MEALEY'S™ LITIGATION REPORT

Construction Defects Insurance

Construction Defect Claims: A 2022 Update Part II

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Commentary

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[Editor's Note: Thomas F. Segalla, Michael T. Glascott, Ashlyn M. Capote, Adam R. Durst and Sean P. Hvisdas are partners and Samantha M. McDermott is an associate 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

In Part I of this publication, the authors discussed insurance coverage construction defect cases from the first half of 2022. Many construction defect cases analyze when a construction defect claim constitutes an occurrence and whether business risk exclusions bar coverage. A frequent principle underlying the decisions is that a liability insurer is not intended to be a guarantor of an insured's poor workmanship.

A question raised in some of the cases below is what happens when an entity seeks additional insured coverage under a policy issued to a subcontractor, and the claim is for the subcontractor's allegedly faulty work. In other words, should the analysis focus on whether there is damage to property outside of the purported additional insured's work because it is the one seeking coverage, or should the focus should be on the named insured's work since it is the policyholder? In *Acuity v. M/I Homes of Chicago, LLC*, No. 1-22-0023, 2022 Il. App (1st) 220023 (Ill. App. 1st Dist. 6th Div. 2022), discussed below, the appellate court grappled with the issue and urged the state supreme court to provide guidance – although the court ultimately decided the case without making any definitive conclusion.

Another question raised by several of the cases discussed below is the amount of specificity required regarding third-party property damage in order to trigger coverage. For example, in *Indian Harbor Ins. Co. v. Houston Cas. Co.*, No. 21-cv-02404-RMR-NRN, 2022 U.S. Dist. LEXIS 117857, 2022 WL 2439089 (D. Colo. July 15, 2022), the court explained that "mere allegations and conclusory statements" regarding damage to property other than the insured's work would not satisfy the trigger of coverage. The court's decision in *Am. Fam. Mut. Ins. Co. v. Sinha*, No. 1-21-1201, 2022 Ill. App. Unpub. LEXIS 1570 (Ill. App. 1st Dist. 2nd Div. Sep. 20, 2022) was very similar.

These cases, which are included in the nationwide construction defect cases from the second half of 2022, are discussed below in Part II.

Alabama

1. *Frankenmuth Mut. Ins. Co. v. Ivan's Painting, LLC,* No.: 7:21-cv-00945-RDP, 2022 U.S. Dist. LEXIS 227707, 2022 WL 17813753 (N.D. Ala. Dec. 19, 2022).

Additional Insured Coverage

The insured was a subcontractor hired to help paint and clean window units at the construction of a new home. The general contractor's contract with the insured required that the general contractor be named an additional insured under the subcontractor insured's CGL policy. The subcontractor allegedly damaged windows, and the homeowners demanded the general contractor replace them. The general contractor and the insured sought coverage under the subcontractor's policy, and the insurer denied coverage.

The insurer's position was that the only property damaged was the subcontractor's own work, which is not an occurrence. The homeowner, which intervened in the declaratory judgment action filed by the insurer, argued along with the general contractor that the homeowner's damage was limited to the window glass being scratched, but the subcontractor worked only on the window frames. Thus, they argued that the damages sought were not for the subcontractor's own work.

The court focused on the fact the subcontractor used a liquid while working on the frames to protect the glass from scratches, which demonstrated that the subcontractor anticipated the possibility that scratches could occur. The court concluded that the resulting damages to the glass were within the purview of the subcontractor's own work, so there was no occurrence.

Arizona

1. *Elite Performance LLC v. Echelon Prop. & Cas. Ins. Co.,* No. CV 20-00552-TUC-RM (LAB), 2022 U.S. Dist. LEXIS 147411 (D. Ariz. Aug. 16, 2022).

Magistrate Recommends Summary Judgment for Carrier based on CGL Business Risk Exclusions

The insured, a contractor, allegedly performed subpar work on an owner's building. The contractor's insurer denied coverage for the alleged damages. The owner and contractor entered into a consent judgment of $475,000, and the owner assigned its rights under the policy to the owner. The owner sued the insurer for breach of contract and bad faith, seeking the judgment and additional damages. On cross motions for summary judgment, a federal magistrate judge offered recommendations for rulings on whether the policy covered the contractor's allegedly subpar work.

The owner argued that the work constituted property damage to its building because the insured drilled a hole in an electrical panel, removed insulation from busing, and broke a pipe while performing its work. The insurer argued that the policy's Damage to Property Exclusion under subsections j(5) and j(6) and the Impaired Property Exclusion barred coverage.

