THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM HORRY COUNTY
Court of Common Pleas

Steven H. John, Circuit Court Judge

Case No. 2004-CP-26-0084

Crossmann Communities of North Carolina, Inc.
and Beazer Homes Investment Corp., ... *Appellants*,

vs.

Harleysville Mutual Insurance Company and
Cincinnati Insurance Company,

Of Whom Cincinnati Insurance Company is ..... *Respondent*.

APPELLANTS' FINAL REPLY BRIEF

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ARGUMENT IN REPLY

Appellants -- Crossmann Communities of North Carolina, Inc. and Beazer Homes Investment Corp. (collectively "**Beazer**") -- by and through their undersigned counsel, respectfully submit this Reply Brief to address the following arguments raised by Respondent Cincinnati Insurance Company ("**Cincinnati**").

I. Standard Of Review

"When the purpose of the underlying dispute is to determine whether coverage exists under an insurance policy, the action is one at law.... [and] [w]here the action presents a question of law,... th[e] Court's review is plenary and without deference to the trial court." *Crossmann Communities of North Carolina, Inc, v. Harleysville Mut. Ins. Co.*, 395 S.C. 40, 717 S.E. 2d 589 (2011) ("***Crossmann II***"). It is a fundamental principle that, "[a]n action to construe a contract is an action at law." *McGill v. Moore*, 381 S.C. 179, 185, 672 S.E.2d 571, 574 (2009).

Despite the clear standard of review, Cincinnati argues that the issues before this Court revolve around the application of the "time on risk" formula, and that the Circuit Court's May 23, 2012 Order should be given deference. The issues before this Court, however, are not limited to the application of the "time on the risk" formula, but instead center on whether the limits of the **Underlying Policies**[1] that sit beneath the **Cincinnati Policies**[2] have been exhausted by

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1 As used herein, the "Underlying Policies" refers to the primary insurance policies underlying Cincinnati Policy Number CCC 444 58 40. "Indiana, Massachusetts Bay and Regent are the three (3) underlying carriers for which Cincinnati provided excess coverage." [May 23, 2012 Order, p. 8 (R. p. 64).]

payment of claims, which is fundamentally a question of interpretation of the terms in the Cincinnati Policies.

Because this appeal involved interpretation and application of terms in the Cincinnati Policies, this Court should conduct a *de novo* review of the Circuit Court's May 23, 2012 Order, and should not blindly apply the abuse-of-discretion standard sought by Cincinnati.

II. The Trial Court Erred In Concluding That The Limits Of The Underlying Primary Policies Have Not Been Exhausted

The limits of the Underlying Policies have been exhausted by payment of claims by Beazer and its insurers. As such, the excess coverage provided by the Cincinnati Policies has been triggered.

First, it is undisputed that Beazer and its insurers (other than Cincinnati and Harleysville Mutual Insurance Company ("**Harleysville**")) paid $16.77 million to resolve the seven lawsuits filed by homeowner plaintiffs in Horry County, South Carolina that are at issue in this coverage litigation (the "***Underlying Lawsuits***"). [2007 Final Judgment, p. 8 (R. p. 8).] As Beazer discussed in its Initial Brief, the entire amount of that $16.77 million figure should count towards exhaustion of the Underling Policies. Cincinnati, however, argues that using the $16.77 million figure is inappropriate because it is in "direct conflict with the parties' Stipulation..." entered prior to trial. [Initial Brief of Respondent Cincinnati Ins. Co., pp. 17-18.] It is correct that, prior to trial before

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2 As used herein, the "**Cincinnati Policies**" refers to the umbrella commercial general liability ("**CGL**") insurance policies Cincinnati sold to Crossmann Communities of North Carolina, Inc. as the first named insured, including Policy Number CCC 444 58 40, which was in effect from July 1, 1998 to July 1, 2002.

