

THE STATE OF SOUTH CAROLINA
In The Supreme Court

APPEAL FROM CHARLESTON COUNTY
Court of Common Pleas

B. Hicks Harwell, Jr., Circuit Court Judge

Case No. 2002-CP-10-4390

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

v.

Auto-Owners Insurance Co., Inc., Appellant.

**AMICUS BRIEF OF HARLEYSVILLE MUTUAL INSURANCE COMPANY
IN SUPPORT OF PETITION FOR REHEARING**

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Introduction

Pursuant to Rules 213, 221, and 224 of the South Carolina Appellate Court Rules Harleysville Mutual Insurance Company (“Harleysville”) hereby submits this amicus brief in support of the Appellant’s petition for rehearing in the above-referenced matter. A motion for leave to file this brief has been filed contemporaneously herewith. The petition for rehearing of this Court’s March 10, 2007, opinion in Auto Owners Insurance v. Newman and Trinity Construction, Op. No. 1383 (S.C. Sup. Ct. filed March, 10, 2008) (Shearouse Adv. Sh. No. 9 at 63) (hereinafter also as “Opinion or “Op.”) should be granted, as it overlooks or misapprehends several matters of fact and law, conflicts with other opinions of this Court, and with respect to certain aspects of the opinion, places this Court into an extreme position outside the majority of jurisdictions considering the issues.

Statement of Interest

Harleysville Mutual Insurance Company (“Harleysville”) is a casualty insurance company that writes property and casualty insurance policies around the country, including in South Carolina. Harleysville has substantial experience with the specific coverage issue in this case. Harleysville was the prevailing party in Brosnahan Builders, Inc. v. Harleysville Mut. Ins. Co., 137 F. Supp. 2d 517 (D. Del. 2001) in which the United States District Court for the District of Delaware found that a subcontractor’s faulty work did not constitute an occurrence and, therefore, there was no coverage under the Commercial General Liability (“CGL”) policy like the one in this case. To date, Harleysville has been involved in hundreds of disputes involving the issue of whether faulty work constitutes an occurrence under an insurance agreement. Moreover,

Harleysville is currently involved in several matters pending in South Carolina in which parallel issues are being disputed. In these actions, Harleysville's CGL policies contain identical language to the CGL policy in this case, including the "subcontractor's exception" to the "your work" exclusion.

Because of its extensive experience in similar litigation, Harleysville is very familiar with the circumstances and background of the claims at issue in this case and it is respectfully submitted that Harleysville's experience with the coverage questions in this case would be of assistance to the Court.

Argument Summary

The Opinion, which addresses issues related to CGL insurance policies, is in direct conflict with this Court's prior holding in L-J v. Bituminous Fire and Marine Insurance Company, 366 S.C. 117, 621 S.E.2d 33 (2005), and does not offer an explanation to clarify the inconsistencies between the two cases, which were based upon similar fact patterns. The Opinion also overlooks key facts in this case, including the actual allegations from the complaint in the original action between the home owner and the contractor. The Opinion also misapprehends the meaning of the "subcontractor's exception" to the "your work" exclusion, and fails to consider the type of events stemming from a subcontractor's negligence which are covered under a CGL policy. Further, the Opinion is inconsistent with the general insurance interpretation law of this State because in it, the Court looked first to an exclusion in the insurance policy to find the existence of coverage.

Finally, this Court's Opinion awards the insured damages for the repair and replacement of faulty work – costs not recoverable under a CGL policy regardless of

whether the Court maintains its conclusion that faulty workmanship can result in an occurrence. The Court overlooked the important public policy that a general contractor should not be allowed to hire sub par subcontractors and then look to the insurer for coverage when the subcontractor fails to properly perform work. Accordingly, as detailed below, this Court should grant the rehearing petition.

Law/Analysis

I. This Court's Opinion is inconsistent with previous opinions of this Court.

In L-J v. Bituminous, this Court held that CGL policies do not provide coverage for faulty workmanship, even if the work was performed by subcontractors, because CGLs only cover "occurrence[s]" and "faulty work" is not an occurrence. See L-J v. Bituminous, 366 S.C. at 119, 621 S.E.2d at 34 (2005). In Newman, this Court reaches the opposite conclusion by relying on an exception to an exclusion contained in the policy – i.e., the "subcontractor exception." However, this same exception existed in the policy at issue in L-J. In addition, in both L-J and in Newman, all work was performed by subcontractors on behalf of the general contractor. The allegations in both cases related to faulty work. Thus, the same result should have been obtained in Newman and L-J.

