

IS THAT PRODUCT LIABILITY CLAIM COVERED?

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Commercial General Liability ("CGL") insurance policies broadly provide defense and indemnity coverage for claims of bodily injury and property damage asserted against an insured. Product manufacturers are frequently called upon to defend against claims that their products caused bodily injury or property damage. Construction companies, for example, also face significant exposure for claims arising out of alleged faulty workmanship or defective construction. These policyholders look to their insurance companies to provide them with a defense against any such claims, and for indemnity in the event of a judgment or a settlement.

If the policyholder is able to establish that a claim falls within its policy's coverage grant, the burden then shifts to the insurer to prove that an exclusion or other policy provision operates to preclude coverage. Insurers often attempt to minimize or eliminate their exposure to products liability claims by citing the "your product" or "your work" exclusions (among others) that appear in standard-form CGL policies. Insurers have also attempted to argue that the underlying claims asserted against the policyholder do not constitute an "occurrence" under the CGL policy.

Although there are many reasons why an insurer may disclaim

coverage for a claim that involves faulty products or workmanship, this article addresses these critical policy provisions, as they are among the most frequently cited.

Property damage caused by an occurrence

The standard CGL policy provides coverage for "property damage" that is caused by an "occurrence." The term "occurrence" is often defined as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." (See CG 00 01 12 07, Sec. V, ¶ 13). While that definition may seem fairly straightforward, many insurance coverage disputes alleging faulty workmanship or construction defects focus on the issue of what constitutes an "occurrence" under a standard CGL policy.

Insurers typically contend that faulty workmanship or defective products do not constitute an occurrence because doing so arguably shifts the burden to the insured to demonstrate that there is an "occurrence," thereby relieving the insurer of its burden to prove that a coverage exclusion applies. However, courts have increasingly rejected these arguments over time. In fact, the majority view is that faulty workmanship triggers an occurrence if resulting property is damaged. (See, e.g., *BPI, Inc. v.*

Nationwide Mut. Ins. Co., 235 W. Va. 303, 311 (W. Va. 2015) (collecting cases)).

Recently, courts in North Dakota, West Virginia, Connecticut, and Georgia all rejected insurers' "no occurrence" arguments in the context of construction defect cases. (See *K&L Homes, Inc. v. Am. Family Mut. Ins. Co.*, 829 N.W.2d 724 (N.D. 2013); *Cherrington v. Erie Ins. Prop. & Cas. Co.*, 231 W. Va. 470 (2013); *Capstone Bldg. Corp. v. Am. Motorists Ins. Co.*, 67 A.3d 961 (Conn. 2013); *Taylor Morrison Servs. v. HDI-Gerling Am Ins. Co.*, 746 S.E.2d 587 (Ga. 2013)).

Pennsylvania is another jurisdiction that has recently shifted course. For years, courts determined that contractual claims of faulty workmanship or product defects did not constitute occurrences in Pennsylvania. See for example, *Kvaerner Metals Div. of Kvaerner U.S., Inc. v. Commercial Union Ins. Co.*, 589 Pa. 317, 322 (2006). In *Kvaerner*, the court held that a coke oven battery that failed to meet specifications did not constitute an occurrence. The *Kvaerner* decision was limited to situations where a defective product did not cause damage to anything other than the product itself, although court decisions that followed *Kvaerner* did not recognize this critical distinction. Nevertheless, in 2013, a Pennsylvania appellate court held that claims asserted against a manufacturer constituted an occurrence, and found coverage because the underlying claims alleged damage to persons or property other than the insured's product.

In *Indalex, Inc. v. National Union Fire Ins. Co. of Pittsburgh, PA*, 83 A.3d

418, 425 (Pa. Super. 2013), *appeal denied*, 627 Pa. 759 (2014), several lawsuits were filed against Indalex alleging that windows and doors it supplied to a residential construction project were defectively designed or manufactured, resulting in water leakage that caused physical damage to the underlying plaintiffs' residences. Relying on *Kvaerner*, the insurer asserted that faulty workmanship and product defects do not qualify as an "occurrence" under the policy. The court disagreed and found that the insurer owed Indalex a duty to defend because the underlying claims alleged property damage to property other than Indalex's product.

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An increasing number of jurisdictions are joining the majority view that faulty products and defective construction can constitute "occurrences" under most CGL policies, particularly where such products or work cause damage to other property. Therefore, policyholders should not assume that there is no coverage if their products or work cause bodily injury or property damage.

