Case No. 11-40512

IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

EWING CONSTRUCTION CO., INC.,

Plaintiff – Appellant

v.

AMERISURE INSURANCE COMPANY,

Defendant – Appellee

On Appeal from the United States District Court
For the Southern District of Texas, Houston Division

BRIEF OF AMICI CURIAE ASSOCIATED GENERAL CONTRACTORS OF AMERICA, TEXAS BUILDING BRANCH – ASSOCIATED GENERAL CONTRACTORS OF AMERICA, TEXO – THE CONSTRUCTION ASSOCIATION, ASSOCIATED GENERAL CONTRACTORS – HOUSTON CHAPTER, AMERICAN SUBCONTRACTORS ASSOCIATION, INC., ASA OF TEXAS, INC., AND ASSOCIATED BUILDERS AND CONTRACTORS OF TEXAS IN SUPPORT OF APPELLANT EWING CONSTRUCTION CO., INC.'S PETITIONS FOR PANEL REHEARING AND REHEARING EN BANC

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Defendant – Appellee

CERTIFICATE OF INTERESTED PERSONS

The undersigned counsel of record certifies the following listed persons or entities have an interest in the outcome of this case. These representations are made in order that Judges of this Court may evaluate possible disqualification or recusal.

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By: */s/ Patrick J. Wielinski*
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BRIEF OF AMICI CURIAE

IDENTITY AND INTEREST OF AMICI CURIAE

The following Amici Curiae tender this brief in support of the Petitions for Panel Rehearing and Rehearing En Banc filed by Appellant.

The Associated General Contractors of America ("AGCA") is a trade association of commercial construction contractors. Formed in 1918, the AGCA represents more than 32,000 firms in nearly 100 chapters throughout the United States. Among the association's members are more than 7,000 of the nation's leading general contractors, more than 11,000 specialty contractors, and more than 13,000 material suppliers and service providers to the construction industry. Members engage in all phases of commercial, residential and heavy construction.

Texas Building Branch – Associated General Contractors of America ("Texas Building Branch") is a statewide Texas branch of the AGCA, with the Texas Building Branch consisting of eleven commercial building chapters located throughout the State of Texas. The membership of these eleven chapters includes approximately 370 general contractors and 3,890 specialty contractors, subcontractors and suppliers, all doing business in Texas. Amicus Curiae Associated General Contractors – Houston Chapter ("Houston – AGC") is the local chapter serving over 700 Houston-area members of AGCA.

TEXO – The Construction Association ("TEXO") is the largest commercial contractors association in Texas and is affiliated with the national organization Associated Builders and Contractors, Inc. ("ABC") and AGCA. With over 1,900 members in north and east Texas, TEXO provides innovative programs, quality services and strategic alliances focusing on governmental representation, safety, health and environmental issues, craft workforce development, professional training and community networking events.

Associated Builders and Contractors of Texas ("ABC of Texas") is a state trade association representing merit shop contractors who strongly subscribe to free enterprise principles. ABC of Texas consists of seven local ABC chapters in Texas, representing over 1700 members. Those chapters include Greater Houston, Texas Gulf Coast (Freeport), Texas Mid Coast (Victoria), Texas Coastal Bend (Corpus Christi), South Texas (San Antonio), Central Texas (Austin) and TEXO (Dallas – Fort Worth and East Texas).

The American Subcontractors Association ("ASA") is a national organization of construction trade contractors. Founded in 1966, ASA leads and amplifies the voice of trade contractors to improve the business environment in the construction industry and to serve as stewards for the community. ASA emphasizes ethical and equitable business practices, quality construction, membership diversity, integrity, and a safe and healthy work environment. ASA

has 5,000 members nationwide, including 500 members from five Texas chapters in Houston, North Texas, San Antonio, the Rio Grande Valley, and statewide. These chapters make up ASA of Texas, Inc., which also is sponsoring this brief.

Although Amici Curiae are not parties to this appeal, this brief has been submitted through the undersigned independent attorneys, who were paid a fee by Amici Curiae to prepare it.

INTRODUCTION

In light of the importance of the issues before this Court to the construction industry, the Amici Curiae, except AGCA, previously sponsored an amici curiae brief in support of Appellant Ewing Construction Co., Inc. ("Ewing") in this appeal. Because of the unprecedented holding of this Court and its likely effect, not only upon the construction industry but also the insurance brokers and agents that service it, Amici Curiae are compelled to take the similarly unprecedented action of filing this second brief in support of rehearing.[1] Due to the potentially negative impact of the Court's opinion to insurance coverage for construction insureds on a national basis, AGCA, the national organization of the Associated General Contractors, joins in this brief.

