BINDING AUTHORITY

Insurance Coverage Decisions: Issued Today - Impact Tomorrow

Randy J. Maniloff
maniloffr@whiteandwilliams.com

October 27, 2011

Sweet Defective-Home Alabama: Supreme Court Addresses The "Occurrence" Issue

"Sub-Contractor" Exception Applies – But Not To A Sub-Contractor's Own Work

Earlier this week I was in Las Vegas where I had the privilege of speaking at the CPCU Society's Annual Meeting (and paying $9 for a Diet Coke at a restaurant – Really, I have the receipt to prove it). In any event, at one point during the trip I was walking into a casino and was approached by a man who looked really down on his luck. "Please sir, can you help me?," he asked. "My wife is very sick and she needs medicine. I'll take anything you can spare," he pleaded. He seemed really sincere and I concluded that he was not just a professional pan-handler. So I was getting ready to put my hand in my pocket, but then hesitated at the very last second. "I'd like to help you," I said. "Really, I would. But how do I know you won't take this money and go straight into the casino and gamble with it?," I asked. "Oh, you don't have it worry about that," he assured me. "I got gamblin' money."*

While of course Nevada is well-known for gamblin' money, it is also the home of a fair amount of construction defect litigation. Personally, with the exception of the bathroom sink in my hotel room not draining as quickly as I would have liked, I saw no evidence of Nevada's wide-spread construction defect problems during my trip. But there was certainly a construction defect coverage development taking place elsewhere while I was there.

Last Friday the Supreme Court of Alabama issued a decision concerning coverage for construction defects that will likely cause a lot of people to take notice. *Town & Country Property, LLC v. Amerisure Insurance Co.* involves fairly pedestrian facts as these cases go. For convenience, I quote directly from the opinion as it succinctly summarizes things:

"In January 1999, Jones–Williams contracted with Town & Country Property to construct an automobile sales and service facility for T & C in Bessemer. Jones–Williams then entered into contracts with various subcontractors to construct the facility, **doing none of the actual construction work itself**; construction was completed in August 1999. Town & Country Ford then leased the facility from Town & Country Property and began operating a Ford automobile dealership on the premises. Thereafter, T & C discovered various defects in the facility. Jones–Williams was notified of the defects and apparently made some attempts to correct them; however, on October 3, 2002, T & C sued Jones–Williams in the Jefferson Circuit Court, asserting various tort and contract claims stemming from the alleged faulty construction of the facility. Jones–Williams notified its insurer, Amerisure, of the action, and Amerisure agreed to provide a defense in accordance with the terms of the Amerisure policy. T & C's claims against Jones–Williams were tried before a jury, and on September 4, 2007, the jury returned a verdict in favor of T & C, awarding Town & Country Ford $34,100 and Town & Country Property $616,000. Following the entry of a judgment on the verdict, Amerisure indicated that it would not indemnify Jones–Williams for the judgment entered against it, and on October 30, 2007, T & C initiated the action underlying these appeals, alleging that the award entered against Jones–Williams was covered by the Amerisure policy and seeking payment from Amerisure. Amerisure denied liability and filed a counterclaim seeking a judgment declaring that there had been no occurrence or accident triggering coverage under the Amerisure policy and that, even if there had been an occurrence, the policy excluded coverage for damage caused by Jones–Williams's own faulty work. T & C argued that the faulty construction of the facility was itself an occurence triggering coverage and that the damage was not the result of Jones–Williams's work but the work of the subcontractors Jones–Williams had employed." *Town & Country Property* at 3-4 (emphasis added).

For starters, the *Town & Country Property* court was not writing on a clean slate. This was not the first time that the Supreme Court of Alabama has addressed coverage for construction defects. The court summarized the state of the law in Alabama, concerning coverage for construction defects, as follows: "[W]e may conclude that faulty workmanship itself is not an occurrence but that faulty workmanship may lead to an occurrence if it subjects personal property or other parts of the structure to 'continuous or repeated exposure' to some other 'general harmful condition' ... and, as a result of that exposure, personal property or other parts of the structure are damaged." *Id.* at 14.