CGL insurance policies have been the subject of much litigation in this State over the past four years. In 2005, after two oral arguments and an earlier version of the opinion, this Court issued the final version of its opinion in L-J. In L-J, this Court held that a subcontractor's negligent or faulty work that results in damage to the work product alone does not constitute an occurrence and, therefore, the damage consisting of or caused by the negligent or faulty work is not covered under the CGL policy. Id. at 124,

621 S.E.2d 36. In L-J, the Court's analysis focused on ensuring that the ultimate responsibility for the damage resulting from the faulty work was borne by the one causing the damage – the subcontractor. Id. at 124, 621 S.E.2d 37. Further, this Court has generally held that faulty workmanship is not even an insurable risk. Century Indem. Co. v. Golden Hills Builders, Inc., 348 S.C. 559, 563-64, 561 S.E.2d 355, 357 (2002). This reasoning has been, and is, sound.

This Court was not alone in its holding in L-J. Recently, the Supreme Court of Pennsylvania relied on this Court's analysis in L-J to find that faulty or defective work was not a covered occurrence under CGL policies. See Kvaerner Metals Div. of Kvaerner United States, Inc. v. Commercial Union Ins. Co., 589 Pa. 317, 908 A.2d 888 (Pa. 2006) (citing to L-J and finding that faulty work of subcontractors did not constitute an occurrence under the CLG policy). Furthermore, as recognized by the Pennsylvania Supreme Court in acknowledging this Court's adoption of the majority position in L-J, "the majority of Courts have held that coverage under a CGL policy is not triggered by poor workmanship which causes injury to the work product itself." Id. at 335, 908 A.2d at 899.

This majority approach has been consistently recognized for several years and courts from many states have declined to find coverage for faulty work under CGL policies. See Essex Ins. Co. v. Holder, 2008 Ark. LEXIS 138 (Ark. 2008) (finding that faulty work did not constitute an occurrence under the CGL policy); See also Burlington Ins. Co. v. Oceanic Design & Constr. Inc., 383 F.3d 940, 948-49 (9th Cir. 2004) (predicting Hawaii courts would find no coverage); Travelers Indem. Co. v. Miller Bldg. Corp., 97 FED. APPX. 431, 434 (4th Cir. 2004) (predicting North Carolina courts would

find coverage only to extent defects damage carpet supplied by owner, not builder); Acuity v. Burd & Smith, 2006 ND 187, 721 N.W.2d 33, 39 (N.D. 2006); Kvaerner Metals Div. of Kvaerner U.S., Inc. v. Commercial Union Ins. Co., 589 Pa. 317, 908 A.2d 888, 899-900 (Pa. 2006); Auto-Owners Ins. Co. v. Home Pride Cos., 268 Neb. 528, 684 N.W.2d 571, 577 (Neb. 2004); Corder v. William W. Smith Excavating Co., 210 W. Va. 110, 556 S.E.2d 77, 82 (W. Va. 2001); Pursell Constr. Inc. v. Hawkeye-Security Ins. Co., 596 N.W.2d 67, 70 (Iowa 1999); Commerce Ins. Co. v. Betty Caplette Builders, Inc., 420 Mass. 87, 647 N.E.2d 1211, 1214 (Mass. 1995); Dodson v. St. Paul Ins. Co., 1991 OK 24, 812 P.2d 372, 378 (Okla. 1991); Peerless Ins. Co. v. Brennon, 564 A.2d 383, 386 (Me. 1989).

This Court's opinion in Newman departs from the majority rule and offers no rationale for its change of course. Accordingly, this Court's Opinion in Newman warrants rehearing in order to address the apparent inconsistencies with its opinion in L-J, other cases from this Court, and other jurisdictions following L-J.

II. This Court failed to look to the allegations of the underlying complaint from the original action in Newman v. Trinity.

The Court in L-J held that the party seeking coverage under a CGL policy must plead damages beyond the faulty work. In line with this requirement, the Court in L-J, noted that the general liability policy may "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." Id. at 123, n.4, 621 S.E.2d at 36, n.4. Yet, in Newman this Court failed to consider the underlying pleadings in the action originally filed by Newman against Trinity Construction, Inc. in Charleston

County. Newman v. Trinity Construction Co., Inc., C/A No. 00-CP-10-2549 (Chas. Co. Ct. of Comm. Pleas filed March 3, 2000).

The original pleadings in the suit by Newman against Trinity Construction were not in the Record before the Court. However, a review of the Complaint in that action online in the Charleston County Court of Common Pleas reveals that Newman only sought damages for faulty construction work. Further, the only pleading in the Record before this Court provides that in the action by Newman against Trinity, the allegation was: “that Trinity was negligent relative to the construction of a residence for Newman.” (R. p. 21).

Here, the policyholder, Trinity Construction, breached its contract to construct a house pursuant to state and local building codes by improperly installing the stucco siding. The only damage alleged in the complaint was the faulty work itself. The general contractor was entirely responsible for the proper building of the house. The underlying complaint does not allege any third party damage, only faulty work. Therefore, there is no accident under which the faulty workmanship could be considered an occurrence.

The policyholder breached the construction contract, for which there is no coverage under the policy. Hence, this Court departed from its previously announced analytical model and found coverage despite the indication that in the underlying pleadings, no third party damage was alleged to have occurred. Rehearing is thus warranted.

