MEALEY'S™ LITIGATION REPORT

Construction Defects Insurance

Construction Defect Claims: A 2021 Update Part I

by
Thomas F. Segalla,
Michael T. Glascott,
Ashlyn M. Capote,
Adam R. Durst,
Sean P. Hvisdas
and
Samantha M. McDermott

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Commentary

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Thomas F. Segalla,
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[Editor's Note: Thomas F. Segalla, Michael T. Glascott, Ashlyn M. Capote and Adam R. Durst are partners and Sean P. Hvisdas and Samantha M. McDermott are associates at Goldberg Segalla LLP. Any commentary or opinions do not reflect the opinions of Goldberg Segalla LLP or LexisNexis®, Mealey Publications™. *Responses are welcome.]*

Introduction

Construction defect insurance coverage cases, especially in the liability context, are typically replete with analyses regarding whether the alleged damages were the result of an occurrence or whether any business risk exclusions preclude coverage. Many of the cases discussed below are no different, although the breadth of issues reminds us that the disputes are particular to the policy and facts at issue in any given case. Not only do the cases below include discussions about legal principals – such as whether the insured has adequately plead a bad faith claim - but also include an analysis of numerous policy provisions outside of those typically referred to as the business risk exclusions, such as the Continuous or Progressive Injury and Damage Exclusion, Professional Services Exclusion, and Mold Exclusion.

In the cases discussed below, we also see the interplay between determinations made in the underlying action and the impact that they have on the coverage issues. For example, in *Starr Surplus Lines Ins. Co. v. Cushing Hosp., LLC*, 527 F. Supp. 3d 1327 (W.D. Okla. 2021), the court made determinations regarding coverage based on the findings that were issued in an underlying arbitration decision. Conversely, courts are also at times constrained by the lack of findings in an underlying action. In *Barton v. Nationwide Mut. Fire Ins. Co.* 524 F. Supp. 3d 1219 (N.D. Ala. 2021), homeowners obtained a judgment against the insured and sought to collect the judgment from the insured's carrier, but the court concluded that the lack of itemized damages in the judgment resulted in an inability to determine which of the damages were covered by the Commercial General Liability (CGL) policy.

Both of these cases, along with various other construction defect insurance coverage decisions from the first half of 2021, are discussed below. The authors look forward to discussing the construction defect cases from the latter half of 2021 in Part II of this publication.

Alabama

Barton v. Nationwide Mut. Fire Ins. Co., 524 F. Supp. 3d 1219 (N.D. Ala. 2021).

Lack of Itemization in Arbitration Award

Homeowners obtained a $900,000 judgment against a contractor and then sought to collect that judgment from the general contractor's CGL insurer. Half of

the judgment was for faulty work and the other half was for emotional distress resulting from the faulty work. The majority of the court's analysis was related to the evidence of what the damages were, the cause of specific items of damage, and how much the cost to repair those items was. However, the court explained that it was difficult to discern how much of the $900,000 judgment was for covered damages because there were no findings in the underlying action in that regard. Because the motion for summary judgment in the underlying action had been unopposed by the contractor, the homeowners had essentially provided round figures for their damages instead of itemized damages.

The court explained that there were various potential policy provisions that impacted coverage, such as lack of occurrence, the Damage To Property Exclusion, and the Mold Exclusion. However, the court noted that some of the damages appeared to be the result of an occurrence. The court also noted that the subcontractor exception to the Damage To Property Exclusion appeared to apply to some items and that not all of the damages were barred by the Mold Exclusion. The court also explained that the claims against the contractor for wanton and intentional behavior were not covered. However, given the lack of itemization regarding the damages in the property damage action, the court could not discern how much of the judgment was covered. Because the homeowners had failed to provide the court with sufficient information to decide the issue, the court entered judgment for the insurer.

Arizona

Developers Sur. & Indem. Co. v. Coyote Creek Constr., No. CV-20-00914-PHX-SRB, 2021 U.S. Dist. LEXIS 94688 (D. Ariz. Jan. 11, 2021).

Conditions to Coverage Are Ripe to Litigate

The insured was hired by a homeowner to construct a residential home. Thereafter, the insured hired a subcontractor to install porcelain tile flooring at the project. The subcontractor began installing the flooring, but large cracks developed, after which the insured retained a new subcontractor to install the flooring. Despite the insured's continued efforts to repair the flooring, defects persisted, and the homeowners sued the insured for breach of contract, breach of express and implied warranties, breach of the covenant of good faith and fair dealing, unjust enrichment, and *res ipsa* negligence. The insured tendered the lawsuit to its general liability insurer, which agreed to defend under a reservation of rights.

The insurer thereafter commenced a declaratory judgment action against the insured seeking a declaration of no coverage for the claims and damages sought by the homeowners on the basis that, among other things, (1) there was no coverage due to defective workmanship not constituting "property damage" caused by an "occurrence," (2) because the claims were otherwise excluded under the policy, and (3) because the insured failed to comply with certain conditions of coverage. The insured filed a motion to dismiss the insurer's complaint on the basis that the court should not entertain the declaratory judgment action based on the factors set forth in *Brillhart v. Excess Ins. Co. of America*, 316 U.S. 291 (1942) and its progeny. The court, however, denied the motion as it pertains to determining whether the insured failed to comply with certain conditions of coverage (e.g., the requirement that the insured procure hold harmless agreements with its subcontractors), which it deemed ripe to litigate.

Practice Point: Courts need not abstain from determining coverage based on whether an insured complied with certain conditions of coverage in connection with an underlying suit alleging construction defects.

