

THE STATE OF SOUTH CAROLINA
IN THE SUPREME COURT

RECEIVED

JUN - 4 2007

S.C. SUPREME COURT

APPEAL FROM CHARLESTON COUNTY
Court of Common Pleas
B. Hicks Harwell, Jr., Circuit Court Judge

Trial Court Case No. 2002-CP-10-4390

Auto-Owners Insurance Co., Appellant,

v.

Virginia T. Newman and
Trinity Construction, Inc., Respondents.

AMICUS CURIAE BRIEF OF
SOUTH CAROLINA COMMUNITY ASSOCIATIONS INSTITUTE

George E. Mullen
Daniel F. Oberklein
MULLEN WYLIE, LLC
70 Arrow Road, Suite 1
Post Office Box 5969
Hilton Head Island, South Carolina 29938
(843) 785-6969
Fax #: (843) 785-6711
Attorneys for the Amicus Petitioner

TABLE OF CONTENTS

TABLE OF AUTHORITIES	iii
QUESTIONS PRESENTED FOR REVIEW.....	1
STATEMENT OF THE CASE.....	1
STATEMENT OF THE FACTS.....	2
ARGUMENT.....	5
A. THE EXISTENCE OF “PROPERTY DAMAGE” IS UNDISPUTED.....	7
B. CONTINUOUS AND REPEATED EXPOSURE TO MOISTURE IS AN “OCCURRENCE” UNDER THE CGL POLICY’S COVERAGE GRANT	7
1. “OCCURRENCE” MUST BE DETERMINED USING THE POLICY DEFINITION AND NOT COMMINGLED AND CONFUSED WITH OTHER CONCEPTS IN OTHER PARTS OF THE POLICY	7
2. THE POLICY’S DEFINITION OF “OCCURRENCE” EXPRESSLY PROVIDES THAT CONTINUOUS AND REPEATED EXPOSURE TO SUBSTANTIALLY THE SAME GENERAL HARMFUL CONDITIONS IS AN “ACCIDENT”	12
3. READING THE INSURANCE POLICY AS A WHOLE REQUIRES A FINDING THAT WATER INTRUSION RESULTING FROM A SUBCONTRACTOR’S DEFECTIVE WORK CAN BE AN OCCURRENCE	14
C. EVEN THOUGH THE DAMAGE WAS SUSTAINED TO A PART OF TRINITY’S WORK PRODUCT, THE POLICY EXCLUSIONS DO NOT EXCLUDE COVERAGE IN THIS CASE.....	15
1. THE “FAULTY WORKMANSHIP” AND “YOUR WORK” EXCLUSIONS DO NOT EXCLUDE COVERAGE IN THIS CASE.....	15
2. CONTINUOUS AND REPEATED EXPOSURE TO MOISTURE IS NOT EXPECTED OR INTENDED BY THE GENERAL CONTRACTOR	19
D. NUMEROUS DECISIONS IN THIS STATE AND ELSEWHERE HAVE RECOGNIZED THAT PROGRESSIVE DAMAGE CAN RESULT FROM AN OCCURRENCE UNDER A CGL POLICY	21
CONCLUSION.....	24

TABLE OF AUTHORITIES

South Carolina Cases

<i>Boggs v. Aetna Cas. & Sur. Co.</i> , 272 S.C. 460, 252 S.E.2d 565 (1979)	13, 21
<i>C.D. Walters Constr. Co. v. Firemans Ins. Co. of Newark</i> , 281 S.C. 593, 316 S.E.2d 709 (Ct. App. 1984)	22
<i>Century Indemnity Co. v. Golden Hills Builders, Inc.</i> , 348 S.C. 559, 561 S.E.2d 355 (2002)	16
<i>Fritz-Pontiac-Cadillac-Buick v. Goforth</i> , 312 S.C. 315, 440 S.E.2d 367 (1994)	6
<i>Joe Harden Builders, Inc. v. Aetna Cas. & Sur. Co.</i> , 326 S.C. 231, 486 S.E.2d 89 (1997).....	22
<i>L-J, Inc. v. Bituminous Fire and Marine Ins. Co.</i> , 366 S.C. 117, 621 S.E.2d 33 (2005).....	passim
<i>Stewart v. State Farm Mut. Auto. Ins. Co.</i> , 341 S.C. 143 533 S.E.2d 597 (Ct. App. 2000).....	6
<i>Yarborough v. Phoenix Mut. Life Ins. Co.</i> , 266 S.C. 584, 592, 225 S.E.2d 344, 348 (1976)	6

Federal Court Cases

<i>Amerisure Mut. Ins. Co. v. Paric Corp.</i> , No. 4:04CV430-DJS, 2005 U.S. Dist. LEXIS 30383 (E.D. Mo., Oct. 21, 2005)	23
<i>Bituminous Casualty Corp. v. R.C. Altman Builders, Inc.</i> , No. 2:01-4267-DCN, 2006 U.S. Dist. LEXIS 53354 (D.S.C., July 28, 2006).....	10
<i>Essex Builders Group, Inc. v. Amerisure Insurance Co.</i> , 429 F. Supp. 2d 1274 (M.D. Fla. 2005).....	24
<i>French v. Assurance Co. of America</i> , 448 F.3d 693 (4 th Cir. 2006)	21, 23
<i>Okatie Hotel Group, Inc. v. Amerisure Ins. Co.</i> , C.A. No. 2:04-2212-23, 2006 U.S. Dist. LEXIS 2980 (Jan. 13, 2006).....	8, 23

Pennsylvania Mfrs. Assoc. Ins. Co. v. Dargan Construction Co.,
C.A. No. 4:05-113-25-TLW-TER, 2006 U.S. Dist. LEXIS 53366
(D.S.C., July 13, 2006) 9, 11, 23

Stonehenge Engineering Corp. vs. Employers Ins. of Wausau,
201 F.3d 296 (4th Cir. 2000) 22

Zurich American Ins. Co. v. Sumter Hotel Group L.P.,
C.A. No. 3:06-561-CMC, 2007 U.S. Dist LEXIS 29093
(D.S.C., April 19, 2007) 10,11

Other State Cases

American Family Mut. Ins. Co. v. American Girl, Inc.,
673 N.W.2d 65, 78 (Wis. 2004) 14

Lee Builders, Inc. v. Farm Bureau Mutual Ins. Co.,
137 P.3d 486, 494 (Kan. 2006) 13, 14, 23

Swank Enterprises, Inc. v. St. Paul Fire and Marine Ins. Co.,
154 P.3d 52 (Mont. 2007) 24

Travelers Indemnity Company of America v. Moore & Associates, Inc.,
216 S.W.3d 302, 309 (Tenn. 2007)..... 17, 20, 23

QUESTION PRESENTED

Does continuous and repeated exposure to moisture intrusion, caused by faulty workmanship, constitute an “occurrence,” even when the only damage is to the contractor’s work product itself?

