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**INSURANCE COVERAGE FOR CONSTRUCTION DEFECTS:
ARE PERFORMANCE BONDS STILL RELEVANT?**

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INTRODUCTION¹

Most involved in the construction industry, including contractors, owners, and insurance and surety claims representatives, would likely agree that there is a clear and discernible dividing line between the risks covered by general liability insurance coverage and those that are addressed by performance and payment bonds. Bonds, of course, are intended to guard against the consequences of a contractor's failure to perform in accordance with the contract requirements; insurance coverages are intended to protect the owner and the general public if the contractor damages something or someone during the course of the work. Accordingly, it is often assumed that if a loss, cost, or expense is covered under a performance or payment bond, it would not be covered under a general liability policy, and vice-versa.

Additionally, the traditional view, especially among general liability insurance underwriters is that the consequences of poor workmanship are not covered by insurance products. This concept is exemplified by the oft-quoted passage from the New Jersey Supreme Court:

¹ The author gratefully acknowledges the assistance of Shirley Cox, Drake Blackmon and James Harred in the preparation of this article. The issues discussed herein have been the subject of several excellent articles and publications, including Berry and McNally, *Recent Developments in Insurance coverage for Construction Defects*, Reuters, *Commercial General Liability*, coverage for Construction Defects and Ostrager and Newman, *Insurance Coverage Disputes*, 4th Edition.

The consequence of not performing well is part of every business venture; replacement or repair of faulty goods and works is a business expense, to be borne by the insured-contractor in order to satisfy customers.

There exists another form of risk in the insured-contractor's line of work, that is, injury to people and damaged property caused by faulty workmanship. Unlike business risks of the sort described above where, one the tradesmen commonly absorbs the costs attendant upon the repair of his faulty work, the accidental injury to property or persons substantially caused by his unworkmanlike performance exposes the contractor to almost limitless liabilities. While it may be true that the same neglectful craftsmanship can be the cause of both a business expense of repair and a loss represented by damage to persons and property, the two consequences are vastly different in relation to sharing the costs of such risks as a matter of insurance underwriting.²

Much has changed since the famous *Weedo* case. The economic expansion and building boom of the last decade or so has, among other things, spawned a firestorm of litigation over construction defects and deficiencies. A survey of the reported cases suggests that the risks addressed by surety bonds and standard commercial general liability insurance policy are no longer mutually exclusive. In some jurisdictions, courts have found insurance coverage for construction problems and consequences thereof which traditionally would not constitute either an "occurrence" or "property damage" so as to come within the umbrella of insurance coverage. Moreover, changes to the insurance contract – in particularly exceptions to exclusions for work performed by subcontractors – have broadened the scope of coverage for construction defects significantly beyond traditional expectations.

This paper is intended as a guided tour of the boundary between the coverages provided by surety bonds and insurance policies. Our focus will be on how the courts have interpreted the "occurrence" requirement for coverage under the basic insuring agreement and, assuming that a given claim scenario presents an "occurrence", what is required to constitute "property damage" for coverage purposes, and how the various "builder's risks" exclusions have been interpreted recently. Our objective is to assist the surety claims professional in how to "use" the principal's pre-existing, pre-paid insurance coverage as a means to reduce the surety's exposure.

I. COVERAGE BASICS – THE FORTUITY REQUIREMENT

A fundamental assumption in the insurance marketplace, existing no doubt from the first cups of coffee served at Lloyds, is that insurance is not available for losses that the insured is aware of, has planned, or is substantially certainly will occur. As stated by a New York Judge:

² *Weedo v. Stone-E-Brick, Inc.*, 405 Atl.2d, 792 (NJ 1979).

The concept of insurance is that the parties, in effect, wager against the occurrence, or non-occurrence of a specified event; the carrier insures a risk, not a certainty.³

The “fortuity” requirement is often said to be implicit in every contract of insurance. As stated by Professor R.E. Keeton:

A requirement that the loss be accidental in some sense in order to qualify as the occasion for liability of an insurer is implicit, when not expressed, because of the very nature of insurance.⁴

Prior to 1966, the standard general liability insurance policy incorporated the “fortuity” element by use of the term “accident” in the basic Insuring Agreement. Thereafter, the ISO standard form comprehensive general liability (CGL) policy was modified to provide coverage for:

All sums which the Insured shall become legally obligated to pay as damages....caused by an “occurrence”...