The court agreed that the exclusions barred coverage for all of the alleged damages. With regard to the electrical panel, it was either part of the real property on which the insured was performing work or, in the alternative, it was property that must be replaced due to the insured's work. Additionally, to the extent the building was unable to be used, any such damage fell within the Impaired Property Exclusion as it was impaired due to the insured's improper work. Thus, the court recommended that the district court judge grant the insurer's motion for summary judgment.

California

1. *Gonsalves & Santucci Inc. v. Greenwich Ins. Co.,* No. 2:22-cv-03757, 2022 U.S. Dist. LEXIS 210850 (C.D. Cal. Oct. 11, 2022).

Damages from Subcontractor's Defective Workmanship do not Constitute "Property Damage" and are Otherwise Excluded

The insured was a subcontractor retained to provide construction services for the foundation system for the construction of a new airport concourse. The insured subcontracted with another entity to provide services related to the project's foundation system, which included the installation of "torque down pile" units. The owner of the project subsequently sued the insured, alleging the piles were improperly installed and were otherwise defective.

The insured placed its CGL insurer on notice of the dispute, claiming that the underlying litigation alleged property damage via injury to the soil, other subcontractors' work, the pile units themselves, as well as loss of use of the surrounding soils, the entire concourse foundation area, and other subcontractors' materials. The insurer refused to defend, claiming that

the allegations in the underlying litigation did not seek damages because of "property damage" covered under its policy, and because any allege "property damage" was excluded by the Damage to Property Exclusion under j(5) and the Impaired Property Exclusion.

The court decided in favor of the insurer when summary judgment motions were heard, holding that allegations of damage to the piles themselves and broken soil arising from their defective installation, did not amount to property damage under California law. The court also held that the loss of use of the area into which the piles were installed and the loss of use of materials and equipment of other subcontractors did not constitute covered property damage, and were otherwise merely non-covered intangible economic loss.

The court also held, in the alternative, that even if property damage was alleged, the Damage to Property Exclusion under j(5) and the Impaired Property Exclusion would have barred coverage.

2. *Travelers Indem. Co. v. Boudreau Pipeline Corp.,* No. 2:21-cv-07380, 2022 U.S. Dist. LEXIS 144069, 2022 WL 4596693 (C.D. Cal. July 29, 2022).

Duty to Defend Triggered for Potentially Covered "Property Damage," but Determination on Duty to Indemnify Premature

The insured was contracted by a developer to construct and install a sewer lift station to service a nearby development, the purpose of which was to transport waste from the development to the sewer line owned by the city. After the project was completed and put to its intended use, the system began to fail. The developer filed suit against the insured, alleging the insured was responsible for certain property damage associated with the failure, as well as costs incurred in performing repairs at the project. The insured thereafter tendered the suit to its commercial general liability insurer, which agreed to defend under a reservation of rights.

In the coverage suit, the insured argued that the insurer owed a duty to defend. The insurer, which did not address its defense obligations, argued that the categories of damages alleged in the underlying action would not trigger its indemnification obligation. As to the duty to defend, the court determined that at least one of the categories of damages alleged in the underlying action (i.e., that the entire sewer system was damaged as a result of the insured's defective work installing the sewer lift station) was potentially covered, thus triggering the insurer's defense obligation. As to the insurer's indemnity obligation, the court held that a determination on indemnity was premature because liability in the underlying action had not yet been established.

Colorado

1. *Indian Harbor Ins. Co. v. Houston Cas. Co.,* No. 21-cv-02404-RMR-NRN, 2022 U.S. Dist. LEXIS 117857, 2022 WL 2439089 (D. Colo. July 15, 2022).

Damage to Other Property – Faulty Workmanship

In this coverage dispute between Houston Cas. Co. ("HCC") and Indian Harbor, Indian Harbor had issued payment to its insured (the general contractor) under a Subcontractor Default Insurance policy, which covered losses caused by a subcontractor's default. HCC had issued a CGL policy to the owner, which also covered certain enrolled contractors, including the general contractor and the subcontractor that had allegedly installed faulty balconies. Following a notice of claim sent by the owner to the general contractor for the balconies, HCC denied coverage because it claimed that the damage was only to the work itself.

After issuing payments in connection with the allegedly faulty balconies, Indian Harbor sued HCC for reimbursement. The sole issue was whether the damage was considered "property damage" as defined by the HCC policy, which included "physical injury to tangible property, including all resulting loss of use of that property."