III. The “subcontractor’s exception” would not be rendered meaningless under L-J.

In its Opinion, this Court states:

[T]o interpret the term “occurrence” as narrowly as Auto-Owners suggests would mean that any time a subcontractor’s negligence damaged any part of the contractor’s overall project, a CGL insurer could deny coverage under the policy. This would render both the “your work” exclusion and the subcontractor’s exception to the “your work” exclusion in the policy meaningless.

Opinion at 69-70. This is not accurate, and this Court overlooks the scenarios in which a subcontractor *could* perform negligent or faulty work that could result in an occurrence which would be covered under the policy. The “subcontractor exception” language is not rendered meaningless, as set forth below.

If there is an occurrence, and thus coverage, but the occurrence was the result of faulty workmanship and only the work itself was damaged, the “your work” exclusion applies. However, there are various types of events that are covered by the subcontractor’s exception to this exclusion. One such example set forth in the National Underwriter Fire, Casualty and Surety Bulletins is as follows. Assume the insured is a general contractor that built an apartment building using various subcontractors to complete the work. See National Underwriter Co., Fire, Casualty & Surety Bulletins, Public Liability, A 3-14 (2001).¹ Also assume a subcontractor installed all wiring in the apartment building. Id. After the building is complete and put to its intended use, a defect in the building’s wiring causes the building to sustain substantial fire damage. Id. As a result, the named insured general contractor is sued by the building’s owner. In this scenario the damage sustained as a result of the fire is an occurrence, even though it resulted from the faulty work of a subcontractor. Id; see also) Kalchthaler v. Keller

¹ Courts often look to the FC&S Bulletin in considering policy language because insurance experts contribute to the bulletin which outlines examples of when coverage is *triggered*. See e.g. Prudential-LMI Commercial Ins. Co. v. Reliance Ins. Co., 27 Cal. Rptr. 2d 841, 844 (Cal. Ct. App. 1994) (stating with reference to the FC&S Bulletin: “It is difficult to characterize as objectively unreasonable an interpretation which would result in coverage which is proffered by insurance industry experts.”).

Constr. Co., 224 Wis. 2d 387, 399-400, 591 N.W.2d 169, 174 (Wisc. Ct. App. 1999 (citing to the same hypothetical regarding faulty wiring work performed by a subcontractor). Fire damage resulting from a subcontractor's faulty workmanship is an occurrence because it is not reasonably foreseeable or expected from the standpoint of the insured. See e.g. M. Mooney Corp. v. U.S. Fidelity & Guar. Co., 136 N.H. 463, 468 618 A.2d 793, 796 (N.H. 1992) (stating that insurer conceded and court agreed that fire damage caused by subcontractor's improperly installed chimney was unexpected from the standpoint of the insured and that the fire was the result of an occurrence). In such an instance, an occurrence would exist, the insurer could point to the "your work" exclusion, but then the "subcontractor exception" would provide an exception to the exclusion, and thus coverage.

Another example is as follows. Assume that a subcontractor failed to properly construct the foundation of a new home. After the home is complete, the new homeowner moves into the home. The new homeowner then hires a landscaping company to plant shrubs near the house. During the landscaping project, while using a Bobcat machine to dig a hole for a shrub, the landscaper bumps the foundation of the home with the machine. Due to the poorly constructed foundation, after the landscaper hit the home with the machine, a collapse of all or some portion of the home occurs. This event would also be a covered occurrence under the policy even though it would not have happened but for the subcontractor's poor work.

The above scenarios should be contrasted with what occurred here as fully expected in Charleston it rained repeatedly. The resulting moisture intrusion from the improperly applied stucco and the subcontractor's failure to install flashing surprised no

one – not even the insured contractor. Trinity Builders’ expert testified that “the obvious consequence of not doing this . . . is wood rot underneath the stucco.” (Resp. Br. at p. 11). Therefore, the Contractor knew or at the very least would reasonably foresee that moisture damage would be the consequence of improperly installed stucco and cannot now claim that it did not expect the resultant damage.

It is not unexpected that rain will fall and, therefore, rain cannot be considered an accident or occurrence. The CGL policy defines the word “occurrence” as “an accident, including continuous or repeated exposure to substantially the same general harmful conditions.” Compare L-J v., 366 S.C. at 122, 621 S.E.2d at 35; with R. p. 245. The word “accident” is not defined in the CGL policy, but South Carolina’s courts have found it to mean “an effect which does not ordinarily follow and cannot be reasonably anticipated from the use of those means, an effect which the actor did not intend to produce and cannot be charged with the design of producing” Ducker v. Central Sur. & Ins. Corp., 234 S.C. 228, 230-31, 107 S.E.2d 342, 343 (1959). However, fortuity – the chance or unforeseen event – is the touchstone of an accident. It is defined by the limits of the insured’s contract. Here, the CGL policy states that it does not apply to “property damage that is expected or intended from the standpoint of the insured.” Where the insured is a general contractor, who agreed to build the home (or other project) in a good and workmanlike manner, he cannot be heard to say it was an accident when he fails to keep his promise.