Tapestry on Cent. Condo. Ass'n v. Liberty Ins. Underwriters Ins., No. CV-19-01490-PHX-MTL, 2021 U.S. Dist. LEXIS 59924 (D. Ariz. Mar. 29, 2021).

Contractual Liability and Construction Defect Exclusions

The insured was a condominium association that was sued by a unit owner on the basis that the insured improperly placed a lien on the unit owner's units due to a dispute over unpaid assessments, parking spots, and alleged construction defects. The insured tendered the lawsuit to its liability insurer, which denied coverage on the basis that, among other things, the policy did not provide coverage for any "Construction Defect."

The insured commenced a lawsuit against its liability insurer, which was resolved when the insurer agreed to defend the insured for the duration of the unit owner's lawsuit.

The unit owner's lawsuit proceeded to trial, where the jury ruled that the insured breached the implied covenant of good faith and fair dealing and entered a judgment for more than $1.5 million. The insurer denied any obligation to indemnify the insured for the judgment pursuant to the Contractual Liability Exclusion applicable to "liability of any insured under any contract." The denial also relied upon the Construction Defect Exclusion.

The insured then filed a second declaratory judgment action against its insurer, asserting claims for breach of contract and bad faith.

On summary judgment motions, the court found that the Contractual Liability Exclusion applied to the judgment on its face, but that there was a question of fact as to whether it was properly communicated to the insured because that particular exclusion was not raised until after the judgment. As to the Construction Defect Exclusion, the court found that because the jury in the underlying action did not indicate its finding was based on construction defects at the condominium, a question of fact existed as to whether the exclusion applied.

Practice Point: Indemnity is determined based on the basis of an insured's liability, and if that basis is unclear, a question of fact may exist as to the application of certain coverage defenses, so long as those coverage defenses have not been waived.

Vasquez v. Ameriprise Ins. Co., No. 19-536-TUC-CKJ, 2021 U.S. Dist. LEXIS 63195 (D. Ariz. Mar. 30, 2021).

Exclusion for Loss Caused Directly or Indirectly by Defective Workmanship

The insured submitted a claim with its first-party property insurer when its polybutylene plumbing system ruptured, causing water damage to the insured's residence. The insured replaced the entire plumbing system, including portions that were not leaking. The insurer, however, denied coverage for the replacement costs. The insured acknowledged that the policy did not provide coverage for replacement of a defective system, but claimed it was entitled to coverage for the costs to access and remove the system, i.e., the "tear-out" coverage. The insured commenced suit against its insurer for such costs.

On summary judgment motions, the insurer argued that the insured's claim for "tear-out" coverage was barred by the policy's exclusion for defective/inadequate construction, design, and workmanship, since the tubing was, in fact, defective. The court agreed, finding the losses in this case, including the repair/replacement of the plumbing, water damage, and the necessary tear-out costs, were caused directly or indirectly by the defective piping.

California

Associated Indus. Ins. Co. v. Mt. Hawley Ins. Co., 3:20-cv-00507-H-DEB, 2021 U.S. Dist. LEXIS 93605 (S.D. Cal. May 12, 2021).

Breach of Contract Exclusion

The insured was retained to construct a building for an individual. After completion of the building, the individual sued the insured alleging the insured constructed the property in a defective manner, causing various forms of damage. The insured thereafter tendered the lawsuit to its liability insurer whose policy incepted in September 2005. That insurer denied coverage for the lawsuit pursuant to a Continuous or Progressive Injury and Damage Exclusion because its investigation determined that the insured's construction was completed in May 2005, months before the policy became effective. After the insurer's disclaimer of coverage, the individual amended his complaint in the underlying action to assert the insured's work was not complete until February 2006.

The insured's liability insurer that issued policies before September 2005 agreed to defend the insured in the underlying action and subsequently settled that action. The pre-September 2005 insurer thereafter commenced a suit against the post-September 2005 insurer for equitable contribution for its litigation and settlement costs in connection with the underlying action.

Though not raised in its initial denial letter, the post-September 2005 insurer moved for summary judgment on the basis that coverage was barred, in its entirety, pursuant to a Breach of Contract Exclusion that barred coverage for, *inter alia*, "'property damage' . . . arising directly or indirectly out of . . . Breach of express or implied contract." The court determined that each claim by the insured in the underlying action shared the same operative factual allegations: that the insured constructed the individual's property in

a defective matter, which is, at a minimum, incident to or connected with the individual's allegations that the insured breached its contract by constructing the building in a defective manner. As such the court found that coverage was barred under the post-September 2005 policies pursuant to this exclusion.
Practice Point: Even claims for negligent construction can constitute a claim that "arises out of" a breach of contract.

Guastello v. AIG Specialty Ins. Co., 61 Cal. App. 5th 97 (Cal. Ct. App. Feb. 19, 2021).

Expert Opinion on Continuous and Progressive Damages May Trigger Coverage

The insured was a subcontractor that built a retaining wall for a homeowner that collapsed years after it was completed, causing damage to a nearby residential lot. The homeowner sued the insured for negligently designing and constructing the retaining wall. The insured thereafter tendered the lawsuit to its liability insurer that issued the policy in effect when the retaining wall was built. The liability insurer denied coverage on the basis that the collapse and related property damage occurred six years after its policy period expired, and was therefore outside the scope of coverage. The homeowner took a default judgment against the insured and thereafter sued the insurer to enforce the default judgment.