Indian Harbor argued that, although much of the damage was to the balconies and therefore to the subcontractor's own work, portions of the balconies would need to be replaced as part of the repair of the defective work. The court found that the argument required "a labored analysis of individual components,"

which was contrary to Colorado law. The court also rejected the "mere allegations and conclusory statements" within the owner's notice of claim, which it said failed to create an issue of fact that there was damage to third-party property.

Connecticut

1. *B&W Paving & Landscape v. Emplrs Mut. Cas. Co.,* No. 3:21-cv-01624, 2022 U.S. Dist. LEXIS 225783 (D. Conn. Dec. 15, 2022).

Extrinsic Expert Evidence Triggers Duty to Defend

The insured subcontractor performed asphalt work in connection with a large construction project. The owner sued the general contractor as a result of allegedly defective work, and the general contractor filed a third-party action against the subcontractor. The general contractor alleged that if the general contractor were liable in the lawsuit, the subcontractor's improper installation of asphalt in the parking lots caused the damages.

The general contractor's pre-suit expert found that thin layers of asphalt contributed to water intrusion into the base and subbase and, therefore, the deficient paving contributed in some degree to the detrimental effects on the base and subbase materials.

After the suit was filed, the insurer denied coverage. According to Connecticut law, courts may consider evidence extrinsic to the underlying complaint when determining if a carrier has a duty to defend, but only if those extrinsic facts support a duty to defend. Further, under Connecticut law, "property damage" from defective construction work only includes damage caused to other, non-defective property but does not include the insured's own defective work.

The dispute centered on the general contractor's pre-suit expert report, which the insurer argued was inadmissible because it included opinions (rather than facts) that other underlying defendants' work could have been defective. The court, reviewing other cases, opted to consider the report, observing that other courts in the state relied on similar extrinsic evidence. The court also refused to recognize a line between "extrinsic 'facts' that objectively and clearly establish coverage … and other types of evidence." The court found that the underlying complaint combined with the general contractor's expert report triggered a duty to defend. The general contractor's third-party complaint claimed damage related to paving was caused by the subcontractor's defective work, and the general contractor's report raised at least a possibility that the subcontractor's faulty work damaged the base and subbase installed by another contractor.

Florida

1. *Cincinnati Specialty Underwriters Ins. Co. v. KNS Grp., LLC,* No. 21-13628, 2022 U.S. App. LEXIS 27949, 2022 U.S. App. LEXIS 27949, 2022 WL 5238711 (11th Cir. 2022).

Alleged Damage from Insured's Work Triggers Duty to Defend

The insured subcontractor was hired by a general contractor to perform work in the construction of a casino. The owner was unhappy with the quality of the work performed, and therefore sued the general contractor, who in turn filed a third-party complaint against the insured-subcontractor asserting claims for breach of contract, negligence, common law indemnification, and contractual indemnification. The subcontractor tendered its defense to its general liability insurer, which commenced coverage litigation seeking a declaration that it did not owe defense or indemnification to the subcontractor in connection with the third-party action.

As to the subcontractor, the court found that its insurer owed a duty to defend since the owner's complaint (for which the general contractor sought indemnification) alleged property damage to something other than the insured's work. Specifically, it alleged the general contractor's (and therefore the subcontractor's) faulty installation of the glass panels at the project, which were supplied by a third party, were damaged, thus reasonably triggering coverage. The court also determined these allegations were not otherwise excluded by business risk exclusions j(5) or j(6) since it was not clear the alleged damage was within the "natural and intended scope" of the insured's operations, i.e., whether the subcontractor caused damage to the glass façade, to other property, or whether another contractor's work was involved. For this reason, the court determined that the in-

surer did not conclusively establish that the exclusions barred coverage.

2. *Colony Ins. Co. v. Coastal Constr. Mgmt., LLC,* No. 8:21-cv-2541, 2022 U.S. Dist. LEXIS 199825, 2022 WL 16636697 (M.D. Fla. Nov. 2, 2022).

Insured's Liability as Construction Manager is Barred by Professional Services Exclusion

The insured was a developer hired for construction of a 228-unit apartment complex. Upon completion of the project, the owner identified numerous defects and deficiencies. The owner commenced suit against the developer, among others, asserting causes of action for breach of contract and negligence. The developer sought coverage in connection with the lawsuit from its commercial general liability insurer, which provided a defense under a reservation of rights. The insurer then commenced coverage litigation seeking a declaration that it did not owe the developer coverage in connection with the owner's lawsuit based on, inter alia, the policy's Professional Services Exclusion. The exclusion barred coverage for property damage "arising out of the rendering or failure to render any professional service[,]" including "inspection, supervision, quality control, architectural or engineering activities done by or for you on a project on which you serve as construction manager" and "engineering services, including related supervisory or inspection services."