In essence, the supreme court described Alabama's view on coverage for construction defects in a manner that is consistent with many courts around the country – Damage to the insured's own defective work is not considered to have been caused by an "occurrence," but consequential damage caused by the insured's defective work is considered to have been caused by an "occurrence."

At issue in *Town & Country Property* was how these rules apply to an insured that built a structure, that turned out to be defective, where the insured used various subcontractors and did none of the actual construction work itself. In other words, the insured was a

"paper GC," which is not an uncommon scenario as those involved with these types of claims can attest.

The *Town & Country Property* court set out a lengthy discussion of the history of the CGL policy with respect to the "your work" exclusion and the "sub-contractor" exception. As you would expect, the court addressed (1) the 1973 version of the ISO CGL form, which precluded coverage for property damage to work performed by *or on behalf of* the named insured (*i.e.*, no subcontractor exception); (2) the 1976 Broad Form Property Damage Endorsement, which eliminated the "on behalf of" language, thereby providing coverage for the insured's completed work when the damage arose out of work performed by a subcontractor; and (3) the 1986 version of the ISO CGL Form, in which the subcontractor exception aspect of the Broad Form Property Damage Endorsement was added directly to the body of the ISO CGL policy in the form of the express "sub-contractor" exception to the "Your Work" exclusion. *Id.* at 7-9.

The *Town & Country Property* court described the "Your Work" exclusion and "Sub-Contractor" exception as follows:

In practical effect, the your-work exclusion and the subcontractor exception operate to exclude coverage for property damage caused by work performed by the insured contractor on his own behalf but to restore coverage for property damage caused by work performed by a subcontractor on behalf of the insured contractor. Both the your-work exclusion and subcontractor exception are implicated, however, only if there is first determined to be an "occurrence."

Id. at 10-11.

Following all of this background, the *Town & Country Property* court held that no coverage was owed for damages that represented the costs of repairing or replacing the faulty work itself -- notwithstanding that such work was performed by a sub-contractor of the insured.

On the other hand, coverage was owed for damaged personal property—e.g., computers and furnishings—or otherwise non-defective portions of the facility. "Those damages would constitute 'property damage' resulting from an 'occurrence,' and they would be covered under the terms of the Amerisure policy in light of the fact that all the construction work in this case was performed by a subcontractor and therefore the damage suffered as a result of that construction work would fall within the subcontractor exception to the your-work exclusion." *Id.* at 18-19.

<u>In summary</u>, simply because the defective work was performed by a sub-contractor, the "sub-contractor" exception to the "Your Work" exclusion did not create coverage for such defective work. This defective work was still not caused by an "occurrence," and, therefore, not covered. Instead, the subcontractor exception provided coverage for damage to non-defective portions of the facility (*i.e.*, the named insured's non-defective work that was damaged by the work of a subcontractor).

A copy of the October 21st decision from the Supreme Court of Alabama in *Town & Country Property, LLC v. Amerisure Insurance Co.* is attached.

Please let me know if you have any questions.

Randy

Randy J. Maniloff
1650 Market Street | One Liberty Place, Suite 1800 | Philadelphia, PA 19103-7395
Direct 215.864.6311 | Fax 215.789.7608
maniloffr@whiteandwilliams.com | whiteandwilliams.com

The views expressed herein are solely those of the author and are not necessarily those of his firm or its clients. The information contained herein shall not be considered legal advice. You are advised to consult with an attorney concerning how any of the issues addressed herein may apply to your own situation. The term "Binding Authority" is used for literary purposes only and is not an admission that any case discussed herein is in fact binding authority on any court. If you do not wish to receive future emails addressing insurance coverage decisions, please send an email to the address listed above with "unsubscribe" in the subject line. No animals were harmed in the drafting of this e-mail.