Occurrence has, in turn, become defined as:

An accident, including continuous or repeated exposure to conditions, which results, during the policy period, in bodily injury or property damage *neither expected nor intended from the standpoint of the insured.*

With some slight modification, the “occurrence” element is maintained in most contemporary insurance policies. The current CGL insuring agreement reads as follows:

We will pay those sums that the Insured becomes legally obligated to pay as damages because of “bodily injury” or “property damage” to which this insurance applies...this insurance applies to “bodily injury” and “property damage” only if:

(1) the “bodily injury” or “property damage” is caused by an “occurrence” that takes place in the “coverage territory”; and

(2) the “bodily injury” or “property damage” occurs during the policy.⁵

The current CGL policy contains four exclusions which are commonly referred to as “builder’s risk” or “work product” exclusions. The most frequently discussed is exclusion (L), commonly referred to as the “your work” exclusion. The CGL policy excludes from coverage the following types of damages:

³ *Larsen v. Roanoke International Agency*, 875 F.2d 856 (2nd Cir. 1989).

⁴ *R.E. Keeton Insurance Law* §5.4(a) (at p.288 1971).

⁵ Form #CG 00 01 07 98, Insurance Services Offices, Inc. 1997.

(L). Damage to Your Work

“Property damage” to “your work” arising out of it or any part of it and included in the “products completed operations hazard”.

This exclusion does not apply if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor.⁶

In order for a “construction defect” to constitute or to be covered under the standard ISO CGL policy, the defect must be both an “occurrence” and result in “property damage” within the meaning of the policy. Additionally, the damage must not fall within the scope of any of the policy exclusions. Not surprisingly, the courts have varied in their approaches to determining whether a construction problem constitutes an “occurrence”, if so, whether there are “property damages” within the meaning of the policy, and if so, whether such damage is excluded.

II. INTERPRETING THE INSURANCE CONTRACT – TRADITIONAL RULES OF CONSTRUCTION

Once the insurance contract has been drafted and introduced into the marketplace, it is subject to interpretation and enforcement by the judicial system. Over the years the courts have developed an extensive network of “rules of policy construction” which may, on occasion, lead to a result which may be inconsistent with the intent of the underwriter. It is not surprising, therefore, that courts have differed as to the interpretation as to what constitutes an “occurrence” and “property damage” within the meaning of a general liability insurance policy.

There is near universal agreement that insurance contracts, like all agreements, should be interpreted as to effectuate the intent of the parties at the time the contract was formed.⁷ A proper interpretation of an insurance contract requires that it must be “read as a whole” to determine what the parties reasonably intended.⁸

An insurance policy will be given its “plain meaning” without resort to rules of construction unless there is an “ambiguity”.⁹ Most courts have stated and agree that clear and unambiguous terms in an insurance policy are to be taken and understood in their plain, ordinary, and popular sense, and that any clause in a policy is valid so long as it is “clear, unambiguous and not in contravention of public policy”.¹⁰ If an insurance contract is not “clear and unambiguous”, what result? First, most courts hold that extrinsic evidence – that is, evidence outside the written contract – can be consulted to determine the “true intent of the parties”. Thus, if it is determined that a word or phrase in an insurance policy is reasonably susceptible to more than one meaning or construction, a court can look outside the policy in an effort to determine what the parties to the insurance contract actually intended. Alternatively, a

⁶ “Your work” is defined as “work or operations performed by you or on your behalf” and “materials, parts or equipment furnished in connection with such work or operations”.

⁷ See *Uniroyal, Inc. v. Home Insurance Company*, 707 F.Supp. 1368 (E.D.N.Y. 1988).

⁸ See *Enterprise Tools, Inc. v. Export-Import Bank of the United States*, 799 F.2d 437 (8th Cir. 1986).

⁹ See *National Fidelity Life Ins. Co. v. Karaganis*, 811 F.2d 357 (7th Cir. 1987).

¹⁰ See *Reska v. Farm Bureau Mutual Ins. Co.*, 314 NW2d (MI 1982).

court can apply any number “rules of construction”, the most famous and universally applied of which is undoubtedly the “contra-insurer rule”. As stated by the Supreme Court:

The general rule...is...that where a policy of insurance is so framed as to leave room for two constructions, the words used should be interpreted most strongly against the insurer.¹¹

The rule of construction in favor of the insured and against the insurer is undoubtedly rooted in the notion that contracts of insurance, which are prepared by insurance companies, are intended for their own financial benefit. The majority of jurisdictions employ some version of this rule, often in conjunction with a variation on this theme which is known as “reasonable expectations” doctrine. Under the “reasonable expectations” test, policy language should be construed so as to achieve the objectively reasonable expectations of the insured. This tool for policy interpretation has become very popular, and appears to be followed in at least 32 jurisdictions.¹² In some courts, application of the doctrine of “reasonable expectation” does not require the court to determine that ambiguity exists.

