SUPREME COURT OF THE STATE OF CONNECTICUT

S.C. 18886

CAPSTONE BUILDING CORPORATION AND
CAPSTONE DEVELOPMENT CORPORATION

VS.

AMERICAN MOTORISTS INSURANCE COMPANY

AMICUS CURIAE BRIEF OF AMERICAN SUBCONTRACTORS ASSOCIATION IN SUPPORT OF PLAINTIFFS-APPELLANTS CAPSTONE BUILDING CORPORATION AND CAPSTONE DEVELOPMENT CORPORATION

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STATEMENT OF INTEREST OF AMICUS CURIAE

The American Subcontractors Association ("ASA") is a national non-profit corporation supported by membership dues paid by approximately 5,000 member companies throughout the country. Membership is open to all commercial construction subcontractors, material suppliers and service companies. ASA members represent the combined interest of both union and non-union companies, and range from the smallest private firms to the nation's largest specialty contractors. Hundreds of ASA's member companies are located here in Connecticut. ASA dedicates itself to improving the business environment in the construction industry, with an emphasis on ethical and equitable business practices, quality construction, membership diversity, integrity, and a safe and healthy work environment.[1]

The issues before this Court on appeal profoundly impact ASA's member companies, as well as the thousands of Connecticut citizens who are gainfully employed by these companies. The scope of insurance coverage available to subcontractors, suppliers, general contractors, homebuilders, and all other participants in the construction industry, including ASA members, under the standard commercial general liability ("CGL") insurance policy is before this Court. Coverage for property damage to a construction project arising out of defective workmanship turns upon the interpretation of language, particularly the definitions of "occurrence" and "property damage" in the standard CGL policy, the first issue

[1] Pursuant to §67-7 of the Connecticut Rules of Appellate Procedure, the undersigned counsel certifies that counsel for no party wrote this brief in whole or in part and did not contribute to the cost of the preparation or submission of this brief. All costs and fees were paid by ASA.

certified by the Northern District of Alabama to this Court. This brief is limited to the consideration of that issue.

The issue of whether property damage arising out of defective or faulty construction work constitutes an "occurrence" of "property damage" under a standard CGL policy issued to a construction insured has been the subject of much litigation between insurers and their insureds, particularly over the past ten years. ASA, either alone or in conjunction with other construction service organizations, has sponsored the filing of amicus curiae briefs on this issue in numerous appeals, including *United States Fire Ins. Co. v. J.S.U.B., Inc.*, 979 So.2d 871 (Fla. 2007); *Auto-Owners Ins. Co. v. Pozzi Window Co.*, 984 So.2d 1241 (Fla. 2008); and *Lamar Homes, Inc. v. Mid-Continent Casualty Co.,* 242 S.W.3d 1 (Tex. 2007).

Insurance plays a critical role for the members of ASA in managing the serious risks inherent in the construction industry, and those members have a significant interest in being able to rely on their insurers to provide coverage for risks for which they paid substantial premiums. The filing of this amicus curiae brief by the ASA lends a broader industry perspective to the issues before this Court in that it addresses matters and policies relevant to the disposition of this case, particularly with respect to the proper interpretation of, and public policy bases for, CGL insurance policies.

LAW AND ARGUMENT

INTRODUCTION

The issues before this Court are of great concern to Connecticut's construction industry and to the public at large. The members of the ASA, and others engaged in the business of construction within the State of Connecticut, confront the issues before this Court on a regular basis as they attempt to manage the considerable risks inherent in construction. Connecticut contractors and subcontractors strive, and overwhelmingly succeed, in providing quality construction services to owners and other contractors, but inadvertent mistakes do occur, and these mistakes can result in property damage. Connecticut contractors have long paid substantial premiums for liability insurance to provide some measure of protection from liability for any property damage arising out of their subcontractors' mistakes. Appellee American Motorists Insurance Company ("AMICO") would subvert this traditional means of managing the risk of such mistakes, eliminating insurance coverage for that risk. While AMICO is free to withhold such coverage, AMICO would have to revise the policy forms that it has used for decades and put its insureds on notice of that change in coverage.

In considering these questions, this Court will have its first opportunity to interpret and apply the term "occurrence," essentially defined as an "accident," in the relevant insurance policies. The circumstances under which this task reaches this Court, however, are no "accident." Rather, they are the result of a studied attempt by insurers such as AMICO to significantly reduce the coverage provided by the 1986 version of the standard form of commercial general liability ("CGL") insurance without actually changing the terms of the policy itself.

The CGL policy, and particularly the 1986 policy form, provides a large measure of coverage for construction defects to nearly all participants in the construction process, including general contractors, subcontractors, material and equipment suppliers, and project owners. In consideration for substantial premiums, commercial insurance carriers have agreed to provide this coverage, and over time, it has become a critical element of any construction project.

