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Insurance Coverage ALERT

The Amazing Disappearing "Accident" Requirement in Occurrence-Based Liability Policies

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Scottsdale Insurance Company v. R.I. Pools, Inc., 2013 WL 1150217 (2nd Cir. 2013)

In the recent Second Circuit case of *Scottsdale Insurance Company v. R.I. Pools, Inc.,* 2013 WL 1150217 (2nd Cir. 2013), the court concluded that faulty workmanship claims constitute an "occurrence" under a commercial general liability (CGL) policy where there is an exception in the policy's "your work" exclusion for work performed by a subcontractor.

The insured installed swimming pools for residential customers and it employed outside companies to supply and shoot concrete into the ground. Three years after installing pools for 19 customers, the insured received complaints that their pool's concrete was flaking, cracking and deteriorating. The pools were losing water and, in some instances, were unusable.

The insured's general liability carrier initially provided the insured with a defense, but then filed a lawsuit seeking a declaration that it had no obligation to provide coverage for the faulty workmanship claims. The district court granted summary judgment in favor of the insurer, concluding that defects in the insured's workmanship could not be considered an "accident" within the policy's definition of "occurrence." The insurer was also awarded reimbursement of the defense costs it had paid.

On appeal, the U.S. Court of Appeals for the Second Circuit reversed, noting that the district court's analysis essentially read the subcontractor exception to the "your work" exclusion out of the policies. The policies, which defined the term "occurrence" as an "accident," incorporated the following "your work" exclusion:

> This insurance does not apply to:
>
> ...
>
> "Property damage" to "your work" arising out of it or any part of it....
>
> 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 sub-contractor.

Relying on the subcontractor exception to the "your work" exclusion, the court observed that "defects in the insured's own work in some circumstances are covered." The court therefore concluded that the

policies at issue “unmistakably include defects in the insured’s own work within the category of an ‘occurrence.’”

In reaching its decision, the court distinguished its previous ruling in *Jakobson Shipyard, Inc. v. Aetna Casualty and Surety Company,* 961 S.W.2d 387 (1992), where the court held that faulty workmanship was not an “accident.” The court observed that the *Jakobson* policy did not contain the additional subcontractor clauses found in the policies involved in this case.

The court noted that the fact that the defects in the insured’s work constitute an “occurrence” does not mean they are covered under the policies. According to the court, there is a further hurdle in the form of the express exclusion for the insured’s work, subject to the exception when the work was performed by a subcontractor. The court observed that the issue of whether or not the insured’s liability for defects in its own work is covered turns on whether or not the subcontractor exception to the “your work” exclusion applies.

Practice Note

Following *Scottsdale,* a CGL accident-based “occurrence” policy that incorporates a “your work” exclusion with a subcontractor exception will provide coverage for faulty workmanship and defect claims where the work was done by a subcontractor. Although courts should still enforce the exclusion for the insured’s own work, damages from defects in the insured’s work performed by a subcontractor will be covered. As a result of *Scottsdale*, insurers should carefully review their policy language and, in particular, the language of the “your work” exclusion before denying coverage based on the “occurrence” requirement in the insuring agreement.
