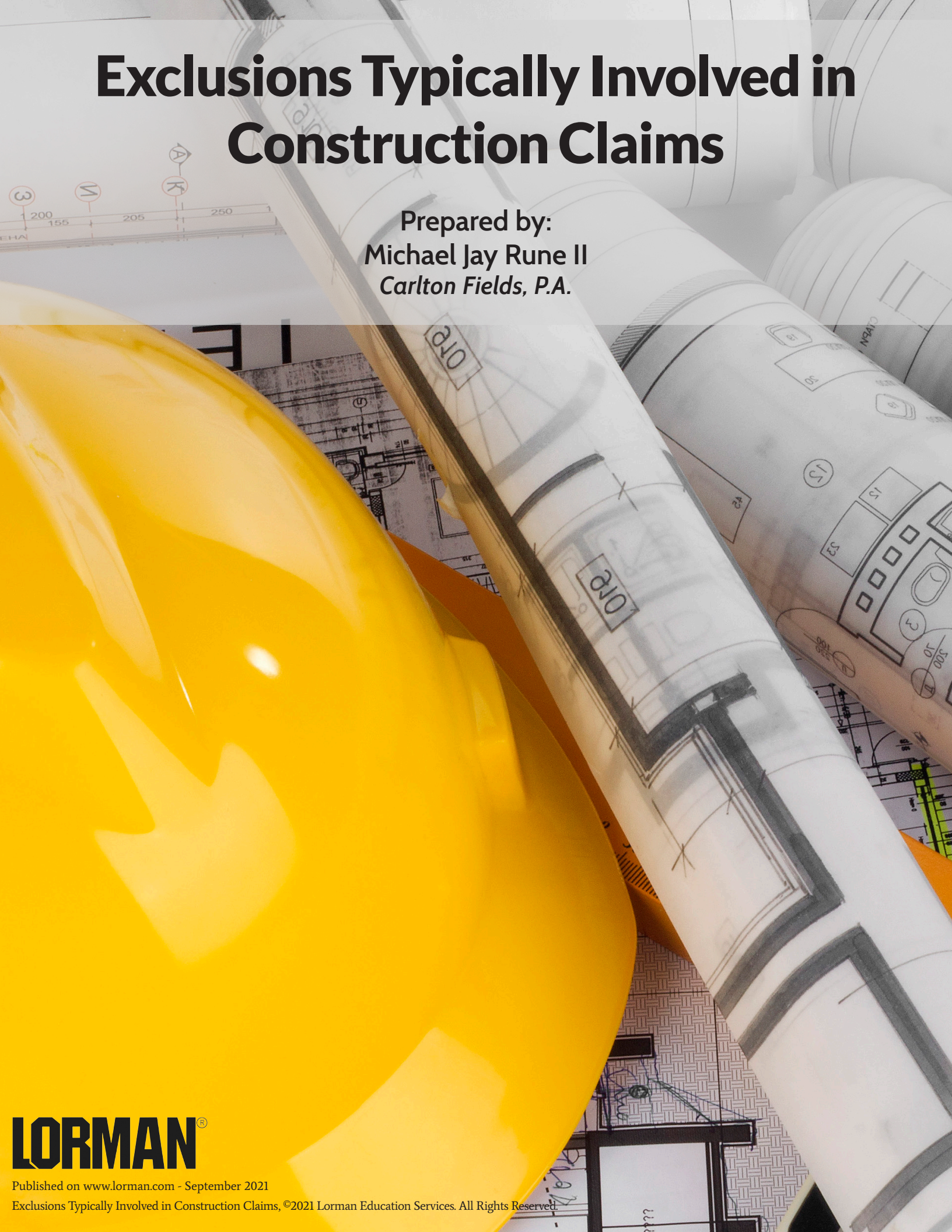
# Exclusions Typically Involved in Construction Claims

Prepared by:
Michael Jay Rune II
*Carlton Fields, P.A.*



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**Exclusions Typically Involved in Construction Claims:**

In the construction context, there are numerous exclusions that have a significant impact on the coverage available under a CGL policy. Generally, CGL policies exclude from coverage: property damage to the insured's product and/or property damage to work performed by or on behalf of the insured; damage to property in the care, custody, and control of the insured; damage after completion of the building; and design defect.

