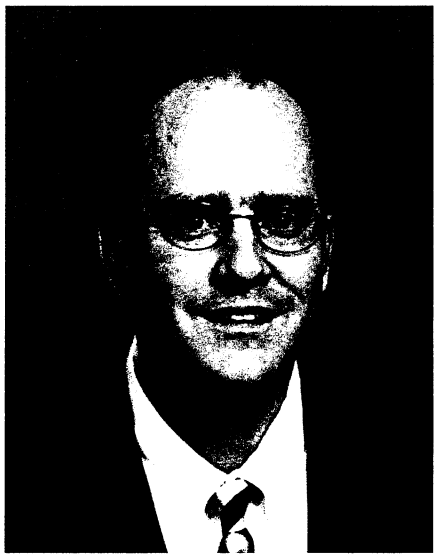
General Contractors, General Contractors—

There is Coverage Under the CGL Policy for Defective Work Performed by a Subcontractor



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Florida courts have consistently taken the position that Comprehensive General Liability (hereafter "CGL") insurance policies do not cover defective work performed by a general contractor. In the past, this rule also included defective work performed by a subcontractor on a general contractor's behalf. *LaMarche v. Shelby Mutual Insurance Co.*, 390 So. 2d 325 (Fla. 1980); *Auto-Owners Ins. Co. v. Marvin Dev. Corp.*, 805 So. 2d 888 (Fla. 2d DCA 2001); *Lassiter Constr. Co. v. Am. States Ins. Co.*, 699 So. 2d 768 (Fla. 4th DCA 1997); *Home Owners Warranty Corp. v. Hanover Ins. Co.*, 683 So. 2d 527 (Fla. 3d DCA 1996). Recently, there was a dramatic departure from this position *in J.S.U.B., Inc. v. United States Fire Ins. Co.*, 30 Fla. L. Weekly D 774 (Fla. 2d DCA 2005).

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J.S.U.B. involved a builder of new homes. Id. at *1. After completion of the project, some of the homes suffered damages when the exterior walls moved or sank. Id. at *2. This damage was determined to be the result of defective work related to soil acquisition, compaction, and testing. Id. The defective work related to the soil was performed exclusively by subcontractors. Id. Coverage was sought by the builder under its CGL policy[1]. Id. The insurer denied coverage and "maintained that the policies did not cover damage to the Builder's own work or product that resulted from the Builder's or a subcontractor's faulty workmanship." Id. This is commonly referred to as the "Damage to Your Work" exclusion to CGL policies.

In *J.S.U.B.*, the trial court relied on *La Marche v. Shelby Mutual Insurance Company*, 390 So. 2d 325 (Fla. 1980) and held that the CGL policies did not cover the damages caused by a subcontractor. On appeal, the builder challenged this contention by pointing out that portions of the standard language in CGL policies have changed since *La Marche*, as well as the fact that the Florida Supreme Court essentially broadened CGL coverage in 1998 with its holding in *State Farm Fire & Casualty Company v. CTC Development Corporation*, 720 So. 2d 1072 (Fla. 1998). *J.S.U.B.*, 30 Fla. L. Weekly D at *11.

The focal point of the *J.S.U.B.* court's holding involved the "Damage to Your Work" exclusion. However, the J.S.U.B. policy also contained an exception to the "Damage to Your Work" exclusion, which stated "[t]his 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." Id. at *4. The insurer argued that the court need not look at exclusions or exceptions because if the policy doesn't allow for coverage, then an exclusion cannot create such coverage. Id. at 16. However, the court agreed with the appellant's contention that "the policies must be read as a whole and no part of the policies should be viewed as having no effect at all." Id. at *17. "This argument is consistent with the dictates of CTC Development that reading a policy's coverage provisions together with its exceptions may provide support for a conclusion that the policy provides coverage for a given occurrence." *J.S.U.B.*, 30 Fla. L. Weekly D at *17. If the court were to adopt the insurer's argument, then the subcontractor exception would be completely ignored and have no effect at all. The *J.S.U.B.* court declined to go this route. After finding that the policy as a whole provided coverage for the defective work, the court then determined that the "Damage to Your Work" exclusion did not apply because of the exception for work performed by a subcontractor.

In order to reach its conclusion regarding the subcontractor exception, the *J.S.U.B.* court first examined whether the policy as a whole covered the instant situation.