STATEMENT OF THE CASE

This Court’s decision in *L-J, Inc. v. Bituminous Fire and Marine Ins. Co.*, 366 S.C. 117, 621 S.E.2d 33 (2005) has caused tremendous confusion in the insurance industry, and *L-J*’s application to coverage in construction defect litigation has been the subject of much debate. A number of carriers interpret *L-J* as a complete bar to coverage of construction disputes, while a number of other carriers read *L-J* as extending the coverage for contractors. Additionally, several decisions of the U.S. District Court for the District of South Carolina have reached different and irreconcilable results when applying *L-J*, further compounding the uncertainty.

Members of South Carolina chapter of Community Associations Institute (“SCCAI” or the “Amicus Peitioner”), have become snarled in the dispute and uncertainty among CGL carriers and their insured contractors, resulting in inability to resolve construction disputes with carriers who are denying coverage. The Amicus Petitioner represents the interests of property owners around the State of South Carolina that are claimants in a variety of construction cases against developers, contractors, sub-contractors and materialmen who are insured by the Appellant and other insurance carriers in South Carolina under similar or identical insurance

policies. Accordingly, questions of coverage and the duty of the liability insurance company to defend and ultimately satisfy a claim brought against its insured (i.e., a negligent general contractor) are of great importance to the property owners that the Amicus Petitioner represents.

Accordingly, the Amicus Petitioner now respectfully asks this Honorable Court to review the present case by focusing squarely on the plain language of the insurance policy and affirming the trial court's finding of coverage. To the extent that this Court's previous decision in *L-J*, which involved an insurance policy with identical language, reaches a contrary result, the Amicus Petitioner urges the Court to clarify that decision in order to reach a result that remains faithful to the insurance policy's language.

STATEMENT OF THE FACTS

- 1) Auto-Owners issued a Commercial General Liability (CGL) policy to Trinity Construction, Inc. ("Trinity"), which policy is essentially the Insurance Services Office (ISO) 1986 Standard CGL policy. Trinity had this coverage with Auto-Owners in effect from July 1993 to July 2000. (R. p. 2).
- 2) In **Section I – Coverages** of the commercial general liability policy issued by Auto-Owners, the insuring agreement defines under what circumstances it will grant coverage for an event:
 1. Insuring Agreement
 - a. We will pay those sums that the insured becomes legally obligated to pay as damages because of ... "property damage" to which this insurance applies....
 - b. This insurance applies to "property damage" only if:

- (1) The “property damage” is caused by an “occurrence” that takes place in the “coverage territory”; and
- (2) The “property damage” occurs during the policy period.

(R. p. 237).

- 3) The policy defines “occurrence” as “an accident, *including continuous or repeated exposure to substantially the same general harmful conditions.*”

(R. p. 245, emphasis added).

- 4) The policy defines “property damage” as “[p]hysical injury to tangible property...” (R. p. 246)

- 5) The policy excludes coverage for “[t]hat particular part of any property that must be restored, repaired or replaced because ‘your work’ was incorrectly performed on it.” (R. p. 239, § j(6)).

- (a) The policy excepts from this exclusion “property damage” included in the “products-completed operations hazard.” (R. p. 239).

- (b) The policy defines “products-completed operations hazard” as “all . . . ‘property damage’ occurring away from premises you own or rent arising out of . . . ‘your work’ except: (1) products that are still in your physical possession; or (2) work that has not yet been completed or abandoned.”

- 6) The CGL policy purchased by Trinity includes the “products-completed operations hazard” coverage, for which Trinity paid an additional annual premium of \$783. (R. pp. 267-268).

- 7) The policy excludes coverage for “ ‘Property damage’ to ‘your work’ arising

out of it or any part of it and including in the 'products-completed operations hazard.'" The policy goes on to provide that "[t]his exclusion does not apply if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor." (R. p. 246, § *l*).

- 8) Trinity used subcontractors to build the residence at issue in the present case, as stipulated by the parties. (R. p. 3).
- 9) Trinity's subcontractors negligently applied the stucco to the exterior of Ms. Newman's house and failed to properly flash the windows and doors. Both of these deficiencies are building code violations and deviations from industry standards. (R. pp. 95-101).
- 10) Construction of the residence was completed on or before May 28, 1999, when the Certificate of Occupancy was issued. (R. p. 2).
- 11) Since completion, the house has been subjected to continuous and repeated exposure to water and moisture intrusion resulting in rot and decay of the building components. (R. pp. 108-09)

ARGUMENT

The construction and insurance industries are once again in a stand-off over the scope of coverage of their insurance contracts in South Carolina. *L-J* failed to provide answers; rather, the decision only created more confusion and inconsistencies in construction litigation. The Amicus Petitioner urges this Court to seize the opportunity to define the obligations and expectations from CGL policies.

The Court must distinguish between (1) the “property damage”; (2) the “occurrence”; and (3) the “business risk” exclusions. Far too often and far too many courts have mistakenly commingled and intertwined these elements of coverage, resulting in appellate opinions that interchange the terms and concepts of occurrence, property damage, and excluded damages. This improper analysis has resulted in convoluted opinions devoid of rational analysis based on the plain language of the insurance policy.

