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"Occurrence" – Where We Have Been – Where We Are Now – Where We Are Heading

I. History of Term "Occurrence" in Liability Policies

Overview of Changes in Definition and Interpretation (1966, 1973, 1976 and 1986)

A working knowledge regarding the evolution of the Courts' interpretation of the term "occurrence" appearing in the insuring agreement of the Commercial General Liability Policy is highly beneficial to claims specialists and coverage counsel alike. This historical background provides persons responsible for analyzing and making coverage determinations on property damage claims the necessary foundation to understand where the Courts are today and how they got here. For as the Tenth Circuit Court of Appeals recently advised, "The history and development of CGL policies guide our interpretation of the Policy at issue here." *Black & Veatch Corporation v. Aspen Insurance (UK) Ltd.*, 882, F.3d 952, 959 (10th Cir. 2018).

The 1966 Occurrence Form Moves Beyond Accidental Sudden Event

The standardized accident form provided by the National Bureau of Casualty Underwriters (NBCU) and used by insurers between 1955 and 1966 covered property damage caused by an accident. *American Family Mut. Ins. Co. v. American Girl, Inc.,* 268 Wis.2d 16, 33, 673 N.W.2d 65 (2004), 16 Eric Mills Holmes, *Holmes' Appelman on Insurance* § 117.3, 240 (2d ed. 2000). However, the CGL policy form did not define what comprised an accident. In response to litigation over this issue and the Courts' interpretation that an accident required a sudden event, the occurrence form was introduced to remedy this judicially imposed limitation. 16 Holmes, *supra*, § 117.4, 297.

The 1966 Occurrence Form Broadens Coverage Grant in the Insuring Agreement

The significant change made to the 1966 CGL policy form was the introduction of coverage for an "occurrence," a defined term which incorporated not only the fortuity concept of accidents, but also "exposure to conditions." *Cypress Point Condominium Association, Inc. v. Adria Towers, L.L.C.*, 226 N.J. 403, 416-17 (2016). The latter addition provided "coverage for accidental events that were not abrupt and short lived, such as seepage and long-term exposure to hazardous substances." *Appleman on Insurance,* Law Library Edition § 16.02[3][a][iv], LexisNexis (2015). This change had a

broadening effect on the scope of coverage provided by the CGL insuring agreement. The 1966 CGL Policy extended coverage to "damages because of . . . bodily injury or property damage . . . caused by an occurrence," defining occurrence to mean "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…."

Although the explicit change to the occurrence form expanded coverage beyond a sudden event such as a fire or roof collapse, it also expressly added that the resulting bodily injury or property damage had to be "neither expected nor intended" by the insured.

The 1973 ISO Form Further Clarified the Meaning of an Occurrence By Revising the Definition to Include "Continuous or Repeated" to Exposure language, however Business Risk Exclusions for the Insured's Work and Product Significantly Limited the Broad Grant of Coverage

In the 1973 ISO CGL form, the drafters revised the definition of "occurrence" to mean "an accident, including continuous or repeated exposure to conditions, which results in bodily injury or property damage neither expected nor intended from the standpoint of the insured." The additional language "continuous or repeated" served to further clarify the broader grant of coverage beyond the abrupt and sudden accident. Notably, the business risk exclusions contained in the 1973 ISO form had a major impact on coverage litigation as well as how the "occurrence" policy came to be interpreted by many courts. The foregoing judicial contract interpretation was greatly influenced by a 1971 law review article, Nebraska Law School Professor Roger C. Henderson's *Insurance Protection For Products Liability And Completed Operations – What Every Lawyer Should Know* and the New Jersey Supreme Court decision *Weedo v. Stone-E-Brick, Inc.*, 81 N.J. 233, 405 A.2d 788 (1979) which quoted the article at length.

