



CONSTRUCTION

THOMAS F. SEGALLA
Goldberg Segalla

ELLEN H. GREIPER
Goldberg Segalla

MATTHEW S. LERNER
Goldberg Segalla

SUZIN L. RASO
Goldberg Segalla

navigant.com

About Navigant

Navigant Consulting, Inc. (NYSE: NCI) is a specialized, global professional services firm that helps clients take control of their future. Navigant's professionals apply deep industry knowledge, substantive technical expertise, and an enterprising approach to help clients build, manage and/or protect their business interests. With a focus on markets and clients facing transformational change and significant regulatory or legal pressures, the Firm primarily serves clients in the healthcare, energy and financial services industries. Across a range of advisory, consulting, outsourcing, and technology/analytics services, Navigant's practitioners bring sharp insight that pinpoints opportunities and delivers powerful results. More information about Navigant can be found at navigant.com.

EMERGING TRENDS AND CHANGING PERSPECTIVES ON CONSTRUCTION DEFECT CLAIMS

In courts across the country, the tide is turning in the litigation of construction defect claims. In the past year, several jurisdictions, through either decisional or statutory law, have switched directions in interpreting the relevant terms, conditions, limitations, exclusions, and endorsements of insurance policies that are applicable to construction defect claims.

Such a switch is evident in the decision earlier this summer of the Supreme Court of West Virginia in the case of *Lisbeth Cherrington, et al. v. Erie Insurance Property and Casualty Co.*, in which the court came to its decision through a historical analysis of the coverage and liability issues raised. "With the passage of time," the court noted in its decision, "comes the opportunity to reflect upon the continued validity of this court's reasoning in the face of juridical trends that call into question a former opinion's current soundness."

As courts in various jurisdictions undergo a similar soul-searching process, it is crucial for insurers, insureds, and their counsel to assess the law in the relevant jurisdiction from the decisional case law and statutory enactments. The following survey examines cases from across the United States in 2013 that have had a significant impact on litigants in the construction industry, from both the coverage and litigation perspectives. Each case includes analysis as well as a practice note offering practical takeaways for those involved in a construction defect or coverage dispute.

COVERAGE

Alabama

Faulty Workmanship Is Not an Occurrence

Owners Insurance Co. v. Jim Carr Homebuilders LLC (Sup. Ct. Sept. 20, 2013)

The Supreme Court of Alabama in the case of *Owners Insurance Co. v. Jim Carr Homebuilders LLC* made it clear that faulty workmanship only qualifies as an “occurrence” under a commercial general liability policy if that work damages personal property or other parts of the building outside the scope of the work being performed by the insured contractor. Faulty workmanship by itself does not constitute an occurrence. The court concluded that there was no damage to personal property or property of others; therefore, there was no “occurrence.” In reaching its decision, the court relied on its previous ruling in the case of *Town & Country Property LLC v. Amerisure Insurance Co.*, 111 So. 3d 699, 705 (Ala. 2011) where the court contrasted two distinct factual scenarios discussed in the case of *United States Fidelity & Guaranty Co. v. Warwick Development Co.*, 446 So. 2d W21 (Ala. 1984) (no “occurrence” found) and *Moss v. Champion Insurance Co.*, 442 So. 2d 26 (Ala. 1983) (“occurrence” found).

Practice Note: The policy involved did not contain a “subcontractors exception,” which might affect future holdings in Alabama. See footnote 4 of the decision.

Colorado

Timing and Interpretation of “Intended Use” Critical as Court Finds Insurer Has Duty to Defend

Bituminous Cas. Corp. v. Hartford Casualty Ins. Comp., 2013 U.S. Dist. LEXIS 33907 (D. Colo. March 12, 2013)

This liability insurance coverage dispute arises out of the construction of a condominium development in Durango, Colorado. In the underlying action, the homeowners’ association commenced against, among other parties, Rivergate Lofts Partners and Genex Construction, LLC for damages for the defective construction of the condominium development. The underlying case settled for \$6.9 million. However, a dispute remains between Bituminous Casualty Corporation, which insured Genex, and Hartford Casualty Insurance Company, which insured Rivergate.

Hartford asserted third-party claims against Canal Insurance Company’s Motion (the third-party defendant), suing for declaratory judgment and for equitable contribution. Hartford sought a declaration to determine Canal’s obligations and for contribution if the district court determined that Hartford owed any defense or indemnity obligation to Genex with respect to the underlying action. Both claims were based on the premise that Canal owed a duty to defend and/or indemnify Genex in the underlying action.

Canal issued two separate general liability insurance policies, which provided coverage for “property damage” caused by an “occurrence” during the applicable policy periods — March 31, 2002 to March 31, 2003 and March 31, 2002 to March 31, 2004. The policies were “occurrence” policies. Canal initially agreed to defend Genex under a reservation of rights but later withdrew from Genex’s defense in the underlying action.

The district court concluded that Canal had a duty to defend Genex in the underlying action. The homeowners’ association’s complaint in the underlying action alleged, among other things:

47. Upon information and belief, these and other errors, deficiencies and defects, for which the Defendants are legally liable, have caused and continue to cause the Association actual property damages and/or other losses, and consequential damages to, and the loss of use of, various elements of the Project, over time from the date those areas were first put to their intended use.

Canal relied on the allegations that the association was not created until November 2004 and that its damages to the various elements of the project began from the date those areas were put to their intended use. Canal argued that the project was not, and could not have been, put to its intended use prior to that time because the association was not formed until November 2004. As such, Canal argued that the association could not have been damaged until after it was formed, which was beyond both of Canal’s policy periods.

The district court rejected Canal’s argument, noting that the date the association was formed was not controlling. It reasoned that the complaint in the underlying action linked the association’s damages to when the areas of the project were put to their intended use. The district court stated, “The issue is whether the intended use of the project began only upon completion of the Project, which appears to have occurred outside the date of policy coverage, or before — and if so, whether that occurred during the period of time Canal insured Genex.”

The district court noted that, although the complaint does not specify what period the construction of the project and/or the alleged negligence of the defendants occurred, the alleged facts potentially fell within the scope of coverage. The district court also noted that Canal had not disputed that the construction of the project occurred at least in part during the period of time it insured Genex. Because the underlying complaint demonstrated that there was the potential that the alleged facts fell within the scope of coverage, the district court concluded that Canal owed a duty to defend Genex.

Practice Note: In determining how to interpret the “intended use” language contained in the underlying complaint, the court relied on *EMC Ins. Cos. v. Mid-Continent Cas. Co.*, 884 F. Supp. 2d 1147 (D. Colo. 2012). Although the EMC case concerned the interpretation of a “products completed operations hazard” provision, the court relied on the case because the complaint in EMC contain a similar allegation concerning “intended use.”

Policy Endorsements Held to Be Against Public Policy

Greystone Construction, Inc. v. Nat'l Fire & Mar. Inc. Co., 2013 U.S. Dist. LEXIS 46707 (D. Colo. March 31, 2013)

This coverage dispute stems from the defendant National Fire & Marine Inc. Co.'s denial of defense to its insureds, the plaintiffs Greystone and Brannan, in state actions alleging construction defect. The underlying actions ultimately settled; however, the plaintiffs contended that the defendant National Fire had a duty to defend in the underlying suits and had a duty to indemnify them for the settlement payment.

