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February 4, 2010

Construction Defect: The Road Not Taken – by the Sixth Circuit

Appeals Court Addresses Two Different Paths For Analyzing CD Claims

My wife often chides me for choosing the wrong route to get somewhere. She sighs that if I had made a left here or a right there we would have arrived earlier. I don't have Nav in the car. I have Nag. But, truth be told, she is right. I do sometimes take the long way to get somewhere because I like going the way I know. I don't mind arriving two minutes later if it means taking the familiar route. Besides, half the time I don't even want to go where it is that we are going anyway.

However, when it comes to coverage for construction defects, the road chosen most definitely does matter. There is very little that policyholders and insurers agree upon when it comes to CD claims. But if there is one common ground, it is that no coverage is owed for the cost to repair or replace an insured's defective work. But any agreement on that point is sure to be short-lived -- as there are two different ways to arrive at that conclusion. And that's when the bickering starts again.

No coverage is owed for the cost to repair or replace an insured's defective work because either (1) the faulty work is not "property damage" and/or was not caused by an "occurrence" or (2) the faulty work is "property damage," that was caused by an "occurrence," but coverage is precluded by the "your work" exclusion. Same outcome – No coverage. But which route the court chooses to get to that destination can make a world of difference.

Earlier today the 6th Circuit Court of Appeals issued an opinion (published) that provides a straightforward example of why, if your destination is a construction defect claim, it matters a lot if you make a left here or a right there.

In *Cincinnati Ins. Co. v. Beazer Homes Investments, LLC*, the Sixth Circuit, applying Indiana law, addressed coverage for water damage to homes that Beazer Homes's predecessor had built as a general contractor. The damage was allegedly caused by faulty workmanship performed by Beazer subcontractors. Specifically, coverage was sought for the cost of repairing damage to properly constructed components of the homes that had been damaged by the water intrusion. *Beazer* at 1-2.

The Sixth Circuit was quick to explain that "Beazer sought coverage not for repair of the faulty work by the subcontractors, but for damage to *other* components of the houses caused by water
intrusion that resulted from the allegedly faulty workmanship." *Beazer* at 8 (italics in original). The district court had held that such damage was neither property damage nor caused by an occurrence and, therefore, was not covered. *Id*

While seemingly acknowledging that no coverage was owed for damage to its own work, Beazer argued that the case law to that effect "involved repairs only to the faulty components themselves, not the properly constructed parts of the houses that were damaged as a result of the faulty components." *Id.* at 10.

The Sixth Circuit was not moved. It responded that Beazer's argument ignored the Indiana Supreme Court's decision in *Ind. Ins. Co. v. DeZutti*, 408 N.E.2d 1275, 1280 (Ind. 1980) -- that the entire house is the general contractor's work. "Beazer, in other words, cannot successfully argue that damage to a properly constructed component of a house due to faulty workmanship on another component is 'property damage' under a CGL policy." *Id.*

The Sixth Circuit also concluded that the damage to the homes was not caused by an "occurrence." *Id.* at 15. [Although the court stated that it did not need to reach this issue because of its "no property damage" conclusion.]

Here is the real crux of the case and the take-away [although it is not explained by the court in so many words] – Beazer argued that coverage was owed on the basis of the "sub-contractor exception" to the "your work" exclusion. However, the Sixth Circuit responded that exclusions can not be interpreted to enlarge coverage. *Id.* at 11. "If the insuring cause does not extend coverage, one need look no further." *Id.* at 12. (citation omitted).

In other words, because Beazer failed to satisfy the policy's insuring agreement requirements – "property damage" caused by an "occurrence" – the court had no reason to reach the exclusions – in particular, the "your work" exclusion and, more importantly for Beazer, the exclusion's "sub-contractor exception."

Getting back to the beginning – while it is not disputed that no coverage is owed for the cost to repair or replace an insured's defective work, it matters which route is taken to get there:

- If a court rules that faulty workmanship is not "property damage" and/or was not caused by an "occurrence," then the claim never gets past the insuring agreement and the insured has no ability to reach the "sub-contractor exception" to the "your work" exclusion, in an effort to obtain coverage for the cost of repairing its properly constructed work that had been damaged by a sub-contractor's faulty work.

- If a court rules that faulty workmanship is "property damage," that was caused by an "occurrence," and, hence, the insuring agreement is satisfied, coverage for the insured's faulty workmanship is still precluded – now by the "your work" exclusion. But, alas, the insured can now reach the "sub-contractor exception" to

the "your work" exclusion, in support of a claim for coverage for the cost of repairing its properly constructed work that had been damaged by a sub-contractor's faulty work.

two roads diverged in a wood, and I --
I took the one less traveled by,
And that has made all the difference.

-- *Robert Frost*
[Wikipedia – How else would I know that.]

A copy of the Sixth Circuit's February 4 decision in *Cincinnati Ins. Co. v. Beazer Homes Investments, LLC* can be accessed here:

http://www.ca6.uscourts.gov/opinions.pdf/10a0021p-06.pdf

If you have any questions, please let me know.

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