On summary judgment motions in the coverage action, the insurer argued the homeowner's alleged damages occurred after its policy expired and were therefore outside the scope of coverage. The homeowner, however, argued that it alleged continuous and progressive destabilization and damage to the homeowner's lot and perimeter wall beginning before the relevant policy expired. The court found that the homeowner's argument, which was supported by an expert declaration, created an issue of fact as to the timing (or triggering) of the relevant insurance policy.
Practice Point: Absent exclusions to the contrary, when continuous or progressive damage first manifests itself during an insurer's policy period, the insurer may remain obligated to indemnify the insured for the entirety of the ensuing damage or injury.

United Specialty Ins. Co. v. Navigators Ins. Co., No. 20-cv-08620-JSW, 2021 U.S. Dist. LEXIS 193602 (N.D. Cal. May 3, 2021).

Notice-Prejudice Rule Applies to Sunset Provision

In 2009, the insured was retained to perform masonry work on a home construction project, including stonework on the home's exterior. After completion of the stonework, the home suffered water intrusion through the stonework exterior. The homeowner thereafter sued the general contractor, who filed a cross-complaint against the insured, asserting causes of action for breach of contract, negligence, and express indemnity. The insured tendered the lawsuit to its liability insurer that issued it a policy that expired in 2010. The insurer denied coverage due to the insured's failure to provide notice of the suit within the time proscribed by the policy's sunset clause, which required any claim or suit be reported to the insurer within three years after the expiration of the policy. The insured thereafter tendered the lawsuit to its liability insurer that issued it policies after 2010. The post-2010 insurer agreed to defend the insured under a reservation of rights. The post-2010 insurer thereafter resolved the case after a policy limit demand from the homeowner, and sued the pre-2010 insurer for, among other things, equitable contribution.

The pre-2010 insurer moved to dismiss the coverage action by the post-2010 insurer on the basis that the sunset provision vitiated coverage for the suit. The post-2010 insurer opposed the motion, asserting California's notice-prejudice rule, which requires an insurer disclaiming coverage based on late notice to show prejudice as a result of the insured's delay. The post-2010 insurer asserted that because the pre-2010 insurer failed to demonstrate prejudice, its motion to dismiss must be denied. The court agreed with the post-2010 insurer, finding the notice-prejudice rule applied to the policy's sunset provision, and as such, the post-2010 insurer properly stated a claim for which relief could be granted.

Lexington Ins. Co. v. QBE Specialty Ins. Co., No. 19-cv-05947-BLF, 2021 U.S. Dist. LEXIS 38631 (N.D. Cal. Feb. 25, 2021).

Statute of Limitations for Equitable Contribution

The insured, a concrete contractor, tendered an underlying construction defect lawsuit to one of its liability insurers, which agreed to defend the insured in connection with the lawsuit, and subsequently settled the lawsuit on the insured's behalf. The liability

insurer then commenced a declaratory judgment action against an insurer that issued a liability policy for the policy period following the first liability insurer's policies. The lawsuit sought certain declaratory relief and equitable contribution in connection with the costs expended in the defense and indemnification of their mutual insured in the lawsuit, alleging the second liability insurer's policy should contribute to the insured's defense and indemnification. The second liability insurer filed a motion for summary judgment, claiming the first liability insurer's claims were barred by the two-year statute of limitations under California Code of Civil Procedure § 339.

The court agreed with the second liability insurer, finding the two-year statute of limitations under California Code of Civil Procedure § 339 applied to both the first insurer's claim for declaratory relief and equitable contribution because the coverage action was commenced more than two years after the insured was dismissed with prejudice from the underlying action. Importantly, the court rejected the first insurer's argument that the statute should have been equitably tolled since the first insurer failed to provide any explanation as to why it waited so long to file its suit. As such, the court granted the second insurer's motion for summary judgment.

Practice Point: Equitable tolling of the statute of limitations may be invoked only when the plaintiff can show timely notice of the claim, lack of prejudice to the defendant, and reasonable and good faith conduct by the plaintiff.

Colorado

McCaffrey v. Great N. Ins. Co., No. 18-cv-1052-WJM-KLM, 2021 U.S. Dist. LEXIS 17098 (D. Colo. Jan. 29, 2021).

Scope of Appraisal Decision

In 2015, the insured began a home renovation project that included the installation of a pergola adjacent to its kitchen. During the construction, it was discovered there was potential water intrusion with a rotting wall framing and/or mold growth behind the stucco on the rear elevation of the home. As a result, the insured submitted the claim to its homeowner's insurer for the water damage. Upon completing its investigation, the insurer agreed to pay for costs to repair the interior water damage that ensued from construction defects in the home's original construction, as well as the costs to restore areas opened up during the intrusive investigation. The insurer also, however, invoked exclusions in the policy for "faulty planning, construction or maintenance," "the gradual or sudden loss exclusion," and a "fungi-mold" exclusion. The insured and insurer continued to disagree about the insurer's coverage position and the proper amount of plaintiff's loss, at which point the insurer issued a written demand to the insured for appraisal.

Each party retained its own appraiser, and then agreed to an umpire, who met with the appraisers and issued a decision addressing only the cost to repair the damage to the home's exterior caused by the intrusive testing. The insured thereafter commenced suit against the insurer, claiming the umpire improperly reduced the scope of the appraisal to the costs of repairs associated with the intrusive testing, ignoring that the scope of the appraisal also included the amount of loss for the damage to the home from the water damage claim originally reported. The court agreed, finding that even though coverage for the water damage claim was, at least in part, subject to a coverage dispute, the demand for the appraisal included a request for a determination of the actual cash value of the costs to bring the home to its pre-intrusive testing condition, which included the costs for the insured's water damage claim. As such, the court granted the insured's motion to vacate the appraisal decision.