The Amicus Petitioner suggests a fresh approach in reviewing this case. Instead of relying upon statements in previous judicial opinions that hopelessly commingle the various coverage concepts and confuses the issues, this Court should instead focus on the language of the insurance policy. While the end result of the analysis may remain the same, the clarity of this new approach will provide a framework for consistency in coverage disputes.

This Court’s *L-J* opinion contains three broad statements that illustrate the results of commingling the various coverage concepts:

- 1) Equating damage with occurrence (“[W]e hold that the *damage* in this case did not constitute an *occurrence*.” *L-J*, 366 S.C. at 123, 621 S.E.2d at 36 (emphasis added).)

- 2) Stating that a CGL policy does not cover faulty workmanship that damages the work product alone (The CGL policy “provide[s] coverage ... , *not in cases where faulty workmanship damages the work product alone.*” *L-J*, 366 S.C. at 123; 621 N.E.2d at 36, n.4 (emphasis in original)).
- 3) Declaring that faulty workmanship never constitutes an occurrence.

These broad statements have resulted in decisions that are contrary to the insurance policy’s language and have caused tremendous confusion as other courts (most notably, the U.S. District Courts in South Carolina) have read *L-J* and tried to apply it to cases before them. In fact, as seen in the discussion below, two federal judges in South Carolina have found that *L-J* extends coverage, and two other federal judges in South Carolina have interpreted *L-J* to deny coverage.

Fortunately, this rampant confusion that results from commingling the coverage concepts can be avoided by simply adhering to the language of the insurance policy. In any insurance coverage case, there are three questions that must be answered to determine if the loss is covered: (1) Was there property damage?; (2) Was there an “occurrence”?; and (3) If so, then is coverage defeated by any applicable exclusion in the policy? In performing this analysis, the focus must remain squarely on the language of the policy, which forms the insuring agreement between the parties.¹

¹ This Court must enforce, not write, contracts of insurance and we must give policy language its plain, ordinary, and popular meaning. *Stewart v. State Farm Mut. Auto. Ins. Co.*, 341 S.C. 143 533 S.E.2d 597 (Ct. App. 2000) (citing *Fritz-Pontiac-Cadillac-Buick v. Goforth*, 312 S.C. 315, 440 S.E.2d 367 (1994)). All of the policy provisions should be considered, "and one may not, by pointing out a single sentence or clause, create an ambiguity." *Yarborough v. Phoenix Mut. Life Ins. Co.*, 266 S.C. 584, 592, 225 S.E.2d 344, 348 (1976). The meaning of a particular word or

A. THE EXISTENCE OF “PROPERTY DAMAGE” IS UNDISPUTED.

The trial court found that the wood deterioration and rot to the substructure and sheathing of the Newman residence constituted property damage, which Auto-Owners has not disputed. The insurance policy broadly defines property damage as “physical injury to tangible property.” The policy does not distinguish “tangible property” that is the work of the insured contractor from other property, nor does it distinguish “damage” to work of the insured contractor from damage to other work. The concept of “your work” and the insured contractor’s work product does not come into play until the analysis turns to the policy exclusions. Any physical injury to any tangible property is “property damage” under the insurance policy.

B. CONTINUOUS AND REPEATED EXPOSURE TO MOISTURE IS AN “OCCURRENCE” UNDER THE CGL POLICY’S COVERAGE GRANT.

1. “OCCURRENCE” MUST BE DETERMINED USING THE POLICY DEFINITION AND NOT COMMINGLED AND CONFUSED WITH OTHER CONCEPTS IN THE “EXCLUSIONS” PART OF THE POLICY .

The most troubling error in this Court’s *L-J* opinion and the federal court opinions applying *L-J* is the convoluted discussion of “occurrence.” Rather than simply applying the policy’s definition of “occurrence,” the courts have commingled various policy exclusions and a distorted definition of property damage with “occurrence” to create a legal quagmire. Under a proper analysis, concepts such as “your work,” “faulty workmanship,” and the insured contractor’s work product,

phrase is not determined by considering the word or phrase by itself, but by reading the policy as a whole and considering the context and subject matter of the insurance contract. *Id.*

which are found in the policy exclusions, must not be considered until after it has been determined that there was an “occurrence.”

The Auto-Owners policy defines “occurrence” as “an accident, *including continuous or repeated exposure to substantially the same general harmful conditions.*” (R. p. 245, emphasis added). The lower court found, as a result of improper flashing and improper installation of stucco, that the Newman home has been subjected to continuous and repeated water intrusion, damaging the wood structure and substructure of the house and the sheathing beneath the stucco exterior. (R. pp. 108-09). This resulting water intrusion clearly constitutes a “*continuous or repeated exposure to substantially the same general harmful conditions,*” which is specifically defined to be an “occurrence” under the policy language quoted above.

The definition of “occurrence” makes no attempt to define or limit what property may be damaged by the harmful conditions. “Property damage” is a completely separate concept from “occurrence” and must be analyzed separately, as discussed above. In *L-J*, this Court stated, “we hold that the *damage* in this case did not constitute an *occurrence.*” *L-J*, 366 S.C. at 123, 621 S.E.2d at 36 (emphasis added). The *damage* is not the *occurrence*; the damage is the *result* of the occurrence. This faulty treatment of “damage” as a type of “occurrence” misreads the policy language and has caused great confusion among other courts. For example, in *Okatie Hotel Group, Inc. v. Amerisure Ins. Co.*, C.A. No. 2:04-2212-23, 2006 U.S. Dist. LEXIS 2980 (D.S.C., Jan. 13, 2006), Judge Duffy stated that “the property damage to Plaintiff’s hotel – caused by exposure to the harmful conditions

of leaks and moisture – constituted an ‘occurrence’ under the CGL policies issued by Defendant to Devcon.” Although the *Okatie Hotel* court reached the correct result and found there was an “occurrence,” the opinion is infected by the mishandled treatment of “occurrence” from *L-J*. In contrast, the court in *Pennsylvania Manufacturers’ Association Insurance Co. v. Dargan Construction Co.*, C.A. No. 4:05-113-25-TLW-TER, 2006 U.S. Dist. LEXIS 53366 (D.S.C., July 13, 2006), correctly explained that “[s]ince the policy defines an occurrence as ‘an accident, including continuous or repeated exposure to substantially the same general harmful conditions,’ the water exposure meets the requirements of the definition of ‘occurrence.’” *Id.* at *11. This simpler analysis, which adheres to the insurance policy’s definition of “occurrence,” provides clarity in reaching the correct result.

