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COZEN O'CONNOR

The Georgia Supreme Court Expands the Definition of "Occurrence" in Construction Defect Cases

On July 12, 2013, the Georgia Supreme Court expanded covered damages in construction defect cases by broadening the definition of "occurrence," yet left in place the insurer's right to deny coverage based upon the lack of "property damage" and the business risk exclusions. *Taylor Morrison Services, Inc. v. HDI-Gerling America Insurance Company*, No. S13Q0462, 2013 WL 3481555 (Ga. July 12, 2013). Specifically, the court held that damage to the insured's property or work may constitute an "occurrence." *Id.* at *3. This decision follows the court's March 2011 refusal to adopt Georgia federal decisions holding any damage flowing from an insured's intentional work does not constitute an "occurrence." *American Empire Surplus Lines Ins. Co. v. Hathaway Dev. Co., Inc.*, 288 Ga. 749, 752, 707 S.E.2d 369, 371-72 (2011). *Taylor Morrison* also expanded upon *Hathaway's* holding that "an occurrence can arise where faulty workmanship causes unforeseen or unexpected damage to other property" by including the insured's work and property in the definition of "occurrence." *Taylor Morrison*, 2013 WL 3481555 at *3.

The *Taylor Morrison* decision defines "damage to other property," holding it is not necessarily limited to a non-insured's damaged property, but may also include damage to the insured's work. *Taylor Morrison*, 2013 WL 3481555, at *3. In other words, "'an occurrence,' as the term of art is used in a standard CGL policy, does not require damage to the property or work of someone other than the insured." *Id.* However, the court specifically refused to examine how the "other property" definition applies when only the insured's work is damaged. *Id.* at *3, n.10. (refusing to address, in the context of an occurrence, the line of demarcation between the insured's defective and non-defective work that are a part of the same project). *Id.* at *3, n.10.

Taylor Morrison also held that fraud will typically not constitute an occurrence but that breach of warranty, depending upon the allegations asserted, could. *Id.* at *6-7. Whether a breach of warranty may constitute an occurrence depends upon whether the insured acted intentionally. *Id.* at *6. This holding is a departure from previous Georgia Court of Appeals cases seemingly blanket holdings that fraud, breach of contract, and breach of warranty do not constitute an occurrence. *Custom Planning & Dev., Inc. v. Am. Nat'l Fire Ins. Co.*, 270 Ga. App. 8, 10, 606 S.E.2d 39, 41 (2004).

Taylor Morrison was a construction defect case in which the general contractor and homebuilder, Taylor Morrison Services, Inc. (Taylor Morrison), was sued by 16 homeowners in a California class action lawsuit alleging damage to more than 400 homes. The plaintiffs accused Taylor Morrison of failing to properly construct the homes' concrete foundations, which eventually failed resulting in physical damage, such as cracks in floors and driveways and warped and buckling flooring. *Taylor Morrison*, 2013 WL 3481555, at *1. The class action plaintiffs asserted five causes of action, including fraud and breach of express and implied warranties. *Id.*

Taylor Morrison's insurer filed a declaratory judgment action in the U.S. District Court for the Northern District of Georgia seeking a declaration of non-coverage. The Northern District of Georgia granted summary judgment to the insurer finding that there was no occurrence because the only property damage at issue was damage to the insured's work, i.e., the homes Taylor Morrison constructed, not damage to other property. *Id.* at *2. Taylor Morrison appealed the district court's decision to the 11th Circuit Court of Appeals. *Id.*

The 11th Circuit, in turn, certified the following two questions to the Georgia Supreme Court:

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 itself.

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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 claims being defended not be for breach of contract, fraud or breach of warranty from the failure to disclose material information.

Id. at *1-2. The Georgia Supreme Court answered the first question in the negative, the second question as to fraud in the affirmative, and the second question as to breach of warranty in the negative. *Id.* at *1. The court declined to answer the second question as it related to breach of contract because a breach of contract claim was not alleged in the case before it. *Id.* at *1, 6, n.14.

An Occurrence Can Result from Damage to the Insured's Property or Work.

In discussing the first certified question, the Georgia Supreme Court acknowledged that *Hathaway* held faulty workmanship can be an occurrence where property of someone other than the insured is damaged by the insured's faulty work. *Id.* at *2. *Hathaway*, however, did not address whether faulty workmanship can amount to an occurrence where the damage results only to the insured's work. *Id.*

After examining the ordinary meaning of the word "accident," the court noted that accident "is not used usually and commonly to convey information about the nature or extent of injuries worked by [an unintended or unexpected] happening, much less the identity of the person whose interests are injured." *Id.* at *3. Thus, the court held that an occurrence did not require damage to the work or property of someone other than the insured. *Id.*

To support its ruling, the court noted that coverage, or lack thereof, under a CGL policy is not predicated solely on whether there has been an occurrence. *Id.* Rather, CGL policies contain several other provisions and exclusions that "have their own roles to play .... The sounder analytical approach is to avoid conflicting the several requirements of the insuring agreement and exclusions, and instead, to let each serve its proper purpose." *Id. citing* Evans & Berry, GA. GEN. LIABILITY INS., at § IV. J, p. 19 (2010); *Am. Family Mut. Ins. Co. v. Am. Girl, Inc.*, 268 Wis.2d 16, 673 N.W.2d 65, 76(III)(B)(ii) (Wis. 2004).