This Court’s Newman Opinion actually renders the policy’s *coverage* provisions meaningless, because each and every instance of faulty work performed by a subcontractor resulting in damage to anything other than the subcontractor’s own work

will now be covered. In fact, the Court's opinion, as set forth more fully below, even allows for the recovery for the faulty work of the subcontractor on the basis that it must be removed and replaced to correct damage to other work. This Court should grant rehearing and correct this result.

IV. An exception to an exclusion cannot create coverage under an insurance policy.

This Court's Opinion is inconsistent with case law from South Carolina and other jurisdictions holding that an exclusion in an insurance contract cannot create coverage under the policy. This Court states that: "[t]he facts of this case establish exactly the type of property damage the CGL policy was intended to cover after the 1986 amendment to the 'your work' exclusion." Opinion at p. 69. Yet, looking to an exclusion in the first instance to find coverage under an insuring agreement is inconsistent with the law of this state and many other jurisdictions. Exclusions exclude coverage and do not create coverage.

In L-J, this Court reversed the lower court's decision granting coverage. In doing so, this Court held that the "occurrence" definition had not been met and stated that "[b]ecause we find that the faulty workmanship does not constitute an 'occurrence,' we do not address [the other issues presented, including issues related to exclusions] to determine whether the policy exclusions apply." Id. at 125, 621 S.E.2d at 37. Other courts in South Carolina follow the rule that an exclusion in an insurance policy cannot create coverage. Engineered Products, Inc. v. Aetna Casualty & Sur. Co., 295 S.C. 375, 378-379, 368 S.E.2d 674, 675-76 (Ct. App. 1988) (internal citations omitted) (an exclusion does not provide coverage, but limits coverage).

A large number of courts across the country have also stated that “occurrence” does not include construction defects and construction defects do not constitute “property damage,” including in policies containing the subcontractor’s exception to the “your work” exclusion. An Oregon Supreme Court case, Oak Crest Construction Co. v. Austin Mutual Insurance Co., 998 P.2d 1254 (Or. 2000), is just one example. The plaintiff in that case was a general contractor that had to remove and replace its subcontractor’s defective painting work. The court ruled in favor of the insurer, noting that the term “‘accident’ has a tortious connotation,” meaning that there must be a breach of a duty of due care. Id. at 1257 (internal citation omitted). Absent such a breach, there cannot be an accident. As a result, the court correctly denied coverage under the policy.

The United States Court of Appeals for the Fourth Circuit, applying Virginia law, has also recently ruled that an exclusion cannot create coverage. In Travelers Indem. Co. v. Miller Bldg. Corp., 142 Fed. Appx. 147 (4th Cir. 2005), a subcontractor was hired to perform site development and selected defective fill material. Id. at 148. Like South Carolina, Virginia law is that breaches of contract and construction defects do not constitute occurrences. Id. at 149. The policyholder nonetheless contended that exclusion / in the policy created coverage. The court rejected this argument, stating: “Because the damage to the Wal-Mart store was not unexpected and, therefore, not an ‘occurrence,’ and because an exception to an exclusion does not grant or extend coverage, Travelers is not required under this policy to indemnify Miller for Wal-Mart’s damages.” Id. at 150.

This Court’ Opinion thus improperly relies on the existence of the subcontractor’s exception to the “your work” exclusion in the CGL policy and finds that the adoption of

this exception by the Insurance Services Office (“ISO”) created coverage under the policy. This holding is inconsistent with insurance contract interpretation generally and rehearing is thus warranted.

V. Even if the events in this case are found to be an “occurrence”, the repair and replacement of the defective stucco work should not be covered.

In Newman, in addition to finding coverage for the substrate, the Court erroneously ruled that the cost of repair and replacement of the stucco (defectively applied by the subcontractor) was covered by the CGL policy at issue. Opinion at p. 71. This places South Carolina in an extreme minority position on this issue. Your *amici* has not been able to locate one other decision where a court has expressly addressed the recovery of the cost of repair and replacement and found coverage to exist under a policy such as the one at bar. However, a number of courts around the country have found that direct repair/replacement costs for the defective or faulty workmanship itself is *not* covered by a standard CGL policy, even where other resulting damage may be covered. MW Builders, Inc. v. Safeco Insurance Company of America, 2008 U.S. App. LEXIS 3912 (9th Cir. 2007) (holding that costs for actual replacement of EIFS stucco was not covered by CGL policy despite coverage for other damages caused by defective installation); Nabholz Construction Company v. St. Paul Fire and Marine Insurance Company, 354 F.Supp.2d 917 (E.D.Ark. 2005) (cost of repair of defectively installed roof not covered by CGL policy although Plaintiff could recover damages resulting from roof leak); United Capitol Insurance Company v. Special Trucks, Inc., 918 F.Supp. 1250 (N.D. Ind. 1996) (cost arising from repair of defectively-built truck not covered under CGL policy despite coverage for other damages arising from crash); Acuity v. Burd & Smith Construction, Inc., 721 N.W.2d 33 (N.D. 2006) (finding damages for repair or

replacement of a defective roof were not covered under CGL policy, but damages to interior of building caused by the faulty roof were covered); McDonald Construction Company v. Bituminous Casualty Corporation, 279 Ga. App. 757 (Ga. App. 2006) (cost for replacing defectively installed tiles not covered under CGL policy).