the Circuit Court, Cincinnati, Harleysville, and Beazer stipulated that "[i]f the trial Court finds that there has been an occurrence or occurrences, then the Court shall find that Plaintiffs' insured loss [under the "Policies," defined in the Stipulation to be only the Harleysville and Cincinnati insurance policies] is $7.2 million..." [Stipulation, ¶ 1 (R. p. 2228).] Paragraph 1 of the Stipulation has nothing to do with exhaustion of the Underlying Insurance. Cincinnati, and Beazer did not make any stipulation related to the amount of exhaustion of the Underlying Insurance. In fact, both Cincinnati and Beazer specifically reserved the right to argue whether the Underlying Insurance had been exhausted. [Stipulation, ¶ 9 (R. p. 2229).] Instead, Paragraph 1 of the Stipulation relates to coverage -- the amount of damage alleged in the *Underlying Lawsuits* that meets the definition of "occurrence" under only the Cincinnati and Harleysville insurance policies.

The Circuit Court erred by applying a coverage analysis applicable only to Harleysville and Cincinnati to a question of exhaustion of the underlying insurance policies issued by insurers other than Harleysville and Cincinnati. When Cincinnati and Beazer entered into the Stipulation in January 2007, they did not alter or even address the method of proving exhaustion of the Underlying Insurance. Whether an excess insurer's coverage has been triggered depends on the relevant language of the excess insurance policy. *National Union Fire Ins. Co. v. Travelers Ins. Co.*, 214 F.3d 1269, 1273 (11th Cir. 2000). The Cincinnati policies provide that exhaustion of the limits of the underlying insurance is by "payment of claims": "If the limits of 'underlying insurance' have been exhausted by payment of claims, this policy will continue in force as 'underlying

insurance.'" [Cincinnati Policies, p. BZH104341 (R. p. 1023).] The Circuit Court correctly found that the language in the Cincinnati Policies regarding exhaustion -- that exhaustion occurs by "payment of claims" -- is ambiguous and should be construed in favor of coverage and against Cincinnati. [March 1, 2012 Hearing Transcript, p. 105, lines 11-20 (R. p. 945) ("I find that to be confusing and/or ambiguous, so I think with the contract law and insurance law, the policy must be construed to the benefit of the insured and against the insurance company that there is coverage..."); May 23, 2012 Order, p. 12-14 (R. p. 68-70).] *See also Crossmann II*, 395 S.C. 40, 47, 717 S.E.2d 589, 592-93 (2011) (noting that ambiguities in an insurance contract must be construed against the insurer). Thus, "payment of claims" by both Beazer and its insurers serve to exhaust the limits of the Underlying Insurance, and the payment of claims test for exhaustion must be very broadly construed in favor of Beazer and against Cincinnati. *See Trinity Homes, LLC and Beazer Homes Invs., LLC v. Ohio Cas. Ins. Co. and Cincinnati Ins. Co.*, 629 F.3d 653, 658-59 (7th Cir. 2010). The undisputed $16.77 million in payments by Beazer and its insurers (other than Cincinnati and Harleysville) to resolve the *Underlying Lawsuits* serve to exhaust the Underling Insurance.

Second, the Circuit Court held, and Cincinnati does not contest, that out-of-state payments may count towards exhaustion of the Cincinnati Policy limits. [May 23, 2012 Order, p. 14 (R. p. 70).] *See also, Trinity Homes, LLC and Beazer Homes Invs. LLC v. Ohio Cas. Ins. Co. and Cincinnati Ins. Co.*, 629 F.3d 653, 658-59 (7th Cir. 2010). Beazer presented evidence to the Circuit Court that payment of claims by Beazer and its insurers exceeded the maximum $6 million

