Supreme Court Finds Insurance Coverage for Damage Caused by Faulty Construction

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In a recent case titled Cypress Point Condo. Ass'n v. Adria Towers, L.L.C., 226 N.J. 403 (2016), the Supreme Court of New Jersey examined whether rain water damage caused by a subcontractor's faulty workmanship constitutes "property damage" and an "occurrence" under a property developer's commercial general liability (CGL) insurance policy. This case was decided August 4, 2016.

Facts of the Case

This dispute arose out of the construction of Cypress Point, a condominium complex in Hoboken, NJ. Co-defendants Adria Towers, LLC, Metro Homes, LLC, and Commerce Construction Management, LLC (collectively, the developer) served as the project's developer and general contractor, and subcontractors carried out most of the work. During construction, the developer obtained four CGL insurance policies from Evanston Insurance Company, covering a four-year period, and three from Crum & Forster Specialty Insurance Company, covering a subsequent three-year period (collectively, the policies). The policies, which are modeled after the 1986 version of the standard form CGL policy promulgated by the Insurance Services Office, Inc. (ISO), provide coverage for "those sums that the insured becomes legally obligated to pay as damages because of 'bodily injury' or 'property damage' . . . caused by an 'occurrence' that takes place in the 'coverage territory' . . . [and] . . . occurs during the policy period."

Under the policies, "property damage" includes "[p]hysical injury to tangible property including all resulting loss of use of that property," while an "occurrence" is defined as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." The policies also contain an exclusion, for "Damage to Your Work" (the "your work" exclusion), which eliminates coverage for "'[p]roperty damage' to 'your work' arising out of it or any part of it and included in the 'products-completed operations hazard.'" Notably, this exclusion "does not apply if the damaged work or the work out of which the damage arises was performed on [the insured's] behalf by a subcontractor."

After completion of the complex, several residents began experiencing problems, such as roof leaks and water infiltration around windows in units and common areas. Plaintiff the Cypress Point Condominium Association (the Association) brought an action against the developer and several subcontractors, alleging faulty workmanship during construction and claiming various consequential damages. Ultimately, a question arose as to whether the Association's claims were covered by the insurers' CGL policies. Subsequently, the insurers moved for summary judgment, arguing, in part, that they were not liable because the subcontractors' faulty workmanship did not constitute an "occurrence" that caused "property damage" as defined by the policies. The trial court agreed and granted the motion.

In a published decision, Cypress Point Condominium Association, Inc. v. Adria Towers, L.L.C., 441 N.J. Super. 369, 373 (App. Div. 2015), the Appellate Division reversed, holding that, under the plain language of the CGL policies, the unintended and unexpected consequential damages caused by the subcontractors' faulty workmanship constituted "property damage" and an "occurrence." The NJ Supreme Court granted the insurers' petitions for certification. 223 N.J. 355 (2015).

The NJ Supreme Court's Analysis

The Supreme Court decided the merits of this dispute by determining whether the policies issued by the insurers to the developer provide coverage for the Association's claims of consequential water damage caused by the subcontractors' faulty workmanship. In answering this question the Court followed a three-step process. First, it examined the facts of the Association's claims to ascertain whether the policies provide an initial grant of coverage. If so, the second step considered whether any of the policies' exclusions preclude coverage. Finally, in step three, the Court determined whether an exception to a pertinent exclusion applies to restore coverage.

The policies at issue insure against liability for "property damage" that "is caused by an 'occurrence.'" "Property damage" is defined as: (a) Physical injury to tangible property including all resulting loss of use of that property. All such loss of use shall be deemed to occur at the time of the physical injury that caused it; or (b) Loss of use of tangible property that is not physically injured. All such loss of use shall be deemed to occur at the time of the "occurrence" that caused it.

