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Advanced Issues in Insurance Coverage

Now What? Implications Following the Ohio Northern Univ. v. Charles Construction Services, Inc. Case

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I. THE DECISIONS FROM THE OHIO SUPREME COURT.

A. *Westfield Ins. Co. v. Custom Agri Systems*

The Ohio Supreme Court in *Westfield Ins. Co. v. Custom Agri Systems* held that an insurance claim filed by a contractor under its commercial general liability ("CGL") insurance policy for property damage caused by the contractor's own faulty workmanship does not involve an "occurrence" such that the CGL policy would cover the loss. 133 Ohio St.3d 476, 2012-Ohio-4712, 979 N.E.2d 269, syllabus.

Following this decision, Ohio courts found that insurance companies did not owe a duty to defend or indemnity a contractor for property damage claims arising from their own poor workmanship. However, the question arose as to whether a claim for property damage caused by the poor workmanship of a subcontractor (not the insured) would be an "occurrence" and trigger coverage under a CGL policy.

B. *Ohio Northern Univ. v. Charles Construction Services, Inc.*

The *Ohio Northern Univ. v. Charles Construction Services, Inc.* case presented this issue to the Ohio Supreme Court. In October 2018, the Ohio Supreme Court held "that property damage caused by a subcontractor's faulty work is not fortuitous and does not meet the definition of an 'occurrence' under a CGL policy." In reaching this conclusion, the Court declined to adopt the argument presented by Ohio Northern University that the products-completed operations hazard clause provided separate coverage for the work complete by a subcontractor. The Court held that since a claim for poor workmanship is not an "occurrence", the products-completed operations hazard exception to an exclusion has no effect.

Therefore, in Ohio, a contractor is not entitled to coverage under its standard CGL policy for property damage caused to its work regardless if the work was self-performed or if it was completed by a subcontractor. In other words, if a contractor fails to install a roof correctly and the claimant sues seeking damages for the cost to repair and/or replace the roof, there is no insurance coverage under the contractor's CGL insurance policy.

II. WHAT IS NEXT?

A. New Legislation?

At the end of the decision on the *Ohio Northern Univ. v. Charles Construction Services, Inc*. case, the Supreme Court references the legal steps taken in Arkansas addressing the issue of insurance coverage for faulty workmanship claims. In *Essex Ins. Co. v. Holder*, 372 Ark. 535, 261 S.W.2d 456 (2008), the Arkansas Supreme Court held that "[f]aulty workmanship is not an accident; instead it is a foreseeable occurrence… [and] the contractor's obligation to repair or replace its subcontractor's defective workmanship could not be deemed unexpected on the part of the contractor, and therefore, failed to constitute an 'event' for which coverage existed under the policy" *Id*., 459-460.

After this decision was issued by the Arkansas Supreme Court, the Arkansas legislature responded by enacting legislation intended to modify the holding in *Essex Ins. Co*. *See,* Ark.Code Ann. 23-79-155(a)(2).

In Ohio Northers, the Ohio Supreme Court invites the Ohio Legislature to do the same.

1. Arkansas's Legislation.

As mentioned above, the Arkansas legislature acted in response to the *Essex* opinion and enacted legislation modify the impact of *Essex* decision. Ark.Code Ann. 23-79-155(a)(2) states:

> (a) A commercial general liability insurance policy offered for sale in the state shall contain a definition of "occurrence" that includes:
>
> (1) Accidents, including continuous or repeated exposure to substantially the same general harmful conditions; and
>
> (2) Property damage or bodily injury resulting from faulty workmanship.
>
> (b) This section is not intended to restrict or limit the nature or types of exclusions from coverage that an insurer may include in a commercial general liability insurance policy.

2. Colorado's Legislation.

Like Arkansas, Colorado's legislature passed legislation requiring faulty workmanship claims to be considered an "occurrence". Colorado Rev. Statutes §13-20-808 states:

> In interpreting a liability insurance policy issued to a construction professional, a court shall presume that the work of a construction professional that results in property damage, including damage to the work itself or other work, is an accident unless the property damage is intended and expected by the insured. Nothing in this subsection:

(a) Requires coverage for damage to an insured's own work unless otherwise provided in the insurance policy;

(b) Creates insurance coverage that is not included in the insurance policy.

B. New Insurance Policy Endorsements.

For more than a decade, courts across the country have reached varying conclusions on whether faulty workmanship is considered an "occurrence" for purposes of coverage under a standard CGL insurance policy. In response to this debate, some insurance companies have adopted specific endorsements aimed at addressing this issue.

One company termed the endorsement as a "Contractors E&O Endorsement." This Endorsement claims to provide protection if a contractor is held responsible for faulty design, materials, workmanship, or installation.

Other companies have called the endorsement the Faulty Workmanship Coverage Endorsement, or the Damage to Your Work Endorsement. These are not ISO forms, so each endorsement will have its own language. Some examples of the endorsement language are:

A. **SECTION I – COVERAGES, COVERAGE A. BODILY INJURY AND PROPERTY DAMAGE LIABILITY, 1. Insuring Agreement, a.** is amended to include damage which you become legally obligated to pay because of "property damage" that is:

(1) To 'your work", if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor; or

(2) To property other than "your work" or "your work", if the "property damage" is caused by or results from "your product" or "your work";

if such "property damage":

(1) Consists of physical injury to tangible property, including all immediately ensuing resulting loss of use of that property; and

(2) Is included within the "products-completed operations hazard".

"Property damage" for which this Paragraph A provides coverage shall be deemed to be caused by an "occurrence".

However, we will not pay for:

(1) "Property damage" that was a result of willful, wanton or intentional misconduct; or

(2) "Property damage" that was to "defective or faulty work".

C. With respect to the coverage provided under Paragraphs A & B, this endorsement does not serve to limit or restrict the applicability of any exclusion or limitation under this Coverage Part.

While the insurance industry is taking steps to modify their policies to provide contractors with endorsements that modify the definition of an "occurrence", these endorsements do come with some significant limitations:

1. Some insurance companies limit the coverage afforded under these endorsements to $10,000.

2. All of the endorsements (and the legislation), do not provide coverage for faulty work of a contractor that was done intentionally.

3. None of the current products are intended to limit, restrict, or remove any of the exclusions within the CGL policy or other endorsements.

4. Some of the endorsements will only apply to cover faulty workmanship if the work was performed by subcontractor. Thus, some endorsements do not provide coverage for a contractor that self-performs the poor work.

Time will tell how the law in Ohio will continue to develop in the area of construction defect litigation and the corresponding insurance coverage disputes.