

The Construction Defect Coverage Conundrum: Tips for Evaluating Insurance Coverage for Construction Defect Claims

Presented By:



Brian Richardson



Brandon Clapp

swift / currie

Construction Defect Basics

- A construction defect occurs when construction fails to perform as expected or intended and the failure causes physical injury to an individual, the work itself or other property or work
- Construction defect litigation is on the rise
- When property owners or developers sue contractors for construction defect claim, contractors turn to their commercial general liability (CGL) insurers for coverage
- Whether a construction defect claim is covered by a CGL policy requires an understanding of the factual allegations of the claim, the policy and the applicable state law



The Insuring Agreement

The typical CGL policy only provides coverage if a claim alleges “property damage” caused by an “occurrence”

- “Occurrence” usually defined as “an accident, including continuous or repeated exposure to the same general harmful conditions”

States differ on whether faulty work is an occurrence or not

- Historical approach: Faulty work is not an occurrence
- Middle ground: Faulty work may become an occurrence (AL and GA)
- Modern trend: Faulty work is an occurrence

Occurrence must take place during the policy period

- Exposure Theory
- Manifestation Theory (AL)
- Continuous Trigger Theory (GA)
- Injury-in-fact Theory

Defining Property Damage

- “Property damage” is defined as physical injury to tangible property, including all resulting loss of use of that property
- Adjectives “physical” and “tangible” generally limit the scope of coverage for diminution in value damages and economic losses



Products-Completed Operations Hazard

- The basic CGL policy does not provide coverage for completed operations and products hazards
- Products-completed operations hazard provides coverage for claims occurring after construction is completed
- If the policy includes products-completed operations hazard coverage, the policy's exclusions for damage caused by the insured's work or product will be nullified under Alabama law



Common Business Risk Exclusions

Damage to Your Product

"Property damage" to "your product" arising out of it or any part of it.

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.

Damage to Impaired Property

"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.

Other Common Exclusions



Intentional Acts Exclusion



Mold/Fungi Exclusion



EIFS Exclusion



Roofing Exclusion

To Defend or Not to Defend – That is the Question



Identify proper state law

Four corners rule
Reasonable expectations doctrine
Extrinsic evidence



Review the complaint

Identify facts
Identify potential mixed claims
Compare with insurance policy



Review information provided by the insured or claimant

Extrinsic evidence can be considered to resolve coverage in favor of the insured but not to the insured's detriment

Reservation of Rights and Disclaimer Letters



Reservation of Rights

- Send ROR letter at the same time as assigning defense counsel
- Defending without an ROR letter may waive the right to contest coverage
- Must be sent to all insureds
- Include all grounds for forfeiture



Denying Coverage

- Ensure proper investigation is completed
- Discuss factual basis of the claim
- Explain all grounds for denial
- Must be sent to all insureds
- Invite insured to submit additional information for reconsideration

Roll Tide or Go Dawgs?

Key Differences Between Alabama and Georgia Law

- **Trigger of Coverage for Construction Defects**

- Alabama: Manifestation Theory – The time of an “occurrence” is not the time the wrongful act is committed, but the time the complaining party was actually damaged
- Georgia: Continuous Trigger Theory – Exposure during dates of coverage to conditions that result in property damage constitutes an “occurrence”

- **Rip and Tear Costs**

- Alabama: Removal of insured’s work to get to defective work is property damage if the removal was necessary to remediate damage to “other property”
- Georgia: Business risk exclusions likely exclude coverage for removing and replacing defective work

- **Application of Business Risk Exclusions**

- Alabama: “Your work” exclusion will not apply if the insured purchases coverage for damages included in the “products-completed operations hazard”
- Georgia: “Your work” exclusion will be enforced and apply to work performed by the insured

Intervention and Declaratory Judgment Actions

- **Intervening in the underlying action**

- Claims involving potential covered and non-covered claims
- Seek intervention to issue special interrogatories to the jury or jury verdict forms to provide clarity on coverage
- Alabama courts generally disfavor intervention by insurers
- Georgia courts generally permit insurers to intervene

- **Declaratory judgment actions**

- Most called-upon method to adjudicate insurance coverage disputes
- Used to determine the duty to defend when ROR letter is issued
- Used to determine the duty to indemnify after trial or settlement
- Federal court declaratory judgments require diversity of citizenship and proof the amount in controversy exceeds \$75,000



Pass the Trash: Risk Transfer in Construction Defect Claims

Indemnification Agreements

- Common practice for owners to require general contractors to defend and indemnify them for claims arising out of the work and for general contractors, in turn, to require subcontractors to defend and indemnify them and the owner for claims arising out of the subcontractor's work
- States differ on the extent a party can require another to indemnify them for one's own negligence
- General contractor's CGL insurer should identify potential risk transfer upon receipt of claim and make sure to timely place any lower tier contractors on notice

Additional Insureds

- Common practice for owners to require general contractors to name them as additional insureds under the general contractor's CGL policy and for general contractors, in turn, to require subcontractors to name them and the owner as additional insureds
- Not all additional insureds are treated equally, so it is important to know what type of additional insured provision is included in the policy

Other Insurance

- Determine what insurance policy is primary v. excess

QUESTIONS & ANSWERS

s/c

THANK YOU!



Brian Richardson
brian.richardson@swiftcurrie.com
205.314.2404



Brandon Clapp
brandon.clapp@swiftcurrie.com
205.314.2406

swift / currie