Professor Henderson's Law Review Article and the *Weedo* Case Did Not Cite or Analyze the Occurrence Definition Under Either the 1966 or 1973 CGL Policy

Professor Henderson's Law Review Article primarily addressed the 1966 CGL form and changes made regarding certain business risk exclusions for products liability and completed operations. The article did not cite or analyze the definition of an occurrence under the 1966 CGL Policy form. Despite these facts, Professor Henderson's statement that "[t]he risk intended" to be covered "is the possibility that the goods, products or work of the insured, once relinquished or completed, will cause bodily injury or damage to property other than to the product or completed work itself . . ." has been relied upon by courts when analyzing construction defect claims and the issue of whether they constitute an occurrence. The New Jersey Supreme Court's extensive quotation from and affirmation of Professor Henderson's article in *Weedo* started this process.

***Weedo* Court Finds No Coverage for Insured Contractor Under Your Work and Your Product Business Risk Exclusions and Explicitly Explains Occurrence Argument Withdrawn by Insurer, but Uses Occurrence Language in Its Hypotheticals**

The oft cited and quoted *Weedo* decision addressing a claim for the mason contractor's faulty workmanship applying stucco to a home was considered the seminal case addressing the issue of coverage for an insured's construction defects to its own work or product under the 1973 CGL Policy.

The New Jersey Supreme Court advised that "the replacement and repair of faulty goods and works is a business expense," of the responsible contractor and not a risk for which insurance coverage is purchased. *Weedo*, *supra,* 81 N.J. at 239-40. As such, the Court held that both exclusion (n), the insured's product exclusion and exclusion (o), the insured's work exclusion barred coverage for the poor and defective workmanship of the insured which led to cracking stucco necessitating removal and replacement.

Although in a footnote the *Weedo* Court specifically stated that the insurer had withdrawn its earlier argument and therefore the court was not reviewing the issue of whether "absent the exclusions" the Comprehensive General Liability Policy afforded coverage for the claimed property damage, inexplicably covered "occurrence" hypotheticals were posed in the body of the opinion. In addition to quoting Professor Henderson, the New Jersey Supreme Court provided "[a]n illustration . . . to mark the boundaries between 'business risks' and occurrences giving rise to insurable liability." *Id.* The court then advised that bodily injury or property damage inflicted upon a third party from falling stucco is "an occurrence of harm which is the proper subject of risk-sharing as provided by" the 1973 CGL Policy. *Weedo*, *supra,* 81 N.J. at 240-41.

In 1976, ISO Promulgates Broad Form Property Endorsement Effectively Replacing Exclusion (o), Your Work Exclusion With a Narrower Exclusion Restoring Coverage for Property Damage Arising from Completed Work Performed by Subcontractors

In response to the growing number of frustrated contractors dissatisfied with the lack of coverage for work increasingly performed by their subcontractors over which they often had little or no direct control, ISO provided the Broad Form Property Endorsement known as the BFPD. For an additional premium, contractors could purchase coverage "for property damage arising out of completed work that had been performed by subcontractors." *Black & Veatch Corp.*, *supra*, 882 F.3d at 959. ISO's 1976 CGL Form deleted the language "or on behalf of" from its "Your Work" exclusion and the BFPD clarified "that the policy only excluded 'property damage to completed work performed by the named insured.'" *Id. quoting CGL Coverage Guide*, App. A:Broad Form Endorsement, at 295.

ISO Incorporates the BFPD Directly into Its Standard Commercial General Liability form in 1986 By Including Subcontractor Exception in the Policy's "Your Work" Exclusion

Ongoing business concerns of the policyholder community and the insurers desire for "a more attractive [CGL] product" resulted in an agreement that "the CGL policy should provide coverage for defective construction claims so long as the defective work had been performed by a subcontractor rather than the" named insured. *Cypress Point Condominium Association, Inc.*, *supra*, 226 N.J. at 418. In a major change departing from predecessor occurrence policies, in 1986 ISO clarified that the standard form CGL policy explicitly stated that the business risk exclusion for the insured's work had no application when "the damaged work, or the work out of which the damage arises, was performed" by a subcontractor. *American Family Mut. Ins. Co., supra,* 268 Wis.2d at 52-53. In a July 1986 circular, ISO explained the intent and scope of coverage afforded by the 1986 CGL Policy confirming "that the 1986 revisions to the standard CGL policy … specifically 'cover[ed] damage caused by faulty workmanship to other parts of work in progress; and damage to, or caused by, a subcontractor's work after the insured's operations are completed.'" *U.S. Fire Ins. Co. v. J.S.U.B.,*

Inc., 979 So.2d 871, 879 (Fla. 2007)(citing ISO Circular, Commercial Gen. Liab. Program Instructional Pamphlet, No. GL-86-204 (July 15, 1986)).