Greystone and Branan were both contractors engaged in the construction of residential homes. Each obtained commercial general liability policies from both National Fire and American Family. Each of the builders was sued for construction defects in homes it built. The builders sought defense and indemnification from both National Fire and American Family.

Among other arguments, National Fire argued that it had no duty to defend because an exclusion contained in the endorsement to the applicable policy — Endorsement M 5076 — purportedly precluded coverage for damages sought against the insured if the insured requests a defense under an earlier-issued insurance policy. It argued that because Greystone and Branan requested that American Family defend them under their earlier insurance policies, the endorsement provided no coverage for the damages sought in those suits (and, accordingly, that it does not have a duty to defend).

The court found that the paragraph of the endorsement was unenforceable as a matter of public policy. The court stated that the “[o]peration of the endorsement essentially nullified an insured’s coverage if the insured complies with its obligations and asserts its rights under any earlier policy.” The court further noted that “[w]hen, as here, the insured is left without any coverage for damages that may have occurred during a period of time when it believed it had coverage.”

The court also refused to enforce an endorsement to the applicable policy concerning the election of insurance carrier for defense — Endorsement M 5077. In relevant part, Endorsement M 5077 requires the insured to elect which insurance company it would like to provide its defense. If the insured requested another insurance company to provide the defense, National Fire has the “option,” but not “the duty,” to defend the suit. In refusing to apply this endorsement, the court reasoned that the endorsement operates to deny a benefit conferred by National Fire’s policies solely on the basis of the insured having “requested” that another insurer defend its suit. The court noted that “[i]n the situation where there is no overlap in insurance coverage, the insured would be left without a defense if its request to the other insured is denied.

Practice Note: An endorsement that leaves an insured without coverage based on its election to have a co-insurer defend the insured raises public policy concerns. As such, even outside of Colorado, insureds can raise this prudential argument and sidestep certain endorsements.

Georgia

Damage to Insured’s Completed Work Is an “Occurrence”

Taylor Morrison Services, Inc. v. HDI Gerling America Ins. Co., 2013 Ga. LEXIS 618 (Sup. Ct. 7/12/13)

The Georgia Supreme Court answered the following certified questions from the Eleventh Circuit:

1. Whether, for an “occurrence” to exist under a standard CGL policy, Georgia law requires there to be damage to “other property,” that is property other than the insured’s completed work.
2. If the answer to Question One (1) is in the negative, whether for an “occurrence” to exist under a standard CGL policy, Georgia law requires that the claim being defended not be for a breach of contract, fraud or breach of warranty from the failure to disclose material information.

The court answered the first question in the negative and the second question in the affirmative as to fraud and in the negative as to breach of warranty. The court, in reaching its decision, rejected the insurer's argument that an "occurrence" under a CGL policy requires damage to something other than the work of the insured. The court further concluded:

Our understanding of the insuring agreement also is consistent with the strong trend in the case law [that] interprets the term occurrence to encompass unanticipated damage to nondefective property resulting from poor workmanship.

In reaching its decision, the court cited cases from Connecticut, South Carolina, Illinois, Florida, Texas, the Fourth Circuit, and the Tenth Circuit.

Practice Note: The determination of whether there has been an "occurrence" is jurisdictionally specific and requires an assessment of the law in the relevant jurisdiction, as well as a keen understanding of the facts.

Minnesota

Mold Exclusion in Professional Liability Insurance Applies to Construction Business Seeking Recovery

MM Home Builders, Inc. v. Endurance Am. Specialty Ins., 2013 U.S. Dist. LEXIS 36835 (March 18, 2013)

The facts are serpentine in this coverage dispute. Defendant Endurance American Specialty Insurance Inc. issued professional liability insurance (E&O) to Corporate 4 Insurance Agency. Corporate 4 provided insurance services, advice, and counsel regarding insurance to plaintiff MM Home Builders, Inc. during all times relevant to this action and the underlying actions.

Richard Lewandowski owns and controls MM Home Builders. In 2008, MM Home completed a five-building, 38-unit townhome project. Lewandowski, in his individual capacity, began to purchase the townhome units from MM Home. In an attempt to sell the townhomes, an inspector identified a number of construction defects that caused water intrusion and related mold and fungal issues.

Ultimately, Lewandowski filed a lawsuit against MM Home. MM Home tendered defense of the lawsuit to its insurers. One insurer, Granite States Insurance Company, denied coverage. Lewandowski and his wife eventually settled certain claims and, as part of the settlement, they signed a release dismissing claims against MM Home and certain insurance companies. The release reserved to the Lewandowskis, among other things, claims for which any insurer other than the ones part of the settlement agreement would be obligated to indemnify MM Home.

MM Home then served a complaint against Granite State and Corporate 4. Corporate 4 tendered the defense of the suit to its E&O insurance carrier, Endurance. In turn, Endurance notified Corporate 4 that coverage was denied primarily on the mold exclusion contained in the policy. MM Home entered into a *Miller-Shugart* settlement with Corporate 4 and, pursuant to the agreement, the neutral fact finder determined that the damages were \$1.8 million.

In the action at hand, MM Home asserted that it was the assignee of Corporate 4 under the *Miller-Shugart* agreement and it was therefore entitled to seek a declaration of coverage under the E&O policy. MM Home explained in its complaint that one of its insurers, Granite State, denied coverage in the underlying action based on an exclusion in the relevant policy for multi-unit buildings. In turn, MM Home alleged that Corporate 4, as its insurance agent, was negligent in obtaining insurance that excluded multi-unit dwellings, and that MM Home Builders was damaged when construction defects were found in the townhomes as determined by the neutral fact finder.

Endurance moved for summary judgment on the basis that the mold exclusion in the E&O policy applied and, thus, excluded coverage for the damages sought in the case. The district court agreed, granted Endurance's summary judgment motion, and dismissed the matter with prejudice. The district court gave a broad construction to the mold exclusion, reasoning that the exclusion defines itself by the underlying claim — which is based on mold claims — not the activity of the insured. Thus, even though the damages incurred by the abatement of mold in the townhome project arose in the underlying case, the mold exclusion still applied to the claims asserted in the declaratory judgment action because the alleged negligent procurement of insurance flowed from the damages incurred by the abatement of mold in the townhome project.

The district court rejected MM Home's assertion that the doctrine of reasonable expectations afforded coverage to Corporate 4. Noting that Minnesota courts narrowly apply the doctrine of reasonable expectations, the district held that the matter did not involve exceptional circumstances to apply the doctrine. It noted that the mold exclusion was not hidden in the policy and was clear and unambiguous.

The district court also rejected MM Home's argument that the doctrine of illusory coverage applied because Corporate 4 paid a premium for protection against negligent errors and omissions. It noted that there was no evidence in the record that a specific portion of the premium paid by Corporate 4 to Endurance was allocated to cover negligent procurement claims that arose from damages caused by mold due to construction defects. The district court noted that the mold exclusion did not render coverage under the E&O policy to be functionally nonexistent, it simply excluded coverage for damages arising for mold.

Practice Note: In holding that the mold exclusion applied, the district court relied on *Bd. of Regents of Univ. of Minn. v. Royal Ins. Co. of Am.*, 517 N.W.2d 888 (Minn. 1994). That case concerned a plaintiff who sought to enforce an asbestos-related products liability settlement against an asbestos supplier's insurer. The insurer denied coverage based on the pollution exclusion, and the plaintiff argued that as the underlying claims involved product liability, not pollution, the pollution exclusion did not apply. Minnesota's highest court rejected that argument, finding that the exclusion defines itself by characterizing the activity of the pollutant, not the activity of the insured polluter.