[1] The use of the adjective "unprecedented" is not a play on words in the context of this brief. The Court's opinion is truly unprecedented, both under Texas law and the law as overwhelmingly applied by the courts of other states, as well as with regard to the intent behind the contractual liability exclusion and the commercial general liability policy in general.

Amici Curiae respectfully submit that the Court's opinion misapprehends the scope of the coverage issues presented. Its resolution of those issues by the overly broad application of the contractual liability exclusion has left the Texas construction industry with a serious gap in insurance coverage for its work, a gap that did not exist under prior law and is contrary to the purpose of general liability insurance. If the Court's opinion stands, construction insureds and their brokers and agents must now try to manage the risk of allegedly defective construction, apparently without the commercial general liability (CGL) insurance coverage that they have counted on and have been sold for the better part of fifty years.

The purpose of this brief is to assist the Court to understand the far-reaching ramifications of its opinion as a departure from recognized risk management and transfer methods used throughout the construction industry. A cornerstone of risk management in the construction industry is predictability. In turn, a cornerstone of predictability is the ability to purchase insurance products that the construction insured, and its broker or agent, can be reasonably certain will provide coverage for the many and varied risks, including construction defects, that are faced on an everyday basis. Those risks are potentially huge, and if not transferred to insurance, can break a contractor.[2]

[2] For simplicity's sake, the analysis in this brief often uses the generic term "contractor" or "builder." This term includes subcontractors and other participants in the construction industry, unless otherwise indicated.

ARGUMENT AND AUTHORITIES

A. The Opinion Undoes Nearly Fifty Years of Careful Policy Drafting and Interpretation

The Court's application of the contractual liability exclusion to exclude coverage for property damage arising out of an insured contractor's breach of contract robs construction insureds of coverage for which they have paid premiums for decades. This case is the paradigm for that denial, in which the district court found an "occurrence" of "property damage" within the terms of Ewing's CGL policy, and but for the application of the contractual liability exclusion, Ewing was entitled to the benefit of the subcontractor exception to the Your Work Exclusion to preserve coverage. This preservation of coverage for property damage arising out of a subcontractor's work is no happenstance. It developed nearly fifty years ago when the concept of coverage for the insured's work began to receive systematic treatment in the CGL forms, a development that cannot be overlooked in considering the scope and interaction of the contractual liability exclusion within the basic liability insurance.

The 1966 CGL policy. The 1966 revision to the CGL policy effected a major change. It separated the Products Hazard, the risks associated with manufacturers of products, from the Completed Operations Hazard, insuring the risks associated with providers of services, including contractors. The policy included Exclusion (o), providing that the insurance does not apply "to property

damage to work performed by or on behalf of the named insured arising out of the work or any portion thereof, or out of materials, parts or equipment furnished in connection therewith." That straightforward exclusion was applied by the courts to exclude coverage for property damage to the insured's work arising out of its work. This Court applied that exclusion in *Hartford Cas. Co. v. Cruse*, 938 F.2d 601 (5th Cir. 1991).

The 1973 CGL policy. The CGL policy was revised in 1973, but did not change Exclusion (o), the work performed exclusion from the 1966 form. However, in a very significant development, the Insurance Services Office (ISO) promulgated a standard endorsement to the CGL policy in the late 1960's that modified the work performed exclusion. That endorsement became widely offered in 1973, becoming known as the Broad Form Property Damage Endorsement ("BFPDE"). That endorsement modified Exclusion (o) to eliminate the phrase "or on behalf of" from the exclusion, so that the exclusion then applied only "to work performed by the named insured." The intent behind this endorsement was to provide coverage for property damage arising from subcontractor work on behalf of the named insured, but not arising out of work performed by the named insured.

As such, the BFPDE constituted a rudimentary "subcontractor exception" to the work performed exclusion. The BFPDE applied only to property damage within the completed operations hazard (after completion of the work), and despite

the extra premium charged for it, was extremely popular throughout the 1970's and early 1980's. In fact, most CGL policies issued to construction risks included the BFPDE. In *Mid-United Contractors, Inc. v. Providence Lloyds Ins. Co.*, 754 S.W.2d 824 (Tex.App.—Fort Worth 1988, writ denied), the court upheld coverage under Texas law for the insured general contractor for property damage arising out of its subcontractor's work pursuant to the BFPDE.