The court agreed with the insurer, finding that the construction management duties for which the developer was contracted fell squarely within the exclusion because they "by their nature require specialized skill, training, and/or experience."

3. *Granada Inc. Co. v. Sunshine Constr. Group,* No. 22-CA-000035-M, 2022 Fla. Cir. LEXIS 1168 (Fla. Cir. Ct. 2022).

No Coverage under CGL Policy for Allegations of Fraud and Improper Billings in Home Construction

The insured was sued by an individual for damages arising out of the construction of certain homes on a property in Florida. The suit pertained to an alleged scheme by the insured to defraud and related primarily to the deprivation of funds based on allegations of billing improprieties. The insured sought coverage in connection with the suit from its general liability insurer, which commenced coverage litigation seeking a declaration that it did not owe its insured a duty to defend or indemnify. The court determined that the allegations in the underlying complaint did not seek damages because of property damage caused by an occurrence, as was necessary to trigger coverage, and otherwise fell outside the scope of coverage as defined by the policy's Classification Limitation Endorsement.

Georgia

1. *Middlesex Ins. Co. v. Dixie Mech., Inc.,* No. 1:20-cv-04971-JPB, 2022 U.S. Dist. LEXIS 175190, 2022 WL 4484615 (N.D. Ga. Sep. 27, 2022).

Lack of Occurrence

The insured was a subcontractor hired to perform fabrication and welding work. Its insurer asserted that there was no coverage for claims that the subcontractor's work was allegedly defective because it was not the result of any "property damage" resulting from an "occurrence." The court noted that the subcontractor's allegedly faulty workmanship would only be considered "property damage" if the damages were to other property. Because the underlying claims were that there were delays and breaches of contract based on the subcontractor's work, and because there was no allegation that any other property sustained damages, there was no coverage.

Hawaii

1. *St. Paul Fire & Marine Ins. Co. v. Bodell Constr. Co.,* No. 20-cv-00288-DKW-WRP, 2022 U.S. Dist. LEXIS 205619, 2022 WL 16855718 (D. Haw. Nov. 10, 2022).

Questions Regarding Coverage for Arbitration Award

The insured, a general contractor, was sued by a developer after a condominium project allegedly failed to comply with building codes, and the general contractor sought coverage under various CGL policies. Note that we had previously discussed the court's decision regarding a prior motion for summary judgment in Part 1 of this publication from January 2023. In the prior summary judgment motion decision, the court had determined that coverage may have been trig-

gered in some of the policies because there were damages alleged to be the result of subcontracted work.

In this particular summary judgment motion, the insurers asserted that there was no coverage because (1) there was no actual damage to property; (2) the damages sought to repair defective work; and (3) the arbitration award was not for "loss of use" of property. The court ultimately agreed that there was no coverage for some of the damages that had been awarded in the arbitration.

However, the court only granted partial summary judgment to the insurers because there was a question regarding the arbitration award and how much of the award was for damages that were not covered under the policy. In other words, because the arbitration award did not contain clarity regarding the amount awarded for specific items of damages, it was unclear to the court how much of the damages awarded were covered.

Illinois

1. *Acuity v. M/I Homes of Chicago, LLC,* No. 1-22-0023, 2022 Il. App (1st) 220023 (Ill. App. 1st Dist. 6th Div. 2022).

Trigger of Coverage for Additional Insureds

The insured was a subcontractor hired to help build townhomes. The Owners Association sued the general contractor alleging homes were constructed and sold with substantial exterior defects, and the general contractor sought coverage under a CGL policy issued to the subcontractor. The insurer denied coverage because it asserted that the damages were only to repair and replace the construction work.

There was a dispute about whether the analysis should focus on whether the damage was to the subcontractor's own work, since the subcontractor was the named insured under the policy, or whether damages were sought for damages to the general contractor's own work since it was the general contractor seeking coverage. The court never decided the issue but commented that it believed the Illinois Supreme Court should address the issue.

Ultimately, the court concluded that a duty to defend the general contractor was triggered because the Owners Association had alleged that there was damage to "other property." The insurer had asserted that the allegation was conclusory and made only to try and trigger coverage, and that a general reference to a fact without specificity, and without attachment to a particular theory of recovery, did not trigger coverage. The court disagreed based on the expansive duty to defend.

