2020 Construction Conference
September 29 – October 1

Inventive Policyholder & Plaintiff Counsel:
How to Deal with Novel Efforts to Create Coverage

I. What We'll Discuss Today . . .

This session will address a variety of inventive policy arguments espoused by policyholder and plaintiff counsel in an effort to make their own rules and create coverage, as well as provide strategies for responding to these arguments in the ever-changing construction defect litigation arena.

By way of example:

A. Policyholder counsel have recently seized on an isolated part of the *Montrose* language in the insuring agreement to argue that insurers are forced to cover damage taking place after the expiration of the relevant policy period.

B. Policyholder and plaintiff counsel have attempted to create multiple occurrences to access aggregate limits by claiming that negligent construction constitutes one occurrence and negligent misrepresentations/communications in the turnover of the construction project constitute another occurrence, when the damage is plainly a single continuing injury.

Oftentimes, these arguments are made with the added threat of bad faith failure to investigate or settle looming in the background. Such arguments flout the language and intent of CGL policies and attempt to skirt established case law. It is incumbent upon coverage counsel to be prepared to counter these creative arguments with reference to historical treatment of policy language, the intent and genesis of the applicable policy language, and, when possible, contrary case law across the country rejecting these creative approaches.

II. Creative Arguments Made by Policyholder & Plaintiff Counsel – How To Combat Them

A. Policyholder Attempts to Use *Montrose* Language to Force Triggered Policies to Cover Subsequent Damage

i. History of the *Montrose* Language

In 1995, the California Supreme Court in *Montrose Chem. Corp. v. Admiral Ins. Co.,* 10 Cal. 4th 645 (1995) permitted a party to purchase a liability insurance policy to cover property damage that the insured knew existed at the time of the purchase, *so long as the insured's liability for such property damage was still contingent and not a certainty.*

The insurance industry was dissatisfied with the *Montrose* ruling granting coverage for what it considered to be a known loss. As a result, the Insurance Services Office ("ISO") introduced an endorsement in 1999 (colloquially called *Montrose* language) that amended the insuring agreement which qualifies the requirement that "bodily injury or property damage" must occur during the policy period, such that the policy on the risk at the time the insured first knew of "bodily injury" or "property damage" becomes the last policy that can be triggered. This was ISO's attempt at trying to establish an end date to continuous trigger from progressive damage/injury. *See* Craig F. Stanovich, *The Montrose Endorsement – 15 Years Later* (September 2014), https://www.irmi.com/articles/expert-commentary/the-montrose-endorsement-15-years-later.

ii. Sample ISO Form *Montrose* Language From CGL 00 01 10 01

> **c.** "Bodily injury" or "property damage" which occurs during the policy period and was not, prior to the policy period, known to have occurred by any insured listed under Paragraph **1.** of Section **II** – Who Is An Insured or any "employee" authorized by you to give or receive notice of an "occurrence" or claim, includes any continuation, change or resumption of that "bodily injury" or "property damage" after the end of the policy period.

This language has prevented policies from covering continuous injury after the period in which the insured learned of the damage. However, in instances where the damages were unknown to the insured during the period, CGL policies typically may then cover the damage, but only with respect to the damage taking place during the period.

iii. Policyholders in Construction Defect Cases Attempt to Argue That Subsection c. Extends Coverage Past the End of a Given Policy Period

Policyholders now attempt to argue a new interpretation of section 1(c) *Montrose* language, which states that, if there is damage during the period, which was not previously known to the insured, then such damages "include any continuation, change or resumption" after the end of the policy period. Policyholders seize on this language to argue that, once a policy is triggered, this provision forces each triggered policy to cover subsequent damage—even after the policy period ends.

Real World Example: At mediation, in a construction defect litigation involving a townhome complex, policyholder counsel argued that an insurer on the risk for the first two policy periods of an 8-year exposure would be on the risk for all 8 years, the following insurer (who also had two policy periods) would be on the risk for 6 years, and so on.