The Fourth Circuit Court of Appeals has held similarly. French v. Assurance Co. of Am., 448 F.3d 693 (4th Cir. 2006) (applying Maryland law), involved a subcontractor's negligent application of EIFS stucco which resulted in extensive moisture intrusion and water damage to the otherwise non-defective structure and walls of a home. See Opinion at p. 69-70 citing French. The homeowners sued the contractor who subsequently sought coverage under his CGL policy for the cost of repair of the non-defective walls/structure *and* the stucco which was defectively applied by the subcontractor. French at 696.

Although the Court ultimately held that the damage to the non-defective structure and walls was covered under the CGL policy, the cost of replacement of the stucco itself was not covered. In so ruling, the Court said:

For analytical purposes, we deem it necessary to divide the property damage to the Frenches' home into two categories. The first category is the defective EIFS exterior. The second category is the damage to the nondefective structure and walls of the Frenches' home directly resulting from moisture intrusion through the defective EIFS exterior. . . We hold that just as the defective application of the building's stone facade in Lerner did not constitute an 'accident,' and, therefore, not an 'occurrence' under the materially similar CGL policies at issue in Lerner, so does the defective application of the EIFS exterior to the Frenches' home not constitute an 'accident,' and therefore, not an 'occurrence' under the 1986 ISO CGL Policies. . . 'The obligation to repair the facade itself is not unexpected or unforeseen under the terms of the sales contract. Therefore, the repair or replacement damages represent economic loss and consequently would not trigger a duty to indemnify under a CGL policy.'

Id. at 703.

Likewise, the Florida Supreme Court directly confronted the issue of whether the cost of repair/replacement of defective work by a subcontractor is covered by a CGL policy. The case of Auto-Owners Ins. Co. v. Pozzi Window Co., 2007 Fla. LEXIS 2391 (Fla. 2007), involved residential windows manufactured by Pozzi Window Company (“Pozzi”) which were negligently installed by a subcontractor. After moving into the house, the owner complained of water leakage around the windows caused by the subcontractor’s defective installation. The homeowner filed suit against Pozzi, the homebuilder, and the subcontractor. Pozzi subsequently entered into a settlement with the homeowner by agreeing to “remedy the defective installation of the windows.” *Id.* at *4. Thereafter, Pozzi also settled with the builder, and as the builder’s assignee, Pozzi filed a lawsuit against the builder’s insurer, Auto-Owners, for the cost of repair and replacement of the windows.

Auto-Owners paid the homeowner for personal property damage caused by the leaking windows, but refused to provide coverage for the cost of repair or replacement of the windows. Suit was filed in federal court and the Eleventh Circuit ultimately certified to the Florida Supreme Court the question of whether a standard CGL policy covers the cost of repair/replacement of defective work by a subcontractor. See Pozzi Window Company v. Auto Owners Insurance, 446 F.3d 1178 (11th Cir. 2006). In holding that the repair/replacement costs of the windows were ***not*** covered as property damage, Florida’s Supreme Court held as follows:

Auto-Owners does not contend, and there is no indication in the record, that the Builder expected the windows to be defectively installed. Thus. . . the defective installation of the windows in this case, which the Builder did not intend or expect, was an ‘occurrence’ under the terms of the CGL policies. However . . . in order to determine whether the policies provide

coverage, we must also address whether the 'occurrence' caused 'property damage' within the meaning of the policies. . .

The CGL policies define 'property damage' as '[p]hysical injury to tangible property, including all resulting loss of use of that property' . . . [The] subcontractor allegedly installed the windows defectively. Without more, this alleged defect is the equivalent of the 'mere inclusion of a defective component' such as the installation of a defective tire, and no 'property damage' has occurred. . . Accordingly, there is no coverage for the costs of repair or replacement of the defective work.

Pozzi Window Co., 2007 Fla. LEXIS at *14 - *16.

The case of SawHorse, Inc. v. Southern Guar. Ins. Co., 269 Ga. App. 493 (Ga. App. 2006) also presents an analogous situation. In SawHorse, a contractor was hired to add a second floor to a house. A subcontractor failed to install necessary support beams which resulted in damage to the second floor addition as well as the previously existing first floor structure. The contractor sought coverage for both types of damages under his CGL policy. The trial court found the business risk exclusion in the insurer's policy excluded all the damage from coverage.