Likewise, it is error to read into the definition of “occurrence” a requirement that the damage be to property other than the insured contractor’s work product. The concepts of “your work” and the insured contractor’s “work product” must not be considered until the analysis shifts to the policy exclusions, where these concepts are found. In *L-J*, this Court framed the issue as “whether property damage to the work product alone, caused by faulty workmanship, constitutes an occurrence.” *L-J*, 366 S.C. 121, 621 S.E.2d at 35. The Court later stated in footnote 4:

The CGL policy may, however, provide coverage in cases where faulty workmanship causes a third party bodily injury or damage to other property, *not in cases where faulty workmanship damages the work product alone.*

L-J, 366 S.C. at 123; 621 N.E.2d at 36, n.4 (emphasis in original). As a result of this confusion in *L-J*, this error of commingling the “work product” and “occurrence”

issues runs rampant through the U.S. District Court's opinion in *Zurich American Ins. Co. v. Sumter Hotel Group L.P.*, C.A. No. 3:06-561-CMC, 2007 U.S. Dist LEXIS 29093 (D.S.C., April 19, 2007) ("*Sumter Hotel*"), where Judge Currie stated that damages suffered by defectively applied paint were "merely defects in the work product" and "cannot, therefore, constitute an 'occurrence' under South Carolina law absent proof of some resulting damage to other property." *Id.* at *12. The confusion of the "your work" concept with "occurrence" is so pervasive in the *Sumter Hotel* court's analysis that the court devoted only one short paragraph at the end of its opinion to the "your work" exclusion, almost as an afterthought, saying "[s]uch injuries are also excluded under the 'Your Work' exclusion." *Id.* at *18. Any discussion of the damage being confined to the contractor's work product should be centered on this exclusion and should not be focused on the meaning of "occurrence."

The same error is seen on an even larger scale in *Bituminous Casualty Corp. v. R.C. Altman Builders, Inc.*, No. 2:01-4267-DCN, 2006 U.S. Dist. LEXIS 53354 (D.S.C., July 28, 2006) ("*Altman*"), where Judge Norton inferred that construing *L-J* was akin to entering the gates of hell,² (which may explain the hellish decision issued in *Altman*). The court proceeded to hold, based on its reading of *L-J*, that property damage to the work product alone, caused by faulty workmanship, does not constitute an occurrence. Judge Norton does not even consider the policy exclusions related to "your work" or "work product," instead relying almost solely on footnote 4

² "Abandon hope, all ye who enter here." *Altman*, 2006 U.S. Dist. LEXIS 53354 at *1 (quoting Dante, *The Divine Comedy (Inferno)*, Canto III).

of the *L-J* opinion. The *Altman* case alone demands clarification of *L-J*.

Yet another major cause of confusion introduced by *L-J* is the Court's ultimate holding that *faulty workmanship does not constitute an occurrence*. *L-J*, 366 S.C. at 125, 621 S.E.2d at 37. Aside from unnecessarily limiting the concept of "occurrence," this statement is so broad that it leads some courts to automatically find no coverage simply because the case involves faulty workmanship, even where the faulty workmanship causes the "occurrence." In the *Sumter Hotel* case, the court stated:

Under South Carolina law, claims against contractors for faulty workmanship are not covered by CGL insurance policies unless the faulty workmanship causes injury to property *other than the work of the contractor*.

Id. at *7-8 (citing *L-J*) (emphasis added).

The proper analysis addresses the construction defects as a *cause of the "occurrence,"* as recognized by Judge Wooten in *Pennsylvania Manufacturers' Association*:

The defects in the construction of the building are not, in themselves, sufficient to constitute an "occurrence." However, the lawsuit goes on to claim that, "the buildings were defectively constructed, *which has led to substantial water intrusion* resulting in substantial deterioration including rot, rust, mold, mildew, and corrosion of the various components of the buildings." . . . Therefore, the Court concludes that there was an "occurrence" resulting in "property damage" in the underlying lawsuit that would provide for coverage under the CGL policy.

Pennsylvania Manufacturers' Association, 2006 U.S. Dist. LEXIS 53366 at *11-*12.

This analysis correctly recognizes the distinctions between the various coverage

terms and applies them to the facts properly. The Amicus Petitioner urges this Court to adopt the reasoning framework outlined by the *Pennsylvania Manufacturers' Association* court in this simple, yet powerful explanation that construction defects or faulty workmanship can cause an “occurrence” (here, water intrusion) which, in turn, can result in “property damage” (here, deterioration and rotting of the building components). This is precisely the same set of events that happened in the present case.

2. THE POLICY'S DEFINITION OF "OCCURRENCE" EXPRESSLY PROVIDES THAT CONTINUOUS AND REPEATED EXPOSURE TO SUBSTANTIALLY THE SAME GENERAL HARMFUL CONDITIONS IS AN "ACCIDENT."

In determining whether there has been an “occurrence” in the present case, this Court does not need to ascertain the general meaning of the word “accident” because the insurance policy expressly tells us that this word includes “*continuous or repeated exposure to substantially the same general harmful conditions.*” Whatever else “accident” may include is irrelevant to the case at bar, because we *know* that it *does* include “*continuous or repeated exposure to substantially the same general harmful conditions,*” which is what happened at the Newman house at issue in this litigation. It is unnecessary to engage in a legal determination of how the word “accident” should be construed generally because we are faced with a

damage event that is precisely specified to be an “occurrence” by the policy. 3

As mentioned above, the language in the insurance policy in the *L-J* case was identical in all material respects to the policy at issue in the present case. Like the policy here, the Bituminous policy in *L-J* defined “occurrence” as “an accident, including continuous or repeated exposure to substantially the same general harmful conditions.” See *L-J*, 366 S.C. at 122, 621 S.E.2d at 35. To the extent that this Court’s decision in *L-J* holds that damage caused by continuous or repeated exposure to water intrusion is not an “occurrence” under this policy language, the Amicus Petitioner urges this Court to clarify that decision as it completely ignores the “*continuous or repeated exposure to substantially the same general harmful conditions*” clause.⁴ A clear statement from this Court acknowledging and properly enforcing this CGL policy language would speak volumes to the construction and insurance industries and would restore the expectations that players in these fields had when they entered into these insurance contracts.