Lodge at Mt. Vill. Owner Ass'n v. Eighteen Certain Underwriters of Lloyd's of London Subscribing to Policy Number N16NA04360, No. 20-cv-00380-CMA-SKC, 2021 U.S. Dist. LEXIS 58913 (D. Colo. Mar. 29, 2021).

Failure to Comply with Policy's Notice Requirements

The insured is a homeowners' association that sought coverage under certain insurance policies for the costs to repair faulty work performed on one of the buildings in the association by a construction contractor. Specifically, the insured first asserted a claim under a 2016 policy for the costs to repair the faulty workmanship, which was denied because the policy did not include coverage for faulty workmanship. The insured thereafter asserted a claim for alleged "ensuing damage" that happened after the faulty workmanship was completed, which the insurer also denied. After

the insurer's second denial, the insured commenced suit against the insurer alleging breach of contract under the 2016 policy and bad faith denial of its ensuing-damage claim.

During the course of the coverage litigation, the insurer made a motion to amend its complaint to add claims under its 2014 and 2015 policies as well, which also required the addition of those insurer-defendants that issued the policies for those periods. The court, however, denied the insured's motion on the basis that the insured failed to provide the new defendant-insurers with notice of its claims, and thus failed to comply with the notice conditions of those policies. The court held that notice of a loss is a condition precedent to trigger coverage under the policy, and thus amendment to add claims under these new policies, which the new defendant-insurers never previously received notice of, would render any amendment of the complaint futile.

Practice Point: In Colorado, notice of a claim under one policy will only serve as notice under another policy if (1) the same insurance carrier provided both policies and (2) the information contained in the notice is sufficient for both policies. Neither circumstance was present here.

HT Servs., LLC v. Western Heritage Ins. Co., 859 Fed. Appx. 260 (10th Cir. 2021).

Habitational New Construction Exclusion and Exclusion j(6)

The insured was a land developer that was developing a residential community. The homeowners' association for the residential community sued the insured for construction defects relating to a retaining wall and claimed resulting damages. The insured tendered the homeowners' complaint to its liability insurer, which denied coverage and refused to defend the insured in the lawsuit. The insured thereafter settled with the homeowners' association and sued its insurer, asserting claims for declaratory relief, breach of contract, and bad faith.

On motions for summary judgment, the District Court in Colorado determined that the insurer properly denied any duty to defend the insured based on the policies' Habitational New Construction Exclusion and Exclusion j(6), which the court dubbed the "faulty workmanship" exclusion.

The Habitational New Construction Exclusion barred coverage for claims/suits arising out of the insured's work "involving the development [and/or] construction…of…any other type of residential structure including 'multiple unit' residential structures." The court found that though the retaining wall was not a residential structure in and of itself, the exclusion broadly applied to lawsuits "arising out of, relating to or in any way connected with" the construction of residential structures, thus placing claims arising from the retaining wall within the scope of that exclusion.

As to Exclusion j(6), which barred coverage for property damage to "that particular party of any property that must be restored, repaired or replaced because 'your work' was incorrectly performed on it," the court found that the allegations in the underlying complaint, including allegations related to damages purportedly resulting from the defectively constructed retaining walls, fell entirely within the scope of the exclusion.

Georgia

Sky Harbor Atlanta Northeast, LLC v. Affiliated FM Ins. Co., No. 1:17-CV-03910-JPB, 2021 U.S. Dist. LEXIS 48567, 2021 WL 977274 (N.D. Ga. Mar. 15, 2021).

First-Party Coverage Under a Commercial Property Policy

The insured obtained a commercial property insurance policy and submitted a claim for mold damages discovered during renovations to a hotel. The insured sought more than $20,000,000, but its insurer denied coverage because it took the position that the damages existed much earlier than discovery and not as a result of any direct, physical loss as required by the policy's insuring agreement. The insurer also asserted that several exclusions applied including a wear and tear exclusion, a faulty workmanship exclusion, and a mold exclusion. The court agreed with the insurer and explained that there was no evidence damage to the hotel occurred as a result of a fortuitous event and that the evidence demonstrated that the damage had occurred since the original construction.

Meritage Homes of Ga. v. Grange Ins. Co., 528 F. Supp. 3d 1312 (N.D. Ga. Mar 23, 2021).

Work Performed by Subcontractor

The insured is a real estate developer that sought coverage under a subcontractor's CGL policy after being

sued for alleged damages suffered to a home that the insured had built. The insurer denied coverage based, in relevant part, on lack of occurrence. This lawsuit followed, and following discovery, the developer moved for summary judgment.

Much of the court's analysis was with respect to whether the damages sought against the developer by the homeowner were for the subcontractor's own work product. The court concluded that because there was an allegation that the homeowners had lost the use of appurtenances to their home, the damage was to more than just the subcontractor's work. For similar reasons, the court concluded that the Damage To Property Exclusion also did not apply to vitiate the duty to defend. Notably, the court determined that the proper question was whether the damages alleged were to the subcontractor's work because that was the named insured under the policy – rather than damages to the developer's work – given the language in the policy that the terms "you" and "your" refer to the named insured.

Ultimately the court concluded that the insurer had an obligation to defend the developer but that some of the damages sought, and specifically damages to the subcontractor's work product, were excluded under the policy. Thus, the insurer only had an obligation to indemnify for part of the damages. The court also granted the insurer's motion for summary judgment seeking dismissal of the bad faith cause of action because it determined that the coverage obligations were a close call and therefore bad faith damages were not warranted as a matter of law.

Kansas

Nautilus Ins. Co. v. Heartland Builders, 526 F. Supp. 3d 914 (D. Kan. 2021).

"That Particular Part" of the Insured's Work

The insurer issued CGL policies to the insured, which had designed and constructed a home. The homeowners sought arbitration against the insured related to alleged damage to the home, and the arbitration was ultimately litigated.