The appeals court agreed with the trial court that the cost associated with repairing the second-floor damage, which resulted directly from the faulty workmanship, was specifically excluded. The Court said:

There are two kinds of risks that are incurred by a contractor. The first is the business risk borne by the contractor to replace or repair defective work to make the building project conform to the agreed contractual requirements. This type of risk is not covered by the [CGL] policy, and the business risk exclusions in the policy make this clear. The second is the risk that the defective or faulty workmanship will cause injury to people or damage to other property. Because of the potentially limitless liability associated with this risk, it is the type for which. . . commercial general liability coverage is contemplated. . . The risk intended to be insured is the possibility that the. . . work of the insured, once relinquished or completed, will cause bodily injury or damage to property other than to the. . . completed work itself, and for which the insured may be found liable.

[W]e agree with the trial court that the risk associated with repairing [damage to the second floor addition], which resulted directly from faulty workmanship, is specifically excluded. . .Such repair work was necessary to make the second-floor renovation conform to the contract between SawHorse and Hall and Rooks. Because this damage was a risk borne by SawHorse and excluded by the policy, the trial court properly granted Southern Guaranty summary judgment as to this portion of the claim.

Id. at 495 – 497. As to the existing first-floor structure, the court could not determine whether or to what extent the allegedly defective workmanship caused damage to the structure. Therefore, the Court remanded the case for further proceedings. Id. at 497.

This Court's decision to award damages for the cost to repair/replace the defective stucco work in its Newman opinion is also in direct contravention to other reported South Carolina decisions. See Century Indem. Co., 348 S.C. 559, 561 S.E.2d 355 (2002); see also Engineered Prods., Inc. v. Aetna Cas. & Sur. Co., 295 S.C. 375, 368 S.E.2d 674 (Ct. App. 1988) (under policy excluding coverage of insured's liability for damages resulting from restoration, repair, or replacement of its own defective work, insurer had no duty to defend its insured in action seeking compensation for replacement of rack system lost in storm).

The logic from courts in these cases is sound. First, compensating a party by providing coverage under a CGL policy to repair or replace a job which was deficient from the outset essentially serves as double compensation for the negligent party. See Pozzi Window Co. v. Auto-Owners Ins., 446 F.3d 1178, 1185 (11th Cir. 2006) (internal citations omitted) (finding that interpreting the CGL policy as providing coverage for construction deficiencies would enable a contractor to receive initial payment for the work from the homeowner, then receive subsequent payment from his insurance company to repair and correct deficiencies in his own work, and finding such an

approach improper). Here, the general contractor was initially paid to have stucco properly applied to the house. While this Court noted that the stucco had to be removed to access rotten wood (Op. at p. 72), the stucco would have to be removed anyway because it was defectively installed. Therefore, according to the Court's ruling, the general contractor will fully retain payment for the original stucco application, which should have already been done properly, and also be paid again by indemnity to have the stucco reinstalled. This cost should not be borne by the insurer. Additionally, the framework set up by the Court serves as a disincentive for general contractors to supervise the work of their subcontractors. A general contractor who hires poor quality subcontractors, who fails to ensure that they have insurance to cover their own work, or who otherwise mismanages his subcontractors should bear responsibility for those actions.

Furthermore, the Court's decision to provide coverage for the cost to repair or replace defective work will no doubt lead to still more litigation regarding faulty workmanship never intended to be covered by a CGL policy. As one counsel who represents insureds stated after the Newman opinion issued:

For example, the court said there was no occurrence until the water penetrated the faulty stucco. 'If the same contractor built this house in Arizona, where it never rains, there's never an occurrence,' . . . but would the policy kick in anyway?

South Carolina Lawyers Weekly, New decision on CGL coverage clears up confusion from L-J case, Vol. 7, No. 29 at p. 22 (March 17, 2008).²

² The Court's Newman decision has also been recognized as a "*dramatic change* because it [the Court] says you have to do investigative work to assess your damage – meaning taking all the stucco off . . ." Id. (emphasis added).

As this Court rightly noted in L-J, there should be no finding of “occurrence” based on faulty workmanship, and it is beneficial to have the ultimate liability falling “to the one who performed the negligent work--the subcontractor--instead of the insurance carrier. It will. . . encourage contractors to choose their subcontractors more carefully instead of having to seek indemnification from the subcontractors after their work fails to meet the requirements of the contract.” L-J, Inc. v. Bituminous Fire and Marine Insurance Company, 366 S.C. 117, 124 (2005).

This Court’s Newman opinion departs from these sound policies, and reaches an incorrect result.³ Rehearing should thus be granted.