Nevada

Concurrent Cause of a Seismic Design Defect to Houses Defeated an Applicable Exclusion

St. Paul Fire & Marine Ins. Co. v. Del Webb Communities, Inc., 2013 U.S. Dist. LEXIS 37903 (D. Nev. March 19, 2013)

This case concerns coverage for an underlying lawsuit against the defendant for alleged structural seismic design defects. The plaintiff issued an excess insurance policy, which covered the defendants, as insureds. The policy contains an exclusion concerning "the performance of or failure to perform architect, engineer or surveyor professional services."

In December 2009, homeowners in a country club subdivision asserted a class action claim against the defendants for, among other things, alleged structural seismic design defects. The allegations related to 15 models of homes build in the subdivision development designed by the structural engineering firm Bingham Engineering, Inc. for the defendants without the seismic structural design required by the 1994 and/or 1997 Uniform Building Code.

The plaintiffs alleged in their complaint that the class members' common claim is for each of the 15 individual models of single-family homes, and the constructional defect is the total omission of the seismic design required by the Uniform Building Code. In the coverage dispute, the insurer St. Paul argued that the exclusion concerning architect, engineer, or surveyor professional services applied to the claims in the underlying action by the homeowners. The defendants did not dispute that the structural engineering design services rendered by Bingham were professional services that fell within the exclusion. Instead, the defendants argued that "if any cause (act, error, or omission) other than Bingham's allegedly negligent performance of engineering services contributed to the alleged hazardous condition in the homes, the [exclusion] does not apply." The defendants claimed that St. Paul was required to consider evidence beyond the allegations in the underlying action in determining whether the exclusion applied.

Notably, the defendants claimed that they needed additional discovery to determine if there was a concurrent cause that would defeat the exclusion. The district court rejected the defendants' claim, noting that the defendants failed to postulate how the damages sought in the underlying actions could be attributable to anything other than professional services that are the subject to the exclusion. The court noted that (1) the only allegation in the underlying action was that the homes were built using the allegedly defective Bingham plans and were hazardous because they did not meet seismic codes, and (2) the only damages sought in the underlying action were damages relating to curing the design defect. As such, the court concluded that the exclusion applied to the claim asserted in the underlying action.

Practice Note: The decision also analyzes the applicability of the abstention doctrine.

Nevada

Insured's Negligent Acts Found to Be "Occurrence" Despite Insurer's Claim They Occurred Prior to Policy Period

Maryland Cas. Co. v. Am. Safety Indem. Co., 2013 U.S. Dist. LEXIS 34610 (D. Nev. March 12, 2013)

This equitable contribution action arises out of Laird Whipple Concrete's concrete and foundation work as a subcontractor for two projects completed in 1994 and 1995. Laird is the mutual insured of the plaintiffs Maryland Casualty Company and Northern Insurance Company of New York and the defendant American Safety Indemnity Company.

The defendant denied coverage for defense fees and indemnity payments to Laird arising from two construction default lawsuits concerning the two projects. The developers of both those properties were later sued due to a variety of construction defects, including foundation and concrete defects. The suits were brought in 2002 and 2006, respectively, but the respective complaints did not specifically allege when the damage occurred. Laird ultimately settled those claims.

From August 1, 1993 to August 1, 2001, Laird held a series of CGL insurance policies with the plaintiffs insuring against civil liability and providing payment of defense costs. From August 1, 2011 to August 1, 2007, Laird held similar policies with the defendant. Upon notification of the underlying actions, Laird tendered the defense to both the plaintiffs and the defenses because the actions potentially spanned both sets of policies. The plaintiffs ultimately accepted tender of the defense and paid the defense and settlement costs. As noted, the defendant declined tender, asserting that the underlying actions were excepted from coverage by various provisions with the defendant's policies.

The plaintiff filed the lawsuit concerned in this decision against the defendant seeking equitable contribution for a portion of the defense and indemnity costs. The plaintiff alleged that the denial of coverage on the underlying actions was wrongful and, therefore, the plaintiffs were entitled to the amount of defense and indemnity costs that the defendant should have paid. The plaintiffs moved for partial summary judgment seeking equitable contribution from the defendant for defense and indemnification costs paid to Laird.

Among other arguments, the district court rejected the defendant's contention that the underlying actions could not be "occurrences" under its policy because Laird's negligent acts, which resulted in the damaged foundations, occurred before the policy period. An endorsement to the applicable insurance policy defines "occurrence" for the relevant time periods as:

[A]n accident, including continuous or repeated exposure to substantially the same general harmful conditions that happens during the term of this insurance. "Property damage" . . . which commenced prior to the effective date of this insurance will be deemed to have happened prior to, and not during, the term of this insurance.

The district court noted that under Nevada law, the timing of an "occurrence" in CGL insurance policies has generally been construed as the time of the property's physical alteration, not the insured's negligence. Distinguishing the case law for that proposition, the defendant argued that the policy at issue defined "occurrence" differently. The definition of "occurrence" in the case law was defined as "an accident including continuous or repeated exposure to conditions, which results in ... property damage." The defendant argued that replacing "which results in ... property damage" with "that happens during the term of this insurance" requires the finding that "occurrence" as defined in the defendant's policy meant a negligent act of the insured that takes place during the policy period. Thus, under the defendant's definition of "occurrence," the allegations in the underlying actions could not constitute "occurrences" because Laird's negligent act would have taken place at the latest at completion of the foundation and concrete work in 1994 and 1995 respectively, prior to the policy period.

The district court rejected the defendant's argument for these reasons: First, the court reasoned that the terms "occurrence" and "property damage," as set forth in the defendant's policy, were not as clearly distinct as the defendant claimed them to be. The district court noted that the term "occurrence" in the defendant's policy was reasonably susceptible to the case law it cited regarding the timing of an "occurrence" in CGL insurance policies.

Second, the district court noted that had the parties intended to limit coverage to instances where the negligent act of the insured and the resulting property damage occurred in the same policy, the definition of “occurrence” would read, “the negligent act of the insured occurring within the policy period.” The district court noted that the policy’s actual definition of “occurrence” indicated a much broader scope than solely the negligent acts of an insured.

Third, the court relied on the California Court of Appeals’ interpretation of the exact language at issue in *Pennsylvania General Ins. Co. v. Am. Safety Indem. Co.*, 185 Cal. App. 4th 1515, 111 Cal. Rptr. 3d 403 (Cal. Ct. App. 2010). In that case, the California Court of Appeals found the amended definition of “occurrence” was susceptible to the interpretation that “the resulting damage, not the [negligent act of the insured], is still a defining characteristic of the occurrence that must take place during the policy period to create coverage.” *Id.* at 411.

Practice Note: The district court also rejected the defendant’s arguments that (1) the insurance was never implicated in the underlying actions because Laird failed to pay the self-insured retention, and (2) the other insurance provision of its policy required that the defendant’s policy was excess.