per-occurrence and $12 million aggregate limits. In Indiana alone, Beazer made claim payments to settle homeowner construction defect property damage claims of more than $42.7 million. [Trinity Water Intrusion Claims Damage Summary (R. p. 2231).] Cincinnati rests its case on the mere assertion that Beazer "failed to provide records to show that any payments, or even any portions thereof, were made for potentially covered losses related to ensuing damage versus payments that were made for defective construction." [Initial Brief of Respondent Cincinnati Ins. Co., p. 19.] Mr. Berry testified in his affidavit that the Indiana construction defect litigation against Beazer "involved property damage claims by homeowners who claimed that water intrusion had caused damage to their homes," and that declaration was supported by the allegations made by the plaintiffs in the Indiana Litigation. [W. Mark Berry Affidavit, March, 29, 2006, ¶ 29 (R. p. 2226).] As such, Beazer met its evidentiary burden to show that the damage related to the Indiana Litigation was for covered property damage loss. It was then incumbent upon Cincinnati to produce some modicum of evidence that that payments Beazer made to remediate water-related property damage in the Indiana Litigation were not for covered claims. It is undisputed that Cincinnati presented no evidence at all. Any doubt as to the extent of coverage must be resolved in favor of Beazer. *See, e.g., Auto-Owners Ins. Co. v. Madison at Park West Property Owners Ass'n, Inc.*, 834 F. Supp. 2d 437, 443 (D.S.C. 2011) ("However, 'if doubt exists as to the extent or fact of coverage,' South Carolina courts have long held that 'where the clause is one of inclusion it should be

broadly construed for the benefit of the insured while in exclusion cases the same clause is given a more restricted interpretation[].'") (emphasis added).

Third, the entire amount of the undisputed payments of $8,978,828 by the Underlying Insurers must be counted towards exhaustion of the Underlying Insurance. The Underlying Insurers -- Indiana, Regent, and Massachusetts Bay -- did not sign the Stipulation and are not bound by the $7.2 million figure in the Stipulation that, by its clear terms, applies only to Harleysville and Cincinnati. Further, the settlements with the Underlying Insurers were not limited to the *Underlying Lawsuits* in South Carolina, but applied to all past, present, and future claims for insurance coverage by Beazer against those policies. The Beazer-Indiana settlement states that:

> ...each hereby release all claims, including but not limited to, all demands, actions, causes of action, and suits (whether legal or equitable, and whether based on contract, tort, statute, subrogation or otherwise) damages (whether compensatory, punitive, statutory, interest, costs, attorneys' fees, or otherwise) damages (whether compensatory, punitive, statutory, interest, costs, attorneys' fees, or otherwise) judgments, levies, executions, arbitrations, and appraisals, that Crossmann and Indiana have, or may have in the future, or ever have had against each other that, directly or indirectly, arise from or relate in any way to the Underlying Lawsuits, the South Carolina Coverage Action, and the Indiana Policies (attached in Appendix A hereto) including, but not limited to all claims between them that were made in, relate to, or could have been asserted in the South Carolina Coverage Action and in any past, present, or future claim for coverage under the Indiana Policies.

[Indiana Settlement, December 29, 2005, BZH104803 (R. p. 1538) (emphasis added).] The Beazer-Massachusetts Bay Settlement states that:

> The INSUREDS and MASSACHUSETTS BAY hereby release and forever discharge the other from all claims, including, but not limited to, all demands, actions, causes of action, and suits (whether legal or equitable, and whether based in contract, tort,

> statute, subrogation or otherwise), damages (whether compensatory, punitive, statutory, interest, costs, attorneys' fees, or otherwise), judgments, levies, executions, arbitrations, and appraisals, that the INSUREDS and MASSACHUSETTS BAY have, may have, or ever had against each other, whether known or unknown, asserted or unasserted, contemplated or not contemplated, which directly or indirectly arise from or relate in any way to the UNDERLYING LAWSUITS, the COVERAGE ACTIONS and/or the POLICY.