3 See *Lee Builders, Inc. v. Farm Bureau Mutual Ins. Co.*, 137 P.3d 486, 495 (Kan. 2006) (discussed *infra*) (finding that the term “occurrence” is “an even more expansive coverage term than ‘accident’ – because faulty materials and workmanship provided by Lee’s subcontractors caused continuous exposure of the Steinberger home to moisture.”)

4 In the pre-1986 ISO standard CGL policy, “occurrence” was defined as “an accident, including injurious exposure to conditions, which results, during the policy period, in bodily injury or property damage neither expected nor intended from the standpoint of the insured.” In *Boggs v. Aetna Cas. & Sur. Co.*, 272 S.C. 460, 252 S.E.2d 565 (1979), this Court acknowledged and properly enforced the “including injurious exposure to conditions” clause, finding that sewage leaking into a home from a septic tank improperly located uphill from the home constituted an “occurrence” under the contractor’s CGL policy. The comparable language in the post-1986 ISO standard CGL policy at issue in the present case (“continuous or repeated exposure to substantially the same general harmful conditions”) is even more clear, and the same justifications used by the *Boggs* court require this language to be similarly enforced.

3. READING THE INSURANCE POLICY AS A WHOLE REQUIRES A FINDING THAT WATER INTRUSION RESULTING FROM A SUBCONTRACTOR'S DEFECTIVE WORK CAN BE AN OCCURRENCE.

Finally, as one court has observed, if damage resulting from a subcontractor's work cannot be an "occurrence," then the "faulty workmanship" and "your work" exclusions (exclusions j(6) and l, discussed *infra*), and the exceptions thereto, in the insurance policy would be superfluous and meaningless – they would never be operative.

A court need only ask *why* the CGL policy includes an exclusion for property damage to the insured's own work and that of its subcontractors to understand that it would be nonsensical for the policy to include such a provision if this kind of property damage could never be caused by an 'occurrence' in the first place. A court need only ask *why* the CGL policy specifically includes an express exception to the 'your work' exclusion for property damage arising out of the work of a subcontractor to understand that this kind of property damage must be included in the broad scope of the term 'occurrence' in the coverage grant, and that the coverage determination for this kind of property damage must be made based on the construction-specific policy exclusions.

Lee Builders, Inc. v. Farm Bureau Mutual Ins. Co., 137 P.3d 486, 494 (Kan. 2006) (emphasis in original). The very presence of these exclusions in the policy indicates that damage caused by subcontractor's faulty workmanship is an "occurrence" under the policy. *See also American Family Mut. Ins. Co. v. American Girl, Inc.*, 673 N.W.2d 65, 78 (Wis. 2004) ("Why would the insurance industry exclude damage to the insured's own work or product if the damage could never be considered to have arisen from a covered "occurrence" in the first place?")

The Court should also consider the plain language of the “products-completed operations hazard” coverage purchased by Trinity. This coverage for completed operations specifically includes “all property damage . . . arising out of ‘your work’,” without exception for damage to “your work” or “faulty workmanship.” Reading into the definition of “occurrence” a requirement that damage be to property other than the contractor’s work product completely obviates the completed operations coverage for “all property damage arising out of ‘your work’.”

C. EVEN THOUGH THE DAMAGE WAS SUSTAINED TO A PART OF TRINITY’S WORK PRODUCT, THE POLICY EXCLUSIONS DO NOT EXCLUDE COVERAGE IN THIS CASE.

1. THE “FAULTY WORKMANSHIP” AND “YOUR WORK” EXCLUSIONS DO NOT EXCLUDE COVERAGE IN THIS CASE.

The Auto-Owners insurance policy contains several exclusions that are frequently referred to as “business risk” exclusions. The first of these provides:

2. Exclusions

This insurance does not apply to:

* * * * *

j(6): That particular part of any property that must be restored, repaired or replaced because your ‘work’ was incorrectly performed on it.

(R. p. 239). This exclusion, standing alone, would bar coverage for purely “faulty workmanship,” as argued by Auto-Owners. Insurance companies, however, have chosen to sell “products-completed operations hazard” coverage, which specifically restores the coverage excluded by paragraph j(6). Subsection j concludes by expressly stating:

Paragraph (6) of this exclusion does not apply to “property damage” included in the “products-completed operations hazard”.

(R. p. 239). In fact, the insured in this case, Trinity, purchased this “products-completed operations hazard” coverage from Auto-Owners. Accordingly, the “faulty workmanship” exclusion in paragraph j(6) *does not* apply in this case. Any decision to the contrary would disregard the plain language of the policy and deny Trinity the benefit of the “products-completed operations hazard” coverage that it specifically purchased.

Auto-Owners cites *Century Indemnity Co. v. Golden Hills Builders, Inc.*, 348 S.C. 559, 561 S.E.2d 355 (2002), for the proposition that repair or replacement of substrate and substructure of a home is excluded by the faulty workmanship provision. (Brief of Appellant, p. 9). Auto-Owners, however, fails to mention a critical aspect of the *Century Indemnity* case that renders it inapplicable to the case at bar. In *Century Indemnity*, the house was not completed and turned over to the homeowner until after the expiration of the contractor’s CGL policy. Thus, it was not a completed products case, and the “products-completed operations hazard” coverage therefore did not apply. *See id.* at 568 (“The work had clearly had not been completed at the end of the policy period. . . . As a result, the products-completed operations hazard provision does not restore coverage.”) In contrast, the water intrusion and damage to the Newman house occurred after completion. Therefore, the “products-completed operations hazard” coverage that Trinity purchased clearly applies to the claim for damage at the house, and it operates to restore coverage that would otherwise have been excluded by the “faulty workmanship” exclusion.