III. DUTIES AND RESPONSIBILITIES OF THE CGL CARRIER

Whatever the status of the law in a given jurisdiction regarding coverage for construction defects may be, it is useful for the surety to appreciate that presentation of a claim against an insured creates a number of specific duties and responsibilities on the part of the general liability carrier. For example, the law of Alabama imposes rigorous duties on the carrier and defense counsel which essentially provides that any benefit of the doubt with respect to coverage goes to the insured. In the construction defect context, the rules can favor and benefit the surety.

(1) DUTIES UPON RECEIPT OF CLAIM

It is generally agreed that a carrier, upon receipt of a claim or suit against its insured, has the duty to investigate the claim and its policy to determine if it must defend its insured. Ordinarily, the duty to defend will be determined by an examination of the complaint, (the so-called “four corners” test), however, it is also clear that if there is any doubt as to whether the complaint alleges facts within the scope of coverage, the carrier must investigate the background facts and consider evidence which **might** be offered to determine its defense obligation.¹³

¹¹ See *Liverpool & London and Globe Ins. Co. v. Kearney*, 180 U.S. 182 (1901).

¹² The reasonable expectations doctrine is recognized in the court of Alabama, Alaska, Arizona, California, Colorado, Delaware, the District of Columbia, Georgia, Hawaii, Indiana, Iowa, Kansas, Kentucky, Maine, Massachusetts, Michigan, Minnesota, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, New York, North Carolina, North Dakota, Pennsylvania, Rhode Island, Texas, West Virginia, and Wisconsin.

¹³ See *Ladner & Co. v. Southern Guaranty Ins. Co.*, 347 So.2d 100 (Ala. 1977); *Tanner v. State Farm Fire & Casualty Co.*, 874 So.2d 1058 (Ala. 2003).

It is frequently said that the insurer's defense obligation is "broader" than is the indemnity obligation. Accordingly, if the complaint or the background facts and circumstances demonstrate the existence of a claim within the scope of coverage, the insurer must defend, regardless of the ultimate outcome of the claim or suit.

(2) THE ENHANCED OBLIGATION OF GOOD FAITH

Under Alabama law and in most jurisdictions, if the carrier elects to defend pursuant to a unilateral reservation of rights, the carrier inherits an additional obligation of "good faith" which creates additional duties in favor of the insured, including:

- (a) the carrier must perform a complete investigation of the underlying accident/occurrence the nature of the plaintiff's damages;
- (b) the carrier must retain competent defense counsel for its insured, and must make certain that both the insured and counsel appreciate that the insured is the counsel's only client;
- (c) the insurer must keep the insured "fully informed" as to all developments including settlement offers made by the carrier, and
- (d) the insurer must not engage in any conduct which would demonstrate a greater concern for its financial interest than that of its insured.

DUTY TO SETTLE

Regardless of whether the defense is undertaken pursuant to a reservation of rights or not, the carrier is under an obligation to protect its insured from the consequences of an adverse verdict and has a duty to settle under certain circumstances, the breach of which can give rise to the action for "bad faith" by the insured. In determining its obligation to settle, the carrier is required to consider the following factors:

- (a) anticipated range of an adverse verdict;
- (b) the strength and weaknesses of the case;
- (c) the verdict history in the court in question;
- (d) the relative appeal or attractiveness of the case to the fact finder;
and
- (e) prospects for an appeal in the even of an adverse verdict.

A successful navigation through these waters can be a challenge for the CGL carrier, particularly in the context of a complicated construction defect case. The inevitability of defense costs, difficulties and expense inherent in obtaining a judicial declaration of coverage,

and the carrier's desire to avoid extra-contractual entanglements can all assist in developing a favorable climate for settlement, whatever the law of the particular jurisdiction may be.

IV. RECENT DECISIONS

The current state of the law as to coverage for construction defects is a function of the application of these rules of construction by the 51 common law jurisdictions that comprise our judicial system. That there has been some divergence of views as to the appropriate interpretation in the construction defect context should not be a surprise.

Three basic approaches to the interpretation of the CGL Insuring Agreement have developed. We will briefly discuss each of them.