"Your work" and "your product" exclusions

Most CGL policies exclude coverage for property damage to the insured's product. (See CG 00 01 12 07, Sec. I, Coverage A, ¶ 2.k.) "Your product" is typically defined as any goods or products, other than real property, manufactured, sold, handled, distributed or disposed of by the insured.

Similarly, the "your work" exclusion states that the CGL policy will not provide coverage for property damage to "your work arising out of it or any part of it and included in the products-completed operations hazard." (See CG 00 01 12 07, Sec. I, Coverage A, ¶ 2.l.) The purpose of the "your work" exclusion is to prevent a liability policy from acting as a performance bond covering a contractor's work, or serving as a warranty on the quality of the work itself. Instead, the liability policy is intended to protect the contractor when its work damages someone else's property. On the other hand, coverage for faulty workmanship does not necessarily transform a liability policy into a performance bond, because performance bonds are broader than liability policies in that they guarantee completion of a construction contract upon the contractor's default, and benefit the owner of a project rather than the contractor. (See *U.S. Fire Ins. Co. v. J.S.U.B., Inc.*, 979 So. 2d 871, 888 (Fla. 2007)).

In other words, the "your product" exclusion is utilized to avoid coverage for damage to the insured's own product, but usually will not exclude coverage for damage to other property ("third party property

damage”) caused by the insured’s product (see, e.g., *Hartford Fire Ins. Co. v. Thermos L.L.C.*, 2015 U.S. Dist. LEXIS 156373 (N.D. Ill. Nov. 18, 2015)). The “your product” exclusion also will not negate coverage where the insured’s defective product is incorporated into the product of another and causes damage to that other product.

The “your work” and “your product” exclusions are comparable, and both are often cited by insurers in products liability and faulty workmanship claims. For example, in *Thruway Produce, Inc. v. Mass. Bay Ins. Co.*, 114 F. Supp. 3d 81 (W.D.N.Y. 2015), the insurer relied on both exclusions to deny coverage under the policy when the insured supplied poisonous apples that were ultimately incorporated into baby food. The court, however, held that the exclusions did not apply, because the poisoned apples damaged “other property”—the baby food. Similarly, in *Harleysville Worcester Ins. Co. v. Paramount Concrete, Inc.*, 10 F. Supp. 3d 252, 266 (D. Conn. 2014), the court held that the insured’s product (shotcrete), which caused a pool to crack and leak, constituted damage caused by the insured’s product, not to the insured’s product, and as a result, the “your product” exclusion did not apply.

Case law in recent years has confirmed that the “your work” and “your product” exclusions do not preclude coverage for third party property damage. (See *Wood v. Preferred Contrs. Ins. Co. Risk Retention Grp. LLC*, CV 14-128-M-DLC, 2015 U.S. Dist. LEXIS 151140, *10 (D. Mont. Nov. 6, 2015)). For example, damage to carpeting caused by a contractor’s defective installation of windows is covered under most CGL policies. Similarly, faulty materials and workmanship causing a home to be continuously exposed to moisture, producing damage to surrounding structural elements, is covered. (See, e.g., *Pulte Homes of N.M., Inc. v. Ind. Lumbermens Ins. Co.*, 367 P.3d 869 (N.M. Ct. App. 2015)).

In *Magnus, Inc. v. Diamond State Ins. Co.*, 101 F. Supp. 3d 1046, 1049-50 (D. Kan. 2015), a manufacturer supplied defective aluminum adapters to another company, which utilized the adapters in arrows that were being sold to customers. The purchaser subsequently informed the manufacturer that it was experiencing problems with the adapters “seizing,” or becoming permanently affixed to the arrows. As a result, the purchasers’ customers could not remove the broadheads or perform “screw-off functions” on blades or arrow tips. Consequently, the arrows became

worthless or had very little value and the purchasers’ customers were not satisfied with the product.

Eventually, the purchaser sued the manufacturer for lost profits and earnings, and the manufacturer’s insurance company disclaimed coverage, citing among other provisions the “your product” exclusion in the policy. However, the court rejected the insurer’s position and held that because the purchaser was not seeking damages for property damage to the manufacturer’s product, but rather for damages (lost profits) caused by damage to third parties’ property (i.e., its customers’ arrows), the “your product” exclusion did not apply.

In a majority of jurisdictions, standardform CGL policies cover claims of faulty workmanship and product defects for damage caused to other work or other products. Although insurers often cite various policy exclusions, these exclusions do not necessarily apply, and policyholders should carefully review all of the underlying facts and have a complete understanding of their policy’s provisions and exclusions, as well as the applicable law in their respective jurisdictions, in order to determine whether an underlying claim is covered or at least potentially covered.