The court noted that its decision was not inconsistent with and did not overrule Georgia's precedent that "CGL coverage generally is intended to insure against liabilities to third parties for injury to property or person, but not mere liabilities for the repair or correction of the faulty workmanship of the insured." *Id.* This is because an insurer may preclude coverage for damage to the insured's work under other policy provisions such as a lack of property damage and the business risk exclusions. The court, in dicta, noted that property damage might be used to preclude coverage for damage to the insured's defective work itself because "'property damage,' as that term is used in a standard CGL policy, necessarily must refer to property that is not defective, and to damage beyond mere faulty workmanship." *Id.* In addition, the business risk exclusions can preclude coverage for the repair or correction of the insured's defective work. *Id. citing see e.g. SawHorse, Inc. v. S. Guar. Ins. Co.*, 269 Ga. App. 493, 496-497(1)(a), 604 S.E.2d 541 (2004).

The court also rejected the insurer's argument that its interpretation of occurrence was inconsistent with *SawHorse, Inc. v. Southern Guaranty Insurance Company*, 269 Ga. App. 493, 604 S.E.2d 541 (2004), *McDonald Construction Company v. Bituminous Casualty Corporation*, 279 Ga. App. 757, 632 S.E.2d 420 (2006), and *Custom Planning and Development v. American National Fire Insurance Company*, 270 Ga. App. 8, 606 S.E.2d 39 (2004). The court distinguished these cases finding that they do not specifically address whether an occurrence requires damage to something other than the insured's work. *Taylor Morrison*, 2013 WL 3481555, at *4.

Finally, the court noted that its construction of occurrence as not dependent upon the person whose property or work was damaged is consistent with other sister state's decisions, including Connecticut, South Carolina, the 4th Circuit (under both Virginia and Maryland law), Florida, Texas and Wisconsin. *Id.* at *5.

Fraud Is Most Likely Not an Occurrence but Breach of Warranty May Be an Occurrence.

In addressing the second certified question, the court determined that claims for fraud and breach of warranty do not in all instances fail to meet the definition of an "occurrence." *Id.* at 6-7. The

court declined to answer whether breach of contract constituted an occurrence. *Id.* at *1, n. 2, 6, n.14. The court found that where a theory of liability is "absolutely and necessarily" inconsistent with the notion of an accident, "a claim premised upon such a theory of liability could not possibly involve an 'occurrence.'" *Id.* at *6.

The court then held that fraud will usually not constitute an occurrence because to prove fraud in most states, the plaintiff must prove scienter and an intent to induce the plaintiff to act or refrain from acting. *Id.* Thus, where a cause of action requires the proof of intent, no occurrence will result. However, the court cautioned that it was not definitively holding fraud may never constitute an occurrence because intent may not be an element of fraud in some states. *Id.* Nonetheless, the court ultimately held that "in most cases, for an 'occurrence' to exist, the claims must be for something other than fraud." *Id.*

Next, the court held that in certain instances breach of warranties could constitute an occurrence. *Id.* at *7. The court acknowledged that the making of an express warranty is intentional, but held that its breach may not be. *Id.* Therefore, because a breach of a warranty does not necessarily require intentional conduct, it may be an occurrence where the breach was unintentional. *Id.*

As it did in the context of faulty workmanship, the court acknowledged that damages flowing from a breach of warranty may still be precluded from coverage due to the lack of property damage. *Id.* "[I]t generally will only be a breach of warranty of nondefective property from which coverage might arise, as liability for a breach of warranty of the defective property would not involve 'damages *because of*' 'property damage' to the nondefective property." *Id.* (emphasis in original). The court further noted that various policy exclusions might apply to a breach of warranty. *Id.*

Possible Implications for Insurers.

While insurers may no longer deny coverage for the entirety of any damage occurring to the insured's work or property under an occurrence theory, *Taylor Morrison* leaves open the possibility of precluding coverage for such damage under either the lack of property damage or the business risk exclusions.

Finally, insurers may continue to deny coverage in Georgia for claims of fraud as not constituting an occurrence, but must look very carefully at any claims of breach of warranty and breach of contract. Claims for breach of warranty, and likely breach of contract, may only be denied as not constituting an occurrence where the underlying complaint asserts only an intentional breach. Claimants will likely frame their allegations of breach of warranty and contract vaguely and without mention of intent so as to invoke coverage.

Nonetheless, where the damages in claims of breach of warranty or contract are limited to only damages to the insured's defective work, then such damages can likely be precluded as not constituting "property damage." Various policy exclusions may also be relevant.

Please feel free to contact Kenan Loomis or Jennifer Kennedy-Coggins in our Cozen O'Connor Atlanta office if you have any questions or need assistance with the Georgia issue. Contact Kenan at kloomis@cozen.com or 404-572-2066 and Jennifer at jkennedy-coggins@cozen.com or 404-572-2066.