Amicus Curiae does not contend that every construction defect is an "occurrence." Intentionally sloppy or shoddy workmanship that damages a project is not such an "occurrence." But it does not necessarily follow from the fact that if an insured or its subcontractor performed its work in a defective manner, either the insured contractor or its subcontractor expected or intended for the work to be defective. Certainly, those damages resulting from unexpected, unforeseen and unintended mistakes are not, by definition, outside of the coverage of a CGL policy.

If they were held to be outside that coverage, such a holding would depart from the representations that the insurance industry markets to purchasers of CGL policies. That marketing emphasizes the availability of coverage for various categories of defective work, including unexpected and unintended property damage arising out of a subcontractor's work.[2] The policy not only provides this coverage, but through an intricate series of exclusions and exceptions, the policy tailors its precise scope. If these provisions are ignored in favor of a "no 'occurrence' as to defective work" rule, then these policy

[2] The District Court determined that Capstone submitted evidence Court that "subcontractors were retained to perform work on the Hilltop Apartments project." Memorandum Opinion, Document 58, p. 75. Likewise, members of the ASA often use subcontractors to perform parts or even all of their contract work.

exclusions and exceptions serve no purpose whatsoever, and the most basic tenets of insurance policy contract interpretation are of absolutely no moment.

ARGUMENT

Under Connecticut law, insurance policy terms are given their natural and ordinary meaning, and any ambiguity is resolved in favor of the insured. *Wentland v. American Equity Ins. Co.,* 267 Conn. 592, 600–01 (2004). Every provision of a contract of insurance is to be given effect, if possible, and no word or clause eliminated as meaningless, or disregarded as inoperative. *A. M. Larson Co. v. Lawlor Ins. Agency,* 153 Conn. 618, 621-22 (1966). Under these rules of interpretation, AMICO's incomplete analysis of its policies is neither permissible nor persuasive, in that an insurance contract, like any other contract, must be interpreted so as to give meaning to all of its provisions.

I. DEFECTIVE WORK CAN INVOLVE AN "OCCURRENCE" OF UNINTENDED AND UNFORESEEN PROPERTY DAMAGE

The denial of CGL coverage to Capstone for the property damage arising out of the defective work of its subcontractors that performed work on the project ignores the existence of an "occurrence" under the circumstances of this case and the AMICO policy. The starting point of the CGL policy's insuring agreement is a legal obligation to pay damages caused by property damage arising out of an "occurrence." By definition, such property damage is an "accident," in the sense that it is unintended and unforeseen by the contractor. An accident under Connecticut law includes "a lack of intention or necessity, often opposed to design; an unforeseen unplanned event …" *Vermont Mut. Ins Co. v. Walukiewicz,* 290 Conn. 582, 594 (2009).

Under the plain language of the CGL policy, the determining factor is not the intentional nature of the actions that result in property damage, but rather, the unintended

or unforeseen nature of the damages themselves. Certainly not every construction defect involves foreseen or intended property damage caused by the insured contractor or its subcontractors. Such a view exhibits a misunderstanding of the construction industry that insurers seek to insure. Despite the best of efforts, on some occasions, work is performed incorrectly, and that work results in property damage. That type of property damage, unless subject to one or more of the exclusions in the policy, is covered under a CGL policy.

When the conduct before this Court – a general contractor's performance of construction work through subcontractors as to certain items of work – is considered, it is not the type of reckless or intentional conduct that renders the resulting damage highly predictable so as to preclude coverage. Normal business activities simply do not run afoul of the definition of occurrence in the CGL policies issued by insurers such as AMICO to the contractors they insure. Every general contractor or subcontractor performing construction operations in the state of Connecticut intends to perform its construction work, and sometimes that construction work proves to be defective through no affirmative action on the part of the contractor itself. In its truest sense, that defective work is unexpected and unintended. Nevertheless, an insured contractor would have absolutely no coverage for the property damage arising out of those defects according to AMICO. It is patently obvious that a general contractor and its subcontractors do not intend or foresee that that work will be defective. What they do expect is that when property damage arises out of those types of defects, their insurance carrier will step up to the plate and provide the coverage according to the terms of the policy and for which they paid their premium.