VI. The plain language of the policy excludes the cost to repair or replace the defective stucco work.

This Court also overlooked the clear language of the CGL policy that bars coverage for the cost to repair, replace, remove, or dispose of your product or your work even when the work is performed on your behalf. Exclusion 2 (n) of the CGL policy specifically provides that “[t]his insurance does not apply to”:

Damages claimed for any loss, cost or expense incurred by you or others for the loss of use, withdrawal, recall, inspection, repair, replacement, adjustment, removal or disposal of:

- (1) “Your product”;
- (2) “Your work”; or
- (3) “Impaired property”

³ An additional reason why the repair and replacement costs should not be covered was overlooked by this Court. A mere defect in the stucco cannot constitute “property damage” as defined in the policy. “The term ‘property damage’ in an insurance policy has been interpreted to mean damage to property that was previously undamaged, and not the expense of repairing property or completing a project that was not done correctly or according to contract in the first instance.” Prod. Sys., Inc. v. Amerisure Ins. Co., 605 S.E.2d 663, 666 (N.C. Ct. App. 2004) (emphasis added); see also Wm. C. Vick Constr. Co. v. Pa. Nat’l Mut., 52 F. Supp. 2d 569, 582 (E.D.N.C. 1999), aff’d sub nom Wm. C. Vick Constr. Co. v. Great Am. Ins. Co., 213 F.3d 634 (4th Cir. 2000). Hence, rehearing is warranted.

If the product is . . . withdrawn from use by any person . . . because of a known or suspected defect, deficiency, inadequacy or dangerous condition in it.

(R. p. 239). The policy also defines “your work” to mean “work or operations performed by you or on your behalf.” (R. p. 246). Each exclusion in an insurance contract is read and applied independently of every other exclusion. Engineered Products, Inc. v. Aetna Cas. & Sur. Co., 295 S.C. 375, 378-79, 368 S.E.2d 674, 675-76 (Ct. App. 1988) (quoting Weedo v. Stone-E-Brick, Inc., 81 N.J. 233, 405 A.2d 788, 795 (1979)) ([E]xclusions in an insurance policy are to be read independently of each other; they are not to be read cumulatively [and] if any one exclusion applies there should be no coverage, regardless of inferences that might be argued on the basis of exceptions or qualifications contained in other exclusions.); Laidlaw Env'tl. Servs. (TOC), Inc. v. Aetna Casualty & Sur. Co., 338 S.C. 43, 51, 524 S.E.2d 847, 852 (1999); see also LaMarche v. Shelby Mut. Ins. Co., 390 So. 2d 325, 326 (Fla. 1980) noting that “an exclusion does not provide coverage but limits coverage”).

Accordingly, even if the Court was correct in finding the events giving rise to this action constitute an occurrence by working back from the exception to the “your work” exclusion, the plain language of exclusion 2(n) of the policy does preclude coverage for the arbitrator’s award for the cost of “hav[ing] the stucco replaced.” (R. p. 11; Opinion pp. 71-72). The cost to replace, repair, remove or dispose is not covered under this policy even if another party performed the work “on your behalf” – i.e. a subcontractor. As a result, rehearing of this case is warranted at minimum in order to revisit this Court’s approval of coverage for the cost to repair or replace the defective stucco work.

VII. This Court's Opinion in Auto-Owners v. Newman is contrary to sound public policy.

A. By its ruling, the Court has essentially converted CGL policies into performance bonds.

In holding that the CGL policy at issue in this case covers the damages claimed, this Court has departed from its sound rationale in L-J which highlighted a distinction between CGL policies and performance bonds. Specifically, in L-J, this Court held as follows:

W]e hold that the damage in the present case did not constitute an 'occurrence.' If we were to hold otherwise, the CGL policy would be more like a performance bond, which guarantees the work, rather than like an insurance policy, which is intended to insure against accidents. [citations omitted]. A performance bond guarantees that the work will be performed according to the specifications of the contract by providing a surety to stand in the place of the contractor should the contractor be unable to perform as required under the contract. Consequently, our holding today ensures that the ultimate liability falls to the one who performed the negligent work – the subcontractor – instead of the insurance carrier.

L-J, at 366 S.C. at 124 (emphasis added).

By its recent ruling in Newman, the Court has essentially reversed course and it has *de facto* converted the CGL policy at issue into a performance bond. In the present case, the subcontractors' improper application of the stucco was a direct result of failure to live up to proper performance (i.e., correct and non-defective application of the stucco and installation of flashing). Stated otherwise, the defective condition was present in the house prior to its completion. Such a deficiency is much more analogous to a contractor's failure to complete construction properly under its construction agreement, which is a contingency covered by a performance bond. See Hotel Roanoke Conference Ctr. Comm'n v. Cincinnati Ins. Co., 303 F. Supp. 2d 784, 786 (W.D. Va. 2004) (finding

that a CGL policy is not intended to cover poor workmanship because the policy is not designed to be a performance bond). Therefore, this Court should grant rehearing and return to its analysis in L-J to ensure that work is properly performed by contractors and that they, and their subcontractors, are held responsible for their work.