The CGL insurer filed this action seeking a determination that no coverage was owed for the arbitration award for numerous reasons: (1) lack of "property damage"; (2) no "occurrence"; (3) various business risk exclusions applied; (4) coverage was barred by the Expected Injury Exclusion; and (6) the Limitation of Coverage Endorsement applied.

At issue in this summary judgment motion were the Damage To Property Exclusions under j(5) and j(6), the Your Product Exclusion, the Impaired Property Exclusion, and the Limitation of Coverage Endorsement.

J(5) bars coverage for "[t]hat particular part of real property on which you or any contractors or subcontractors working directly or indirectly on your behalf are performing operations, if the 'property damage' arises out of those operations" and j(6) bars coverage for "[t]hat particular part of any property that must be restored, repaired or replaced because 'your work' was incorrectly performed on it." The insurer asserted that all of the damages related to the defective framing were barred by the exclusions. The insured countered that the phrase "that particular part" was ambiguous. The court undertook a lengthy analysis regarding whether the language was ambiguous before declining to make a specific determination in that regard. Instead, the court concluded that it could not decide as a matter of law that some or all of the arbitration award was barred by the exclusions because there was an issue of fact regarding whether the insured was performing operations at the time the damage occurred. However, the court did determine that the exclusions applied to the grading damages.

Relying on precedent, the court concluded that the Your Product Exclusion does not apply to damage to real property, so it determined the exclusion was inapplicable.

The policy's Impaired Property Exclusion barred coverage to "'Property damage' to 'impaired property' or property that has not been physically injured, arising out of: (1) A defect, deficiency, inadequacy or dangerous condition in 'your product' or 'your work'; or (2) A delay or failure by you or anyone acting on your behalf to perform a contract or agreement in accordance with its terms." The court noted that the purpose of the exclusion is to apply in situations where the insured's faulty work impairs property other than its work. Because the damage to the framing was to the insured's own work, the court deemed the exclusion inapplicable.

Finally, after a lengthy analysis regarding the policy's Limitation of Coverage Endorsement, the court concluded that the endorsement was ambiguous because it appeared to be incomplete and appeared to have errors in the drafting.

Louisiana

M.E. v. KRW Constr., LLC, No. 2020-0522, 2021 La. App. Unpub. LEXIS 74, 2021 WL 1438313 (La. App. 1st Cir. Apr. 16, 2021).

Faulty Workmanship and Resulting Flood Damage

This coverage dispute arose from an underlying action resulting from alleged damages to a home. The insured had been hired to perform certain renovations following flood damage. The insured's CGL insurer asserted that there was no coverage, and this decision granted the insurer's motion for summary judgment. In a brief opinion, the court explained that the homeowners had identified specific items of damages, and the "overwhelming majority clearly and directly related to" the insured's workmanship, so the Damage To Property Exclusions under j(5) and j(6) applied to bar coverage.

Maine

Bibeau v. Concord Gen. Mut. Ins. Co., 244 A.3d 712 (Me. 2021).

Earth Movement Exclusion

The insured submitted a claim under his homeowners' insurance policy for damages to his home, including extensive foundation cracks and settlement that led to racking doors and windows, out-of-level floors and stairs, cracking drywall, and other damages. The insured's expert contended that a water line leak that took place eleven years earlier pushed sand and other material under the foundation, compromising its integrity and causing it to drop down or "settle." The insurer's expert concluded that the house was constructed on a non-uniform soil composition that allowed the house to settle at different rates.

The court concluded that the insured's and the insurer's evidence both concluded that the house settled and suffered damage due to "earth movement," which the policy excluded. The court rejected the insured's argument that the Earth Movement Exclusion needed to specifically exclude damage caused by the accidental discharge of water from a water pipe in order to exclude the damages to the home. The court determined that, though the Earth Movement Exclusion typically applied only to losses stemming from natural disasters, the exclusion at issue was not ambiguous because it explicitly referred "earth movement . . . caused by or resulting from human or animal forces or any act of nature." Thus, the exclusion encompassed the cause of loss identified by the insured's expert, which was caused by a human-made interaction beneath the ground.

Minnesota

King's Cove Marina, LLC v. Lambert Commer. Constr. LLC, 958 N.W.2d 310 (Minn. 2021).

Coverage for Miller-Shugart Settlement

A marina hired the insured to serve as the general contractor for certain renovation work. During the renovation work, the marina identified various problems with the renovations and ultimately sued the insured. The insured's carrier agreed to defend the insured, but filed a declaratory judgment action seeking a determination that there was no coverage. While the coverage action was pending, the marina and the insured entered into a *Miller-Shugart* settlement, at which point the marina started a garnishment action against the insured's carrier. The lower court had determined that the carrier owed the insured coverage for the underlying property damage action, but the appellate court reversed. In this decision, the Minnesota Supreme Court affirmed the intermediate court's decision.

As a brief aside, a *Miller-Shugart* settlement is when an insured stipulates to a judgment against it on the condition that the plaintiff will only agree to satisfy the judgment against the insured's insurance carrier. The name arises from the Minnesota Supreme Court's decision in *Miller v. Shugart*, 316 N.W.2d 729 (Minn. 1982).

At issue was whether some or all of the damages to the marina were barred by Exclusion l, which applied to property damage to the insured's work "arising out of it or any part of it and included in the 'products-completed operations hazard.'" The court ultimately rejected the insured's various arguments that the provision was ambiguous, that coverage was illusory, and that the completed operations coverage was completely separate from the language of the exclusion.

