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ALERT

Deciphering The Undecipherable: Insurance Coverage For Construction Defects

By Robert E. Frankel

A common problem for construction trades in construction defect litigation is a lack of comprehension about the nature and cause of the defects being alleged. This problem arises because lawyers are asked to draft complaints before all of the expert investigation has been completed. To ensure recovery for their clients, who have experienced some property damage as a result of defective construction, lawyers will usually join everyone in the chain of distribution of the project. The complaint is often written so generally and incomprehensibly that the only thing understood is that the project was defectively constructed and, as a result, the owner needs to make repairs.

For those in the chain of distribution, the vagueness of the underlying complaint creates confusion in terms of whether there is insurance coverage. This confusion becomes exacerbated by the insurance industry's failure to fulfill promises to policyholders. To wit, insurance companies often improperly deny coverage on the basis that the complaint is incomprehensible and therefore the actual claim has not yet been defined. Alternatively, insurance companies may deny coverage under the assertion that the claim averred is wholly within an exclusion, quite often the "own work" exclusion, which prevents policyholders from insuring against defects in their own work.

For example, imagine that a buyer of new construction discovers that some of his framing has rotted and suspects that the rot resulted from a recently discovered leak, which could have been caused by a number of defects, including a defectively constructed roof. The buyer quickly hires a lawyer. Before having the property investigated, the lawyer sues everyone in the chain of distribution, drafting and serving an undecipherable complaint that alleges extensive property damage caused by defective construction. Is the roofer entitled to insurance coverage in such a suit?

Liability Insurance Policies generally require insurance companies both to defend and to indemnify their policyholders in claims arising under the policy. Under most states' laws, an insurance company's duty to defend is independent of, and broader than, the duty to indemnify. The following rules establish the breadth of this duty.

- First, the duty to defend is normally determined solely from the allegations made against the policyholder in the underlying complaint, and actual facts discovered are generally irrelevant to this determination.
- Second, an insurance company owes its policyholder a duty to defend whenever the liability alleged in the underlying action poten-

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tially or even arguably comes within the scope of the policy coverage. Thus, if there is some doubt as to whether a claim that is within the policy's coverage has been pleaded, the insurer must accept the defense of the claim.

- Third, an insurance company can avoid its defense obligation only by establishing that: (a) the underlying action complaint solely and exclusively describes a non-covered event; and (b) there is no factual or legal basis under which the insurance company might eventually be held liable.
- Fourth, once the duty to defend attaches, the insurance company cannot pick and choose which claims to defend, but, instead, must defend all claims.
- Fifth, any doubts regarding the allegations of the underlying action or the scope of coverage are construed in favor of finding that there is a duty to defend.

Applying these rules to the undecipherable complaint problem yields the inescapable conclusion that the roofer in the above example is, at a minimum, entitled to a defense. In particular, although resolution of the duty to indemnify is generally premature prior to elucidation of facts establishing the nature and cause of the construction defect and the property damage or bodily injury resulting therefrom, the duty to defend is determined solely from a review of the undecipherable complaint. Moreover, because an undecipherable complaint does not clearly establish what happened, the claim is potentially covered. Furthermore, because the complaint is ambiguous, it is too early to discern whether the property damage averred is the roofer's "own work" (which may be excluded) or others' "work" (which is covered). Hence, the roofer is right to expect his insurance company to defend him unless and until the claims asserted against him can be confined to those that are wholly not covered.

Policyholders like the roofer can best protect themselves by taking the time to become educated about insurance coverage, buying insurance from insurance companies with good claims handling records, and refusing to accept "no" in response to their demands for coverage. ■

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