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SC Builder Coverage Law Lives On, But Insurers Get Reprieve

By **Bibeka Shrestha**

Law360, New York (November 28, 2012, 9:32 PM ET) -- Though South Carolina's high court last week upheld a state law declaring that general liability policies cover property damage and injuries from faulty construction, it also ruled the statute cannot apply retroactively, providing some relief to insurers fearing the legislature had rewritten their contracts.

The issue of whether commercial general liability policies cover construction defect claims is hotly contested around the country. Like Arkansas, Colorado and Hawaii, South Carolina has passed legislation to boost CGL coverage for the construction industry.

Although the state's high court backed the law, the ruling did have a bright spot for insurers, according to Laura Foggan, a Wiley Rein LLP attorney who represented amicus curiae American Insurance Association in the case. The decision reinforces that state legislatures cannot introduce different language to policies than what has already been negotiated, she said.

"The way it was crafted provided a new definition of occurrence that would be written into the policy language," Foggan said about the South Carolina law. "The legislature can't just change their terms without providing an insurer opportunity to decide whether it wants to underwrite a particular risk."

South Carolina's Act 26 established that commercial general liability policies have a definition of "occurrence" that includes property damage or injuries from faulty workmanship, just months after the South Carolina Supreme Court decided that damage to condominiums was not covered by a CGL policy because it was not accidental and, therefore, not an occurrence.

Harleysville Mutual Insurance Co. couldn't persuade the court that the legislature had violated the separation of power doctrine or that lawmakers had deprived insurers of equal protection under the law. But the majority of high court judges did agree with Harleysville that the law could not apply to policies issued before May 2011, when Act 26 went into effect, concluding that the legislation had fundamentally changed existing insurance contracts.

But judges who dissented on the issue as well as some policyholder attorneys argued that South Carolina's legislature was only clarifying existing law.

Scott Turner, a policyholder attorney at Anderson Kill & Olick PC, said it was clear that policy drafters at Insurance Services Office — which develops standardized insurance policy language — intended for most property damage claims from faulty workmanship to count as an occurrence. Turner said the South Carolina Supreme Court had been wrong to rule otherwise.

"It did not even reflect the intention of the policy drafters and certainly not the reasonable interpretation and expectation of policyholders," Turner said. "It's frustrating, then, that the statute's corrective action to right a wrong didn't immediately apply to new and outstanding claims but only to policies issued after the … effective date."

Wallace Lightsey, a Wyche PA attorney who represented Crossmann Communities of North Carolina Inc. and Beazer Homes Corp. in the suit, said the legislation hadn't rewritten existing contracts because South Carolina courts had already interpreted CGL policies to provide coverage for construction defect claims.

The South Carolina Supreme Court itself had gone back and revised its initial opinion on the occurrence issue, though it issued its new ruling in the case after South Carolina lawmakers greenlighted Act 26. The high court said that because it had granted a petition for rehearing, the first opinion in Crossmann was never final — the reason the Supreme Court held that state lawmakers had not violated the separation of powers doctrine by passing the 2011 law.

"Had Crossmann I been this court's final opinion, the doctrine might have been implicated," the majority opinion said. "However, given that in Crossmann II we revised our initial decision in Crossmann I, we do not find that the General Assembly, in this instance, retroactively overruled this court's interpretation of a statute."

Michael Aylward, a Morrison Mahoney LLP partner who represents carriers, said the high court had wiggled out of overturning the law, but that states that passed similar legislation after courts ruled out CGL coverage for construction defect claims could see their laws meet a different fate.

"I think this is unique to South Carolina. … Had the court not changed its mind, I think this could have been struck down prospectively also," Aylward said. "It's the odd circumstance that the court itself changed its mind that allows the legislation to pass muster."

According to Foggan, another live question is whether Act 26 and similar legislation in other states violate the commerce clause because they could affect insurance contracts entered into in other states.

"It's very clear that there are open constitutional questions that will likely be litigated in other jurisdictions," Foggan said. "This doesn't resolve going forward the constitutionality of the other statutes."

Attorneys for Harleysville were not immediately available to comment on the decision Wednesday.

Harleysville is represented by C. Mitchell Brown, Dwight Drake, William Wood Jr. and Michael Anzelmo of Nelson Mullins Riley & Scarborough LLP.

Crossmann and Beazer are represented by Wallace Lightsey and William Wilson III of Wyche PA.

Amicus curiae American Insurance Association and Complex Insurance Claims Litigation Association are represented by Laura Foggan of Wiley Rein LLP and Debra Sherman Tedeschi.

The case is Harleysville Mutual Insurance Co. v. The State of South Carolina et al., case number 27189, in the Supreme Court of South Carolina.

--Editing by Elizabeth Bowen and Andrew Park.
