Construction Report

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Third Circuit Addresses Whether Occurrence-Based CGL Policies Cover Claims of Faulty Workmanship—But Raises Another Question

The issue of whether "occurrence"-based CGL policies provide coverage for property damage sustained as a result of faulty workmanship by contractors has been treated unevenly throughout the country. However, a recent decision by the Third Circuit Court of Appeals, applying Pennsylvania law, provided greater clarity on how occurrence-based policies are to be interpreted in the context of construction projects, while also leaving the door open to creative attorneys who may try to recover on such policies from a different angle.

In *Zurich v. R.M. Shoemaker et al.*, No. 12-2238 (3d Cir., March 27, 2013), the Third Circuit affirmed a decision by a federal district court dismissing a contractor's claim against its insurer for property damage incurred as a result of water infiltration allegedly caused by a subcontractor's faulty workmanship. The County of Monmouth, New Jersey, had retained Shoemaker to oversee a project for additions to a county prison. The County claimed that Shoemaker had negligently supervised its subcontractors, and thereby permitted willful misconduct by a subcontractor which, allegedly, led to water infiltration and subsequent damage to structural elements and personal property at the prison. Shoemaker sought coverage through its occurrence-based CGL policies, which defined the term "occurrence" as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions."

Shoemaker's argument relied on a 2007 Pennsylvania Supreme Court opinion, *Donegal Mutual Insurance Company v. Baumhammers,* 938 A.2d 286 (Pa. 2007), in which the court held that an insurer may be required to defend against claims where the insured's negligence enabled the third party's intentional misconduct. However, the Third Circuit did not rely upon the *Baumhammers* opinion, which hinged "upon the randomness of the third party's misconduct--a shooting rampage…from the perspective of the insured, his parents" (the parents were sued for negligence in allowing their son to have a gun and failing to procure mental health treatment for him), and instead relied on a 2006 Pennsylvania Supreme Court opinion, *Kvaerner Metals Div. of Kvaerner U.S., Inc. v. Commercial Union Ins. Co.*, 908 A.2d 888 (Pa. 2006) and a 2007 Pennsylvania Superior Court opinion, *Millers Capital Insurance Co. v. Gambone Brothers Development Co.*, 941 A.2d 706 (Pa.Super.Ct. 2007) and held that faulty workmanship under a contract is not sufficiently fortuitous to qualify as an "occurrence." The Third Circuit explained that "the crucial inquiry dictating whether a general liability insurer must defend its insured under an occurrence-based policy is whether an event was sufficiently fortuitous from the perspective of the insured to qualify as an 'occurrence'." Such policies are not intended to cover contractual liability of the insured where the completed work is not that for which the damaged person had bargained. The Court held that "[f]aulty workmanship--whether caused by the contractor's negligence alone or by the contractor's negligent supervision, which then permitted the willful misconduct of its subcontractors--does not amount to an 'accident' or 'occurrence.'"

Interestingly, in a footnote, the Third Circuit opined that a "more difficult question may be presented when a plaintiff sues a defendant for faulty workmanship without an underlying contract between the parties (such as when the plaintiff sues a subcontractor directly),"and suggested that the lack of a contract could make the event "fortuitous" from the perspective of the insured. Undoubtedly, such a theory is sure to be tested by enterprising attorneys in the near future.