The 1986 CGL policy. Due to the complexities in the 1973 CGL policy, ISO rolled out a major revision to the CGL policy in 1986, attempting to use plainer language (the success of which may be debatable) and to lessen the cumbersome practice of adding endorsements such as the BFPDE to accomplish the desired coverage. As a part of that effort, the exception for subcontractor work was redrafted as an affirmative statement into the CGL form. Again, that coverage applied only to property damage occurring in the completed operations context.[3] The importance of that revision cannot be overstated for the construction and insurance industries. One commentator has observed:

[3] While the subcontractor exception that applies to completed operations losses may be the most frequently encountered extension in the CGL coverage provided to construction contractors, both the BFPDE, as well as Exclusions j(5) and (6) of the 1986 policy provided extended coverage for contractors for losses that take place while construction operations are in progress. This court has upheld coverage on a number of occasions under those endorsements/exclusions. *See, Mid-Continent Casualty Co. v. JHP Development, Inc.*, 557 F.3d 207 (5th Cir. 2009); *Gore Design Completions, Ltd. v. Hartford Fire Ins. Co.*, 538 F.3d 365 (5th Cir. 2008). Nevertheless, the preservation of coverage for an insured contractor as to property damage occurring within the completed operations hazard is generally regarded as the most significant enhancement of coverage for construction insureds.

> The 1986 CGL arrived at the height of the great hard market. Changes in the pollution coverage and the new claims-made CGL took center stage … There was also a substantial change to the coverage for completed operations with the words:
>
> > 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.
>
> This major increase in the scope of coverage was important for those who did not have the broad form property damage endorsement to the CGL.[4]

The Texas Supreme Court recognized the significance of the subcontractor exception in *Lamar Homes, Inc. v. Mid-Continent Casualty Co.*, 242 S.W.3d 1 (Tex. 2007).

The importance of completed operations coverage. Unfortunately, this Court's opinion deprives not only Ewing, but if followed, will likely deprive the construction industry of one of the most valuable components of the CGL policy – completed operations coverage. Completed operations coverage is critical since it covers a construction insured for the long tail post-completion liabilities that accompany most construction projects, particularly multi-family residential projects such as condominiums. While the statute of repose under §§ 16.008-009 of the Texas Civil Practice and Remedies Code is ten years (sometimes extended up to twelve years based on date of discovery), Texas contractors, as well as

[4] George B. Flanigan, *CGL Policies of 1941 to 1966: Origins of Product Liability*, 58 CPCU eJOURNAL 1, 9 (Aug. 2005).

contractors around the United States, have learned that a statute of repose is not necessarily a limitation, but instead an invitation to file suit against the contractor near the end of that period and years after completion of the project.

Another commentator, David Dekker, has acknowledged the "critical importance to the construction industry of the scope of coverage provided by the CGL policy for third party claims of defective construction, particularly claims alleging damage to the work and completed operations of the insured."[5] Dekker follows up his analysis with the observation that contractors are frequently exposed to claims by owners that defective workmanship has caused extensive damage to a completed project. He then asks the question, "Are such claims covered by CGL policies?" *Id.* Unfortunately, the answer per the Court's opinion in this case is apparently "No."

Courts have recognized the purpose for the promulgation of the BFPDE and the revisions to the 1986 CGL policy form was to sell more policies:

> The insurance and policyholder communities agreed that the CGL policy should provide coverage for defective construction claims so long as the allegedly defective work had been performed by a subcontractor rather than the policyholder itself. This resulted both because of the demands of the policyholder community and the view of insurers that the CGL was a more attractive product that could be better sold if it contained this coverage.[6]

[5] David Dekker, Douglas Green & Stephen Palley, *The Expansion of Insurance Coverage for Defective Construction*, 28 CONSTR. LAWYER 19 (Fall 2008).

[6] *United States Fire Ins. Co. v. J.S.U.B., Inc.*, 979 So.2d 871, 879 (Fla. 2008)(quoting 2 Jeffrey W. Stempel, STEMPEL ON INSURANCE CONTRACTS §14.13[D] at 14-224.8 (3d ed. Supp. 2007)).