Here, the Association alleged that water infiltration, occurring after the project was completed and control was turned over to the Association, caused mold growth and other damage to Cypress Point's completed common areas and individual units. Those post-construction consequential damages resulted in loss

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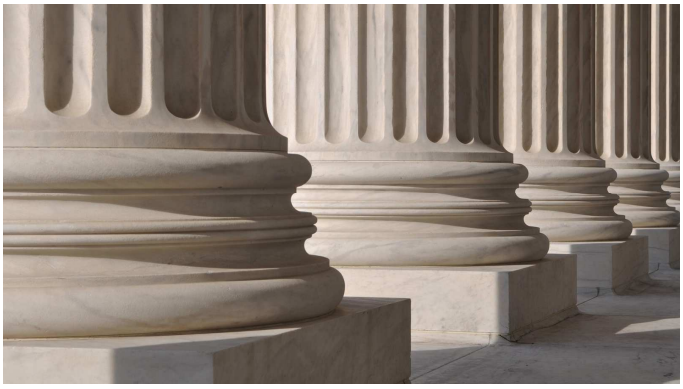
of use of the affected areas by Cypress Point residents and, the Supreme Court held, qualify as "[p]hysical injury to tangible property including all resulting loss of use of that property." Therefore, the consequential damages to Cypress Point were covered "property damage" under the terms of the policies.

Defining an "Accident"

Next, it was noted that the policies define an "occurrence" as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." The term "accident" is not defined in the policies. Thus, the Court stated it must first give meaning to the term "accident" in order to address the threshold question whether the subcontractors' faulty workmanship, and the damages that flowed therefrom, constitute an "occurrence" triggering an initial grant of coverage for the Association's claims. The Court said:

> When interpreting undefined terms within an insurance policy, we "resort to the general rule that the terms in an insurance policy should be interpreted in accordance with their plain and commonly-understood meaning." Morton Int'l v. Gen. Accident Ins. Co., 134 N.J. 1, 56, 629 A.2d 831 (1993) (citation omitted); Longobardi v. Chubb Ins. Co., 121 N.J. 530, 537, 582 A.2d 1257 (1990) ("[T]he words of an insurance policy should be given their ordinary meaning[.]"). This common-sense approach often begins with an examination of dictionary definitions.
>
> Merriam-Webster's dictionary defines "accident" as "an unforeseen and unplanned event or circumstance." Merriam-Webster's Collegiate Dictionary 1419 (11th ed. 2012); see also Black's Law Dictionary 18 (10th ed. 2014) (explaining that "[t]he word 'accident,' in accident policies, means an event which takes place without one's foresight or expectation. A result, though unexpected, is not an accident; the means or cause must be accidental."). A leading treatise on New Jersey insurance law tracks substantially the same language as the dictionary definition for "accident"...

The Supreme Court found that the term "accident" in the policies at issue encompasses unintended and unexpected harm caused by negligent conduct. The Court held that construction of the term "accident" as it relates to an "occurrence" in a CGL policy aligns with both the commonly accepted definitions of "accident" and the legal import given to the term by both this and other jurisdictions.



Applying its definition, the Court went on to determine whether the consequential water damage to the completed, nondefective portions of Cypress Point flowing from the subcontractors' poor workmanship was foreseeable:

> Here, no one claims that the subcontractors intentionally performed substandard work that led to the water damage. Rather, relying on Weedo, the insurers assert that damage to an insured's work caused by a subcontractor's faulty workmanship is foreseeable to the insured developer because damage to any portion of the completed project is the normal, predictable risk of doing business. Thus, in the insurers' view, a developer's failure to ensure that a subcontractor's work is sound results in a breach of contract, not a covered "accident" (or "occurrence") under the terms of the policies. We disagree.

The Supreme Court's Ruling

Under the Supreme Court's interpretation of the term "occurrence" in the policies, consequential harm caused by negligent work is an "accident." Therefore, because the result of the subcontractors' faulty workmanship here -- consequential water damage to the completed and nondefective portions of Cypress Point -- was an "accident," the Court held that it is an "occurrence" under the policies and is therefore covered so long as the other parameters set by the policies are met. Citing Weedo v. Stone-E-Brick, Inc., 81 N.J. 233, 249 (1979) (noting that CGL policies do "not cover an accident of faulty workmanship but rather faulty workmanship that causes an accident").

The judgment of the Appellate Division was affirmed and the matter was remanded back to the trial court for proceedings consistent with the Supreme Court's opinion.