A. This Court Can, and Should, Clarify the Law

This Court has yet to apply the definition of "occurrence" to a construction defect that resulted in property damage. ASA urges this Court to provide the needed guidance and uphold the existence of an "occurrence" that this appeal presents in order to bring Connecticut law in line with the courts in other states that have carefully considered this issue. Despite the fact that the CGL policy issued to construction participants throughout the United States is written on a standard form, predictability of coverage is difficult to attain due to the variance among the states in their treatment of this issue. Sound risk management is based upon predictability, so this state of affairs has been described as "alarming," particularly for contractors doing work in multiple states. See, J. D. O'Connor, *What Every Court Should Know About Insurance Coverage for Defective Construction,* 5 JOURNAL OF THE AMERICAN COLLEGE OF CONSTRUCTION LAWYERS 1 (Winter 2011).

Fortunately, the recent trend has been toward more uniformity in the treatment of "occurrence" under the circumstances of cases like this one. In *U.S. Fire Ins. Co. v. J.S.U.B., Inc.*, 979 So.2d 871 (Fla. 2007), the Florida Supreme Court explicitly reversed prior Florida case law that had been read to hold that providing CGL insurance coverage for the defective work of insured contractors was against public policy. In that case, the court held that unexpected and unintended property damage to a number of homes arising out of the faulty site preparation by a subcontractor constituted an "occurrence" as defined in the insured general contractor's CGL policy.

Other courts recently have also taken the opportunity to clarify the state of the law of occurrence as it applies to construction defects. For example, in *Lamar Homes, Inc. v. Mid-Continent Casualty Co.*, 242 S.W.3d 1 (Tex. 2007), the court held that the existence of

an occurrence depends on whether the property damage is unexpected and unintended from the standpoint of the insured, and not whether the ultimate remedy is in contract or in tort. *Id.* at 16. *See also, Sheehan Constr. Co., Inc. v. Continental Cas. Co.*, 935 N.E.2d 160 (Ind. 2010)(unexpected and unintended property damage arising from the faulty workmanship of subcontractors is not foreseeable from the insured contractor's viewpoint, and is an accident within the CGL policy and constitutes an occurrence); *Travelers Indemnity Co. of America v. Moore & Assoc., Inc.*, 216 S.W.3d 302 (Tenn. 2007)(water damage arising out of defects in a subcontractor's installation of windows was not foreseeable and it amounted to an "accident" because the general contractor had assumed that the installation of the windows would be completed properly); *Architex Assoc., Inc. v. Scottsdale Ins. Co.,* 27 So.3d 1148 (Miss. 2010)("occurrence" cannot be construed to preclude coverage for unexpected and unintended property damage resulting from work performed by subcontractor on behalf of general contractor and the intentional act of hiring subcontractors by general contractor does not preclude the possibility of coverage).

ASA submits that it is not aware of any of its members, nor of any contractors for that matter, that construct a building under the assumption that they or their subcontractor will perform defective work. Taken to its logical extreme, the foreseeability argument would rule out CGL coverage for simple negligence, which always involves the foreseeability of the injury arising out of the negligent actions of the insured. This cannot be the intent of the "occurrence" requirement; neither can the intent be to deny coverage for property damage arising out of unforeseen and unintended construction defects.

II. THE CGL POLICY COVERS UNFORESEEN AND UNINTENDED PROPERTY DAMAGE TO THE INSURED'S WORK

The fixation by insurers such as AMICO on the "occurrence" requirement omits any discussion of the exclusions contained in the CGL policy and their profound effect upon insurance coverage for defective work claims. In this regard one of the key exclusions in the CGL policy is the Your Work Exclusion. Though labeled an exclusion, that provision actually preserves coverage under many circumstances, including the facts of this case. That exclusion states that the insurance does not apply to:

> '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.

The term "your work" refers to the work of Capstone, the insured contractor and its subcontractors. The exclusion applies to property damage that is included in the "products-completed operations hazard," and the apartment project, at the time the property damage occurred, was a "completed operation," since all work had been completed under Capstone's contract.

Capstone subcontracted work under its contract to subcontractors, and that work caused property damage; and for that reason, the exclusion does not apply to this claim. The second sentence of the Your Work Exclusion, often referred to as the "subcontractor exception," explicitly states that the exclusion does not affect coverage where the damage arises out of work performed by a subcontractor on behalf of the named insured. In effect, it expressly preserves that coverage. Focusing on the definition of occurrence under the CGL policy, insurers decline to consider the plain language of the subcontractor exception.

