CLM 2020 Construction Conference
September 30 – October 2
Chicago, Illinois

Hot Topics in CD Coverage – Florida and Beyond

I. DUTY TO DEFEND ISSUES

Contribution

Many (but not all) jurisdictions recognize a right of contribution for defense costs between co-insurers. Florida did not until the 2019 passage of Florida Statute §624.1055. It applies to a "claim, suit, or other action" initiated on or after 1/1/2020. Whether an amended complaint or supplemental claim relates back to a pre-2020 claim making the statute inapplicable is undecided. Under the statute, a defending insurer can seek an apportionment of costs provided that contribution may not be sought from any liability insurer for defense costs that are incurred before the liability insurer's receipt of notice of the claim, suit, or other action. It is thus imperative that all potential coverage is promptly identified.

Appointed defense counsel is a primary source. He/she can seek that information through discovery or statutory requests for insurance information. In apportioning costs, the Court can consider all "equitable factors as the court determines are appropriate". There are no rules. Possible considerations are the: 1) validity of insurer's position in not defending, *i.e*., "good faith" or "bad faith"; 2) strength of coverage defenses; 3) length of time defending insurer has been defending, costs incurred and the extent of its efforts to secure contribution; 4) relative indemnification exposure including "Time on Risk"; 5) respective coverage limits; and, 6) Insurer's costs in bringing the Contribution action. Unfortunately, there is no prevailing-party attorney fee provision. An insurer thus needs to balance its costs of pursuit with its potential recovery. Another consideration is the prospect of making "bad law". The pursuing insurer will need to prove that the non-defending insurer has a duty to defend whereas the non-defending insurer will defend by saying the pursuing insurer has no duty to defend.

Duty to Defend "Right to Repair" Proceedings

Most jurisdictions have "right to repair" statutes which require that a contractor be given notice of the defect, and the ability to repair it before suit can be filed. There is a split in authority over whether these proceedings are covered under a general liability policy. The two main questions addressed by the courts are (1) whether costs incurred in undertaking pre-suit remediation efforts qualify as damages that an insured is "legally obligated to pay" and, (2) whether a "right to repair" proceeding qualifies as a "suit". Irrespective, it is often beneficial for an insurer to be involved in the preliminary investigative process to gather factual information and expert opinion.

II. DUTY TO INDEMNIFY ISSUES

Finding Coverage through "Rip and Tear" - Access Costs

Insurers are increasingly having to pay for the repair of defective work where to do so is necessary to repair covered "property damage". This change greatly affects the value of cases for insurers. For example, without "rip and tear", a carrier would be responsible for paying only the costs necessary to repair damage caused by leaking stucco, but not to repair the stucco itself. Through "rip and tear", however, the insurer would be required to remove and replace the stucco as necessary to repair sheathing damage caused by the leaking stucco.

Finding Coverage through Prevention of Ongoing or Future Damage

An emerging trend is whether coverage can lie for the costs to prevent ongoing or future damage instead of simply repairing existing damage. There is a split in authority on this issue. At least one jurisdiction goes so far as to require coverage for costs solely to prevent imminent future damage.

Number of Occurrences

Courts are split on whether the defective work or the resulting "property damage" is the "Occurrence". The majority of courts follow the "cause" theory. Under it, there could be multiple occurrences within an insured's scope of work. For example, a roofer inadequately tarps a roof during its work and defectively installs tiles and mansards each causing separate damage. This would likely be three occurrences. Some courts draw a distinction where the same defective process is performed multiple times. For example, a painting contractor improperly applies paint on multiple dwellings within a residential development. This may be regarded as one occurrence.

Allocation

Some jurisdictions allow a straight "time on risk" analysis dividing the total damage by the number of days within each insurer's coverage period. This is an option where the damage cannot be quantified to a particular time - period. Other jurisdictions, however, determine an insurer's liability based solely on the "property damage" that actually happened during its period of coverage. This is the insured's burden of proof and expert opinion is critical.

III. INSURER CONCERNS

Inadequate Reservation of Rights Letters Resulting In Waiver or Estoppel

It is important that any agreement to defend be accompanied by an adequate Reservation of Rights letter. These letters must specifically advise the insured of the policy provisions, in relation to the facts, which may serve as limitations to coverage. Not doing so may result in a waiver/estoppel of coverage defenses. In some jurisdictions the ability to recover defense expenditures in the event the claim is not covered must be specifically reserved. It is also good practice to reserve the right to seek a declaration or adjudication of coverage. Non-compliance with statutes may also result in a waiver of certain defenses. For example, in Florida, the failure to comply with the Claim Administration Statute will result in a waiver of "Conditions" defenses. A variety of courts have further held that an insurer is affirmatively obligated to inform its insured of the need to secure a verdict form in the liability action allocating between covered and potentially un-covered damages. A failure to do so may result in an insurer paying for damages not covered under its policy and the judgment would therefore not be enforceable against it. A Reservation of Rights letter alone does not satisfy this requirement.