B. The Court has shifted the burden of ensuring quality construction work away from the General Contractor.

This Court's opinion protects home builders and not the South Carolina home buyer. Protecting home builders is not consistent with this Court's previously announced position as being in the "vanguard" for protection of consumers in the area of home construction. See Reynolds v. Ryland Group, Inc., 340 S.C. 331, 531 S.E.2d 917 (2000) ("South Carolina, through both its courts and legislature, has previously been in the vanguard of protecting consumers, particularly in the area of home construction."); see also Terlinde v. J.F. Neely, Sr., 275 S.C. 395, 271 S.E.2d 768 (1980) (subsequent purchasers of home may sue builder in tort and contract); JKT Co. v. Hardwick, 274 S.C. 413, 265 S.E.2d 510 (1980) (statutory implied warranty of merchantability extends to corporate plaintiff not in privity with defendant); Lane v. Trenholm Building Co., 267 S.C. 497, 504, 229 S.E.2d 728, 731 (1976) ("Our legislature continues to place South Carolina in the vanguard of consumer protection."). In all of the above decisions, this Court time and again refused to allow home builders to escape responsibility for their work, and this Court was stalwart in protecting consumers – home *buyers*.

However, this Court's opinion in Newman already has commentators saying that this Court now "puts the Palmetto State in the vanguard on a vexing issue nationwide" protecting home *builders* and "allows *builders* to now rest assured that what they paid for is going to afford them some coverage." South Carolina Lawyers Weekly, New decision

on CGL coverage clears up confusion from L-J case, Vol. 7, No. 29 at p. 22 (March 17, 2008). South Carolina has become only “one of four in the country that clearly defines coverage – Florida, Texas, and Illinois are the other three.” Id.⁴

The Court’s approach is a drastic change in direction from this Court’s opinion in L-J to the result handed down in Newman. The impact of the Court’s decision will affect a wide range of people in South Carolina, most notably the home buyer because a contractor can walk away from a project knowing that “there is coverage for work that is done by subcontractors” instead of supervising the subcontractor’s work and ensuring the home buyer gets what he or she paid for in the first instance. Id. Further the decision has serious “implications on how the money flows . . . it’s a billions-of-dollars decision.” Id. Now, the insurance company and the home buyer will be left to deal with the problems caused by a contractor and its subcontractors, because the work is arguably guaranteed to be repaired and replaced no matter how poorly it was performed in the first instance.

Further, this Court stated in Newman: “In our opinion, and in the absence of any evidence otherwise, it is unreasonable to believe that Trinity expected or intended its subcontractor to perform negligently.” Opinion at p. 71. This ruling incents contractors to hire subcontractors unknown to them to give them plausible deniability as to whether the subcontractors will properly perform their work. The ruling also provides contractors with an incentive not to monitor their subcontractors during their work. This result is inevitable because the Court’s Opinion ensures that no matter how shoddy the work, the insurance company will now be required to come in and clean up the subcontractors’ mess after “completion” of the project.

⁴ It should be noted that your *amici* has been unable to locate any case from Florida, Texas, or Illinois finding coverage for repair and replacement costs.

Several courts have addressed these points. Those courts addressing the issue have found that the contractor should not reap the windfall of hiring poorly performing subcontractors only to later rely on the Court to step in and find coverage under an insurance policy. See Adair Group, Inc. v. St. Paul Fire & Marine Ins. Co., 477 F.3d 1186 (10th Cir. 2007) (disallowing the contractor's use of subcontractors as an excuse for failing to perform under the construction contract); DCB Construction Co., Inc. v. Travelers Indemnity Co. of Illinois, 225 F. Supp. 2d 1230, 1232 (D. Colo. 2002) (find that a general contractor should not be able to turn its failure to complete construction according to the contract into a covered event by bootstrapping on its subcontractor's negligence, because a commercial general liability insurance policy is not intended to provide an anticipatory guarantee of quality work.).

If this Court's Opinion stands as written, homeowners will no doubt face an increase in poorly constructed homes or poorly performed renovations because the quality of work will no longer be important in the first instance. The Newman case essentially provides the contractor with a "do-over" at the cost of the insurer. This is at odds with this Court's steadfast rulings protecting homebuyers and placing responsibility for poor workmanship on contractors. Rehearing is thus warranted.

Conclusion

For the reasons set forth herein, and based upon the arguments presented by Auto-Owners in briefing and at oral argument and in its rehearing petition, this Court should grant rehearing.

Respectfully submitted,

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April 21, 2008

THE STATE OF SOUTH CAROLINA
In the Supreme Court

APPEAL FROM CHARLESTON COUNTY
Court of Common Pleas

B. Hicks Harwell, Jr., Circuit Court Judge

Case No. 2002-CP-10-4390

Auto-Owners Insurance Co., Inc., Appellant,

v.

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

PROOF OF SERVICE

I, the undersigned Administrative Assistant, of the law offices of Nelson Mullins Riley & Scarborough LLP, attorneys for Amicus Curiae Harleysville Mutual Insurance Company, do hereby certify that I have served all counsel in this action with a copy of the pleading(s) hereinbelow specified by mailing a copy of the same by United States Mail, postage prepaid, to the following address(es):

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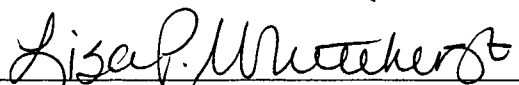
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