The 1986 ISO CGL Standard Form Removes "Expected nor Intended from the Standpoint of the Insured" Phrase from the Definition of Occurrence

In addition to the significant insertion of the subcontractor exception to the Your Work exclusion, the 1986 ISO CGL form revised the definition of occurrence deleting the language "neither expected nor intended from the standpoint of the Insured," somewhat removing this facet from the coverage grant for bodily injury and property damage. *Stonewall Ins. Co. v. Asbestos Claims Mgmt. Corp.*, 73 F.3d 1178, 1205 (2d Cir. 1995). The foregoing intentional language was moved to the exclusions section of policy clearly and explicitly placing the burden of proof on the insurer to show intentional conduct on the part of the insured. *American Family Mut. Ins. Co., supra,* 268 Wis.2d at 79.

Professor Henderson and *Weedo* Revisited With A Clear Majority of States Finding An Occurrence Can Encompass Damage to The Named Insured Contractor's Work Resulting from Faulty Workmanship

A clear trend commencing in the early 2000's emerged with various state supreme courts taking a hard and more comprehensive look at exactly what risks fall within the definition of an occurrence in a CGL Policy. The definition has not changed since ISO revised its standard form in 1986. Notably, when conducting this thorough analysis which included looking back at the evolution of the occurrence policy, Courts were quick to point out that Professor Henderson's 1971 law review article commented on obsolete business risk exclusions in the 1966 CGL Policy and *Weedo* interpreted the insured's work exclusion and insured's product exclusion from the 1973 CGL Policy also no longer in effect. The Wisconsin Supreme Court in *American Family Mut. Ins. Co. v. American Girl, Inc.,* 268 Wis.2d 39-40, 673 N.W.2d 65 (2004), further explained that a certain passage from *Weedo "*(derived from Henderson), re-appear[s] continually in CGL coverage litigation" and has "resulted in some regrettably overbroad generalizations about CGL policies in our case law" as to the initial grant of coverage for an occurrence. *See also, U.S. Fire Ins. Co. v. J.S.U.B., Inc.*, 979 So.2d 871, 879 (Fla. 2007)(agrees that "reliance upon a CGL's exclusions' to determine the meaning of 'occurrence' has resulted in regrettably overbroad generalizations concerning CGL's").

The *American Family Mut. Ins. Co. v. American Girl, Inc.,* 268 Wis.2d 39-40, 673 N.W.2d 65 (2004) and *U.S. Fire Ins. Co. v. J.S.U.B., Inc.*, 979 So.2d 871, 879 (Fla. 2007) cases decided by the Wisconsin and Florida Supreme Courts, respectively, held that the CGL Policy coverage grant for an occurrence includes the faulty workmanship of a subcontractor. Further both decisions emphasized that coverage provided by the CGL Insuring Agreement is not solely limited to torts "because a loss actionable only in contract can never be the result of an 'occurrence' within the meaning of the CGL's initial grant of coverage." *American Family Mut. Ins. Co., supra,* 268 Wis.2d at 76, *U.S. Fire Ins. Co.*, *supra*, 979 So.2d at 885. Indeed, both Supreme Courts agreed that the legal species of the claim did not determine the existence of an occurrence under the CGL policy. Rather, the policy's business risk exclusions were the vehicle that precluded coverage regarding "contract claims arising out of the insured's work or product." *Id.*

The primary focus in recent case law regarding the definition of "occurrence" has concerned property damage claims. If there is faulty workmanship during the course of construction, that typically does not trigger coverage under a CGL policy. However, if there is a faulty workmanship that results in a damage to other property or bodily injury, the CGL policy can be triggered. The current decade has seen the scales tip so that a majority of states now hold that "that construction defects can constitute occurrences and contractors have coverage under CGL policies at least for unexpected property damage caused by defective workmanship done by subcontractors." Christopher C. French, *Revisiting Construction Defects as "Occurrences" Under CGL Insurance Policies*, 19 U. Pa. J. Bus. 101, 122-23 (2016). The following state supreme courts have all determined that the current policy definition of an occurrence can encompass construction defects: Alabama, Alaska, Connecticut, Florida, Georgia, Indiana, Iowa, Kansas, Minnesota, Mississippi, Montana, New Jersey, North Dakota, South Carolina, South Dakota, Tennessee, Texas, West Virginia and Wisconsin. *Id.* at 123-125.