An Insured's Rejection of a Conditional Defense

In certain jurisdictions, an insured is not obligated to accept a defense under a reservation of rights. It can instead reject the reservation and demand an unconditional defense. It can also accept the defense and later reject it if the insurer materially changes its position. Upon proper rejection an insured may take control of its own defense and is not subject to a forfeiture of coverage based on the lack of cooperation. An insured's subsequent settlement of an action against it without the insurer's consent does not relieve the insurer of its obligation to pay under the policy. But, once the insured accepts the defense under a reservation, the insured is obligated to cooperate with the insurer and cannot settle without the insurer's consent.

In circumstances where a "conditional" defense is rejected, an insurer has several options. First, it can reach agreement with an insured on mutually agreeable counsel. In this case the insurer is only required to pay "reasonable" fees. Second, it can afford an unconditional defense and reserve its rights only on indemnity. Other possibilities may exist depending on the facts of the claim.

Perils of Refusing to Defend

There are several perils from refusing to defend. The first is losing the ability to control the defense and gather information. The second is a consent judgment. If a liability insurer is informed of an action against its insured and declines to defend, it is bound to a consent judgment between the claimant and the insured absent a showing of fraud or collusion. The amount of the judgment may exceed the policy limits. The insured, or its assignee, has the burden to prove: (1) that the insurer wrongfully refused to defend the insured; (2) that the insurer had an indemnification obligation under the policy; and, (3) that the settlement with the claimant was reasonable and in good faith. Insurers are also unable to raise any defenses to claims that they believe would have mitigated or voided the damages figured. The rationale being that if the insurer wanted to contest those issues, it should have defended its insured. The amount of a consent judgment cannot be arbitrary. There must be some relation to the potential exposure of the insured. Expert opinion may be necessary, for example, to identify damages that occurred during an insurer's period of coverage. Also, some jurisdictions require that a consent judgment allocate between covered and un-covered damages. The rationale here is that an insurer cannot be made to pay for un-covered damages and the burden of proof is on the insured.

IV. SUCCESSFUL MEDIATION AND SETTLEMENT

Resolving a construction defect case has many moving parts, particularly, liability and coverage issues. Dealing with coverage is in all respects a "mediation within a mediation" given multiple insurer involvement. Success requires the cooperation of the insured, defense counsel and the insurers. The insured and defense counsel are the primary sources of information needed by the insurer to value the case. The insurer must do its "homework" in advance and come prepared to the mediation. By this point, defense counsel and/or the insured should have provided information on all available coverage. The insurers should confer in advance and see if some type of allocation can be agreed-upon. Conversations with multiple mediators have shown common traits necessary to an efficient and successful mediation. These are: 1) all potentially involved insurers must have been placed on notice. This must happen at the earliest possible opportunity; 2) know which insurers are participating and which are not. It is important to reach an agreement with the implicated insurers, particularly those which are

defending, that all insurers who should participate will participate. If it is known that some insurers will not participate, agreement must be reached among the participating insurers on if and how settlement can be achieved without them; 3) everybody must be educated and committed to the process. Insurers are increasingly unwilling to "pay and chase" and an unprepared insurer could block an otherwise obtainable settlement; 4) provide written demands in advance of the mediation. Mediation should not occur until the claimant has a realistic picture of its damages claim as well as the availability of coverage and outstanding coverage issues. Neither the parties nor their insurers can adequately analyze exposure without an understanding of their respective expectations. Claimants should not wait until the day before or the day of the mediation to set forth their demands; 5) resolve insurer allocation issues in advance. While it is sometimes possible for insurers to resolve these issues among themselves, that is uncommon. More often, the mediator facilitates the dialogue and sometimes the insurers participate in a "pre-mediation" insurance mediation. Counsel should not hesitate to get the mediator involved in the insurance aspect of the case prior to the formal mediation session; and, 6) educate the mediator on the insurance issues before the mediation. Often there will be insufficient time for the mediator to become fully versed on insurance issues if they have not already been explained in prior submissions. Provide this information sufficiently in advance of the mediation so that the mediator can map a strategy and perhaps begin discussing the issues with the participating insurers.

V. COVID-19 ISSUES

First Party/Builders Risk (including business income and rental loss)

Coverage requires direct physical loss of or damage to covered property. Whether a facility's exposure to COVID-19 qualifies depends on the jurisdiction. Some jurisdictions find that the loss of use qualifies as "direct physical loss". Other jurisdictions find that contaminants which dissipate or can be cleaned do not qualify as physical damage to property. A governmental closure order alone would likely not qualify.

Third-Party Liability

Coverage grant requires "property damage" or "bodily injury" caused by an "Occurrence". There are typically two components to "Property Damage": 1) physical injury to tangible property (including resulting loss of use); and, 2) loss of use of tangible property that is not physically injured. COVID-19 may therefore qualify as "property damage". The preliminary issue, however, is whether contraction of or exposure to COVID-19 qualifies as an "Occurrence" in the first place.

Potential Exclusions: Virus Exclusion; Communicable Disease Exclusion; Pollution Exclusion, Ordinance Or Law Exclusion; Consequential Loss Exclusion; Loss of Use Exclusion; Loss of Market Exclusion; Acts or Decisions Exclusion; and, common "business risk" exclusions.