Despite the reliance of the insurance industry on broad completed operations coverage to sell policies, and the construction industry's expectation for that coverage, the Court virtually eliminated that coverage in this case.

The contractual liability exclusion has remained constant. Throughout nearly fifty years worth of revisions, the contractual liability exclusion itself has undergone revisions, but has not changed significantly. The 1966 exclusion, which did not change in 1973, stated that the insurance does not apply to "liability assumed by the insured under any contract or agreement except an incidental contract." This formulation was substantially identical to the 1986 exclusion, except that the term "incidental contract" was renamed "insured contract," which was defined to include assumed tort liabilities.

Essentially, contractual liability coverage and the business risk exclusions have "co-existed" in the CGL policy for years, without the contractual liability exclusion being read in the broad-sweeping manner as set out in the Court's opinion, i.e., over-extending it to apply to breach of contract.[7] While this Court expressed "misgivings" in undoing the nearly fifty years of careful drafting, underwriting, marketing –and interpretation – of the contractual liability exclusion so as to disregard the subcontractor exception, it is respectfully submitted that the

[7] This Court has previously declined to uphold this interpretation in *Federated Mutual Ins. Co. v. Grapevine Excavation Inc*., 197 F.3d 720 (5th Cir. (Tex.) 1999).

emasculation of CGL coverage for contractors warrants more than mere misgivings. It warrants rehearing.

While this Court believes it applied the plain language of the policy, under Texas law, an incomplete analysis of an insurance policy is impermissible, in that an insurance contract, like any other contract, must be interpreted as a whole so as to give meaning to all of its provisions. *Kelley-Coppedge, Inc. v. Highlands Ins. Co.*, 980 S.W.2d 462 (Tex. 1998). Consideration of all of the provisions of the CGL policy issued to contractors such as Ewing requires that the contractual liability exclusion be harmonized with the other business risk exclusions that preserve coverage for defective work performed by a construction insured and its subcontractors. This Court should grant the petition of Ewing for rehearing, so that the panel or the Court en banc can restore harmony to the CGL policy.

B. Predictability in the Interpretation of the CGL Policy is Imperative

Traditional insurance risk management of complex construction projects includes insuring against fortuitous or accidental losses. For that reason, predictability as to the existence of insurance coverage for the construction industry is critical, as is well-noted by commentators such as James O'Connor:

> There is an alarming lack of predictability in the construction industry today about whether contractors' CGL policies will cover property damage arising out of defective construction. It is particularly unpredictable for those contractors performing work in multiple states. National contractors, especially, cannot foretell the scope of the coverage in their CGL policies. This problem isn't with the

> policies they procure; virtually every contractor's CGL policy form is identical and mirrors the ISO's standard General Liability Form, the CG 20 10 [sic]. The problem is the identical policy forms are being construed in radically different ways by the courts. As a result, contractors are covered in some states, but bare in others.[8]

O'Connor addresses lack of predictability and uniformity of results among different states. For example, a claim of the type before this Court, i.e. property damage arising out of defective construction performed by an insured contractor's subcontractor, may not be covered in Texas as a result of the Court's opinion, but across the state line would be covered in Louisiana.[9] At the same time, the lack of predictability caused by the Court's opinion may result in a denial of future claims under the same policies, under which the same claims would have been covered prior to the entry of the Court's opinion.[10] This type of circumstance is even more damaging to the construction industry than state-to-state variations in policy interpretation in that neither the construction risk manager, nor its broker, can ever

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[8] James Duffy O'Connor, *What Every Court Should Know About Insurance Coverage for Defective Construction*, JOURNAL OF THE AMERICAN COLLEGE OF CONSTR. LAWYERS, p. 1 (Winter 2011)("O'Connor").

[9] *See Broadmoor Anderson v. National Union Fire Ins. Co. of La.*, 912 So.2d 400 (La. App. 2d Cir. 2005), *cert. denied*, 925 So.2d 1239 (La. 2006). In addition, the Court's opinion puts Texas at odds with other state laws within this Circuit. *See Architex Association, Inc. v. Scottsdale Ins. Co.*, 27 So.3d 1148 (Miss. 2010). This Court's opinion, because of its novel approach, has attracted significant attention nationwide. Now that the Fifth Circuit has ruled on these issues, it is likely that *Ewing* will be relied upon by other courts and insurers, not only in Texas, but nationally.