### 1. Insured's Work Exclusion

In the construction context, the courts have held that replacement or repair of defective work is not covered under a commercial liability policy.[1] "A contrary holding would have the effect of converting the policy into a performance bond rather than liability insurance."[2] For example, if a contractor inadequately shores a wall which collapses damaging another portion of the building and workers, typically a CGL policy would allow recovery for the costs of repairing the work that was damaged and any injuries resulting from the collapse; however, the CGL Policy would not cover the cost of replacing the wall which collapsed.[3] This exclusion has been held to exclude claims for damages to subcontractors work even when there is an exception for subcontractor work in the exclusion.[4]

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[1] *Amerisure Mut. Ins. Co. v. Aucter,* 673 F. 3d 1294 (11th Cir. 2012); *LaMarche v. Shelby Mutual Ins. Co.*, 390 So. 2d 325 (Fla. 1980); *American States Ins. Co. v. Villegas,* 394 So. 2d 222 (Fla. 5th DCA 1981); *Tucker Constr. Co. v. Michigan Mut. Ins. Co.*, 423 So. 2d 525 (Fla. 5th DCA 1982); *Lassiter Constr. Co., Inc. v. American State Ins. Co.*, 699 So. 2d 768 (Fla. 4th DCA 1997); *Home Owners Warranty Corp. v. Hanover Ins. Co.,* 683 So. 2d 527 (Fla. 1996); *USF&G v. Meridian of Palm Beach Condo Assoc., Inc.,* 700 So. 2d ( Fla. 4th DCA 1997).

[2] *C.A. Fielland, Inc. v. Fidelity & Cas. Co. of New York,* 297 So. 2d 122, 125 (Fla. 2nd DCA 1974).

[3] *American Equity Ins. Co. v. Van Ginhoven,* 788 So. 2d 388 (Fla. 5th DCA 2001) (pool repair).

[4] *Tucker Const. Co. v. Michigan Mutual Ins.,* 423 So. 2d 525 (Fla. 5th DCA 1985); *Home Owners Warranty Corp. v. Hanover Ins. Co.,* 683 So. 2d 527 (Fla. 3rd DCA 1996); *Lassiter Constr. Co., Inc. v. American State Ins. Co.*, 699 So. 2d 768 (Fla. 4th DCA 1997).

In *J.S.U.B., Inc. v. US Fire Ins. Co.*,[5] the Second District Court of Appeals radically departed from the long standing Florida precedent and held that the subcontractor exception to the insured's work exclusion means that claims for the defective work of subcontractors **and** any resulting damage are covered under a CGL policy. The Court receded from its own opinion which gave rise to the Supreme Court holding in *La Marche* and recognized the changes to the policy forms were intended to broaden coverage and that defective construction is an occurrence in light of *CTC Development*'s broad definition of accident.[6] Factually, the case involved a claim that exterior wall movement (sinking) was caused by a subcontractor who improperly compacted, tested, and/or filled the soil for the site. The damages claimed involved structural damages to the walls and as well as interior fixtures and finishes. The insurer agreed to cover fixtures and finishes applied by the owner but denied coverage for the insured's own work. The lower court found the damage arose from the improper work of the subcontractor and ruled in favor of the insurer.

In reversing, the Second Circuit held that a subsequent failure of the work of the insured was an "occurrence" and that the subcontractor exception to the exclusion applied providing coverage for the damage (the exception to the exclusion only applicable to complete operations).[7] As to the first part of the analysis the Court concluded in reading the policy as a whole:

> The Insurer argues that workmanship deficiencies that result in later damage to homes should not be considered to be the result of an accident. However, the Insurer's broad policy language that defines an "occurrence" but does not define an "accident", and the broad definition of "accident"

[5] 906 So. 2d 303 (Fla. 2d DCA 2005).

[6] *American Family Mut. Ins. Co. v. American Girl, Inc.*, 673 N.W.2d 65 (Wis. 2004) contains a detailed analysis of the CGL policy changes and reaches the same conclusion that coverage is provided by the exception.

[7] *Ryan Inc. Eastern v. Continental Cas. Co.*, 910 So. 2d 298, 300 (Fla. 2nd DCA 2005).