[Massachusetts Bay Settlement, March 14, 2006, BZH105176 (R. p. 1911) (emphasis added).] Finally, the Beazer-Regent Settlement explicitly applied to claims in Indiana and South Carolina. [*See* Regent Settlement, May 17, 2005, BZH104528, BZH104537 (R. pp. 1264, 1273).] There was no basis for the Circuit Court to make a reduction in the undisputed amount of claim payments by the Underlying Insurers and recognize only claim payments to the South Carolina *Underlying Lawsuits* because the settlements with the Underlying Insurers are not limited to the South Carolina *Underlying Lawsuits*. The Circuit Court therefore erred by not counting the full settlement payments by the Underlying Insurers towards exhaustion of the Underlying Insurance. The settlement payments by the Underlying Insurers were as follows:

Insurer	**Total Payment Amount**
Indiana	$2,700,000[3]
Massachusetts Bay	$3,127,597[4]
Regent	$3,151,231[5]
Total =	**$8,978,828**

3 Indiana Settlement, December 29, 2005, p. 3 (R. p. 1538).

4 Massachusetts Bay Settlement, March 14, 2006, pp. 4, 6 (R. pp. 1909, 1911).

5 Regent Settlement, May 17, 2005, pp. 5, 7 (R. pp. 1262, 1264).

The limits of the Indiana Insurance Company ("**Indiana**") policies have been exhausted. Indiana issued two insurance policies that were in effect from July 1, 1997, until August 29, 1998. [Indiana Settlement, December 29, 2005, p. 1, ¶ 1 (R. p. 1536).] Each of Indiana's policies had a $1,000,000 "each occurrence limit" and a $2,000,000 aggregate limit, for maximum combined totals of $2 million (per occurrence) and $4 million (aggregate).[6] [*Id.*, p. 1, ¶ 2 (R. p. 1536).] Beazer and Indiana settled their coverage disputes with Indiana paying Beazer $2.7 million to extinguish Indiana's obligations under the policies. [*Id.*, p. 3 (R. p. 1538).] That amount exceeds the per-occurrence limits, which should apply, and exhausts the Indiana policies. *See Liberty Mut. Fire Ins. Co. v. J.T. Walker Indus., Inc.*, 817 F. Supp. 2d 784, 789 (D.S.C. 2011) ("The only interpretation of 'occurrence' able to reconcile all of the policy language in a manner consistent with *Crossmann II* is that all of the damage that happens in one policy year constitutes a single 'occurrence,' and therefore progressive environmental damage creates 'a 'separate' occurrence in each policy year.'"). Even if the aggregate limits in the Indiana policy apply to determine exhaustion -- and they do not -- any gaps between the maximum aggregate limits and the claim payments made by Indiana are more than filled by Beazer's payments in South Carolina, Indiana, and Kentucky.

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6 The limits available to Beazer under the Indiana policies are less than the maximum $2 million per-occurrence and $4 million aggregate limits listed in this paragraph. The second Indiana policy period lased only from July 1, 1998 to August 29, 1998, and not for a full year.

Underlying Insurer	Maximum Total Limits of Underlying Policies	Indiana Payments	Maximum Gap
Indiana	$2M per-occurrence limits $4M aggregate limits	$2.7M	$0 per-occurrence limits $1.3M aggregate limits

The limits of the Massachusetts Bay Insurance Company ("**Massachusetts Bay**") policies have been exhausted. Massachusetts Bay issued two policies providing coverage from August 29, 1998, to August 29, 2000. [Massachusetts Bay Settlement, March 14, 2006, p. 3, ¶ 11 (R. p. 1908).] Each policy had a $1,000,000 "each occurrence limit" and a $2,000,000 aggregate limit, for combined totals of $2 million per occurrence and $4 million in the aggregate. [*Id.*, p. 5, ¶ 7 (R. p. 1910).] Beazer and Massachusetts Bay entered into a settlement under those policies, and in addition, Massachusetts Bay made indemnity payments to Beazer. The settlement and indemnity payments totaled to $3,127,597. [*Id.*, pp. 4, 6 (R. pp. 1909, 1911).] Those payments far exceed the $2 million per-occurrence limits. Even if the aggregate limits in the Massachusetts Bay policy apply to determine exhaustion -- and they do not -- any gaps between the maximum aggregate limits and the claim payments made by Indiana are more than filled by Beazer's payments in South Carolina, Indiana, and Kentucky. [*See* Appellants' Initial Brief, pp. 21-27.]