Causes of Action Asserted Against Co-Insurer Survive Motion to Dismiss

N. Am. Specialty Ins. Co. v. Nat’l Fire & Marine Ins. Co., 2013 U.S. Dist. LEXIS 47573 (D. Nev. April 2, 2013)

The case stems from a series of construction defect lawsuits in state court in both Nevada and Arizona. The plaintiffs and the defendant had previously issued insurance policies to entities against which the construction defect lawsuits were eventually filed. The plaintiffs agreed to defend and indemnify those entities; however, the defendant allegedly refused when the entities tendered their respective defenses.

The plaintiffs filed an action in response to the defendant’s alleged refusal to contribute to the payment of the defense costs and indemnification. They asserted five causes of action: (1) equitable contribution, (2) equitable subrogation, (3) equitable indemnity, (4) declaratory relief, seeking a declaration that the defendant had a duty to defend the underlying construction defect lawsuits, and (5) declaratory relief seeking a declaration that the defendant had a duty to indemnify the insured entities. The defendant moved to dismiss the plaintiffs’ complaint or, in the alternative, to sever and transfer certain of the plaintiffs’ claims to the District of Arizona.

The defendant’s motion to dismiss was unsuccessful as to all five causes of action. As to the equitable contribution cause of action, the court stated that the defendant had correctly noted that Nevada had not yet addressed the issue. Nevertheless, the court rejected the defendant’s reliance on case law, noting that the case law upon which the defendant relied did not actually address the pleading standard for equitable contribution. As such, the court found that the defendant failed to persuade it to dismiss this cause of action.

As to the equitable subrogation cause of action, the defendant again relied on California law based on the absence of Nevada law on the subject. The defendant relied on *Fireman’s Fund Ins. Co. v. Maryland Cas. Co.*, 65 Cal. App. 4th 1279, 77 Cal. Rptr. 2d 296 (Cal Ct. App. 1998), where the court set forth eight essential elements of an insurer’s cause of action of equitable subrogation. The defendant argued that the plaintiffs’ complaint should be dismissed because (1) it lacked an allegation that the defendant is primarily liable for any amounts allegedly paid by the plaintiffs, and (2) it failed to allege an exact sum of money that the plaintiffs paid. The court noted that it was unclear whether Nevada courts would require a plaintiff to allege the eight elements set forth in *Fireman’s Fund Ins. Co.* but, even if it did, the court found that the plaintiffs adequately pleaded those elements. The court also found that the plaintiffs adequately pleaded their equitable indemnity cause of action, rejecting the defendant’s claim that the plaintiffs failed to allege that the defendant is primarily responsible for the defense and indemnity payments purported made by the plaintiffs.

Finally, the court rejected the defendant’s claim that the declaratory relief was moot because the underlying cases had settled. The court noted that the defendant met the heavy burden of establishing that no effective relief remained for the court to provide; the defendant advanced conclusory statements in this regard.

Practice Note: Well-pled complaints seeking to gain coverage from a co-insurer will likely defeat motions to dismiss. A complaint asserting more than conclusory statements will likely survive such a motion. On the flip-side, those co-insurers moving to dismiss on the pleadings should focus on those complaints that are bare bones and lack any fact pleading.

South Carolina

Insurer Cannot Seek Equitable Contribution for Its Own Expenses From Another Insurer of a Mutual Insured

Assurance Co. of Am. v. Penn-America Ins. Co., 2013 U.S. LEXIS 45229 (D. S.C. March 27, 2013)

This coverage action stems from construction defect lawsuits arising out of allegedly defective construction of townhomes in South Carolina. The plaintiffs in the underlying construction defect lawsuits allege that, as a result of defective design and construction on the part of the defendants in that underlying action, the plaintiffs sustained continuous and repeated damage since the completion of construction of the townhomes. James Eason, individually and doing business as James Eason & Company, were defendants in the construction defect litigation.

Assurance Company of America issued an insurance policy to James Eason that was in effect from August 25, 2001 to August 25, 2002. Penn-America Ins. Co. also issued a policy of general liability insurance to James Eason that was in effect from August 6, 2003 to August 6, 2004. Both the Assurance policy and the Penn-America policy provide coverage for indemnity and defense of suits. In response to the construction defect litigation, Eason tendered its defense to both Assurance and Penn-America. Assurance agreed to defend Eason in the underlying construction defect litigation pursuant to a full reservation of rights. Penn-America initially denied coverage and refused to defend Eason in the underlying construction defect litigation. Penn-America subsequently agreed to undertake Eason's defense under reservation of rights. At the motion stage, Assurance (through counsel) advised the court that Assurance was seeking to withdraw its defense.

Assurance sought equitable contribution from Penn-America for its own expenses in defending the mutual insured Eason, and moved for summary judgment on that claim. The district court denied Assurance's motion, reasoning that Assurance is not a party to the insurance contract with Penn-America and is without an assignment from the insured Eason. As such, the district court concluded that Assurance had no standing to pursue these claims against Penn-America.

The district court also reasoned that in South Carolina the duty to defend is personal to each insurer, citing *Sloan Constr. Co. v. Central Nat'l Co. of Omaha*, 269 S.C. 183, 236 S.E.2d 818, 820 (1977). It pointed out that the obligation is several and the insurer is not entitled to divide the duty nor require contribution from another absent a specific contractual right.

Practice Note: Check the applicable jurisdiction to determine whether its common law holds that the duty to defend is personal to each insurer. If so, a claim for equitable contribution from another insurer of a mutual insured will most likely fail.

Exclusion J(5) Is a Viable Defense

Bennett & Bennett Construction, Inc. v. Auto Owners Ins. Co., Appellate Case No. 2011-183007 (Sup. Ct. S.C. 7/17/13)

In this action, the general contractor sued its subcontractor and the subcontractor's insurer, contending that there was coverage for the damages caused by the subcontractor. The subcontractor had completed its work, which involved the installation of the brick face on the building. Subsequent to leaving the premises, the subcontractor was hired by the general contractor to clean the face of the brick that the subcontractor had installed. The lower court had held that the incident was an "occurrence" under the subcontractor's policy and that neither exclusion j(5) nor exclusion n applied to bar coverage. The Supreme Court of South Carolina held:

Exclusion j(5) unambiguously excludes coverage whenever the insured or a person acting on the insured's behalf causes damages in the course of working on the property, regardless of whether the insured's work has been completed.

The court also held that exclusion n barred coverage because the insured/subcontractor's work was replaced because of a deficiency or inadequacy in the work.

Practice Note: In addition to fully assessing whether there is coverage under the coverage grant of the policy, all exclusions should be reviewed in the context of the relevant facts.

Texas

Interpretation of “Construction of Residential Property Exclusion with Exception for Apartments”

Am. Empire Surplus Lines Inc. Co. v. Nat’l Fire Ins. Co. of Hartford, 2013 U.S. Dist. LEXIS 39944 (S.D. Tex. March 21, 2013)

This coverage dispute was between two insurers over commercial construction coverage. The coverage dispute centers on exclusion in a policy from the defendant First Specialty Insurance Corporation. The exclusion was contained in an endorsement to the policy, and it stated:

The following exclusion is hereby added to Section I, Coverage A, Bodily Injury and Property Damage Liability under Paragraph 2, Exclusions and to Section I, Coverage B., Personal and Advertising Injury Liability under Paragraph 2., Exclusions:

In consideration of the premium charged, it is understood and agreed that no coverage exists and no duty to defend is provided for:

Any and all claims, including but not limited to, claims for “bodily injury”, “property damage”, “personal and advertising injury”, arising out of, related to, caused by, or associated with, in whole or part, the construction of residential properties, except apartments, but including and not limited to, single family dwellings, duplexes, three and four family dwellings, or complexes, townhomes or condominiums. In the event any apartment to which coverage under this policy applies is converted to a condominium, duplex or multi-family dwelling, then coverage under this policy is excluded for any claims for “bodily injury”, “property damage”, “personal and advertising injury”, arising out of, related to, caused by, associated with, in whole or in part, the construction of said apartments which occur after the conversion of the apartment into a condominium townhome or multi-family dwelling.