Policyholder counsel relied on *Twin City Fire Insurance Co. v. American Casualty Co.,* No. 14-cv-02401, 2016 WL 9115352 to support its position. *Twin City* involved a dispute between two insurers regarding the proper allocation of defense and indemnity costs of their mutual insured arising of an underlying construction defect case that alleged ongoing and continuing property damage. One insurer – Twin City (who insured the policyholder at the end of the total period of coverage) – argued that the Montrose language extends coverage to property damage occurring after the expiration of the policy period. (Thus, the first insurer's time on the risk is the full coverage period, the second insurer is the date of inception of its policy until the end of the coverage period and so on). The United States District Court for the District of Colorado held that the *Montrose* language at subsection c "extends [insurer's] coverage to the continuation of the property damage after the policy period. **Therefore, its time-on-the-risk is the entire coverage period**."

iv. Insurers Can Respond with Reference to the Genesis and Intent of the *Montrose* Language as Explained in Case Law

Insurers responded that the District of Colorado's interpretation seemingly turns the language of the insuring agreement, which requires "bodily injury" or "property damage" to occur during the policy period, on its head. *See Crossman Cmties. of N.C. v. Harleysville Mut. Ins. Co.,* 395 S.C. 40, 53, 717 S.E.2d 589 (2011) (a policy only covers "property damage" that actually occurs within the policy period); *Great American Lloyds Ins. Co. v. Vines-Herrin Custom Homes, LLC,* 596 S.W.3d 370 (Tex. Ct. App. 2020) (same); *Axis Surplus Ins. Co. v. Contravest Const. Co.,* 921 F. Supp.2d 1338, 1347 (M.D. Fla. 2012) (same); *Century Indem. Co. v. Hearrean,* 98 Cal. App. 4th 734, 741, 120 Cal. Rptr. 2d 66 (Cal. Ct. App. 2002) (same).

Additionally, other courts have rejected this interpretation of section 1.c.:

> The unambiguous and clear meaning of Subsection c is to provide liability coverage for "bodily injury" or "property damage" which occurs during the policy period, including any continuation, change, or resumption of those damages after the end of the policy period, *unless* [the insured] knew of that bodily injury or property damage prior to the policy period. Nowhere does Subsection c. purport to expand coverage to include bodily injury or property damage which occurred prior to the policy period, but was unknown to [the insured] until the policy period began.

Essex Ins. Co. v Willco Enterprises LLC, No. 11-CV-247.

Finally, insurers can rely on the intent and nature of Montrose language which was ISO's attempt at trying to establish an end date to continuous trigger from progressive damage/injury. No part of the Montrose language attempted to amend, change or otherwise effect the fundamental requirement that "bodily injury or property damage" must occur during the policy period.

B. Policyholder Attempts to Create Multiple Occurrences from a Single Construction Defect Injury

i. Number of Occurrences Analyses Across the Country

Courts faced with determining the number of occurrences generally apply either a "cause" test or an "effects" test to resolve the number of occurrences issue.

The "cause" test focuses upon the underlying circumstances, which resulted in harm or injury, rather than the number of persons or properties actually injured or damaged. *See Lennar Corp. v. Great American Ins. Co.,* 200 S.W.3d 651, 683 (Tex. Ct. App. 2006) (policyholder was exposed to a new and separate liability for each home upon which its synthetic stucco product was applied); *Mid-Continent Cas. Co. v. Basdeo,* 742 F. Supp.2d 1293, 1347-48 (S.D. Fla. 2010) (applying the "cause" test to determine that three occurrences transpired because each category of damages "resulted from a separate force, distinguishable in time and space."); *Safeco Ins. Co. of America v. Fireman's Fund Ins. Co.,* 148 Cal. App. 4th 620, 633-34 (Cal. Ct. App. 2007) (adopting the "cause" test to hold that damage to downhill property caused by a landslide constituted one "occurrence").