2. *Am. Fam. Mut. Ins. Co. v. Sinha,* No. 1-21-1201, 2022 Ill. App. Unpub. LEXIS 1570 (Ill. App. 1st Dist. 2nd Div. Sep. 20, 2022).

References to Unspecified Other Damages

The insured was a landscaper hired to complete various landscaping projects around a home including constructing a retaining wall and gazebo. The homeowners sued the landscaper following the completion of the project and alleged that the work was defective and deficient.

The landscaper's CGL insurer denied coverage and started this action against the insured and homeowners seeking a determination that no coverage was owed because the damage occurred after the policy was cancelled, there was no occurrence alleged, and based on the policy exclusion for damages to property that must be repaired because the insured's work was incorrectly performed on it. The trial court had granted summary judgment to the insurer, and the appellate court affirmed.

The sole issue was whether the homeowners had alleged damage to property that was not the landscaper's work, and the homeowners insisted that they had by pointing to an allegation in their complaint regarding "extensive property and other damages." They also referenced water infiltration, although that was not mentioned in the complaint. As in the *Acuity* case discussed above, there was a question about whether an allegation regarding "other damages" must be tied to a particular theory of recovery. Here, the court concluded that it must. Thus, there was no occurrence, and the allegations to unspecified other damages did not trigger coverage.

Practice Point: Illinois has adopted the "eighth corners" approach to determining a duty to defend, which requires an insurer to evaluate only the complaint and policy. Because the homeowners were rely-

ing on an allegation of water infiltration that was not discussed in the complaint, it could not trigger the duty to defend.

3. *Cornice & Rose Int'l, LLC v. Acuity,* No. 21 C 6112, 2022 U.S. Dist. LEXIS 175371, 2022 WL 4481448 (N.D. Ill. Sep. 27, 2022).

Other Contractors' Work Fall within Scope of Architect's Work

The insured was an architect hired to design and construct a building. The purchaser of the completed building sued the architect when it discovered that the property was defective, had multiple architectural issues, and overall was not suitable for use unless substantial funds were placed into correcting the issues with the property. The architect sought coverage under its CGL policy from its insurer when the suit occurred.

The insured argued that there was coverage because it was not responsible for most of the items of damages which it said was the result of other contractors' work. For example, there was an allegation that the cabinets were too tall and blocked windows, which the architect said was not its work. The court disagreed because under the contract, the architect was tasked with evaluating the completed work performed by other trades. With respect to allegations regarding lack of ventilation and hazards, the court determined that those were economic losses rather than actual property damage. Thus, there was no coverage.

Indiana

1. *Savers Prop. & Cas. Ins. Co. v. Rockhill Ins. Co.,* No. 1:21-cv-01802-MJD-TWP, 2022 U.S. Dist. LEXIS 187942 (S.D. Ind. Oct. 14, 2022).

Duties Owed to Non-Parties to a Contract may Constitute an Occurrence

The insured, an owner and operator of a landfill, was sued by a class of homeowners within three miles of the landfill who alleged, among other things, that they suffered loss of use of their properties and injuries caused by the release of noxious gases resulting from the improper construction, maintenance, or operation of the landfill. Various insurers were part of the suit and filed various motions. This particular decision related to one liability insurer's motion for summary judgment seeking a declaration that it had no duty to defend or indemnify the insured. The insurer argued that the allegations against the insured did not constitute an occurrence but, rather, alleged professional errors or omissions.

Specifically, the insurer argued that the insured's liability arose out of a contract it entered into to operate the landfill properly, which constituted a business risk. The court rejected this argument, noting that the insured did not owe any contractual duties to the homeowners and, instead, its liability arose from the breach of a duty not to create a nuisance, which exists regardless of any contractual obligations. Therefore, the homeowners alleged an occurrence.

The insurer had also argued that a Professional Services Exclusion precluded coverage because the insured was hired as a sophisticated landfill operator to operate the landfill "in a highly regulated environment subject to the operating permit regulations…" The insurer argued that operation of a landfill's gas collection and odor mitigation systems was a specialized skill that constituted a professional service within the scope of a policy exclusion. The court disagreed noting that, while a gas collection and odor mitigation system may be responsible for the odors, so too could improperly covering the waste with dirt, which is unsophisticated manual labor. Thus, the court found that the insurer had a duty to defend and reimburse another insurer for a pro rata share of defense costs.