THE MAJORITY VIEW: A CONSTRUCTION DEFECT IS AN
"OCCURRENCE" ONLY IF THERE IS DAMAGE TO
"OTHER PROPERTY".

The majority of jurisdictions require a showing of damage to "other property" – that is property other than the work itself – before there can be coverage. Under this approach, a defect in a retaining wall for a swimming pool would not constitute an "occurrence" because there was no damage to anything other than the pool wall itself. The coverage inquiry focuses on whether the thing that is damaged and in need of repair was built or constructed by the insured; if so, there is no "occurrence" and no insurance coverage. Conversely, if the thing that is damaged was the result of faulty workmanship by another contractor other than the insured, the resulting damage may be an "occurrence" and may be within the scope of the insurance policy.

An example of this approach from the Supreme Court of South Carolina is *L-J, Inc. v. Bituminous Fire & Marine Insurance Co.*¹⁴, which involved deteriorating roads which were constructed in 1990. Due to negligence in the preparation of the road bed, failure to compact fill materials during the construction, defects in the design of a drainage system, and poor curb design, the road surfaces begin cracking and the governmental owner sued. The contractor (L-J, Inc.) notified its CGL carrier, who filed a declaratory judgment action to determine whether it was obligated to defend the action. After losing in the Court of Appeals, Bituminous appealed to the Supreme Court, arguing that the lower court had mistakenly ruled that the alligator cracking in the road surface constituted an "occurrence" within the meaning of its policy.

The Supreme Court unanimously agreed, noting that all of the negligent acts of a contractor caused damage to the roadway system only, which does not fall within the contractual definition of "occurrence". The South Carolina court summarized its decision as follows:

While it may be true that the same neglectful craftsmanship can be the cause of both a business expense of repair and a loss

¹⁴ 621 S.E.2d 33 (SC 2005).

represented by damage to persons and property, the two consequences are vastly different in relation to sharing the cost of such risks as a matter of insurance underwriting. In this regard Dean Henderson has remarked: the risks intended to be insured is the possibility that the goods, products, or work of the insured, once relinquished or completed, will cause bodily injury or damage to property other than the product or completed work itself, and for which the insured may be found liable. The insured, as a source of goods or services, may be liable as a matter of contract law to make good on products or risks which is defective or otherwise unsuitable because it is lacking in some capacity. This may even extend to an obligation to completely replace or rebuild the deficient work or product.

This liability, however, is not what the coverages in question are designed to protect against. The coverage is for tort liability for physical damages to others and not for contractual liability of the insured for economic loss because the product or completed work is not that for which the damaged person bargained.¹⁵

The South Carolina court offered an example of what *would* constitute an “occurrence” in the form of a hypothetical bicycle rider who encountered the cracking in road surface and thereby suffers an injury. Such an accident, reasoned the court, would constitute an “occurrence” which would be the subject of the contractor’s CGL policy. The mere damages to the roadway itself are not covered.

MINORITY VIEW #1 – NO “OCCURRENCE” EVEN IF THERE IS
DAMAGE TO “OTHER PROPERTY”

Some jurisdictions, including Illinois, Maryland, and Mississippi, have adopted approaches which are more favorable to the insurance industry, and which focus on the volitional/intentional nature of the construction process. The rationale of these courts is that because the act of building a structure is intentional, the fact that the work product does not meet the specifications or contractual requirements does not generate insurance coverage. As stated by an Illinois Appellate Court:

“If any contractor uses inadequate building materials, or performs shoddy workmanship, he takes a calculated business risk that no damage will take place. If damage does take place, it flows as an ordinary and natural consequence of the contractor’s failure to perform the construction properly or as contracted.”¹⁶

Similarly, the Fifth Circuit, applying Mississippi law, disallowed coverage for damage resulting from roof leaks, noting that the “action of installing the membrane was not accidental

¹⁵ The internal quote is from *Henderson, Insurance Protection for Products Liability and Completed Operations – What Every Lawyer Should Know*, 50 Neb. L. Rev. 415 (1971).