By contrast, the "effects" test focuses primarily on the resulting harm, rather than on the proximate cause of those harms. Therefore, courts applying the "effects" test will look to the total number of persons injured or properties damaged to determine the number of occurrences. *See Lombard v. Sewage and Water Bd. of New Orleand,* 284 So. 2d 905 (La. 1973) (applying the "effects" test to hold there were multiple occurrence where 119 plaintiffs were damaged as a result of the construction of an underground drainage canal);

Other states, such as Oregon, refuse to adopt any particular test, instead opting to analyze the specific policy language at issue. *Interstate Fire & Cas. Co. v. Archdiocese of Portland,* 318 Or. 110, 13 (1993)) "[I]t is the language and structure of the particular insurance policies at issue here, not the general tort law concepts suggested by the certified questions, that govern." *Id.*; *see also California Ins. Co. v. Stimson Lumber Co.,* No. 01-514, 2005 WL 627624 at *7 (D. Or., Mar. 17, 2005) (numerous claims against an insured for damage caused by the failure of its siding constituted one occurrence per policy period).

ii. Policyholders in Construction Defect Cases Attempt to Argue that Negligent Construction is One Occurrence and Negligent Representations in the Turnover of the Building is Another Occurrence

In an effort to maximize insurance recovery, policyholders with aggregate limits greater than their per occurrence limits seek to increase the number of occurrences arising from claims of defective construction.

Real World Example: Policyholder counsel in a construction defect suit with respect to a condominium complex have attempted to create multiple occurrences by claiming that negligent construction constitutes one occurrence and negligent misrepresentations/communications in the turnover of the construction project constitute another occurrence. Policyholder's two-occurrence argument was motivated by a desire to maximize insurance recovery by attempting to trigger the $2M Products-Completed Operations limit in the policy, rather than the $1M each Occurrence limit. [Though we will not address today, policyholder also argued that its defense costs were paid outside of limits – contrary to the terms of the wrap policy and also attempted to create an excess policy limits exposure by accusing the insurer of bad faith].

iii. Insurers Can Defeat Arguments to Maximize Coverage through a Two Occurrence Theory by Reference to the Facts and Simple Logic

Insurer responded to policyholder's creative "two occurrence" theory by reference to the facts of the litigation – the supposed second occurrence of negligent misrepresentations in the turnover of the condo building to unit owners did not cause any damage whatsoever, the damage to the condo building was caused by the faulty construction. Regardless of the application of the "cause" or "effects" test – it is hard to conceptualize a state in which policyholder's two occurrence outcome could be supported by the case law.

Indeed, the fact that an underlying plaintiff asserts multiple theories of liability does not mean that the faulty workmanship can be considered multiple occurrences. *Farmers Ins. Grp. of Oregon v. Nelsen*, 78 Or. App. 213, 217, 715 P.2d 492, 494 (1986) *citing*

Bankert by Habush v. Threshermen's Mut. Ins. Co., 110 Wis. 2d 469, 478, 329 N.W.2d 150, 154 (1983) ("the insurance policy…does not insure against theories of liability. It insures against 'occurrences' which cause injuries").

Moreover, underlying plaintiff would have to prove that the policyholder misrepresented the nature of the condo building construction in order to succeed upon this theory of liability. Thus, such supposed second occurrence would not be covered because most policies exclude from the definition of "occurrence" injury expected or intended by the insured. In order to prove its claim, underlying plaintiff must demonstrate that policyholder either knew about the defects or intended for the plaintiff to rely on the representations, and thus were not an unintended accident. *See Cincinnati Ins. Co. v. Anders*, 2003-Ohio-3048, ¶ 15, 99 Ohio St. 3d 156, 158, 789 N.E.2d 1094, 1097; *Allstate Ins. Co. v. Lane*, 345 Ill. App. 3d 547, 551, 803 N.E.2d 102, 106 (2003)