Underlying Insurer	Maximum Total Limits of Underlying Policies	Massachusetts Bay Payments	Maximum Gap
Massachusetts Bay	$2M per-occurrence limits $4M aggregate limits	$3,127,597	$0 per-occurrence limits $872,403 aggregate limits

The Regent Insurance Company ("**Regent**") policies have been exhausted. Regent issued two consecutive policies underlying the Cincinnati Policies that were in effect from August 29, 2000, through January 1, 2002. [Regent Settlement, May 17, 2005, p. 4, ¶ 19 (R. p. 1261).] Each Regent policy has a $1,000,000 "each occurrence limit" and a $2,000,000 aggregate limit, for maximum combined totals of $2 million (per occurrence) and $4 million (aggregate).[7] [*Id.*, p. 6, ¶ 8 (R. p. 1263).] Beazer and Regent entered into a settlement of claims and Regent made indemnity payments to Beazer for a combined total of $3,151,231. [*Id.*, pp. 5, 7 (R. pp. 1262, 1264).] Those payments exceed the maximum $2 million per-occurrence limits. Even if the aggregate limits in the Regent policy apply to determine exhaustion -- and they do not -- any gaps between the maximum aggregate limits and the claim payments made by Indiana are more than filled by Beazer's payments in South Carolina, Indiana, and Kentucky.

7 The limits available to Beazer under the Regent policies are less than the maximum $2 million per-occurrence and $4 million aggregate limits listed in this paragraph. The second Regent policy period was cancelled after only four months.

Underlying Insurer	Maximum Total Limits of Underlying Policies	Regent Payments	Maximum Gap
Regent	$2M per-occurrence limits $4M aggregate limits	$3,151,231	$0 per-occurrence limits $848,769 aggregate limits

It is undisputed that even if the aggregate limits in the Underlying Policies are applicable to the exhaustion, there is a gap of only $3.02 million for Beazer to fill before the Cincinnati excess policies are triggered.[8] This gap is filled many times over by the undisputed evidence in the record that Beazer paid over $42 million to settle property damage claims by homeowners in Indiana. As a result, the Circuit Court's May 23, 2012 Order dealing with exhaustion should be reversed.

III. The Trial Court Erred in Reversing Its "Joint And Several" Allocation Judgment As To Cincinnati Because Cincinnati Did Not Appeal From the Original 2007 Final Judgment

Cincinnati is bound by the 2007 Final Judgment because it did not appeal that final judgment. *Judy v. Martin*, 381 S.C. 455, 458, 674 S.E. 2d 151, 153 (2009). Although the Circuit Court's 2007 Final Judgment did not decide whether Cincinnati's excess coverage obligation had been triggered, Cincinnati was plainly aggrieved by that Final Judgment, which also held that the property damage at issue in the *Underlying Lawsuits* had been caused by an "occurrence,"

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8 Assuming the aggregate limits apply (and they do not), the maximum gap with respect to the Indiana policies is $1,300,000, the maximum gap with respect to the Massachusetts Bay policies is $872,403, and the maximum gap with respect to the Regent policies is $ 848,769. Thus, the total maximum gap if the aggregate limits apply is $3,021,172.

thereby satisfying the key predicate to coverage under the Cincinnati Policies. Cincinnati was further aggrieved by the "joint and several" aspect of the 2007 Final Order because, if the Supreme Court remanded the case to the Circuit Court for any reason, Cincinnati's liability would be greater under a "joint and several" allocation methodology than under a *pro rata* time-on-the-risk allocation methodology.