> adopted in *CTC Development*, lead to the conclusion that the occurrence here falls within the coverage provisions of the policy.

The Court then found that, unlike the Court in *Lassiter,* the "exclusion does not create coverage" but rather "is consistent with and provides support for the analysis that the insuring provisions" provided coverage.

In addition to the foregoing, the 11th Circuit, in *Carithers v. Mid-Continent Cas., Co.*, 782 F. 3d 1240 (11th Cir. 2015), has recently held that damages for an insured's defective work *are* covered *if* the defective work must be replaced in order to repair covered property damage. In *Carithers,* a balcony was improperly constructed which thereby caused water to seep into the ceilings and walls of the garage and led to wood rot. While the Court recognized that the policy did not cover the defectively constructed balcony, the Court found that to effectuate the repairs to the garage, the balcony would have to be rebuilt. As such, the Court agreed with the lower court's award of damages to the insured for the cost of repairing the balcony, noting "[u]nder Florida law, the [insured] had a right to 'the costs of repairing damage caused by the defective work.. . .' " Because the cost of repairing the balcony was necessarily a part of the cost of repairing the garage, the Court held the policy at issue covered the cost of repairing the balcony.

Even with the *J.S.U.B.* and *Carithers* opinions, it is an uphill battle to recover for damages to an insured's own work. It is important to keep in mind that the insurer bears the burden of demonstrating that an exclusion applies with respect to a claim that would otherwise be covered under a liability policy.[8] Second, as a general rule of contract construction in Florida, insurance policies are to be construed liberally in favor of the insured and strictly against the insurer, and whenever the language is susceptible to two or more constructions, the court must

[8] *U.S. Concrete Pipe Co. v. Bould*, 437 So. 2d 1061, 1065 (Fla. 1983); *Herrera v. C.A. Seguros Catatumbo*, 844 So. 2d 664, 668 (Fla. 3d DCA 2003).

adopt that which is most favorable to the insured.[9] However, exclusions, no matter how poorly drafted, cannot create coverage where coverage does not otherwise exist by the terms of the insurance policy.[10]

### 2. Care, Custody, and Control Exclusion

The care, custody, and control exclusion typically comes into play in the construction context when one contractor is directing the operations of another or has possessory control of its property. The courts have drawn a distinction between ownership and control with regard to this exclusion.[11] For example, there would still be potentially coverage for a property owned by the insured which was damaged as a result of an occurrence which was not in the possessory control of the insured at the time of the loss.[12]

### 3. Completed Operations Exclusion

Completed operations exclusions in a CGL Policy exclude from loss any occurrence or accident which arises after the construction is completed. In an early Supreme Court case, *Nixon v. United States Fidelity and Guarantee Company*[13], a child was killed when a wall in a building collapsed. The Florida Supreme Court held that despite the completed operation exclusion, there was coverage. The rationale of the Florida Supreme Court in *Nixon* was that the completed operations exclusion in essence applied to products and that since the contractor did not make, sell, or deal in products, the exclusion was inapplicable.[14] The apparent pitfall for the insurer was

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[9] *Auto-Owners Ins. Co. v. Anderson*, 756 So. 2d 29, 34 (Fla. 2000); *Abreu v. Lloyd's London,* 877 So. 2d 834, 835 (Fla. 3d DCA 2004).

[10] *Seigle v. Progressive Consumers Ins. Co.*, 819 So. 2d 732, 740 (Fla. 2002); *USF&G v. Meridian of Palm Beach Condo. Assoc., Inc.,* 700 So. 2d 161 (Fla. 4th DCA 1957).

[11] *Phoenix of Hartford v. Halloway Corp.,* 298 So. 2d 195 (Fla. 4th DCA 1981).

[12] *Michigan Mutual Liability Co. v. Mattox,* 173 So. 2d 754 (Fla. 1st DCA 1965).

[13] 290 So. 2d 26 (Fla. 1973).

[14] *Id.* at 28.

that in the coverage section of the policy one of the hazards covered against was "all operations of the contractor." It is readily apparent from the substantive case law that *Nixon* stands primarily on the specific language of the policy, once again illustrating the importance of reviewing the policy language before making a determination as to potential coverage.