In addition to the “faulty workmanship” exclusion of paragraph j(6), there is another similar exclusion that must be considered:

2. Exclusions

This insurance does not apply to:

* * * * *

- l. “Property damage” to “your work” arising out of it or any part of it and including in the “products-completed operations hazard.”

This exclusion does not apply if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor.

(R. p. 239). This “your work” exclusion, however, clearly does not apply in the present case because it specifically includes an exception restoring coverage for damage arising from work “performed on your behalf by a subcontractor.”⁵ In *Travelers Indemnity Company of America v. Moore & Associates, Inc.*, 216 S.W.2d 302 (Tenn. 2007), the Supreme Court of Tennessee was presented with this issue and provided an excellent analysis. After explaining that water intrusion damages to a hotel caused by faulty installation of windows by a subcontractor “are initially excluded by the ‘your work exclusion’ in the general contractor’s CGL policy, the court noted that “[t]he CGL in this case, however, contains a subcontractor exception to the ‘your work’ exclusion.” *Id.*, 216 S.W.2d at 310. In light of this “change in the CGL policy language, . . . damages resulting from the subcontractor’s faulty installation of the windows are not excluded from coverage, even if those damages affected [the general contractor’s] work.” *Id.* The Tennessee court specifically and

forcefully rejected the proposition that damages to the work of the insured contractor arising from faulty workmanship can never be the result of an “occurrence.”

These two exclusions (which *do not* apply in the present case) for damages resulting from “faulty workmanship” to “your work” are at the heart of Appellant’s argument and are a key linchpin in this Court’s *L-J* decision. In its Reply Brief, Appellant argues that “the damage to the house’s substrate is excluded under the policy because the entire house is the insured general contractor’s own ‘work product.’” (Reply Brief of Appellant, p.2). This same reasoning was used by this Court in *L-J*, where the Court framed the issue as “whether property damage *to the work product alone, caused by faulty workmanship, constitutes an occurrence.*” *L-J*, 366 S.C. at 121, 621 S.E.2d at 35 (emphasis added). These exclusions should stand on their own; the Court should not incorporate them into the definition of “occurrence.”

Nevertheless, this Court in *L-J* failed to discuss these two exclusions and the exceptions thereto. The Court simply reached the broad conclusion, as a matter of law, that damages stemming from the insured contractor’s faulty workmanship to his work product are not an “occurrence” and therefore not covered by a CGL policy.

This conclusion, however, simply gets the present case wrong as it completely disregards several critical provisions in the insurance contract. It ignores the definition of “occurrence,” as previously discussed; it ignores the “products-

⁵ The faulty work that allowed the water intrusion at the house in this case was performed by subcontractors, as stipulated by the parties (R. p. 3).

completed operations hazard” coverage that Trinity purchased, and it ignores the subcontractor exception to the “your work” exclusion. This is precisely the outcome that results when the policy exclusions are commingled with the analysis of “occurrence” in a case involving work performed by subcontractors. The wrong outcome is reached in these cases because the court, by improperly finding no “occurrence” and thus not performing a proper analysis of the policy exclusions, never reaches the subcontractor exception and the “products-completed operations hazard” coverage, both of which narrow the scope of exclusions and restore coverage that would otherwise be excluded. Under the facts of this case, the policy language requires a finding that the damages awarded by the arbitrator are covered under the Auto-Owners insurance contract.

2. CONTINUOUS AND REPEATED EXPOSURE TO MOISTURE IS NOT EXPECTED OR INTENDED BY THE GENERAL CONTRACTOR.

Auto-Owners asserts that, even if the damage to the house caused by continuous and repeated exposure to moisture is an “occurrence,” coverage is nevertheless barred by an exclusion that provides as follows:

2. Exclusions

This insurance does not apply to:

* * * * *

- a. “[P]roperty damage” expected or intended from the standpoint of the insured. . . .

(R. p. 237). Auto-Owners is arguing that Trinity Construction expected or intended its subcontractor to apply the stucco and flashing improperly, in violation of the

applicable building codes and industry standards, such that water would intrude into the house. In its Brief, Auto-Owners states that “[t]he evidence offered at trial indicates that Trinity, or a reasonable builder, expects water to reach the substrate because of defective construction.” (Brief of Appellant, p.14). This argument, however, misses one essential point: no reasonable contractor expects defective construction! This point is especially critical where, as here, the faulty work was performed by subcontractors.

In *Travelers Indemnity*, the Supreme Court of Tennessee explained that “the determination of whether an ‘accident’ has occurred under the terms of a CGL requires us to determine whether damages would have been foreseeable *if the insured had completed the work properly.*” *Travelers Indemnity*, 216 S.W.2d at 309 (emphasis added). In other words, no rational person would expect that he or his subcontractors will perform faulty work. Because water intrusion would certainly be unforeseen and unexpected if work is performed properly, it does not trigger exclusion 2(a) for “expected or intended” property damage in the CGL policy.

The *Travelers Indemnity* court provided an instructive example illustrating the absurdity that would result from finding water intrusion damage to be “expected or intended.”

An example is instructive. Travelers concedes that if a contractor improperly installs a shingle that later falls and hits a passerby, this event is unforeseeable and is an “occurrence” or “accident.” However, Travelers simultaneously insists that if a contractor improperly installs windows that leak and cause flood damage to the hotel, this event is foreseeable because it is a natural consequence of improperly installed windows. We are unpersuaded by this distinction. A shingle falling and

injuring a person is a natural consequence of an improperly installed shingle just as water damage is a natural consequence of an improperly installed window. If we assume that either the shingle or the window installation will be completed negligently, it is foreseeable that damages will result. If, however, we assume that the installation of both the shingle and the window will be completed properly, then neither the falling shingle nor the water penetration is foreseeable and both events are "accidents." Assuming that the windows would be installed properly, Moore could not have foreseen the water penetration. Because we conclude the water penetration was an event that was unforeseeable to Moore, the alleged water penetration is both an "accident" and an "occurrence" for which there is coverage under the "insuring agreement."