In its Initial Brief, Cincinnati suggests that Paragraphs 8(c) and 9 of the Stipulation are "inconsistent" with Beazer's position that Cincinnati's liability is "joint and several" because it did not appeal the Circuit Court's 2007 Final Judgment. [Initial Brief of Respondent Cincinnati Ins. Co., p. 21-22.] Beazer's "joint and several" argument is fully consistent with the Stipulation.

As outlined in the Stipulation, the parties (Cincinnati, Harleysville, and Beazer) asked the Circuit Court to determine two primary issues: (a) "did the property damage giving rise to Plaintiffs' claims for coverage arise from an 'occurrence'"; and (b) "In the event the Court finds that there was an occurrence or occurrences, how shall the $7.2 million in insured damages referred to in paragraph 1 above be allocated, whether by 'joint and several' or by 'time on the risk.'" Depending on how the Circuit Court ruled on the two primary issues, the Parties agreed on how the remaining questions would be determined. To that end, Paragraph 8(c) of the Stipulation provides:

> In the event judgment is entered for Plaintiffs, and that the Court determines that "time on the risk" is the proper allocation method, what is the proper period over which the "time on the risk" should be calculated. All parties reserve their right to argue, from the applicable facts and law, the appropriate start date and end date for any pro rata time on the risk allocation period. Alternatively, in

> the event that judgment is entered for the Plaintiffs and the Court determines that "joint and several" is the proper allocation method, whether Harleysville or Cincinnati is entitled to any set-off under South Carolina law in light of Plaintiffs' settlement with other insurers and, if set-off is appropriate, the amount of any such set-off.

[Stipulation, ¶ 8(c) (R. p. 2229).] Paragraph 8(c) merely established how the litigation would proceed before the Circuit Court in the initial proceedings. It does not provide Cincinnati the right to contest final judgments by the Circuit Court without filing an appeal. The second contingency contemplated by Paragraph 8(c) occurred. The Circuit Court found that "joint and several" was the proper allocation method, and at that time, Cincinnati and Harleysville were entitled to argue about any potential set-off. Later, Harleysville appealed the Circuit Court's 2007 Final Judgment and Cincinnati did not. Paragraph (8)(c) does not provide Cincinnati with the right to benefit from Harleysville's appeal without joining in that appeal.

Similarly, Paragraph 9 of the Stipulation provided that, depending on how the Circuit Court ruled on the primary questions, Cincinnati and Beazer could argue over exhaustion:

> The parties agree that Cincinnati can argue to the Court that the underlying insurance has not been exhausted and that Cincinnati has no obligation to "drop down" and cover Plaintiffs for losses in the Underlying Lawsuits, and Plaintiffs can oppose Cincinnati's contention and argue that Cincinnati's policies are presently triggered.

[Stipulation, ¶ 9 (R. p. 2229).] Because the Circuit Court held that under the "joint and several" method of allocation Harleysville was responsible for the full amount of the stipulated damages, Cincinnati and Beazer did not argue whether Cincinnati's Policies were presently triggered. However, Paragraph 9 does not

provide Cincinnati with the right to challenge the Circuit Court's 2007 Final Judgment regarding the scope of coverage under the Harleysville and Cincinnati policies and Cincinnati's "joint and several" liability without appealing that 2007 Final Judgment.

CONCLUSION

Based on the foregoing, Beazer respectfully requests that the Court reverse the May 23, 2012 Order of the Circuit Court on the Cincinnati remand issues and hold that the limits of the insurance policies underlying the Cincinnati Policies are exhausted, and that Cincinnati is liable to Beazer for its share of the damages under the "joint and several" method of allocation in the amount of $5,619,854. In the alternative, the Court should reverse the May 23, 2012 Order of the Circuit Court and hold that the limits of the insurance policies underlying the Cincinnati Policies are exhausted, and that Cincinnati is liable to Beazer for its share of the damages under the time-on-the-risk method of allocation in the amount of $3,038,300.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

The undersigned hereby certifies that Appellants' Final Reply Brief complies with Rule 211(b), SCACR.

Respectfully submitted,

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