

COMMERCIAL *Liability*

THE COMPLEX WORLD OF CONSTRUCTION DAMAGE CLAIMS

Insurance company denials are sometimes overly broad

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Insurance coverage for defective construction claims arising out of property damage that takes place during construction is one of the most complicated areas of insurance coverage law. The simple rule that construction and insurance lawyers should always remember, however, is that the standard Commercial General Liability (CGL) policy provides coverage for damage to non-defective work. Contractors

and lawyers should keep this simple rule in mind whenever facing liability to the project owner or any other party that arises out of a construction claim. Therefore, one should always seek defense fees and indemnity for lawsuits or amounts paid to fix non-defective work.

Courts, insurers and policyholders, unfortunately, have been confused by certain exclusions in the standard CGL form and have made their analysis unduly complicated. This confusion is furthered by



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insurers who make overly-broad denials of coverage based on so-called “business risk exclusions” and claims that insurers are not sureties of contractors for damage that takes place during construction. The potentially applicable exclusions for property damage occurring during construction are the standard CGL exclusions j(5) and j(6), which a Superior Court recently addressed for the first time in *Candid Corporation v. Assurance Company of America*, 2007 WL 1120616.

Preliminary Analysis

Some preliminary analysis should be undertaken before addressing whether a claim arising out of property damage during the construction process is covered. First, there must be an “occurrence” or an accident. Second, the policyholder must give notice to the insurer as soon as the property damage takes place. A common mistake is to simply fix damages that take place during construction and to bear the cost without involving the insurer, only to find out after the fact that some of the damage may have been covered.

Ongoing Operations Exclusions

The primary CGL exclusions that may defeat coverage for an ongoing operations claim are exclusions j(5) and j(6). The exclusions state that this insurance does not

apply to the following property damage:

- j(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

- j(6) That particular part of any property that must be restored, repaired, or replaced because “your work” was incorrectly performed on it. (This exclusion does not apply to “property damage” included in the “products completed operations hazard.”)

The key term in both exclusions is “that particular part.” That is, the

exclusions apply only to damage to “that particular part” of property on which the contractor is actively performing operations at the time of the loss, for j(5), or for

that particular part of the contractor’s work that needs to be repaired because work was incorrectly performed, for j(6). For both exclu-

sions, the key is that damages to already completed, non-defective work are not excluded.

To aid in interpretation, the Insurance Services Office (“ISO”) released an expla-



nation describing how the “that particular part” language limits the applicability of the exclusion. One of the examples given by ISO with regard to j(5) is as follows:

“Consider an insured subcontractor who is erecting steel beams furnished to him by the general contractor. Having erected four steel beams, the subcontractor is in the process of erecting a fifth steel beam and this beam falls, resulting in damage to all five beams.”

In this hypothetical, it is clear that “that particular part” refers to the fifth beam and does not include the non-defective work already finished, even though the other four beams are work done by the subcontractor. Therefore, contractors should not accept a denial from an insurance company just because the damaged property was work done by the subcontractor. Only the defectively performed work is excluded, not all work performed by the subcontractor.

ISO explains the scope of “that particular part” as used in j(5) as follows:

“This clause excludes property on which the insured is actually working at the time of the property damage. It also excludes property damage caused by subcontractors of the insured while they are actually working on the property. Where the damage caused by the insured in the performance of his operations goes beyond damage to the property on which he is working, this section limits the exclusion to the particular part on which he is working.”

This explanation demonstrates that there is both a “time” restriction (only damage occurring while current operations are being performed is excluded) and a “geographic” restriction (only damage to the particular item on which work is being performed is excluded).

ISO also described the scope of “that particular part” in j(6) by the following example:

“This section excludes property damage to the particular part of any property which was in use when damage occurred even though work on that part has been completed and also where it cannot be established that the damage was the result of faulty workmanship. If the insured has installed a valve on a pressure vessel, and, while being tested, the valve fails to function because of a defect in the valve which causes the vessel to explode, only the damage to the valve is excluded.”

Exclusion j(6) is broader than j(5), in that it excludes damage caused to work which must be repaired, whether or not damage took place while work was actively being performed, because it was defectively performed. However, there is still coverage for damage to non-defective work (the vessel) which was damaged by the defective work (the valve).

Connecticut Case Law

Only one Connecticut case has interpreted these exclusions. In *Candid Corp v. Assurance Co of America*, the Superior Court interpreted exclusion j(6). Candid hired Connecticut Building to clean, restore and caulk seams on the steel structure of a building. Candid obtained a judgment against Connecticut Building for damages caused to the windows of the building during the restoration process. Candid then brought a direct action against Connecticut Building’s insurer per the direct action statute, Conn. Gen. Stat. §38a-321. Assurance moved for summary judgment, claiming that exclusion j(6) applied because properly removing paint from the windows was part of

“Connecticut Building’s work.”

In denying the motion for summary judgment and determining that exclusion j(6) may not apply, the court correctly focused its analysis on the cause of the damage. It noted that the plaintiff made two separate allegations of damage to the window panes — from the actions of Connecticut Building while working on the steel structure pursuant to the contract, and from the subsequent process of removing paint that had become caked on the panes.

The court correctly concluded that because some of the damage may have taken place while *Candid* was not working on the windows themselves, j(6) may not apply.

In the end, the court in *Candid* correctly focused on the cause of the damages instead of simply accepting the insurer’s argument that because the damage involved the insured’s work, it should be excluded. Nonetheless, insurers will likely continue to use an overly-broad interpretation of exclusions j(5) and j(6) and are aggressively fighting against coverage for damages to a contractor’s already completed work that arise during construction. Construction industry members should be vigilant to notify insurers of any property damage that occurs accidentally at a work site.

Conclusion

When property damage takes place during the construction process, don’t assume there is no coverage. Give notice to your insurer. And when in doubt, think of the basic rule that if the damage is to non-defective work, there is a possibility that you are entitled to coverage under your CGL policy. ■