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A Defective Precedent for 'Defective Work' in Insurance Coverage

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Litigation following a construction project is as common as a coffee shop in Manhattan. The availability of insurance coverage can be pivotal to the defense and resolution of such lawsuits. However, insurance coverage for construction defects litigation in New York has long been clouded by misunderstandings surrounding the First Department's 1994 decision in *George A. Fuller v. U.S. Fidelity & Guaranty,* 200 A.D.2d 255 (1st Dep't 1994) leave to appeal denied sub nom. *Fuller v. U.S. Fidelity & Guaranty,* 84 N.Y.2d 806 (1994). Insurance companies often cite this case as a basis to deny coverage when there are underlying allegations concerning defective work—a common occurrence following a construction project. That decision has been misconstrued because of old policy language no longer used in the industry. The decision should be re-examined and not so readily cited as a basis to deny coverage.

When a lawsuit alleges property damage and defective construction, the general contractor seeks insurance coverage under commercial general liability policies. Coverage is sought from both its own insurance companies and from the subcontractors' insurance companies, because the subcontractors generally have agreed to name the general

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contractor as an additional insured. A standard exclusion in the CGL policy applies to "Damage To Your Work," and insurance companies sometimes contend that the entirety of the construction project was the general contractor's "work," and thus any damages sought for resulting property damage are excluded because they seek repairs for defective work. The *George A. Fuller* decision and its progeny are often cited for support of this argument.

The 'George A. Fuller' Decision

George A. Fuller involved an underlying lawsuit by an owner of a newly constructed building against a construction manager/general contractor. The owner alleged damages based on construction

defects and inadequate supervision of work by subcontractors in the form of intentional cost-cutting measures that resulted in property damage, or negligent acts affecting the owner's economic interests. *George A. Fuller*, 200 A.D. at 257-58. In the ensuing coverage litigation, the First Department reversed the Supreme Court's holding that coverage was owed because the property damage was the result of an accident. The First Department determined the defective construction was not an occurrence, and stated that the "policy was never intended to provide contractual indemnification for economic loss to a contracting party because the work product contracted for is defectively produced."

On that basis, the court determined that there was no CGL coverage for the claims related to an alleged failure of the general contractor to meet its contractual obligations. In other words, the court held that the property damage itself was to the work performed by the contractor (even if actually performed by a subcontractor), and to afford coverage would impermissibly convert the insurance into a "surety" for the contractor's work. The First Department also held that policy exclusions (j)(5) and (j)(6), "which except from coverage damage to the insured's work product," applied to preclude coverage.

Although *George A. Fuller* remains good law, it has been misconstrued, and has been used in overbroad ways that are not in accord with contemporary CGL policy language. The current language used in a CGL policy makes clear that a general contractor can receive coverage for property damage, even damage resulting from construction defects.

CGL Policy Language and the 'Your Work' Exclusion

Coverage Part A of the standard CGL insurance policy states the insurance company "will pay those sums that the insured becomes legally obligated to pay as damages because of 'bodily injury' or 'property damage' to which this insurance applies." The CGL policy includes an exclusion to Coverage Part A for "Damage To Your Work" (the "Your Work" exclusion). That exclusion (typically listed as exclusion l.) excludes coverage for "'property damage' to 'your work' arising out of it or any part of it and included in the 'products-completed operations hazard'." "Your work" is defined in pertinent part as "work or operations performed by you or on your behalf; and materials, parts or equipment furnished in connection with such work or operations." The "products-completed operations hazard" is a defined term and includes property damage "occurring away from premises you own or rent and arising out of … 'your work.'" It applies, among other things, "when all of the work called for in your contract has been completed"—in other words, when the job is done.

Notably, the "Your Work" exclusion now includes an exception that states: "This exclusion does not apply if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor."

'George A. Fuller' Should be Re-Examined

The First Department did not discuss the "Your Work" exclusion in *George A. Fuller*, even though the building at issue was completed. See *George A. Fuller,* 200 A.D.2d at 258, 261 (referring to the building as "constructed"). Instead, the First Department relied upon case law that pre-dated the 1986 revision to the standard ISO CGL policy form in support of its decision finding no coverage. The 1986 revision to the CGL policy form is significant, as it first included the subcontractor exception to the "Your Work" exclusion.

Prior to the 1986 revisions, it had been found that the standard-form CGL policy "precluded coverage for damage to construction projects caused by subcontractors." *Black & Veatch Corp. v. Aspen Insurance (UK),* 882 F.3d 952, 971 (10th Cir. 2018) (citing Christopher C. French, Revisiting Construction Defects as "Occurrences" Under CGL Insurance Policies, 19 U. Pa. J. Bus. L. 101, 107

(2016)). The subcontractor exception specifically was added to CGL policies following agreement between construction contractors and insurance companies that CGL policies "should cover defective construction claims 'so long as the allegedly defective work had been performed by a subcontractor rather than the policyholder itself,'" (quoting *French,* 19 U. Pa. J. Bus. L. at 108. Thus, coverage should exist under the "Your Work" exclusion and its exception, as seen in policies after 1986, when there is property damage resulting from the work of a subcontractor on a completed building.

Additionally, in *George A. Fuller* the First Department only discussed the policy exclusions (j)(5) and (j)(6). Those exclusions, which use the same language today, state they exclude coverage for the following:

That particular part of real property on which you or any contractors or subcontractors working directly or indirectly on your behalf are performing operations, if the "property damage" arises out of those operations; or

That particular part of any property that must be restored, repaired or replaced because "your work" was incorrectly performed on it.

Exclusion (j)(5) is, by its plain language, limited to property damage that occurs to the part of real property being worked on at the exact time operations are being performed. Exclusion (j)(6) in turn is limited in the CGL policy as not applying "to 'property damage' included in the 'products-completed operations hazard'." The purpose behind these exclusions is consistent with the First Department's observations that a CGL policy is not to be treated as a "surety" agreement for the performance of a construction contract. See *George A. Fuller,* 200 A.D.2d at 260. When work is ongoing at a job site and property damage occurs to the specific location of the work being performed, that risk remains with the ongoing construction project. CGL coverage may not be required to pay the costs associated with addressing such property damage during ongoing construction.

But there is little question that the "Your Work" exclusion and the subcontractor exception, as they are now written, apply for completed operations. The First Department did not consider them in *George A. Fuller*. Subsequent case law has relied upon *George A. Fuller* without due consideration to the particular policy language at issue. See, e.g., *Pavarini Construction v. Continental Insurance,* 304 A.D.2d 501, (1st Dep't 2003). The language of the insurance policy at issue should be construed according to common speech and the policyholder's reasonable expectation, with ambiguities construed against the insurance company and no terms rendered as surplusage. See *In re Viking Pump,* 27 N.Y.3d 244, 257 (2016). Reliance on *George A. Fuller* has led to results contrary to the plain language of today's standard CGL policy, and continues to wrongly deny contractors the coverage they are owed.

George A. Fuller should be re-examined and New York should clarify that, like a majority of states, CGL coverage exists when property damage results from an occurrence caused by defective construction, especially when performed for a general contractor by a subcontractor. See *Black & Veatch,* 882 F.3d at 966 (discussing majority trend by states, including the New Jersey decision *Cypress Point Condominium Association v. Adria Towers,* 226 N.J. 403 (2016)).

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