However, the court ultimately set forth a standard regarding allocations of insured and noninsured claims in a *Miller-Shugart* settlement and determined that a settlement that does not make the allocation is not per se unreasonable. The court adopted "a flexible approach that allows a district court to consider all relevant facts and circumstances in determining the overall reasonableness of the settlement and in allocating the settlement between covered and uncovered claims." Thus, the case was remanded in light of that decision.

Mississippi

Triumph Church of God in Christ v. Church Mut. Ins. Co., No. 5:21-CV-6-KS-JCG, 2021 U.S. Dist. LEXIS 73398, 2021 WL 1519510 (S.D. Miss. Apr. 16, 2021).

Claim for Building Collapse Under a First-Party Policy

A policyholder filed a claim with its first-party carrier following a building collapse, but the carrier denied the claim because it determined that the collapse was a result of construction and manufacturing defects. The policyholder then brought this coverage action for breach of contract and bad faith, and the insurer moved to dismiss the bad faith cause of action. The insurer argued that the coverage decision was the result of the insurer's expert's opinions and therefore not bad faith, but the policyholder countered that the insurer had investigated in bad faith and favored "outcome-oriented" consultants rather than the policyholder's independent experts. Focusing on the standard to dismiss, the court determined that the policyholder's bad faith claim would not be extinguished.

Montana

Safeco Ins. Co. of Am. v. Grieshop, No. CV 20-24-BLG-TJC, 2021 U.S. Dist. LEXIS 62084 (D. Mont. Mar. 31, 2021).

Real Estate Exclusion and Owned Property Exclusion

The insured allegedly made alterations to structural trusses beneath his home while constructing an addition to the property. Subsequent purchasers discovered the damage to the trusses and filed suit against the insured for torts related to the insured's alleged failure to disclose the damaged trusses during the real estate transaction. The insurer defended under a reservation of rights and filed an action to seek a declaration that it had no duty to indemnify the insured based on a Real Estate Exclusion and an Owned Property Exclusion.

Aside from finding that the Real Estate Exclusion applied to all claims, the court also determined that the Owned Property Exclusion applied. The court rejected the insured's argument that the Owned Property Exclusion did not apply because, at the time the buyers discovered the damage to the trusses and filed suit against him, he did not own the property. The policy covered "property damage" caused by an "occurrence." The court, relying on cases regarding the manifestation of an "occurrence," rejected the insured's argument and found that coverage was triggered when property damage occurred, not when an underlying plaintiff asserted that the damages occurred.

New York

First Mercury Ins. Co. v. Nova Restoration of N.Y., Inc., No. 656240/2016, 2021 N.Y. Slip. Op. 30356(U) (N.Y. Co. Sup. Ct. Feb. 1, 2021).

Exterior Insulation and Finish Systems Exclusion

The court was tasked with determining whether two liability insurers were obligated to defend and indemnify their mutual insured, a contractor responsible for performing work on the exterior of a condominium building, in connection with an underlying lawsuit alleging damage as a result of water infiltration allegedly stemming from the insured's work. The liability insurers asserted in their motion for summary judgment that they did not owe such duties on the basis the coverage was barred under an "Exterior Insulation and Finish Systems" (or "EIFS") Exclusion. The exclusion provides, in pertinent part, that there is no coverage for "'bodily injury' or 'property damage' included in the 'products-completed operations hazard' and arising out of . . . [any] work or operations with respect to any exterior component, fixture or feature of any structure if any 'exterior insulation and finish system' is used on any part of that structure."

On summary judgment motions, the court initially found a question of fact regarding where the EIFS was located on the building, and how it was impacted by the insured's work. The court then allowed the par-

ties to obtain additional expert analyses to address the existing questions. Upon doing so, the insurers filed a motion to renew, submitting an analysis from an architect that found that EIFS was installed both at the loss location, as well as throughout the building, and that the insured removed, patched, and performed other work related to the EIFS as a part of its exterior work. The court found that this submission resolved the existing questions of fact, and confirmed that the EIFS Exclusion applied to relieve the insurers of their duty to defend or indemnify the insured.

Oklahoma

Starr Surplus Lines Ins. Co. v. Cushing Hosp., LLC, 527 F. Supp. 3d 1327 (W.D. Okla. 2021).

Continuous or Progressive Injury and Damage Exclusion

The insured was hired to construct a hotel and hired a subcontractor to install the pool. Following arbitration related to the construction defect issues, it was determined that a leak in the pool had caused soil saturation that led to various problems with the building. The owner sought to enforce the arbitration award against the insured's insurer, but the insurer asserted that there was no coverage because the damage to the hotel was the result of the insured's work product and not the result of any occurrence. Applying Mississippi law, the court agreed with the insurer. Specifically, it honed in on the findings in the arbitration, which included a determination that the insured was liable because it had breached its warranty to provide work that was free from defect, which was not an accident. The court also determined that the Continuous or Progressive Injury and Damage Exclusion applied to bar coverage under the latter two policies for which coverage was sought. Therefore, the insurer had no obligation to pay the judgment.

Oregon

Great Northern Ins. Co. v. Crown Pine Timber 4, L.P., No. 3:18-cv-2014-YY, 2021 U.S. Dist. LEXIS 1667 (D. Or. Jan. 5, 2021).

"Property Damage" Caused by an "Occurrence" and Exclusion j(6)

The insured assumed a surface and land lease for timberlands in Louisiana. The owner of the property petitioned a Louisiana court for specific performance of certain terms of the lease. The insured thereafter moved to compel arbitration, which was granted, resulting in dismissal of the state court proceeding. The insured thereafter demanded arbitration. In response to the demand, the property owner counterclaimed, alleging the insured encumbered the timberlands with "a wood supply agreement requiring [the insured] to provide unsustainable volumes of pulpwood and saw logs to certain paper and sawmills" and mismanaged the land in breach of the lease. The insured thereafter tendered the counterclaim to various liability insurers, which denied any obligation to defend.