Plaintiff American Empire Surplus Lines Insurance Corporation and First Specialty both issued insurance policies to ARCI, Ltd. for different policy periods. American Empire and two other insurers were also defending ARCI in a construction defect lawsuit in a Florida state court. In the coverage dispute, American, under its rights of subrogation, sought a declaration that First Specialty was also obligated to defend ARCI in the construction defect lawsuit.

First Specialty issued a General Liability Policy to ARCI, as named insurer for a policy period of January 17, 2003 to January 17, 2004. ARCI performed roofing, sheet metal, and chimney flashing work in 2002 and 2003 in the construction of an apartment complex. In 2006, the apartments in the complex were converted to condominiums. ARCI was later sued in the underlying construction defect lawsuit for its work in the apartment construction.

The party insurers disagree as to the last portion of the exclusion, “which occur after the conversion of the apartment into a condominium, town home or multi-family dwelling.” American Empire claimed that the phrase “which occur” refers to “bodily injury,” “property damage,” and “personal and advertising injury.” The district court rejected that interpretation of the exclusion.

First Specialty contended that “which occur” refers to “claims.” As such, First Specialty argued that those claims were outside of First Specialty’s coverage because the claims for construction defects were made after the conversion of condominiums. The district court agreed, analyzing that portion of the exclusion in light of its surrounding policy language. It noted that the exclusion’s first sentence — the one preceding the sentence with the disputed language — clearly states that it is “claims” that are excluded from coverage; therefore, the district court noted that “it would be strange if the next sentence focused on excluding ‘bodily injury,’ ‘property damage,’ and ‘personal and advertising injury.’”

The district court granted First Specialty’s motion for summary judgment and dismissed the complaint with prejudice.

Practice Note: The impact of this decision is less about the particular exclusion and more about the court’s analysis in determining the intent of the exclusion’s language. This decision is valuable for the legal proposition that the meaning of a phrase in an insurance policy can be analyzed in light of the language that surrounds it.

LITIGATION

Texas

Delay Claim Barred by Residential Construction Liability Act

Brent Timmerman d/b/a Timmerman Custom Builders v. Dale, 2013 Tex. App. Lexis 3906 (5th Dist. March 27, 2013)

Dale hired Timmerman to remodel his condominium. As part of their written contract the parties agreed to perform construction with “reasonable diligence.” The contract contained a provision in which both parties acknowledged the RCLA (Residential Construction Liability Act) “applies to construction defects and any disputes or claims regarding construction defects in connection with the improvements.” Subsequently, Dale terminated the contract and filed suit claiming poor workmanship, overpayment of fees, and unreasonable delay in completing the project. All issues were settled prior to trial except for Dale’s delay claim, in which he sought the fair market rental value of his condominium running from the time the work should have been completed. The court, relying on the legislative intent of the RCLA, noted the purpose of the statute was to modify causes of action for damages resulting from construction defects in residences by limiting and controlling causes of action which otherwise exist. The code provides standards of causation, limits on damages and defenses, and encourages settlement through its procedures by giving notice and allowing the contractor time to cure.

To determine whether a delay claim is a “construction defect,” and giving the statute its plain meaning, the court concluded a claim regarding delay is an action arising from a matter concerning the condominium’s construction. In other words, although Dale’s delay claim may not go to the quality of construction, it concerned the manner in which Timmerman performed the construction and is thus governed by the RCLA. As to Dale’s damage claim, the court found that the RCLA applied, and further, that it limited the claimant’s recovery to specifically prescribed economic damages proximately caused by the construction defect. Accordingly, the lost rental value sought by Dale was not recoverable under the statute.

Practice Note: The court noted the RCLA was adopted to provide a balance between the residential contractor and owner with regard to construction disputes. It does not create any distinct causes of action but prevails over any conflict between it and another law. It similarly limits a claimant’s recovery to enumerated economic damages caused by the construction defect.

In Professional Liability Dispute, Unfavorable Arbitration Award Against Homeowner Upheld Following Failure to Introduce Full Record

Goldman v. Buchanan, 2013 Texas App. Lexis 3086 (5th Dist. March 21, 2013)

Goldman contracted with two professionals: Buchanan, an architect, to design his house, and Lawrence Wallace, a contractor, to build the house. He subsequently sued Buchanan and Wallace for negligence and breach of contract. Based upon the terms of the two contracts, the trial court ordered Goldman’s claims to be submitted to arbitration. Wallace subsequently settled for \$1 million. The arbitrator found the house as designed and constructed had material construction deficiencies. They found Buchanan deviated from his professional standard of care. Goldman was awarded \$840,000. This amount was reduced by Wallace’s settlement to a net award of \$0. Buchanan then moved to confirm the award and Goldman moved to vacate the award.

In his motion papers, Goldman argued the award should be vacated because 1) the arbitrator refused to permit him to obtain evidence of “financial misdeeds” by Buchanan and Wallace and then ruled he failed to provide sufficient evidence that financial misdeeds occurred, and 2) the arbitrator manifestly disregarded Texas Law as it applied to damages. At the hearing in the Trial Court on Goldman’s motion to vacate, counsel attempted to introduce a number of exhibits from the arbitration hearing. Buchanan’s counsel objected with the grounds that Goldman had failed to bring a record of the arbitration hearing to the trial court. Only the final arbitration award was admitted. Due to the insufficiency of the record, the trial court denied the motion to vacate and confirmed the award.

In a de novo review, the Fifth District Court of Appeals affirmed the trial court’s findings. It specifically noted the record introduced below and before them on appeal was insufficient to allow them to vacate the arbitration award due to Goldman’s failure to introduce a record of the arbitration hearing. Accordingly, without the record the appellate court could not conclude that the arbitration award disregarded the law. Goldman’s motion simply failed to show how the requested information was either relevant or necessary for his case.

Practice Note: It is clear that the courts in Texas give great deference to the arbitrator’s awards. The court noted that Texas law favors the arbitration of disputes, and that judicial review of an arbitrator’s award is narrow, focusing on the integrity of the process, not the propriety of the result. The court noted without a record, there could be no appellate review of the arbitrator’s decision.

