

Consequential Damage Caused by Subcontractor's Faulty Work is Covered under Developer's CGL Policy

On August 4, 2016, the New Jersey Supreme Court joined a long list of states' high courts when it affirmed a ruling that consequential damages resulting from a subcontractor's faulty work constituted "property damage" caused by an "occurrence" under the property developer/general contractor's commercial general liability policies. *Cypress Point Condo. Ass'n, Inc. v. Adria Towers, L.L.C.*, No. 076348, 2016 WL 4131662 (N.J. Aug. 4, 2016). There, because the policy exclusion for property damage to the insured's work contained an exception for work performed by a subcontractor, the policies afforded coverage to the developer.

In *Cypress Point*, the plaintiff, a condominium association, brought suit against the developer regarding faulty work performed by subcontractors. Specifically, the subcontractors had "defectively built or installed roofs, gutters, brick facades, exterior insulation and finishing system siding, windows, doors and sealants." As a result, the association claimed that water infiltrated the building, causing damage to steel supports, sheetrock, interior common areas and residential units.

The developer sought coverage for the association's lawsuit under its CGL policies. After the insurers denied, the association named the insurers as defendants and sought a declaration that its claims against the developer were covered. Importantly, the association did not argue that the cost to repair/replace the faulty work was covered. Rather, it claimed that the consequential damage caused by the water infiltration fell within the policies insuring agreement as property damage caused by an occurrence. In support of this argument, the association pointed to the 1986 ISO form that, unlike the 1973 ISO form, contains a subcontractor exception to the "your work" exclusion. The association argued that adding the exception implied that resulting damage from a subcontractor's faulty work would necessarily fall within the insuring agreement of the developer's policy, or the exception would be meaningless.

In response, the insurers argued that CGL policies are intended to provide coverage only for damage caused by faulty workmanship to other property, and not to the project itself. Moreover, the insurers contended that a subcontractor's faulty workmanship does not have the fortuity element required to constitute an occurrence because it is a predictable consequence of the construction business. According to the insurers, because the claims did not satisfy the insuring agreement, consideration of policy exclusions was not necessary.

Prior to *Cypress Point*, there was New Jersey authority to support the insurers' position that the entire project constituted the general contractor/developer's "work," such that a subcontractor's faulty work that damages another part of the project is not property damage caused by an occurrence. See *Pennsylvania Nat. Mut. Cas. Ins. Co. v. Parkshore Dev. Corp.*, 403 F. App'x 770 (3d Cir. 2010); *Pennsylvania Gen. Ins. Co. v. Menk Corp.*, No. CIV.A. 11-0978 JAP, 2011 WL 5864109, at *5 (D.N.J. Nov. 21, 2011) ("[J]ust as in *Parkshore*, the Association's claims all relate to faulty workmanship by or on behalf of Defendants, and the Association does not allege damage to any property other than Defendants' work product — specifically, all of the design and construction at the Saratoga."); *National Union Fire Insurance Co. of Pittsburgh, PA v. Turner Construction Co.*, 119 A.D.3d 103, 107, 986 N.Y.S.2d 74 (1st Dep't 2014) (applying New Jersey law, and holding that "there is no 'occurrence' under a commercial general liability policy where faulty construction damages only the insured's own work, and faulty workmanship by subcontractors hired by the insured does not constitute covered property damage caused by an 'occurrence' for purposes of coverage under commercial liability insurance policies issued to the general contractor, since the entire project is the general contractor's work.").

The New Jersey Supreme Court rejected this reasoning and found instead that a subcontractor's



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faulty work that damages the general contractor's otherwise non-defective work product is an occurrence that causes property damage. It first analyzed existing New Jersey cases interpreting the 1973 ISO form (which does not have a subcontractor exception to the "your work" exclusion and has a different definition of occurrence), such as *Weedo v. Stone-E-Brick, Inc.*, 81 N.J. 233, 405 A.2d 788 (1979) and *Firemen's Ins. Co. of Newark v. Nat'l Union Fire Ins. Co.*, 387 N.J. Super. 434, 904 A.2d 754 (App. Div. 2006). The *Cypress Point* court emphasized that *Weedo* and *Firemen's* were not on point because those cases addressed the cost of replacing defective work, not consequential damages from that work. The repair and replacement of defective work was excluded by the your-work exclusion in the absence of any subcontractor exception.

The *Cypress Point* court found that the water infiltration at the project caused mold growth, damage to the common areas and individual units, and loss of use. It concluded that there was property damage within the terms of the policies. Next, the court rejected the insurers' argument that the subcontractor's faulty work is not an occurrence because it is foreseeable to the developer. Instead, it held that the subcontractor's faulty work, from the standpoint of the developer, is an accident sufficient to satisfy the occurrence definition. Finally, the court stated that there is a "strong recent trend in the case law of most federal circuit and state courts interpreting the term 'occurrence' to encompass unanticipated damage to nondefective property resulting from poor workmanship" under the 1986 ISO form.

The *Cypress Point* decision calls into question the application of *Weedo* and *Firemen's* to a 1986 ISO form policy. However, it is important to note that the court did not hold that a subcontractor's faulty work that must be repaired or replaced is covered. Rather, this case is limited to a subcontractor's faulty work that causes property damage to **another** part of a project. In New Jersey, such consequential damage is now likely covered by the general contractor or developer's CGL policy.