Id. at 309. Applying this same reasoning to exclusion (a), damages caused by water intrusion are not "expected or intended" and therefore not excluded from coverage. The same result was reached by the U.S. Court of Appeals for the Fourth Circuit in *French v. Assurance Company of America*, 448 F.3d 693, 704 (4th Cir. 2006), where the court found exclusion (a) inapplicable, emphasizing that "there is no evidence that [the general contractor] subjectively expected or intended that the nondefective structure and walls of the Frenches' home would suffer from moisture intrusion."

D. NUMEROUS DECISIONS IN THIS STATE AND ELSEWHERE HAVE RECOGNIZED THAT PROGRESSIVE DAMAGE CAN RESULT FROM AN OCCURRENCE UNDER A CGL POLICY.

The damage at the Newman house was a classic case of progressive damage caused by faulty construction. This Court has recognized that progressively-occurring damage can be caused by an "occurrence" under a CGL policy. *Boggs v. Aetna Cas. & Sur. Co.*, 272 S.C. 460, 252 S.E.2d 565 (1979) (finding that an occurrence need not be sudden but may be produced over a period of time); *Joe*

Harden Builders, Inc. v. Aetna Cas. & Sur. Co., 326 S.C. 231, 486 S.E.2d 89 (1997) (finding that defectively constructed concrete columns and floor slabs caused brick walls to crack which constituted an “occurrence”). *See also Stonehenge Engineering Corp. vs. Employers Ins. of Wausau*, 201 F.3d 296 (4th Cir. 2000) (finding that buckled siding, cracks in foundations and sagging balconies in a condominium building caused by construction defects in the balconies, roofs, foundations, basement walls, porches, decks, handrails, pickets, stairs, siding, flashing, and subflooring constituted an “occurrence”).⁶

In *Joe Harden Builders*, this Court examined the trigger of coverage in cases of progressive damage that was caused by faulty construction. The Court rejected the argument that the faulty construction by itself is the occurrence when it rejected the notion that coverage is triggered at time of the negligent act. When this Court held coverage “is triggered at the time of an injury-in-fact and continuously thereafter,” it recognized that there can be more than one cause and, therefore, more than one occurrence in a progressive damage case. *Id.*

⁶ Auto-Owners cites *C.D. Walters Constr. Co. v. Firemans Ins. Co. of Newark*, 281 S.C. 593, 316 S.E.2d 709 (Ct. App. 1984) in support of the proposition that damages flowing from faulty workmanship cannot be an occurrence and are not covered under the policy. This case is distinguishable from the present case because coverage in *C.D. Walters* was rejected based on an exclusion. The court found that the Broad Form Property Endorsement exclusion barred coverage because the contractor’s work was ongoing – it was not a completed products case like the present case is. Contrary to Auto-Owners’ representations in its Brief, the *C.D. Walters* court did not find that no “occurrence” had happened.

Additionally, the insurance policy in *C.D. Walters* was a pre-1986 CGL policy that had different language than the Auto-Owners policy at issue here and does not include the definition of “occurrence” that is used in the post-1986 CGL policy. In *C.D. Walters*, the court was not faced with, and therefore did not address the coverage of, an occurrence involving “continuous or repeated exposure” to harmful conditions.

The Amicus Petitioner has intervened in this action because the conditions found at the Newman house are similar to the most common construction failures that are experienced by the Petitioner's members. As a result of defective construction, water intrudes into a structure, and over time, this water intrusion results in rot and deterioration of the building and its components. Numerous cases from the courts of various states have found that this sort of progressive damage resulting from defective construction can be an "occurrence" and be covered by a CGL policy. See *Okatie Hotel Group, Inc. v. Amerisure Ins. Co.*, C.A. No. 2:04-2212-23 (Jan. 13, 2006) ("the property damage to Plaintiff's hotel – caused by exposure to the harmful conditions of leaks and moisture – constituted an 'occurrence' under the CGL policies issued by Defendant to Devcon."); *Pennsylvania Mfrs. Assoc. Ins. Co. v. Dargan Construction Co.*, C.A. No. 4:05-113-25-TLW-TER, 2006 U.S. Dist. LEXIS 53366 (D.S.C., July 13, 2006) (finding that water intrusion damage of three buildings due to poor workmanship was an "occurrence" covered by a CGL policy); *French v. Assurance Co. of America*, 448 F.3d 693 (4th Cir. 2006) ("the moisture intrusion into the nondefective structure and walls of the Frenches' home was an accident, and therefore, an 'occurrence'"); *Travelers Indemnity Company of America v. Moore & Associates, Inc.*, 216 S.W.2d 302, 309 (Tenn. 2007) ("We conclude that defective workmanship may constitute an 'occurrence.'"); *Lee Builders, Inc. v. Farm Bureau Mutual Ins. Co.*, 137 P.3d 486, 494 (Kan. 2006) ("The damage in the present case is an occurrence – an even more expansive coverage term than "accident" – because faulty materials and workmanship provided by Lee's subcontractors caused continuous exposure of the Steinberger home to moisture.");


Essex Builders Group, Inc. v. Amerisure Insurance Co., 429 F. Supp. 2d 1274 (M.D. Fla. 2005) (finding that water intrusion damage can be an “occurrence”); *Amerisure Mut. Ins. Co. v. Paric Corp.*, No. 4:04CV430-DJS, 2005 U.S. Dist. LEXIS 30383 (E.D. Mo., Oct. 21, 2005) (finding that allegations of water damage from leaks through EIFS and windows could be an “occurrence”); *Swank Enterprises, Inc. v. St. Paul Fire and Marine Ins. Co.*, 154 P.3d 52 (Mont. 2007) (finding that a contractor’s CGL policy provided coverage for stripping improper paint from and repainting filter tanks and pipes, when the harm was caused by the painting subcontractor selecting the wrong type of paint for the job).