Kansas

Economic Loss Doctrine Found Inapplicable to Tort Claim by Private Homeowner Against Contractor

Coker v. Siler, 2013 Kan. App. Lexis 29 (May 3, 2013)

In 2006, J.M.C. Construction purchased a partially built house from Michael Siler. After purchase, Chaney, president of J.M.C., personally installed the main water line into the residence. Subsequently, Coker purchased the home from J.M.C. The sales contract included a one-year express warranty provision that provided that the seller warrants all improvements on the property for defects in materials and workmanship. Once Coker took possession of the home, he began to experience high water bills. Eventually he learned that the water main had separated from a coupling and water was flowing under the home and damaging the foundation, causing the home to shift. Coker sued the defendants for negligence, breach of implied warranty, and strict liability. At the trial level, Coker's case was dismissed via summary judgment motion. The trial court relied on *Prendiville v. Contemporary Homes, Inc.*, 32 Kan. 847 (2004), which at the time was good law. The court found that the economic loss doctrine barred Coker's negligence, strict liability, and breach of warranty claims. Subsequent to the trial court's decision and prior to the appeal, the Kansas Supreme Court overruled *Prendiville* in *David v. Hett*, 293 Kan. 679, 270 P.3d 1101 (2011). In *David*, the appellate court determined that the economic loss doctrine does not bar homeowners seeking to recover economic losses resulting from negligent construction. Using *David*, the court found the economic loss doctrine should not apply as a bar to a homeowner. However, the court found no implied warranty existed between Coker and Chaney since there was no underlying contract to which Chaney was a party as an individual. Instead, the court found Chaney was liable to Coker in his individual capacity as a plumber because he owed a duty to Coker since Coker was a third party who was damaged as a result of his work.

Practice Note: Under Kansas law, the economic loss doctrine no longer applies to homeowner claims against construction contractors. However, tort claims by the homeowner will only survive if there is a duty imposed by law independent of the underlying construction contract.

Florida

Economic Loss Rule Held to Apply Only in Product Liability Cases

Tiara Condominium Association, Inc. v. Marsh & McLennan Companies, Inc., 2013 U.S. App. Lexis 7583 (11th Cir. 2013)

This matter arises out of a contract between Tiara, the association responsible for managing a condominium, and its insurance broker, Marsh. Apparently, the condominium tower managed by Tiara sustained damage from two hurricanes in 2004. The condominium association claimed the broker caused part of its losses by failing to procure an adequate policy of insurance for the condominium. The U.S. Court of Appeals for the Eleventh Circuit found Florida Law to be unclear and certified a question to the Supreme Court of Florida specifically dealing with Florida's application of the economic loss rule. The question, as certified by the Florida Supreme Court, was: "Does the economic loss rule bar an insured's suit against an insurance broker where the parties are in contractual privity with one another and the damages sought are solely for economic losses?" The Florida Supreme Court traced the history of the rule and noted its origin in product liability cases. However, as the court noted, the rule was eventually expanded and found to apply in situations where contractual privity between the parties existed. The court noted there was an "unprincipled extension of the rule" and it was time to "recede from our prior rulings to the extent that they may have applied the economic loss rule to cases other than product liability." Accordingly, the Supreme Court returned the economic loss doctrine to its origins in products liability, finding expansion of the rule unwise "in practice."

Practice Note: The concurring opinion of one of the justices reflects the concerns that the ruling undermines Florida prior contract law, repudiating reasoning in the court's prior decisions, and encourages future breach of contract claims to be accompanied by tort claims.

Court Clarifies Proper Measure of Damages in a Construction Defect Claim

Kritikos & Jupiter Holding Co., LLC v. Andersen, 2013 Fla. App. Lexis 6549 (4th Dist. April 24, 2013)

In 2003, Kritikos purchased property and hired Peter Gluck, an architect, to design a home. Gluck's corporation, ARCS, contracted with Kritikos to act as construction manager. Gluck did not have a Florida contractor's license so, in turn, he entered into a construction agreement with Andersen Builders, a licensed general contractor from Florida. The Andersen agreement was for specific services to be performed by Anderson, including coordination and supervision. The agreement appeared to be a construction management agreement. The original construction budget estimate was \$4 million. However, by the original completion date, the home was only 60 percent complete and the projected cost of completion had doubled to \$8 million.

Four months after the original completion date, Andersen was terminated. Andersen filed suit against Kritikos for breach of contract, unjust enrichment, and foreclosure of a construction lien. Kritikos pleaded an affirmative defense of set off and countersued Andersen for breach of contract, negligence, and a fraudulent lien based upon claims of construction defects, overcharges by Andersen, and delay damages.

The trial court entered a directed verdict against Kritikos denying his affirmative defenses and finding against his construction defect counterclaim. The trial court specifically noted there was no evidence introduced for the cost of correcting the work. The court felt the plaintiff needed to show the defects were repaired and show the actual costs of the repairs rather than estimates. It was Kritikos' position that much of the defective work was subject to a design change so the proper measure and proof of damages was an estimate of what it would have cost to complete the work according to the original contract. The Court of Appeals found the trial court had misapplied *Barile Excavating & Pipeline Co. v. Kendall Props. Inc.*, 462 So.2d 1129 (Fla. 4th DCA 1984) in granting a directed verdict in favor of Andersen as the *Barile* facts concerned a project where the owner actually completed the work pursuant to the contract. Thus, in *Barile*, the measure of damages was the actual cost to complete the construction work not an estimate of same. The instant matter was different factually from *Barile*, so the court found the proper measure of damages for construction defect was the cost of correcting defects, except in certain instances where the corrections involve an unreasonable destruction of the structure, the cost of which is grossly disproportionate to the results to be obtained. If, in the course of making repairs, the owner elects to adopt a more expensive design, the recovery should be limited to what would have been the reasonable cost of repair according to the original design. Based upon the above, the case was remanded to the trial court for a new trial on damages.

Practice Note: The proper measure of damages in a construction defect claim is the cost of correcting the defect unless the corrections involve an unreasonable destruction of the structure and a cost which is grossly disproportionate to the results obtained. In this matter, the Court of Appeals noted the difference between the measure of damages where an owner actually completes work that a contractor failed to complete, versus the cost of correcting defects once work had been completed.

New Jersey

Court Enforces Arbitration Agreement Built Into Unit Owner Purchase Agreement

Hudson Tea Building Condominium Association, Inc., et. al. v. Block 268, LLC, et. al., 2013 N.J. Super. Unpubl. Lexis 978 (App. Div. April 29, 2013)

The plaintiff, a condominium association, and multiple individual unit owners brought suit against the defendant alleging various statutory, tort, and contract claims related to construction defects. The defendant moved to dismiss the claims of all individual owners in a pre-answer motion arguing the individual unit owner claims were barred by the mandatory arbitration provision built into each sales agreement. At the trial court level, the motion was denied. The Appellate Division reviewed. The court initially noted that New Jersey views "arbitration as the favored method of resolving disputes," and that arbitration clauses are generally viewed broadly. They found the subject arbitration clause was broadly written to cover "any and all disputes with seller." Further, the court found that although the provision excluded damages for common elements of the building, the issue of whether the defect is within a common element or is unit specific is for the arbitrator to decide.

Practice Note: The court took pains to note that New Jersey favors arbitration as a method of resolving disputes and that its courts have broadly construed arbitration clauses to encompass tort and contract claims. The question of whether the parties were subject to arbitration was deemed a question of law for the court. It is clear that the courts in New Jersey encourage arbitration of disputes.

