pays the next \$1 million of damages on behalf of the named insured landlord, the tenant's umbrella insurer is willing to pay the balance of the damages of \$500,000 on behalf of the landlord as an additional insured. The tenant's umbrella insurer then seeks contribution from the landlord's umbrella insurer, seeking contribution by limits (the landlord's umbrella insurer should contribute 44 percent or 4/9th of the \$500,000 according to the tenant's umbrella insurer). With this resulting order of coverage, the landlord is likely to allege the tenant has failed to comply with its promise to provide coverage to the landlord as an additional insured on a "primary and noncontributory" basis.

## **Noncontributory—Other Insurance Condition CU 24 78 11 16 or CX 24 33 11 16**

In late 2016, ISO introduced two endorsements to be used with its "Commercial Umbrella Liability Form" (CU 00 01 04 13) and its "Commercial Excess Liability Form" (CX 00 01 04 13). Both endorsements are titled "Noncontributory—Other Insurance Condition" and are designated by the forms numbers listed above.

### **Half a Loaf**

As the title suggests, these endorsement address only contribution—*and not the order of coverage*. Despite replacing the umbrella and excess liability other insurance condition, both endorsements reiterate that the umbrella/excess insurance will be excess of all other liability insurance—unless that liability insurance is specifically written as excess.

The noncontributory endorsements state that if the named insured has so agreed in writing in a contract or agreement, the insurer will not seek contribution from a liability policy purchased by an additional insured as a named insured. As these are scheduled endorsements, the additional insured also must be scheduled.

The workings of these endorsements are yet to be determined, but the endorsements appear to apply only when the liability policy of the named insured (listing the additional insured) and the liability policy of the additional insured (as the named insured) are both excess to any other insurance. In other words, both policies are on the same level—the umbrella or excess policy listing the additional insured will not seek contribution from the umbrella or excess policy in which the additional insured is a named insured.

Using the failure to comply illustration above, the noncontributory endorsements would prevent the tenant's umbrella insurer from seeking contribution from the landlord's umbrella insurer for the \$500,000 paid on behalf of the landlord by the tenant's umbrella insurer.

## No Effect on the Order of Coverage

The ISO's "Noncontributory—Other Insurance Condition" endorsements have no apparent effect on the order of coverage. As above in the failure to comply illustration, the CGL purchased by the landlord in its own name (as a named insured) will still be required to respond *before* the umbrella insurance purchased by the tenant for the benefit of the landlord as an additional insured. As this is not the order of coverage generally understood as "primary and noncontributory," the ISO noncontributory endorsement does not appear to bring about compliance with the promise to include an umbrella policy as "primary and noncontributory."

## Conclusion

There are several major national insurers that offer umbrella policies that address both primary (who goes first) and noncontributory (no sharing), either within the policy form itself or by endorsement, if requested.

By way of example, here is wording from an insurer's umbrella other insurance condition:

However, if you specifically agree in a written contract or agreement that the insurance provided to any person or organization that qualifies as an insured under this insurance must apply on a primary basis, or a primary and noncontributory basis, then insurance provided under Coverage A is subject to the following provisions:

This insurance will apply before [primary or order of coverage] any "other insurance" that is available to such additional insured which covers that person or organization as a named insured, and we will not share [noncontributory] with that "other insurance," provided that the injury or damage for which coverage is sought is caused by an "event" that takes place or is committed subsequent to the signing of that contract or agreement by you.<sup>3</sup> [Brackets added.]

The above addresses both issues when promising to be "primary and noncontributory"—the order of coverage as well as giving up rights of contribution. Certainly, the above is not the only wording that would comply with the promise to be "primary and contributory," but appears to be clearly worded and understandable.

<sup>1</sup> CX 00 01, April 2013, page 4

<sup>2</sup> This presumes that the order of coverage will be determined by the policy wording and not wording extrinsic to the policy, such as an indemnity provision in a construction contract.

<sup>3</sup> Excess Follow-Form and Umbrella Liability Insurance EU 00 01 07 16 © 2016 The Travelers Indemnity Company. All Rights Reserved.

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