In *L-J*, the Court noted the “majority rule” that faulty workmanship standing alone, resulting in damages only to the work product itself, does not constitute an “occurrence.” The Amicus Petitioner suggests that this is not the majority rule considering post-1986 CGL policies, and clearly it is not the trend as evidenced by the cases cited above, all decided since *L-J*.

CONCLUSION

For the foregoing reasons, the Amicus Petitioner respectfully asks this Court to affirm the judgment of the trial court, clearly stating that continuous and repeated exposure to water intrusion caused by faulty workmanship constitutes an “occurrence,” including where the resulting damage is only to the contractor’s work product.

Respectfully submitted,


George E. Mullen (S.C. Bar #4130)
Daniel F. Oberklein (S.C. Bar #75295)
MULLEN WYLIE, LLC
70 Arrow Road, Suite 1
Post Office Box 5969
Hilton Head Island, South Carolina 29938
(843) 785-6969
Fax #: (843) 785-6711
Attorneys for the Amicus Petitioner

May 31, 2007
Hilton Head Island, South Carolina

THE STATE OF SOUTH CAROLINA
IN THE SUPREME COURT

RECEIVED

JUN 4 2007

APPEAL FROM CHARLESTON COUNTY
Court of Common Pleas
B. Hicks Harwell, Jr., Circuit Court Judge

S.C. SUPREME COURT

Trial Court Case No. 2002-CP-10-4390

Auto-Owners Insurance Co., Appellant,

v.

Virginia T. Newman and
Trinity Construction, Inc., Respondents.

PROOF OF SERVICE

I hereby certify that a true and correct copy of the Amicus Curiae Brief of South Carolina Community Association Institute was served on this 1st day of June 2007 via First Class U.S. Mail, postage prepaid, upon the following counsel of record:

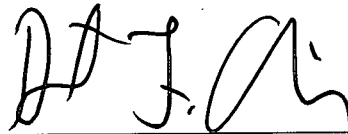
[ADDRESSES AND SIGNATURE ON FOLLOWING PAGE]

John L. McCants, Esquire
Ellis, Lawhorne & Sims, PA
P.O. Box 2285
Columbia, SC 29202
Attorney for Appellant, Auto-Owners Insurance Co., Inc.

Joseph K. Qualey, Esquire
Qualey & Beck, LLC
23 Broad Street
Charleston, SC 29401
Attorney for Respondent Virginia T. Newman

Michael S. Seekings, Esquire
Leath, Bouch & Crawford, LLP
P.O. Box 59
Charleston, SC 29402
Attorney for Respondent Virginia T. Newman

Frank M. Cisa, Esquire
Cisa & Dodds, LLP
622 Johnnie Dodds Boulevard
Mt. Pleasant, SC 29464
Attorney for Respondent Trinity Construction, Inc.



Daniel F. Oberklein

THE STATE OF SOUTH CAROLINA
IN THE SUPREME COURT

RECEIVED

JUN - 4 2007

APPEAL FROM CHARLESTON COUNTY
Court of Common Pleas
B. Hicks Harwell, Jr., Circuit Court Judge

S.C. SUPREME COURT

Trial Court Case No. 2002-CP-10-4390

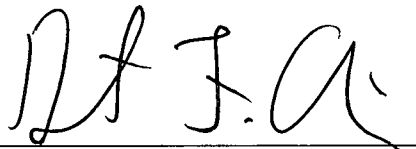
Auto-Owners Insurance Co., Appellant,

v.

Virginia T. Newman and
Trinity Construction, Inc., Respondents.

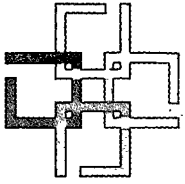
CERTIFICATE OF COUNSEL

The undersigned certifies that the Amicus Curiae Brief of South Carolina
Community Associations Institute complies with Rule 211(b), SCACR.



George E. Mullen (S.C. Bar #4130)
Daniel F. Oberklein (S.C. Bar #75295)
MULLEN WYLIE, LLC
70 Arrow Road, Suite 1
Post Office Box 5969
Hilton Head Island, South Carolina 29938
(843) 785-6969
Fax #: (843) 785-6711
Attorneys for the Amicus Petitioner

May 31, 2007
Hilton Head Island, South Carolina



MULLEN WYLIE

A T T O R N E Y S

RECEIVED

NOV 07 2007

November 6, 2007

S.C. SUPREME COURT

70 Arrow Road

P.O. Box 5969

Hilton Head Island, SC 29938

Phone: (843) 785-6969

Fax: (843) 785-6711

The Honorable Daniel E. Shearouse
Clerk, Supreme Court of South Carolina
P.O. Box 11330
Columbia, SC 29211

Re: *Auto Owners Ins. Co. v. Newman et al.*
Civil Action No. 2002-CP-10-4390

Dear Mr. Shearouse:

I am writing pursuant to Rule 208(b)(7), SCACR, to provide the Court with a citation of supplemental authority in support of the Amicus Curiae Brief filed by South Carolina Community Associations Institute in the above-referenced matter. The recent decision of the Supreme Court of Texas in *Lamar Homes, Inc. v. Mid-Continent Casualty Company*, No. 05-0832, 2007 Tex. LEXIS 797, 50 Tex. Sup. J. 1162 (August 31, 2007), supports the argument, contained on pages 21 through 24 of the Amicus Brief, that the greater weight of authority, particularly among recent decisions, recognizes that continuous and repeated exposure to harmful conditions, caused by faulty workmanship, constitutes an "occurrence" even when the only damage is to the contractor's work product itself.

Sincerely yours,

MULLEN WYLIE, LLC

Daniel F. Oberklein

George E. Mullen

Robert L. Wylie, IV

Francis E. Grimball

James E. Lady

Glynn L. Capell

Paige Fowler Bellamy

Arthur T. Meeder

Daniel F. Oberklein

cc: John L. McCants, Esquire
Joseph K. Qualey, Esquire
Michael S. Seekings, Esquire
Frank M. Cisa, Esquire
Kenneth E. Ormand, Jr., Esquire