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News Concerning Insurance Coverage Issues

COZEN O'CONNOR

Pennsylvania Court Holds Defectively Designed Windows and Doors May Give Rise to an "Occurrence"

On December 3, 2013, the intermediate Pennsylvania Court of Appeals decided *Indalex, Inc. v. National Union Fire Ins. Co. of Pittsburgh, PA,* and concluded that an "occurrence" under a commercial umbrella liability policy may arise in the context of defectively manufactured components used in a home, which resulted in alleged property damage and bodily injury. This holding is the first appellate level decision in Pennsylvania in recent years to find an insured occurrence in the context of claims by homeowners.

The Underlying Claims

The insured, Indalex, was a distributor of doors and windows. The court described these as "an off-the-shelf product." The underlying lawsuits claimed that Indalex's windows and doors were defectively designed or manufactured and resulted in water leakage that caused physical damage, such as mold and cracked walls, and also caused "personal injury," presumably from exposure to mold. Indalex was sued directly by homeowners, as well as by contractors or product suppliers who had been sued by homeowners.

The claims asserted causes of action based upon strict liability, negligence, breach of warranty, and breach of contract. The court concluded that the pleadings framed the role played by Indalex "in terms of a bad product [it distributed], which can be construed as an 'active malfunction,' and not merely bad workmanship."

The Insurance Coverage Dispute: the Court Finds Coverage After Distinguishing Prior Cases That Held Faulty Construction Is Not an "Occurrence"

Indalex submitted a claim for defense and indemnity to its general liability insurer and also to National Union, its umbrella insurer. The National Union policy provided coverage for, among other things, bodily injury or property damage "… caused by an 'occurrence' …." The policy defined occurrence, as an "accident, including continuous or repeated exposure to conditions, which results in bodily injury or property damage neither expected nor intended from the standpoint of the Insured." National Union declined Indalex's claim, asserting there was no occurrence triggering coverage.

The court began by addressing the Pennsylvania Supreme Court's decision in *Kvaerner Metals Division of Kvaerner U.S., Inc. v. Commercial Union Ins. Co.*, 908 A.2d 888 (Pa. 2006). There, the court concluded that faulty workmanship in constructing a coke oven battery was not an occurrence, as to "hold otherwise would be to convert a policy for insurance into a performance bond." The *Indalex* court concluded that *Kvaerner* premised its conclusion on "the fact that the underlying complaint contained only claims for breach of contract and breach of warranty," whereas Indalex was subject to tort claims. Relatedly, the court concluded it was improper for the trial court to apply Pennsylvania's "gist of the action" doctrine in a coverage action for purposes of characterizing the underlying claims as purely contractual.

The court next undertook to distinguish its prior decision in *Millers Capital Ins. Co. v. Gambone Bros. Development Co., Inc.*, 941 A.2d 706 (Pa. Super. 2007). (Cozen O'Connor represented the prevailing insurers both in *Kvaerner* and in *Gambone*). The court concluded that the underlying claims in *Gambone* had turned exclusively upon a claim for "breach of warranty." Further, the only damages, the court stated, were to the insured's work product.

The court held that neither *Kvaerner* nor *Gambone* was controlling, because, it concluded, neither

Richard C. Mason
Member

rmason@cozen.com
Phone: (215) 665-2717
Fax: (215) 665-2013

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case involved (1) tort claims, or (2) injury to property other than the insured's own work product. In contrast, the underlying claims in *Indalex* involved "an off-the shelf product that failed and allegedly caused property damage and personal injury." The claims were described as "a bad product, which can be construed as an 'active malfunction,'" and thus not merely "faulty workmanship."

In addition, the court deemed the policy before it as distinguishable from the policy in *Kvaerner*. The policy in *Indalex* included a clause providing that an occurrence meant injury "neither expected nor intended from the standpoint of the Insured." The policy in *Kvaerner* omitted the quoted language. The court stated this omission meant "the insured's subjective viewpoint," was relevant, and therefore a duty to defend arose insofar as "damages such as mold-related health issues were arguably not expected."

Observations

Indalex may be appealed to the Pennsylvania Supreme Court, which has discretion whether to accept the case. The Pennsylvania Supreme Court ordinarily would hear an appeal if, for example, it concludes that *Indalex* is in conflict with other Superior Court decisions or with the Supreme Court's own *Kvaerner* decision.

The Superior Court limited its holding in four respects. **First**, the court emphasized that the result was substantially driven by the insured's role as a distributor of "off-the-shelf products." **Second**, the court noted that the damage here was to persons and property other than the insured's work product. **Third**, the court relied on the presence of tort claims rather than mere breach of contract/breach of warranty claims. **Fourth**, the court indicated that a policy containing a definition of occurrence that does not include the "standpoint of the insured" clause might warrant a different result. Accordingly, whether *Indalex* applies to a particular claim will require a careful and nuanced analysis of the underlying clams, the law and the insurance contract wording.

Please feel free to contact Richard Mason at rmason@cozen.com or (215) 665-2717 if you have any questions or need assistance with this issue.