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According to the court, "[t]he policies here contain broad insuring language covering property damage that is caused by an 'occurrence' in the coverage territory that takes place during the policy period." Id. at *11. "Occurrence" is defined in the policy as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." Id. However, the policy did not define "accident," which was left for the court to consider. Id. The court relied on *CTC Development* for its analysis of the term "accident," as "the pertinent insuring provisions" in *CTC Development* were similar to the J.S.U.B. provisions. *CTC Development* held that "accident" includes not only "accidental events", but also "injuries or damages that are neither expected nor intended from the standpoint of the insured." *CTC Development,* 720 So. 2d at 1074. In reaching this conclusion, the CTC court strayed from "an earlier, more restrictive definition of 'accident.'" *Hardware Mutual Casualty Co. v. Gerrits,* 65 So. 2d 69 (Fla. 1953). The *J.S.U.B.* court determined that the broad language of the policy combined with the broad definition of accident adopted by the Florida Supreme Court "lead to the conclusion that the occurrences here fall within the coverage provisions of the policies." *J.S.U.B.*, 30 Fla. L. Weekly D at *14. In other words, the *J.S.U.B.* court held that the policy did cover this "occurrence," and that the subcontractor exception trumped the "Damage to Your Work" exclusion. Therefore, the builder could receive coverage from his CGL policy for the defective work of his subcontractors.

The implications of this case will likely be far-reaching, as this is the first time an appellate court in Florida has allowed a contractor to recover from a CGL policy for the defective work of a subcontractor. Since subcontractors often perform a large amount of work for general contractors, this decision should have a substantial impact on the industry. Despite the fact that CGL policies have included the subcontractor exception for years, courts continued to overlook it and have repeatedly held that the contractor could not receive coverage from the policy. With the *J.S.U.B.* decision, a Florida court followed the apparent intent of the policy. This decision follows the path of a few other states[2], and it will be interesting to see the future implication of the *J.S.U.B.* decision in both Florida and the rest of the nation.

Policy Provisions[3]

SECTION I - COVERAGES
COVERAGE A BODILY INJURY AND PROPERTY DAMAGE LIABILITY

1. INSURING AGREEMENT
   a. 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. . . .
   b. 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 period.

2. EXCLUSIONS
   This insurance does not apply to:
   Damage To Property
   "Property damage" to:
   [*4] (5) That particular part of real property on which you or any contractors or subcontractors working directly or indirectly on your behalf are performing operations, if the "property damage" arises out of those operations; or
   (6) That particular part of any property that must be restored, repaired or replaced because "your work" was incorrectly performed on it.
   Paragraph (6) of this exclusion does not apply to "property damage" included in the "products-completed operations hazard."
   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.
   m. Damage To Impaired Property Or Property Not Physically Injured
   "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
   [*5] your behalf to perform a contract or agreement in accordance with its terms.
   This exclusion does not apply to the loss of use of other property arising out of sudden and accidental physical injury to "your product" or "your work" after it has been put to its intended use.

SECTION V - DEFINITIONS

8. "Impaired property" means tangible property, other than "your product" or "your work," that cannot be used or is less useful because:
a. It incorporates "your product" or "your work" that is known or thought to be defective, deficient, inadequate or dangerous; or
b. You have failed to fulfill the terms of a contract or agreement; if such property can be restored to use by:
a. The repair, replacement, adjustment or removal of "your product" or "your work"; or
b. Your fulfilling the terms of the contract or agreement.
13. "Occurrence" means an accident, including continuous or repeated exposure to substantially the same general harmful conditions.
16. "Products-completed operations hazard":
a. Includes all "bodily injury" and "property damage" occurring
[*6] away from premises you own or rent and arising out of "your product" or "your work" except:
(2) Work that has not yet been completed or abandoned . . . .
17. "Property damage" means:
a. Physical injury to tangible property, including all resulting loss of use of that property. . . .
20. "Your product" means:
a. Any goods or products, other than real property, manufactured, sold, handled, distributed or disposed of by:
(1) You; . . . .
21. "Your work" means:
a. Work or operations performed by you or on your behalf; and
b. Materials, parts or equipment furnished in connection with such work or operations. ■

Footnotes

[1] The J.S.U.B. CGL policy is reproduced at the conclusion of this document

[2] *Fejes v. Alaska Ins. Co. Inc.*, 984 P. 2d 519 (Ak. 1999)
Lee Builders, Inc. v. Farm Bureau Mut. Ins. Co., 104 P.3d 997 (Kan. Ct. App. 2005)
O'Shaughnessy v. Smuckler Corp., 543 N.W.2d 99 (Minn. Ct. App. 1996)
Kalchthaler v. Keller Constr. Co., 591 N.W.2d 169 (Wis. Ct. App. 1999)

[3] The CGL policy provisions are reproduced as they appear in *J.S.U.B., Inc. v. United States Fire Ins. Co., 30* Fla. L. Weekly D 774 (Fla. 2d DCA 2005).