In addition, the following four states have enacted statutes to the effect that construction defects constitute occurrences: Arkansas, Colorado, Hawaii, and South Carolina. *Id.* at 125. In general, the new statutes apply only to policies issued on or after the effective dates of the statutes, not to existing or expired policies. Additionally, recent court decisions stemming from these statutes tend to find coverage not for the faulty construction itself, but only for consequential damage to other property.

Specifically, Colorado was the first state to pass legislation addressing whether defective construction is an occurrence. Section 13-20-808 of the Colorado Code, effective May 21, 2010, creates a presumption that a construction defect is an accident and therefore an "occurrence" within the meaning of the standard CGL insurance policy, unless the insured intended the property damage to occur when the work was performed. Colorado common law continues to apply to earlier issued policies.

Additionally, Hawaii Rev. Stat. § 431:1-217 provides that "the term 'occurrence' shall be construed in accordance with the law as it existed at the time that the insurance policy was issued." Notably, the statute does not state what the law should or would be after its May 19, 2010 enactment. Thus, Hawaii courts will be left to determine whether the statute was intended to change the existing law regarding coverage for faulty construction.

Further, Arkansas Code Section 23-79-155, enacted March 23, 2011, requires CGL policies in Arkansas to contain a definition of occurrence that includes "property damage or bodily injury resulting from faulty workmanship." It is unclear whether the statute is intended to include in the definition of "occurrence" damage to the insured's own work and/or damage to other non-defective work performed by the insured or its subcontractors.

Finally, South Carolina Code § 38-61-70, effective May 17, 2011, was prepared in response to the South Carolina Supreme Court unpublished opinion in *Crossman Communities of North Carolina, Inc. v. Harleysville Mutual Insurance Company*, 2011 WL 93716 (Jan. 7, 2011). South Carolina Code § 38-61-70 provides that CGL policies insuring construction professionals for liability arising from construction related work must contain, or be deemed to contain, a definition of "occurrence" that includes: (1) an accident, including continuous or repeated exposure to substantially the same general harmful conditions and (2) property damage or bodily injury resulting from faulty

workmanship, exclusive of the faulty workmanship itself. The statute has been found to be constitutional – despite efforts to challenge it – however, the retroactive application of the statute was held to be unconstitutional.

Three significant property damage cases addressing the definition and scope of occurrence in the CGL policy have been decided in the last three years. First, in *Cypress Point Condominium Association, Inc. v. Adria Towers, LLC*, 226 N.J. 403 (2016), the New Jersey Supreme Court interpreted the 1986 ISO standard CGL form policy and pointed out that its prior decision in *Weedo* as well as "its progeny were based upon [business risk] exclusions contained within the pre-1986 CGL policy" and not whether the claimed damages resulting from the contractor's faulty workmanship fell within the definition of an occurrence and initial grant of coverage. After pointing out that the decision in *Weedo* was irrelevant to the insurers' arguments, the Court held that the "subcontractor's faulty workmanship" resulting in "consequential water damage" to other parts of the condominium complex that had been completed without flaws or defects, was an "accident" and as such an occurrence under the policies at issue. *Id.* at 428.

Second, in *Westfield Insurance Co. v. National Decorating Service, Inc.*, 863 F.3d 690 (7th Cir. 2016) decided under Illinois law, the Seventh Circuit Court of Appeals rejected the insurer's argument that there was no duty to defend the additional insured general contractor and others because the failure of its subcontractor to apply a thick enough coat of paint to the exterior of a newly constructed condominium building resulting in water leaks did not constitute an accident or occurrence. The Court of Appeals recognized that damage to a construction project that occurs as a result of a construction defect does not constitute an accident or occurrence under Illinois law. However, the Court went on to note that negligently performed work or defective work can give rise to an occurrence under a CGL policy in Illinois where the policy defines an occurrence to include not only an accident but also, "continuous or repeated exposure to conditions." Since the policy involved was the 1986 CGL form and the underlying complaint alleged that the painting subcontractor was negligent, that was enough to satisfy the policy's occurrence requirement.