A. The Historical Development of the CGL Policy Supports Coverage

This Court should not depart from the plain language of the CGL policy. Admittedly, there is a perceived tension between CGL coverage for defective work and what insurance underwriters have traditionally referred to as an uninsured business risk, that is, ordinary business risks that the insured can control. This perception gained momentum with the 1966 revisions to the CGL form promulgated by the Insurance Services Office ("ISO"), the industry organization responsible for drafting the industry-wide standard forms. The Work Performed Exclusion in the 1966 revisions (Exclusion (o)), broadly excluded coverage for property damage arising out of "work performed by or on behalf of the named insured." The exclusion was retained in the 1973 revision of the form, but that same year, ISO promulgated the Broad Form Property Damage Endorsement ("BFPDE") to the standard policy form. That endorsement expanded the coverage under the 1973 form by modifying the Work Performed Exclusion to delete from it the reference to work performed "on behalf of" the named insured, that is, work performed by subcontractors. The intent was to provide an insured contractor with coverage for property damage arising out of the defective work of its subcontractors. 21 ERIC MILLS HOLMES, HOLMES' APPLEMAN ON INSURANCE §132.9[D] (2d ed. 2002).

The policies before this Court are written on a form that was revised in 1986. Those revisions were widely hailed throughout the insurance industry both for their simplification and reduction of the number of forms, as well as their use of more plain language. 20 ERIC MILLS HOLMES, HOLMES' APPLEMAN ON INSURANCE §129.1[C] (2d ed. 2002). One of the simplifications sought by ISO was to clarify the limitations on the business risk concept previously introduced in 1973 by the BFPDE. Due to the popularity of the enhanced

coverage provided by the BFPDE, one major revision was the explicit insertion of the exception for work performed by subcontractors into the Your Work Exclusion, as part of the standard coverage of the policy. That revision affirmatively stated and confirmed the existence of completed operations coverage for property damage arising out of the work of subcontractors.

Of course, the addition of the express subcontractor exception into the CGL policy form made the coverage more attractive to construction insureds, as recognized by the Florida Supreme Court in *U.S. Fire v. J.S.U.B.*:

> [T]he 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 (which wanted this sort of coverage) and the view of insurers that the CGL was a more attractive product that could be better sold if it contained this coverage.

979 So.2d 879, quoting from 2 Jeffrey W. Stempel, *Stempel on Insurance Contracts* §14.13[D] at 14-224.8 (3d ed. Supp. 2007). The subcontractor exception unambiguously preserves from exclusion coverage for the property damage claim of Capstone on the AMICO policies, and in light of the history and purpose of the provision, it is disingenuous to attempt to avoid it through the definition of occurrence.

B. Case Law Overwhelmingly Supports Coverage for Property Damage to the Insured Contractor's Work Arising Out of Subcontractor Work

Recent cases overwhelmingly uphold coverage for property damage due to the subcontractor's defective work. In addition, most of these recent cases also address the primary issue before this Court: whether unforeseen and unintended property damage constitutes an occurrence under the insured contractor's policy. After answering that question affirmatively, these cases proceed to preserve coverage under the subcontractor

exception. Such cases include: *Lamar Homes, Inc. v. Mid-Continent Casualty*, 242 S.W.3d at 11 (when a general contractor becomes liable for damage to work performed by a subcontractor or for damage to the general contractor's own work arising out of a subcontractor's work, the subcontractor exception preserves coverage); *U.S. Fire v. J.S.U.B.*, 979 So.2d at 878-80 (applying the subcontractor exception to property damage to the homes in a subdivision arising out of defective site preparation by a subcontractor); *Travelers Indemnity Co. of America v. Moore & Assocs.*, 216 S.W.3d at 310 (damages resulting from the subcontractor's faulty installation of windows are not excluded from coverage, even if those damages affected the general contractor's own work); *American Family Mutual Ins. Co. v. American Girl, Inc.*, 673 N.W.2d 65 (Wis. 2004)(the damage to an insured contractor's work caused by a subcontractor is within the subcontractor exception to the 1986 CGL policy form); *Sheehan Constr. Co., Inc. v. Continental Cas. Co.*, 935 N.E.2d at 171-72 (applying the subcontractor exception, determining that it would serve no purpose if there was not an initial grant of coverage in the policy for unexpected and unforeseen property damage arising out of faulty work).

In accord with this authority, coverage for the risk of defective work of Capstone's subcontractors is preserved under the AMICO policy.

CONCLUSION

Amicus Curiae asks that the Court answer Question Number 1 as certified by the Northern District of Alabama in the affirmative, upholding the existence of an "occurrence" of "property damage" under the circumstances before this Court on this appeal.

Respectfully Submitted,

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CERTIFICATION OF SERVICE

This is to certify that a copy of the foregoing Amicus Curiae Brief of American Subcontractors Association in Support of Plaintiffs-Appellants Capstone Building Corporation and Capstone Development Corporation was served this 2nd day of May, 2012, via United States first-class mail, postage prepaid, to the parties of record as follows:

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CERTIFICATE OF COMPLIANCE

American Subcontractors Association hereby certifies that this Brief is in compliance with the formatting, briefing and other requirements set forth in the Conn. Prac. Bk. §67-2 *et. seq*.

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