[10] Texas applies the "injury in fact" trigger so that multiple CGL policies may apply to construction defect claims involving property damage that occurred in the past. *Don's Building Supply, Inc. v. OneBeacon Ins. Co.*, 267 S.W.3d 20 (Tex. 2008). Thus, policies that were purchased by construction insureds from their brokers and agents in the past may no longer provide coverage for claims that have been previously regarded to be covered.

accurately predict whether a CGL policy will respond to what was previously regarded as an insurable covered loss.

In addition, the ISO CGL policy form is used throughout the entire United States to insure all sorts of businesses from nursing homes, to dry cleaners, to small businesses, including smaller contractors and subcontractors, as well as the largest contractors in the world. Thus, the lack of predictability created by this Court's opinion will likely go well beyond the construction industry and may result in a significant reduction of coverage for any insured that does business via contract. If for no other reason, Amici Curiae request the Court to grant rehearing to determine whether the loss of fifty years of predictability in insurance coverage is warranted by an over-extension of *Gilbert v. Underwriters.*

Negative effect on contractual risk transfer. The construction industry has traditionally transferred risk by virtue of indemnification and hold harmless agreements. And the contractual liability exclusion's exception for "insured contracts" extends the coverage under the CGL policy to these types of agreements. These agreements are found in nearly every construction contract, which is the very reason the CGL policy provides contractual liability coverage.

As of January 1, 2012, Chapter 151 of the Texas Insurance Code renders void as against public policy any indemnity clause or additional insured requirement that indemnifies the indemnitee for its own negligence or breach of

contract. Therefore, an upper tier on a construction project, such as a general contractor, is no longer able to tender its defense or seek indemnity from lower tiers for allegations involving the general contractor's own fault. Unfortunately, in light of the Court's opinion, a general contractor has nowhere to look for protection for the type of completed operations claim that is before this Court. A yawning gap has been created which pre-*Ewing* CGL coverage previously filled. Again, predictability as to coverage has been lost.

Other fall-out of the opinion. The Court's opinion has already spurred ongoing commentary on insurance coverage law chat rooms. Lawyers that represent insurers against their insureds can hardly restrain themselves from proclaiming "the end of construction defect coverage in Texas."[11]

Hopefully, the death of construction defect coverage is "greatly exaggerated." Nevertheless, in light of the Court's opinion, resolution of construction defect claims in Texas has already become more difficult, with insurers already relying on the opinion to take coverage from the table. Because the Court's opinion preserves coverage for property damage to third party work and property, this availability of coverage for property damage to third party property will place higher priority on the CGL coverage of subcontractors and

[11] The URL address for a representative chat room, *Insurance Coverage Litigation Forum*, sponsored by LinkedIn, is: http://www.linkedin.com/groupItem?view=&srchtype=discussedNews&gid=2941767&item=127372992&type=member&trk=eml-anet_dig-b_pd-ttl-cn&ut=1QrdnREoqc7lk1.

other lower tiers. That subcontractor coverage will assume increased importance when funding construction defect settlements for the simple reason that the subcontractor's own work (subject to exclusion) is a smaller component of the overall project. However, it is customary that the general contractor maintains CGL insurance with broader coverage and higher limits than lower tier subcontractors. Unfortunately, in light of the Court's opinion, general contractors may not be able to access that coverage through the subcontractor exception.

CONCLUSION

If not withdrawn, the Court's opinion drastically, and without good reason, alters the landscape of CGL insurance coverage that has been in place for nearly fifty years for construction insureds in Texas, and also in the United States. For that reason, Amici Curiae request that this Court grant Appellant's Petition for Panel Rehearing or, in the alternative, Appellant's Petition for Rehearing En Banc.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, the undersigned, hereby certify that a true and correct copy of the Brief of Amici Curiae Associated General Contractors of America, Texas Building Branch – Associated General Contractors of America, TEXO – The Construction Association, Associated General Contractors – Houston Chapter, American Subcontractors Association, Inc., ASA of Texas, Inc., and Associated Builders and Contractors of Texas in Support of Appellant Ewing Construction Co., Inc.'s Petitions for Panel Rehearing and Rehearing En Banc was electronically served upon counsel of record, as indicated below, via the Court's CM/ECF system on this 6th day of July, 2012.

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