In numerous other cases where the exclusion operation was more carefully or broadly worded, and the coverage portion of the policy did not create an ambiguity, the completed operations exclusion applied to bar the claim.[15] For example, in *Sandpiper Construction Co. v. USF&G Co.,*[16] the roof of a newly constructed building collapsed six months after the building was completed by the general contractor. Despite the holding in the *Nixon* case, the District Court found that the policy exclusion for completed operations applied.[17]

**B. <u>Subrogation:</u>**

An insurer which pays a claim for its insured is surrogate to an insured's rights against a person or persons who may also be responsible for causing a claim which was satisfied.[18] Subrogation may arise through contract or at common law.[19]

In the construction context; however, due to common requirements that one of the contracting parties maintain the other parties as additional insurers has ramifications for an insurer's subrogation claim. In addition, most standard form agreements concerning construction contain waivers of subrogation clauses.

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[15] *Auto-Owners Ins. Co. v. Marvin Corp.*, 805 So. 2d 888, 891 (Fla. 2d DCA 2001); *Lassiter Constr. Co., Inc. v. American States Ins. Co.*, 699 So. 2d 768, 769 (Fla. 4th DCA 1957); *Tucker Constr. Co. v. Michigan Mutual Ins. Co.*, 1123 So. 2d 525, 527 (Fla. 5th DCA 1982).

[16] 348 So. 2d 379 (Fla. 2d DCA 1977).

[17] *Id.* at 380.

[18] *Underwriters of Lloyd v. City of Lauderdale Lakes*, 382 So. 2d 702, 704 (Fla. 1980).

[19] *Dade Co. School Bd. v. Radio Station WQBA*, 731 So. 2d 638, 646 (Fla. 1999).

The law is well established in Florida that a subrogation insurer stands in the shoes of its insured and has no greater rights than the insured had.[20] The law is equally well established in the State of Florida that an insurance company cannot maintain a subrogation action against its own insured.[21] In the context of construction contract, the courts have consistently held that subrogated insurers are not entitled to recover against parties to a construction contract where one party is obligated to obtain insurance covering the risk or requires to name the other parties and the named insured under the policies.[22]

The prohibition against subrogated insurers applies even if the contracting party did not carry out its contractual duty to name other parties as an additional insured under the insurance contract. As the court in *Norland Industries*[23] summarizing the holding in *Smith v. Ryan* explained:

> In Smith an owner and contractor entered into a contract which provided the owner would carry fire insurance on the premises and that the contract or would be a named insured in all policies. The owner did obtain fire insurance but failed to have the contractor named as an insured on the policy. The contract further provided that if either party should suffer damage in any manner because of the wrongful act or negligence of the other party, the damaged party would be reimbursed by the other party. After a fire damaged the property, the insurance company paid the owner for losses and then brought suit against the contractor alleging negligence. The court affirmed the trial court's summary judgment in favor of the contractor, declaring that the contract clearly required the owner to name the contractor's insured in the fire insurance policy and the insurer could not maintain a subrogation suit against its own insured.[24]

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[20] See, *e.g., Cas. Index., Exchange v. Penrod Brothers, Inc.,* 632 So. 2d 1046, 1047 (Fla. 3d DCA 1994).

[21] See, *Travelers Ins. Co. v. Warner,* 679 So. 2d 324, 330 (Fla. 1996) ("The fundamental principal of insurance law"); *Continental Ins. Co. v. Kennerson,* 661 So. 2d 325, 327 (Fla. 1st DCA 1995); *Ray v. Earl,* 277 So. 2d 73, 76 (Fla. 2d DCA 1973) ("Basic rule of law").

[22] *Dyson and Co. v. Flood Engineering,* 523 So. 2d 756, 758 (Fla. 1st DCA 1988); *IN v. EL Nezlek, Inc.,* 480 So. 2d 1333, 1335 (Fla. 4th DCA 1986); *Housing I and V, Corp. v. Carris,* 389 So. 2d 689,690 (Fla. 5th DCA 1980); *Smith v. Ryan,* 142 So. 2d 139, 141 (Fla. 2d DCA 1962).

[23] *U.S. Fire Ins. Co. v. Norland Industries, Inc.,* 428 So. 2d 325, 326 (Fla. 1st DCA 1983).

[24] *Id.*