Ohio

Lack of Clarity on Exclusions Allows Express and Implied Warranty Claims to Continue

Gerling & Associates, Inc. v. Gearhouse Broadcast Pty Ltd., 2013 U.S. Dist. Lexis 33104 (U.S.D.C. for the Southern District of Ohio, Eastern Division March 11, 2013)

At issue was whether defendant Gearhouse could pursue both express and implied warranties in a construction defect action. The court answered in the affirmative and allowed both theories to proceed. The court compared Ohio Revised Code §1302.29 A & B to the contract provision at issue and found the provisions did not comport with the statute's requirements in that it failed to conspicuously state that it excludes all other implied warranties, capitalize the language, offset the terms, or present same in contrasting type. Accordingly, all warranty claims were allowed.

Practice Note: When drafting a warranty, the drafter must ensure that the warranties that are excluded must be conspicuous in nature by using bold, offset, or contrasting type or by capitalizing same in order for the warranty disclaimer to be effective.

Louisiana

Once Arbitration Is Required, Court Will Not Review Failure to Follow Procedural Rules

Southgate Penthouses, LLC v. Mapp Construction, 2012 1242 (La. App. 1 Cir. April 26, 2013); 2013 La. App. Unpub. Lexis 261

This appeal involves three separate matters in which Southgate was the appellee. The appellant was Concrete Coatings; Southern Division Inc.; Stained Floor, LLC; and Southern States Plumbing, Inc. The underlying facts arise out of the development and construction of an apartment/rental complex. Southgate entered into a contract with Mapp Construction, Inc. to build the project. Due to the size of the project, Mapp retained a number of subcontractors. Southgate claimed a number of construction defects in the project. Mapp in turn filed a third-party action and brought in a number of subcontractors. The contract between Mapp and Southgate contained an American Arbitration Association (AAA) arbitration provision. At arbitration, an award was issued to Southgate, which it subsequently moved to confirm in court. Mapp and its subcontractors moved to vacate the award. The present appeal ensued.

The court found that all the parties were bound by contract and court order to resolve their contractual disputes through arbitration by AAA. The procedural rules of AAA, therefore, govern the fact finding and procedures. Two defendants, Concrete Coating and Stained Floors, were subject to the arbitration rules and the awards against them. The court found that Southern States was subject to misconduct and an improper exercise of power by the arbitrator; therefore, it found that the award had no legal validity and the award was vacated.

Practice Note: The Louisiana courts defer to the findings of AAA arbitration panels. Louisiana law allows vacating of an arbitration award only where it is procured by fraud, corruption, or misconduct, or where arbitrators exceed their power. In reviewing the arbitration award the court found that these four conditions had been met and therefore vacated the arbitration award against Southern States.

Colorado

Arbitrator's Findings and Conclusions Are Sufficient for Issue Preclusion in Construction Defect Claim

White River Village, LLP v. Fidelity and Deposit Company of Maryland v. Jonathan Reed & Associates, Inc., 2013 U.S. Dist. Lexis 41276 (Col. March 25, 2013)

White River Village as the owner in a construction project brought suit against Fidelity who issued the payment and performance bond for the general contractor, S&S Joint Venture. Fidelity counterclaimed and brought third party claims which sought to enforce the terms of the S&S Joint Venture contract agreement with White River and Reed & Associates. The Court ordered Fidelity's counterclaim and third party claim to arbitration but found White River claims were created by virtue of the performance bonds and are therefore not subject to arbitration. After arbitration, Fidelity brought a motion for summary judgment seeking to dismiss all White River Village claims based upon issue and claim preclusion, claiming that issues relevant to White River claims were resolved in arbitration. The Court analyzed each of White River Village's claims under the arbitration decision and to the extent the issues were resolved at arbitration awarded summary judgment.

Practice Note: The court took pains to discuss the standards for summary judgment, issue preclusion and claim preclusion. It noted the elements required to apply the doctrine; issues were identical to that adjudicated, the prior action was adjudicated on the merits, litigants were parties to the arbitration, and the parties had a full and fair opportunity to litigate issues in arbitration. The court found issue preclusion effectively barred these issues in the current litigation.

Minnesota

Two-Year Statute of Limitations Found to Have Lapsed Where Major Construction Defect Noted in Inspection Reports

Lee v. Gorham Builders, Inc., 2013 Minn. App. Unpub. Lexis 350 (April 22, 2013)

The Lees initiated the instant action in June 2011 alleging statutory warranty claims under Minn. Stat. §327A.02 and common law claims alleging defects to the home they purchased. As part of the purchasing process, they had the home inspected and an inspection report was issued in May 2009. The court found the Lees were time barred from bringing either cause of action because the report was sufficient to provide them

notice of “major construction defects” as defined by Minn. Stat. §327A.01, subd. 5 and required by Minn. Stat. §327A.02 as well as under the common law. Notably, the report found structural defects as well as moisture problems such as mold and wood rot. The Lees argued that repairs to their home by another contractor tolled the statute of limitations and that they relied upon the defendant to fix their home. The court denied the plaintiff’s common law and warranty claims on the grounds they were barred by the statute of limitations.

Practice Note: It appears that the Minnesota court was taking a stand by adhering to the two-year discovery rules found in the Minnesota statutes. The facts of this particular case, while draconian, show that the homeowner must carefully review inspection reports to determine if they are on notice of defective conditions, thus starting the clock for statute of limitations purposes.

South Carolina

Arbitration Claim Found Unenforceable Due to Clause’s Preclusion of Contractor Liability

Smith v. D.R. Horton, Inc., 2013 S.C. App. Lexis 125 (April 17, 2013)

The Smiths purchased a home built by Horton. The purchase agreement contained an arbitration clause. Alleging defects in the home, the Smiths filed the instant action against Horton and his subcontractor. Horton moved to compel arbitration. In denying Horton’s motion, the Circuit Court found: 1) The arbitration provision was unconscionable; 2) the purchase agreement was merged into the deed, which did not contain an arbitration provision; and 3) the arbitration provision failed to mention the SCUAA (South Carolina Uniform Arbitration Act). The Court of Appeals affirmed the lower court’s decision. They agreed with the lower court’s findings that the agreement as well as the arbitration provision was unconscionable because it was one-sided, forced the Smiths to waive a number of legal remedies and mandated arbitration. In finding the arbitration provision itself to be unconscionable, the court refused to sever it from the rest of the agreement, noting that it would be rewriting the contract rather than fulfilling the intent of the parties.

Practice Note: The arbitration clause in this case was clearly unenforceable due to the fact that it precluded contractor liability for any monetary damages. The court found that there was no consideration given in exchange for the rights of the purchasers, who were not of equal bargaining power. By refusing to sever the arbitration clause, the court noted that its validity was distinct from the substantive validity of the contract as a whole.

California

Appellate Court Will Not Disturb a Lower Court’s Finding When It Is Based on the Credibility of the Parties

Charles Virzi Construction Inc. v. G. Kevin Studer, 2013 Cal. App. Unpubl. Lexis 1584 (4th Dist. March 4, 2013)

Charles Virzi (hereinafter Charles) is a licensed general contractor and owner of Charles Virzi Construction, Inc., which also holds a general contracting license. Studer asked Charles to determine if a house he was considering to purchase could be cost-effectively remodeled. Studer subsequently purchased the house and hired Virzi Construction to remodel the house. Initially, the parties had a dispute over the type of agreement they would enter regarding the remodeling. Charles proposed a “cost-plus contract” while Studer wanted a “fixed-price contract.” They further disagreed on the contractor’s profit margin and allegedly agreed to “12 percent.” Charles provided a copy of Virzi Construction’s standard form contract, leaving the price blank, and Studer proposed a budget including a 10 percent contractor profit margin. At some point, Studer needed to submit the contract and budget to Wells Fargo for a loan. Since Studer was pressured for time, Charles signed the contract and allowed Studer to use the figure containing the 10 percent profit margin. Both Charles and Studer agreed to further work and filled out new contract documents with Charles including a 12 percent commission and Studer a 10 percent profit margin. Eventually, there was a breakdown in the relationship and Virzi Construction filed a mechanic’s lien.