Kentucky

1. *Ky. Farm Bureau Mut. Ins. Co. v. Trent,* No. 2021-CA-0813-MR, 2022 Ky. App. Unpub. LEXIS 761, 2022 WL 17839506 (Ky. Ct. App. Dec. 22, 2022).

Occurrence and Faulty Workmanship

The insured was hired to design a residential building and prepare cost estimates for building the new residence. The insured and the property owners entered into a construction management agreement. The property owners alleged that the insured learned of a design defect which increased the cost of framing

the house prior to construction but proceeded with construction anyway. Therefore, the property owners sued for fraud in the inducement and negligent design.

The liability insurer argued that it did not owe coverage in this case because the policy provided liability coverage for "bodily injury" or "property damage" caused by an "occurrence." Here, the insurer argued there are no allegations for "property damage" or "bodily injury" and fraud does not constitute an accident which is part of the definition of an "occurrence." The insured and the property owner asserted that mental anguish and anxiety constituted "bodily injury" under the policy, but the court never addressed this issue. The property owners argued that there was an "occurrence" because the court should view an "accident" within the "occurrence" definition as being an unintended consequence. It also argued the "your work" exclusion was ambiguous. The court noted the doctrine of fortuity is required in determining if something is an accident. To determine if an event was an accident for purposes of CGL coverage, courts must consider: (1) whether the insured intended the event to occur; and (2) whether the event was a chance event beyond the control of the insured. The court concluded that "faulty workmanship" is not an accident so long as the actions leading to the property damage were under the insureds control and the insured intended to take those actions. The court also held that the "your work" exclusion is not ambiguous and that the defect in this case was the result of the insured's work, so coverage was not owed.

Louisiana

1. *Opelousas Hotel Group LLC v. DDG Constr. Inc.,* No. 6:18-CV-01311, 2022 U.S. Dist. LEXIS 233382 (W.D. La. Dec. 29, 2022).

The Discovery of the Alleged Damages may be a Key Coverage Defense

An owner sued the insured, a general contractor, for damages arising out of the insured's alleged failure to construct a hotel in accordance with the timelines set forth by its contract with the owner. The insured did not perform any work itself but, rather, subcontracted all of the work. The insurer issued a series of CGL and excess policies to the insured that were in effect between 2013 and 2016. On June 1, 2017, the owner issued a written notice of default to the insured for its "lack of progress and finishing the hotel on time, [and] lack of manpower." Seven days later, the owner terminated the insured. In December 2018, the owner filed suit against the insured, insurer, and other parties for breach of contract, breach of warranties, negligent supervision and construction, and professional negligence arising out of alleged construction defects discovered by a replacement general contractor hired after the insured's termination.

The insurer moved for summary judgment contending that the alleged construction defect damages did not manifest before the replacement general contractor discovered the alleged defects in September 2017, a few months after the insurer's last policy terminated in June 2017, and because various policy exclusions apply. The court determined that there was no occurrence alleged against the insured. Though the owner alleged damage caused by the construction defects, no party could point to damage that affected other property. The court also agreed with the insurer that manifestation of any damages took place after the insurer's last policy terminated, rejecting arguments that disputed material facts called into question the precise timing of manifestation.

Nevada

1. *Am. Fire & Cas. Co. v. Unforgettable Coatings, Inc.,* No. 2:21-CV-1555 JCM (NJK), 2022 U.S. Dist. LEXIS 139503, 2022 WL 3143991 (D. Nev. Aug. 5, 2022).

Coverage Questions for Arbitration Award

The insured was hired to paint properties in a community. Following the conclusion of the project, the Homeowner's Association sued the insured alleging that the work was defective, and the dispute was arbitrated. The insurer defended the insured during arbitration but sought a declaration that it did owe coverage for the award. The decision contains few details regarding the damages listed in the arbitration award and the basis for the insurer's denial, but the court agreed with the insurer that all of the items in the award were not covered under the policy.

New Hampshire

1. *Hutton Constr., Inc. v. Cont. W. Ins. Co.,* No. 21-cv-706-PB, 2022 U.S. Dist. LEXIS 117395, 2022 WL 2440354 (D.N.H. July 5, 2022).

Stop-Work Causes Delay Damages – Some Covered, Some Not

The insured was a subcontractor whose allegedly faulty masonry work caused a building inspector to issue a stop-work order for an entire building project, causing the general contractor to incur delay damages. The general contractor demanded that the subcontractor reimburse it for the damages, and the subcontractor's insurer denied coverage.