The insurers commenced suit against the insured seeking a declaration that they did not owe a duty to defend in connection with the arbitration. Among the bases for the insurers' denial of coverage was their position that the counterclaim did not allege any "property damage" caused by an "occurrence," since the counterclaim was exclusively based on the insured's breach of the lease agreement and only sought economic damages. The court disagreed. The court noted that while the counterclaim was based on a breach of the lease agreement, it also alleged the insured violated industry standard/best practices that are directed to maximize the value of the property owner's forests. It deemed these allegations (i.e., those related to the insured's breach of industry standards) separate from the allegation relating to breach of the lease, which it said could constitute an occurrence under Oregon law.

As to the existence of "property damage," the court recognized that the insured's mismanagement of the property could lead to numerous forms of physical damage to tangible property, including damages to portions of the leased space itself (e.g., mismanaged roads resulting in divots, mismanaged soil erosion damaging the landscape, etc.). As such, the court found that the allegations in the counterclaim sufficiently alleged "property damage" caused by an "occurrence," such that the insurers owed a duty to defend.

However, one of the insurers argued that it owed no such duty because coverage was barred by its policy's Exclusion j(6), which was applicable "to that part of any property that must be restored, repaired or replaced because 'your work' was incorrectly performed on it." The court found that because the insured's

work on the property was ongoing, and the counterclaim only addressed the insured's obligation with respect to work on its property, the exclusion barred coverage for the counterclaim, and that specific insurer owed no duty to defend.

Hospitality Mgmt. v. Preferred Contrs. Ins. Co., 3:18-cv-00452-YY, 2021 U.S. Dist. LEXIS 126275 (D. Or. Mar. 17, 2021).

"Property Damage" Caused by an "Occurrence"

An owner of an apartment complex sued its general contractor for certain defects sustained during renovations of the complex. The general contractor thereafter commenced a third-party action against the insured, a subcontractor responsible for installing/repairing windows, siding, roof vents, and related components at the project. The sole claim against the insured was one for contribution. The insured tendered the lawsuit to its liability insurer, which retained counsel to defend the insured's interests. All parties in the lawsuit reached a global settlement weeks before trial. The insured assigned its coverage claims against its insurer to the general contractor. The insured then brought a coverage action against its insurer alleging breach of contract and bad faith failure to settle.

On summary judgment motions, the court first found that the stipulation, what it termed as adjudicated liability against the insured, was covered under the liability insurer's policy. Specifically, the court found that the insured performed two separate scopes of work at the project – i.e., windows/siding and vents/related components and that the work was defective and caused physical injury to tangible property that fell within coverage because there was property damage to the apartment building apart from the defective workmanship that occurred during the relevant policy periods. The court similarly determined that the separate scopes of work constituted separate occurrences, as the harmful conditions arising therefrom were distinct.

In rendering its decision, the court found that two of the four policies issued by the insurer were implicated by the loss (with the coverage under the latter two being barred by the policies' "Ongoing Operations Exclusion"), rendering the insured entitled to $2 million in coverage in connection with the underlying action, and thus $2 million on its breach of contract claim. The court also went on to hold that the insured satisfied the elements of its claim for bad faith failure to settle, entitling the insured to the full amount of the stipulated judgment.

Pennsylvania

Berkley Specialty Ins. Co. v. Masterforce Constr. Corp., 515 F.Supp. 3d 285 (M.D. Pa. 2021).

Fraudulent Conduct

The insured, a roofing company, told homeowners that it would install a roof on their residence, but the insured allegedly subcontracted the installation without the homeowners' knowledge. That subcontractor failed to properly install the roof, which then leaked and caused damages. Additionally, the slope of the homeowners' roof was allegedly too shallow for the application of the insured's proposed roofing system, necessitating significant design and repair work, including replacement of the entire roof. The insurer defended but reserved its right to deny indemnity. Ultimately, there was a substantial verdict based on the insured's violations of the Pennsylvania Home Improvement Consumer Protection Act and Unfair Trade Practices and Consumer Protection Law. The trial court determined that the insured and subcontractor "intentionally conspired to deceive" the homeowners, leading to trebled damages and attorneys' fees.

The insurer then filed suit against the insured, seeking a declaration that it had no duty to indemnify the insured for the judgment. The insurer and insured cross-moved for judgment on the pleadings. The court determined that the underlying action essentially arose from faulty workmanship. The insured argued that Pennsylvania state intermediate appellate court decisions supported a finding that faulty workmanship may be a covered "occurrence" when the workmanship damages third-party property, but the court rejected this argument.

Instead, relying on Pennsylvania intermediate appellate and supreme court cases, as well as cases from the Third Circuit, the court predicted that the Pennsylvania Supreme Court would not find that reasonably foreseeable damages to third-party property were sufficiently fortuitous or accidental to satisfy a liability policy's definition of "occurrence." The trial court essentially ordered the insured to reimburse the

homeowners for faulty workmanship and damage to the insured's product or work, which was not be an "occurrence" as a matter of law.

South Carolina

Lendlease US Constr. v. Nat'l Fire Ins. Co., No.: 4:19-cv-00959-JD, 2021 U.S. Dist. LEXIS 180377 (D.S.C. June 14, 2021).