Virzi Construction then sued Studer and Wells Fargo, asserting causes of action including breach of contract, conversion, foreclosure of mechanic’s lien, and declaratory relief. Virzi Construction claimed Studer requested extra work above and beyond the contract but failed to pay for it. Studer filed a cross complaint against Virzi Construction and Charles. He asserted causes of action for breach of contract, fraud, and negligence. He alleged Virzi Construction failed to timely complete the work and that it undertook work without request and without authorization. At trial, Virzi Construction called Charles as both its fact and expert witness. Charles testified the parties never agreed or discussed to a fixed-price contract. Further, he called various subcontractors to testify about the work. He also called an expert general contractor, expert electrician, and the city’s senior building inspector. Studer’s expert general contractor seemed to particularly move the court, especially his in-depth knowledge of the insufficiency of the work in comparison to the work actually performed. This was further supported by the senior building inspector’s testimony and the court’s own site visit. The trial court then entered an award for Studer.

At the appellate level, Charles and Virzi Construction were highly criticized by the court. The court initially noted they submitted an improper brief and felt their arguments were simply a regurgitation of the arguments below rather than an actual appellate brief. The court then walked through each of their arguments and determined that the trial court was correct in its conclusion. The Fourth Appellate District Court noted in each instance that Charles and Virzi Construction were arguing matters of credibility and the trial court simply found Studer and his witnesses more credible.

Practice Note: The court refused to retry this case on appeal. It noted that Virzi's appeal was misguided, relying on a rehearing of the evidence instead of analyzing the record.

Nevada

Statute of Limitations for Construction Defect Claims May Be Contractually Reduced

Holcomb Condominium Homeowners' Association Inc. v. Stewart Venture, LLC, 2013 Nev. Lexis 24; 129 Nev. Adv. Rep. 18 (April 4, 2013)

Holcomb Condominium is a community developed by Stewart Venture. Holcomb Condominium Homeowners' Association (HCHA) is the homeowners' association for Holcomb Condominium. Paul McKinzie, Luther David Bostrack, and Q & D Construction were involved in the development and construction of the condominium. Martha Allison represented both individual purchasers and Stewart Venture in the sale of the condominium during July and August 2002. In 2007, HCHA served a Notice of Construction Defect Claims pursuant to NRS 40.645. In 2009 HCHA filed a constructional defect complaint on behalf of itself and all Holcomb homeowners. The district court, relying on NRS 116.4116, found HCHA's claim to be time barred. The Supreme Court, in reviewing the lower court decision, found that the provision regarding the statute of limitations was not in a "separate instrument" as required by NRS 116.4116 since the arbitration agreement that contained the provision was attached to and incorporated into each unit's purchase contract.

Practice Note: Whether a party could contractually modify a statutory limitation was an issue of first impression for this Nevada court. However, the court noted that in other jurisdictions, it is well established that in absence of a statute to the contrary, a provision in a contract may limit the time to bring an action on the contract to a period less than that prescribed in statute.

Mandatory Arbitration Clause Found Sufficient to Compel Arbitration on FRCP 12(b)(6) Motion in Construction Defect Action

Greystone Nevada, LLC v. Anthem highlands Community Association, 2013 U.S. Dist. Lexis 60018 (Nev. April 25, 2013)

Anthem Highlands Community Association filed a Notice of Construction Defect as to Greystone Nevada and U.S. Home Corp. pursuant to NRS 116.3102(D). The notice stated Anthem, in its statutory representative capacity, was making a claim against Greystone for the installation of plumbing systems with defective yellow brass components. According to the complaint filed by Greystone, each of the individual homeowners had previously entered into an agreement with Greystone to arbitrate potential disputes. Anthem moved to dismiss due to lack of subject matter jurisdiction (lack of diversity) and Greystone filed an offensive FRCP 12(b)(6) motion seeking to force the homeowner to arbitrate. In granting Greystone's motion, the court noted that although FRCP 12(b)(6) motions generally only permit the court to examine the pleadings, where a pleading refers to an outside document, the court is allowed to consider the documents without converting the motion into one for summary judgment.

Practice Note: The Nevada courts continued to uphold arbitration provisions in construction defect cases. It appears that a plethora of these cases have arisen due to the increase in construction activity in Nevada, which has resulted in an exceedingly high number of construction claims.

Court Will Dismiss Unsupported Claims When Notice Filed Under NRS §40.645 Contains Insufficient Information

Richmond American Homes of Nevada, Inc. v. Stanton, 2013 U.S. Dist. Lexis 35402 (Nev. March 11, 2013)

Prior to suit, Stanton filed a Notice of Construction Defect pursuant to NRS §40.645 on behalf of himself and all homeowners who were similarly situated. Stanton resided in Sunrise Valley Estates and claimed each home was built with defective Aspen horizontal cased evaporator coil frames. In support of the notice, he retained an expert who examined some of the homes in the development from the exterior and observed signs of the rust and decay emanating from coil frames. However, he only actually inspected a single home from the interior to actually observe the defective unit. In response to the notice, Richmond filed a complaint seeking declaratory relief and specifically alleged the notice was insufficient to give notice as to all unnamed similarly situated homeowners. Stanton

eventually moved for summary judgment and Richmond moved for declaratory relief. The court denied the summary judgment motion and granted declaratory relief as to the unnamed “similarly situated owners,” but allowed the case to proceed as to the named defendants. In its discussion, the court specifically noted the insufficiency of the expert’s report and its failure to comport with the “reasonable threshold test.” The reasonable threshold test required the expert to confirm the defect in at least one home of each subset of homes included within the scope of the extrapolated notice. Here, the expert only examined and inspected the defect in one home out of the entire 316-home development. The court noted the single inspection was not a valid and representative sample sufficient to give notice for all similarly situated owners.

Practice Note: The court notes that the requirements for pre-litigation construction defect notices are strictly reviewed. Said notice must meet a reasonable threshold by describing the alleged defect and stating it in reasonable detail the location such that a contractor can have an opportunity to cure same. Representative samples must be used, considering the size and markings of subsets. Notice is not deemed reasonable unless the defect is confirmed to exist in more than one home in each subset.



*Editor’s Note: This article was originally published in **Mealy’s™ Litigation Report: Construction Defects** (Vol. 14, #11, December 2013). Permission to reprint this article was gratefully granted by Thomas F. Segalla, Ellen H. Greiper, and Matthew S. Lerner are partners and Suzin L. Raso is an associate in the Construction, General Liability, and Global Insurance Services Practice Groups of the law firm Goldberg Segalla. The firm has 11 offices in New York, New Jersey, Pennsylvania, Connecticut, and the United Kingdom. Any commentary or opinions do not reflect the opinions of Goldberg Segalla. Copyright © 2013 by Thomas F. Segalla, Ellen H. Greiper, Matthew S. Lerner, and Suzin L. Raso.*