¹⁶ *Viking Construction Management v. Liberty Mutual Ins. Co.*, 831 NE2d 1, p. 8 (Ill.App.Ct. 2005).

nor unintended to implicate coverage under the policy". Accordingly, the resulting damages were a foreseeable result of faulty workmanship and not an "accident".¹⁷

MINORITY VIEW #2 – NO DAMAGE TO "OTHER PROPERTY" IS
REQUIRED TO CONSTITUTE AN "OCCURRENCE"

A few insured – friendly jurisdictions have jettisoned any requirement for damage to "other property" and hold that damage to work performed by a contractor is covered – period. As a common thread uniting the approach of these jurisdictions is the absence of a definition for the "accident" which is utilized in the internal definition of "occurrence" in the standard CGL policy. Two good examples are from Wisconsin:

"The windows leaked. This is an accident. So, we have property damage caused by an occurrence and the policy applies."¹⁸

And from Florida:

"The term 'accident' encompasses not only accident events, but also injuries or damages neither expected nor intended from the standpoint of the insured".¹⁹

An example of the trend toward expansion of coverage for construction defects is provided by the Tennessee Supreme Court's recent decision in *Travelers v. Moore & Associates, Inc.*, which involved an arbitration demand which alleged water entry and resulting damages to wall and floor systems. The insured (Moore & Associates), was the design/build contractor for the project; Moore subcontracted the installation of the windows. Upon receipt of the arbitration demand, Moore asked Travelers to defend; Travelers declined, and filed a declaratory judgment action in which it sought a determination that it had no duty to defend or indemnify Moore, reasoning that because the damages sought by the owner were caused by alleged faulty workmanship, there could be no coverage under the general liability policy.

In rejecting Travelers' arguments, the Tennessee court reviewed and distinguished a previous decision (*Vernon Williams*) which held that there was no coverage for faulty work. The *Williams* decision had been based in large part upon the *Weedo* case. However, the Tennessee Supreme Court concluded that neither *Weedo* nor *Williams* was properly decided because they both focused on the *exclusions* and not upon the Insuring Agreement of the CGL policy. Accordingly, the Tennessee court's analysis focused on whether the allegations of the claimant against Moore constituted an "occurrence".

In finding that there was an "occurrence", the court noted that the policy defined an "occurrence" as an "accident", and the Tennessee law defines an "accident" to include negligent acts causing damages which are not intended or expected. Viewing the "foreseeability of damage" issue from the perspective of the insured, the court next concluded

¹⁷ *ACS Construction Co., Inc. of Mississippi v. GCU*, 332 F.3d 885 (5th Cir. 2003).

¹⁸ *Kalchthaler v. Keller Construction Co.*, 591 NW2d 169 (Ws.Ct.App. 1999).

¹⁹ *State Farm v. CTC Development Corp.*, 720 So.2d 1072 (Fl. 1998).

that it would be illogical to assume that Moore expected or intended that the windows would be improperly installed by its subcontractor, and that defining the term “accident” in such a restrictive manner would “render a CGL (policy) almost meaningless”. The centerpiece of the Tennessee court’s reasoning was its “defective shingle” analogy. An improperly installed shingle which falls from the roof causing injury to a passerby would clearly constitute an “occurrence” within the meaning of the policy. A shingle which admits water into the building and causes damage, said the court, should be treated no differently. Any concerns that such an interpretation will transform the CGL policy into a performance bond – such as was voiced by Travelers – were unfounded, because whether coverage exists for an “occurrence” within the meaning of the Insuring Agreement will still depend upon whether coverage is ultimately excluded on one or more of the policy exclusions.

Having determined that the defective window installation constitutes an “occurrence”, the court had little difficulty in finding an allegation of “property damage” in the arbitration demand:

We conclude that Hilcomb’s claim is not limited to faulty workmanship and does in fact allege “property damage”. Moore’s subcontractor allegedly installed the windows defectively. Without Moore, this alleged defect is the equivalent of the “near inclusion of a defective component” such as the installation of a defective tire, and no “property damage” has occurred. The alleged water penetration is analogous to the automobile accident that is caused by the faulty tire. Because the alleged defective installation resulted in water penetration causing further damage, Hilcomb has alleged “property damage”. Therefore, we conclude that Hilcomb has alleged damages that constitute “property damage” for purpose of the CGL.

Finally, the court considered whether the “your work” exclusion barred the Hilcomb claim. Because of the subcontract exception, the court concluded that although the phrase “your work” referred to the hotel which was designed and built by the insured, the “subcontractor exception” removed the claim from the exclusion. Accordingly, Travelers was ordered to defend its insured.

V. THE PROPERTY DAMAGE REQUIREMENT

Assuming that an “occurrence” has taken place, fitting a construction defect claim within the four corners of the CGL policy requires a showing of “property damage”, which is defined as follows:

- (a) physical injury to tangible property, including all resulting loss of use of that property. All such loss of use shall be deemed to occurred at the time of the physical injury that caused it or
- (b) loss of use of tangible property that is not physically injured. All such loss shall be deemed to occur at the time of the occurrence that caused it.