In coverage litigation, the insurer moved for partial summary judgment regarding whether those delay damages fell within the scope of a CGL policy. The stop-work order remained in place for 13 months, during which time water seeped into the building through defective masonry walls and the unfinished roof, damaging the general contractor's interior work, including sheetrock, metal studs, and insulation. After the stop-work order was lifted, the general contractor spent two additional months to complete the work, and the subcontractor remedied the masonry work at its own expense. The general contractor incurred delay damages as a result of the stop-work order and the additional two months to complete and repair the interior damages. As a result, it demanded that the insured reimburse it for the delay damages.

The insurer argued that the property damage was not caused by an "occurrence" and that the delay damages were not a covered form of "property damage." The court determined that damage to non-defective property caused by defective workmanship is not an occurrence absent an intervening event or exposure that occurs fortuitously and, together with the defective work, harms non-defective property. The court also disagreed with the subcontractor's argument that the stop-work order was an intervening event that would satisfy the fortuity requirement. Relying specifically on the subcontractor's knowledge of the building inspector's concerns before issuance of the stop-work order, the court held that even if the stop-work order could be a fortuitous intervening event – which the court doubted – it was not in this case.

The court did find, however, that the delay damages could constitute property damage during the two months that the general contractor was repairing the interior damages. Specifically, the court determined that the water damage was property damage, and because the delay damages naturally flowed from covered property damage, the policy covered those damages.

Pennsylvania

1. *Erie Ins. Exch. v. Glenn M. White Builders,* No. 1174, 2022 Phila. Ct. Com. Pl. LEXIS 13 (Phila. Ct. Com. Pl. Sep. 13, 2022).

Philadelphia Trial Court Reconfirms Faulty Workmanship is not an Occurrence

After the completion of construction, various homeowners commenced arbitration actions against the developer in which they alleged damages arising from faulty workmanship in the construction of their homes, including in the stone veneer and roofing systems. The developer hired various subcontractors, including one to perform stone veneer work and another to perform roofing and siding work. This particular decision pertained to the insurer's obligation to provide coverage to the subcontractors.

The insurer moved for default judgment against the subcontractors, seeking a ruling that it had no duty to defend or indemnify them in alleged faulty workmanship lawsuits and certain arbitration actions commenced by homeowners. The developer opposed the insurer's motion, but the subcontractors did not.

The court, relying on Pennsylvania precedent and a case in a federal court arising out of the same arbitrations against the developer but by a different insurer against another insured, agreed with the insurer that the allegations of faulty workmanship did not satisfy the policies' definition of an "occurrence." Further, the court rejected the developer's arguments relying on case law governing the relationship between a commercial landlord and tenant. Finally, the court determined that there was no need to consider the applicability of policy exclusions and entered judgement in the insurer's favor.

Texas

1. *Colony Ins. Co. v. First Mercury Ins. Co.,* No. A-20-CV-474-RP, 2022 U.S. Dist. LEXIS 227466 (W.D. Tex. Oct. 13, 2022).

Coverage Limited to "Property Damage" Occurring During Policy Period

The insured was sued for damages stemming from an allegedly defective roof it installed that allowed damage to occur within the structure. Following a jury trial, a judgment was entered against the insured for reasonable costs of repairs, lost rental income as a result of the construction defects, disgorgement, and attorneys' fees, plus interest. Following the judgment, the matter was settled by the insured's two general liability insurers that issued policies to the insured for consecutive annual policy periods, the first insurer covering the years 2013 to 2014, with the second insurer covering the years 2014 to 2016. The second insurer thereafter commenced suit against the first, arguing that it had no duty to contribute to the settlement and therefore was entitled to reimbursement.

The second insurer argued that the property damage at issue began before its policy period took effect. In contrast, the first insurer argued that its policy only covered "property damage" that occurred during its policy period, and that it did not cover any damage that continues past the policy's expiration date, since an endorsement modified the insuring agreement to reflect as much. The court sided with the first insurer, noting that the precedent cited by the second insurer did not address coverage under policies whose language explicitly provides that coverage is limited to property damage that occurs during the policy period. The court went on to deny the second insurer's request for reimbursement, noting that the second insurer failed to present any evidence that the amount it contributed toward indemnity was for property damage that took place before its policy incepted.

2. *Liberty Ins. Corp. v. Omni Constr. Co.,* No. 4:21-cv-02119, 2022 U.S. Dist. LEXIS 172364, 2022 WL 4454368 (S.D. Tex. Sept. 23, 2022).