Additional Insured Coverage

A property owner sued several general contractors as a result of alleged damages to a seven-building property. One of the general contractors sued sought additional insured coverage under a policy issued to one of the subcontractors. The insurer denied the general contractor additional insured coverage for several reasons including lack of insured status and a Residential Construction Defect Exclusion. The court denied the insurer's motion on most grounds based on issues of fact, but the court did conclude that there was no coverage under one of the policy periods as a matter of law based on the policy's insuring agreement, which limited coverage based on when an "Authorized Insured" first knew of the property damage.

South Dakota

Union Ins. Co. v. Klingenberg, CIV 20-4028, 2021 U.S. Dist. LEXIS 54678, 2021 WL 1102189 (D.S.D. Mar 23, 2021).

Coverage for Damages to Home Sought Under Husband's DBA's Liability Policy

This coverage dispute arose from an underlying property damage action wherein a homeowner sued her husband, who had also served as the general contractor on the homebuilding project. Damage to the home was caused following a retaining wall collapse. The husband operated a plumbing and heating business under a DBA, and it sought coverage from its CGL insurer. The CGL insurer asserted that there was no coverage because (1) it insured the DBA as a plumbing and heating contractor rather than as a general contractor; (2) the policy excluded coverage for property owned by the insured; and (3) various business risk exclusions applied. The insurer also sought rescission of the DBA's policy as a result of alleged misrepresentations.

The court ultimately concluded that there was no coverage for the property damage lawsuit because the husband owned the property that he was being sued for damaging and because the Damage to Property Exclusions under j(5) and j(6) also applied to bar coverage.

Texas

Tejas Specialty Group, Inc. v. United Specialty Ins. Co., No. 02-20-00085-CV, 2021 Tex. App. LEXIS 4360 (Tex. Ct. App. June 3, 2021).

Texas's Eight-Corners Rule

The insured, a subcontractor to the general contractor, tendered its defense to its CGL carrier for a third-party complaint by a general contractor in a construction defect case. Relying only on the allegations in the third-party complaint, the insurer declined to defend the insured because the allegations in that complaint alleged that the insured knew about the damages caused by the alleged construction defects. In subsequent litigation brought by the insured against its insurer, the parties disagreed about whether the complaint was within the scope of Texas's eight-corners rule or whether the insurer's defense obligations were fixed only by the third-party complaint's allegations, focusing on a split in trial courts' treatment of the duty to defend law. The Texas Appellate Court declined to answer this question and, in reversing the trial court's summary judgment in the insurer's favor, found that the third-party complaint alleged facts sufficient to trigger the insurer's duty to defend.

Specifically, the insurer contended that the third-party complaint alleged that the work on the project was substantially complete by March 9, 2017, but the insurer's policy went into effect on October 1, 2017. The third-party complaint also alleged that the owners of the construction project had observed or knew of the damage beginning in the middle of 2017. Thus, the insurer contended that the complaint alleged sufficient facts to show that the damage was ongoing prior to the policy's effective date and excluded according to the insuring agreement. The court disagreed and noted that the third-party complaint was against six contractors who signed contracts between 2014 and 2016. The third-party complaint itself was filed in 2019, but it did not allege when the work was performed or completed by each subcontractor and, therefore, it was possible that the insured could have performed work leading to the defects after the policy took effect.

The insurer also contended that a mid-2017 manifestation of damage meant that the work giving rise to that damage had to have taken place before manifestation. The court rejected this argument because the third-party complaint did not include any allegations linking the insured's work to the alleged manifested damages, which left open the possibility that the insured's work could have led to other damages that were not the ones that manifested in mid-2017. That possibility was fatal to the insurer's contention that it had no duty to defend its insured against the third-party complaint.

Washington

T-Mobile USA, Inc. v. Selective Ins. Co., No. C 15-1739JLR, 2021 U.S. Dist. LEXIS 64282 (W.D. Wash. Apr. 1, 2021).

Additional Insured Coverage and the Professional Services Exclusion

The insured was retained by T-Mobile to construct a cell phone tower on the rooftop of a building. The owner of the building thereafter commenced suit against T-Mobile alleging that the cell tower damaged the building. T-Mobile thereafter commenced its own third-party action against the insured, while also seeking additional insured coverage from the insured's liability insurer. The insurer, however, denied T-Mobile's tender on the basis that T-Mobile did not qualify as an additional insured under its policy. Specifically, the insurer determined that T-Mobile's tender, which was based exclusively on a certificate of insurance issued by the insurer's agent, was insufficient to satisfy the provisions set forth in the blanket additional insured endorsement in the insurer's policy.

While the trial court initially agreed with the insurer's determination, on appeal, the trial court's determination was reversed, and the United States Court of Appeals for the Ninth Circuit found that the insurer was bound by the representations made by its agent in the certificate of insurance, rendering T-Mobile an additional insured under the policy. The insurer argued, however, that regardless of T-Mobile's insured status, coverage was barred by the policy's Professional Services Exclusion, applicable to property damage arising out of the rendering, or failure to render, "professional architectural, engineering or surveying services," because the insured was retained to perform architectural and engineering services. The court did not agree as it pertained to the insurer's duty to defend. Specifically, the court, reading the allegations in the underlying complaint broadly, found that the allegations could be construed as arising from the type of construction negligence to which other courts have refused to apply similar exclusions.

Practice Point: When determining an insurer's duty to defend, the allegations in the complaint must be liberally construed. ■

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11600 John F. Kennedy Blvd., Suite 1655, Philadelphia, PA 19103, USA
Telephone: (215)564-1788 1-800-MEALEYS (1-800-632-5397)
Email: mealeyinfo@lexisnexis.com
Web site: http://www.lexisnexis.com/mealeys
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