Given this definition and the positive language restricting coverage to damage “to which the insurance applies”, most courts have held that the cost of repairing and replacing defective work is not covered. Other “property damage” must be present before there can be coverage. An example from Georgia, a contractor was engaged to install a second story on a one-story building. The contractor damaged both the first and second stories during construction. The damage to the original structure was found to be within the scope of coverage; the damage to the second story, which was the insured’s work product was not.²⁰

In a similar example from Alabama²¹, a school board sued for leaks to the interior of the building and its roof membrane damaged by recurring roof leaks. The Alabama Supreme Court held the damages for repairing the defective roof were excluded from coverage, but the claim for damages involving the ceiling, floor, and other building components triggered the carrier’s duty to defend and indemnify.

A few jurisdictions, including Florida, appear to hold that once it is determined that there is damage to “other property” apart from the insured’s own “work product”, all damages to the structure are within the scope of coverage. This was the holding of an intermediate Florida appellate court in *J.S.U.V. v. U.S. Fire Insurance Company*²² which involved several homes built by a contractor which experienced extensive damage due to faulty foundations. The Appellate Court ruling has resulted in a split of authority among the Florida Appellate Courts, which will be addressed in the near future by the Florida Supreme Court. The reasoning of the Florida Appellate Court appears to be similar to that of the Tennessee Supreme Court in the recent *Travelers* decision.

VI. THE “BUILDER’S RISK” EXCLUSIONS

The current ISO CGL policy contains four exclusions which may apply to construction defect claims. Like all exclusions, courts will interpret them narrowly, so as to minimize any loss of coverage in favor of the insured. While the “builder’s risk” exclusions are frequently lumped together for purposes of judicial review, they are intended to address separate and distinct hazards arising out of the work and products performed by the insured.

EXCLUSION J – DAMAGED PROPERTY

Like all of the “builder’s risk” exclusions, exclusion J is tedious. In pertinent part, it purports to exclude coverage for injury to real property damaged during the course of operations (subsection 5) and that particular part of any property that must be restored, repaired or replaced because “your work was incorrectly performed on it”. If this damage to the work or other property occurs after completion of the contractor’s operations, these exclusions are inapplicable.

²⁰ *Sawhorse, Inc. v. Southern Guaranty Ins. Co. of Georgia*, 604 SE2d 541 (Ga. Ct. App. 2004).

²¹ *U.S.F & G v. Bonitz Insulation Co.*, 424 So.2d 569 (Ala. 1982).

²² 906 So.2d 303 (Fla. Dist. Ct. App. 205).

EXCLUSION L – DAMAGE TO YOUR WORK

This exclusion provides that damage to the contractor's work is excluded from coverage. The work product exclusion does not apply if the damaged work was performed by a subcontractor.

EXCLUSION M – DAMAGE TO IMPAIRED PROPERTY OR PROPERTY NOT PHYSICALLY INJURED

This exclusion is most frequently involved in situations where defective or deficient work has caused "loss of use" of the finished product. It has been applied to eliminate coverage for damages arising out of the improper installation of a portable ice rink²³ and in denial of the claim for loss of use of a building which was not "physically injured".²⁴

EXCLUSION N – RECALL OF PRODUCTS, WORK OR IMPAIRED PROPERTY

This section broadens and extends the scope of exclusion (M). It does not follow the format of the insuring agreement or the other exclusions which make exceptions in the case of work performed by subcontractors. Here again, exclusion M – like all of the "builder's risk" exclusions – will not apply when there is "property damage" to "other property".

CONCLUSION

Notwithstanding the expansion of CGL coverage for construction defects in some jurisdictions, the risks addressed by traditional performance and payment bonds and general liability coverages are separate and distinct. CGL policies have no application in the typical contractor default scenario, where the problem is essentially that the work has not been finished. However, where poor construction techniques, questionable design, sloppy contract administration, or exposure to weather or toxic chemicals caused damage or deterioration to the contractor's work product, the surety's interest in the contractor's general liability insurance program will be enhanced. A basic understanding of the law of jurisdiction and how coverage for construction defects is or could be interpreted may assist the surety in mitigating or in some cases avoiding a loss.

²³ 847 F. Supp. 947 – (Md.Fla. 1994).

²⁴ *Westfield Ins. Co. v. Coastal Group, Inc.*, 2006 WL 120041 (Oh. Ct. App. January 18, 2006).