Third, in the ongoing case of *Black & Veatch Corporation v. Aspen Insurance (UK) Ltd.*, 882, F.3d 952 (10th Cir. 2018), the Tenth Circuit Court of Appeals recently addressed the district court's partial summary judgment for the insurer finding no coverage for damage to multi-million dollar jet bubbling reactors resulting from internal components constructed by a subcontractor. The Court of Appeals undertook a thorough review of the history and development of CGL policies, New York intermediate cases and state supreme court decisions interpreting the definition of an occurrence to predict that the New York Court Appeals "would join the clear trend among state supreme courts holding that damage from faulty subcontractor work constitutes an 'occurrence' under the CGL policy at issue. *Id.* at 971.

Duty to Defend

The duty to defend is broader than the duty to indemnify and states differ (some vastly) on this analysis. Some only allow a four corners review of the complaint and no extrinsic evidence to determine coverage (Florida, Louisiana, Maine, Pennsylvania, etc). In this scenario, the complaint must sufficiently cite facts that could arguably be covered under the insurance policy. Other states have a broader approach, allowing facts outside of the complaint to be considered in determining

whether there is a duty to defend. States vary on how liberal to go in this analysis. For example South Carolina, Oklahoma, New York, Washington, Michigan (and several others) allow extrinsic evidence outside of the complaint to establish coverage. A few states allow extrinsic evidence to establish AND/OR negate coverage (California, Minnesota, Missouri, Montana, South Dakota, West Virginia, etc). And finally, other states are not totally clear or have conflicting laws on this subject (ie- New Mexico, Nevada). The bottom line is to know your state's laws. This can get confusing for claims handlers covering multiple states, but is crucial. Construction defect cases are often complicated involving more than one contractor's work and intensive factual analysis. The foregoing cases from Oregon, Michigan and New Mexico demonstrate that even making a determination as to whether there has been an alleged occurrence under the law can be far from clear. *See, Fountain Court Homeowner's Ass'n v. Found Dev. LLC,* 360 Or.341 (2016). *See also*, *Employer's Mutual Cas. Co. v. Mid-Michigan Solar, LLC,* 2016 WL 1578999 (Mich. App. April 19, 2016). *See also*, *Hartford Fire Ins. Co. v. Gandy Dancer, LLC,* 864 F. Supp 2d 1157, (D.N.M. 2012).

Bad Faith Implications

Duty to defend is a critical analysis in the management of a claim. Not only is the insurer responsible for the insured's reasonable defense costs if it failed to properly defend, in some states the insurer loses the right to raise coverage defenses. There are several examples of this (ie, Illinois, Arkansas, New Mexico, North Carolina, Connecticut, Montana, etc), but one state, in particular, that has rather drastic consequences for insurer's is Washington. Washington has significant penalties for an improper declination of a defense, including treble damages under the Washington Insurance Fair Conduct Act, treble damages up to $25,000 under the Washington Consumer Protection Act, and coverage by estoppel (see *Safeco v. Butler*, 118 Wash.2d 383 (1992). In other words, if the insured was wrong on the duty to defend, it not only is exposed to treble damages and attorney's fees, but is also barred from asserting any coverage defenses. In construction cases with potentially millions in dispute, wrongfully denying a defense in Washington can be a very costly mistake.

In some states, sending a ROR creates a potential conflict. In this scenario, an insurer may be required to retain independent counsel to defend the insured (in addition to counsel already retained by the insurer to defend its insured). California has some of the stronger laws in this area, holding that the insurance company must pay the reasonable cost for hiring independent counsel by the insured where the ROR brings about divergent interests. *San Diego Federal Credit Union v Cumis Ins. Society, Inc*., 162 Cal App 3d 358 (1984)

What to do? Defend under ROR, be absolutely correct in your coverage denial, or accept claim and handle in good faith.