Liquidated Damage and Delay Costs do not Constitute "Property Damage" Caused by an "Occurrence"

The insured was retained to provide general contracting services for building a hotel. The owner of the project initiated an arbitration against the insured, alleging the insured breached its contractual obligations in connection with the project. The insured requested coverage in connection with the arbitration from its general liability insurer. The insurer tried to investigate the claim, but discovered the insured was out of business. The insured did not appear or participate in the arbitration, which resulted in a $5,000,000+ judgment for the insured's alleged breach of contract, plus arbitration expenses and attorneys' fees. The insurer then commenced suit against the insured and owner seeking a declaration that it did not owe coverage in connection with the arbitration award.

After determining Ohio law applied to the coverage dispute, the court found that the insurer's policy did not provide coverage for the damages specified in the arbitration award. Specifically, the arbitration award consisted primarily of liquidated damages, economic losses, and other losses stemming from the insured's defective work or delay. Under Ohio law, such damages do not constitute "property damage" caused by an "occurrence," and are, therefore, not covered.

3. *Mid-Continent Cas. Co. v. JTH Customs, Inc.,* No. 1:21-cv-00520-LY, 2022 U.S. Dist. LEXIS 117470, 2022 WL 2441855 (W.D. Tex. July 4, 2022).

"Property damage" and "defective work" Exclusions do not Preclude Duty to Defend

The insured was a homebuilder retained by a property owner to "build and/or design" a house at the owner's plot. The owner claimed that after moving into their house, which had not yet been completed, they began to experience problems such as mold, electrical issues, drainage, etc. The owner commenced suit against the insured, asserting claims for breach of contract, breach of warranties, conversion, common law and statutory fraud, breach of fiduciary duty, money had and received, unjust enrichment, and violation of various deceptive trade practices statutes. The insured tendered the suit to its general liability insurer, which agreed to provide the insured with a defense subject to a reservation of rights.

In the coverage litigation, the insurer argued that it owed no duty to defend or indemnify its insured in connection with the owner's suit on the basis that the

only claims by the owner were for the insured's defective work, which were barred by the policy's defective work exclusion. The insurer argued in the alternative that the policy's property damage exclusions (i.e., j(5) and j(6)) applied to bar coverage for damage to any part of the property because the insured was the general contractor working on the entire property. The court found that the defective work exclusion, which barred coverage for "costs associated with the removal or replacement of the defective, deficient or faulty work," did not bar coverage for the entirety of the claim, since there were allegations of damages to work that was not itself defective, deficient, or fault. Similarly, the court found that exclusion j(6) was inapplicable because there were allegations of damages to non-defective work. As to j(5), which the court said applied only to damage that occurs during the performance of construction operations, there was a question of fact regarding whether any of the alleged damage occurred after the project's completed. As such, the court determined the insurer owed a duty to defend.

Washington

1. *Corliss Condominium Owners Assn. v. Natl. Sur. Corp.,* No. C21-0200 TSZ, 2022 U.S. Dist. LEXIS 172671 (W.D. Wash. Sep. 23, 2022).

No Coverage under First-Party Property Policy

In this first-party property case, the insured sought coverage from two insurers on the risk between 2008 and 2013 for water intrusion to its building constructed in 1991. The insured and the insurers retained experts to inspect the building to determine the cause of the loss. The insured's expert concluded that wind-driven rain caused the water intrusion and that certain construction defects contributed to the intrusion. The insurers' expert determined that the construction defects were the primary cause of the damage combined with improper maintenance. The insurers, relying on their expert's conclusions, disclaimed based on policy exclusions for inadequate or defective construction of maintenance.

In the insured's suit for coverage, the insured and the insurers moved for summary judgment. The insured argued that the insurers must cover the water intrusion damages because the efficient proximate cause of the loss was wind-driven rain, a covered peril under the all-risk policies. The court, focusing on causation, determined that the insured's expert generally agreed with the insurer's expert's opinions that a properly constructed and maintained building should not be affected by wind-driven rain unless there was a pre-existing pathway in which the rain could enter. The court also focused on the insured's expert's deposition testimony that he would not expect to find the water damage at the insured's property if he designed the weather-resistant system himself. Thus, the court concluded that defective construction – not wind-driven rain – initiated the sequence of events that caused the water damage.

The court also rejected the insured's argument that water damage caused by wind-driven rain was an ensuing loss and, therefore, was an exception to the exclusion. Rather, the court found other cases in the district persuasive and agreed with those cases that such an interpretation would swallow the exclusion whole. ■

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