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ALERT

Pennsylvania Superior Court Opens Door to Coverage of Faulty Workmanship Claims

By Darin J. McMullen

Pennsylvania policyholders can more confidently challenge insurance companies' denials of faulty workmanship claims following the Pennsylvania Superior Court's recent opinion in *Indalex Inc. v. National Union Fire Ins. Co. of Pittsburgh, PA*, 2013 Pa. Super 311 (Dec. 3, 2013). The *Indalex* decision reverses a nearly decade-long trend of Pennsylvania decisions narrowing the scope of insurance coverage for construction and defect-related claims under commercial general liability insurance policies. Equally important, the *Indalex* ruling dealt a blow to the insurance industry's continual efforts to win overbroad expansion of the rulings in *Kvaerner Metals Div. of Kvaerner U.S., Inc. v. Commercial Union Ins. Co., Millers Capital Ins. Co. v. Gambone Bros. Dev. Co., and Erie Ins. Exchange v. Abbott Furnace Co.*, which found that claims of faulty workmanship in some circumstances may not constitute coverage-triggering "occurrences."

Indalex, a manufacturer of windows and doors, was sued by contractors and property owners alleging that Indalex's products were defective and resulted in water intrusion and leakage that caused physical damage, including the presence of mold and cracking in walls. Moreover, the underlying individual plaintiffs alleged that personal injuries also arose from these defects. The underlying complaints asserted claims of negligence, strict liability and breach of contract, as well as breach of warranty.

Following a denial of coverage, Indalex filed suit in the Allegheny County Court of Common Pleas, seeking a determination that it was entitled to defense and indemnity. National Union contended that, under Pennsylvania law and the *Kvaerner* ruling, the underlying claims failed to allege an occurrence triggering coverage under the commercial general liability insurance policy. The trial court ultimately granted National Union's motion for summary judgment, holding that *Kvaerner* precluded because there was no "occurrence" as defined under the policy.

On appeal, the Superior Court focused on the meaning of "occurrence" as defined in the policy, and in light of the Pennsylvania Supreme Court's decision in *Kvaerner* and the Superior Court's own subsequent decisions in *Gambone* and *Abbott*. The Superior Court analyzed *Kvaerner*, which held that claims of faulty workmanship did not "present the degree of fortuity contemplated by the ordinary definition of 'accident'" to establish an "occurrence."

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The court noted, however, that the underlying complaint in *Kvaerner* alleged only property damage from faulty workmanship to the work product itself. Additionally, unlike the underlying complaints in *Indalex*, *Kvaerner* involved only claims for breach of contract and breach of warranty, rather than tort claims.

Although the Superior Court could have likely distinguished *Indalex* from *Kvaerner* without further analysis, it nevertheless continued to analyze and distinguish its own decisions subsequent to and relying upon *Kvaerner*. In addressing *Gambone* the Superior Court again drew a distinction based on the fact that affirmation of summary judgment was predicated on the fact that the Superior Court panel "in Gambone focused on the allegations of faulty workmanship in what they had characterized as the product itself, the home."

In its continuing effort to provide much-needed clarification and limitation to *Kvaerner* and its progeny, the Superior Court next addressed its opinion in *Abbott*. The underlying complaint in *Abbott* not only alleged faulty workmanship and damage to the policyholder's property, but also alleged damage to other property, raising the question of whether a negligence claim was properly pleaded. The Superior Court in *Abbott* applied the "gist of the action" doctrine to determine whether the gravamen of the complaint sounded in contract or tort, notwithstanding the specific causes of action asserted. The *Abbott* court ultimately concluded that the underlying complaint failed to adequately plead a negligence claim, and that "the gist of the action, therefore, was a breach of contract that was not an occurrence."

The *Indalex* court determined neither *Kvaerner*, *Gambone* nor *Abbott* compelled a holding that Indalex was not entitled to coverage. Again the Superior Court went to great lengths to differentiate the holdings in each of the prior rulings, noting that *Kvaerner* was limited to situations where the underlying claims sounded in breach of contract and warranty and the only damages were to the policyholder's work product. The court next explained that *Gambone* was unique in the fact that it alleged claims against a homebuilder and the "product" at issue was the home itself, unlike an "off the shelf product" that caused both property damage and personal injury. Moreover, the *Indalex* court distinguished the fact that in *Gambone*, the issue was faulty workmanship with the application of stucco, whereas in *Indalex*, the allegations were in the nature of an "active malfunction" and not merely faulty workmanship.

Finally, the court stated that although it applied the "gist of the action" doctrine in *Abbott*, the Pennsylvania Supreme Court had not expressly adopted the doctrine; and its application of the doctrine in *Abbott* was consistent with New Jersey law, which governed the underlying claims in that case. Importantly, the court noted that it would be inconsistent with the duty to defend to apply the "gist of the action" doctrine in the context of a duty to defend analysis, since the doctrine seeks to boil claims down to their essential theory, whereas the duty to defend requires an insurance company to defend so long as one of many alleged claims triggers coverage. Thus, an important limitation was placed on the *Abbott* decision and its reli-

ance on the "gist of the action" doctrine.

Following this analysis of the *Kvaerner* trilogy, the *Indalex* court held that coverage under the commercial general liability policy was triggered because the underlying complaints against Indalex alleged defective products resulting in property loss to property other than Indalex's own products or property. Moreover, the underlying complaints also alleged personal injury claims. Accordingly, the court concluded that such claims constituted an "occurrence" and coverage was not precluded under *Kvaerner* and *Gambone*, neither of which had any precedential authority warranting denial of coverage.

In the wake of *Indalex*, the insurance industry will no doubt be quick to characterize the decision as limited in its scope based on the unique facts of the case. While accurate to suggest the decision was, of course, rendered based on specific facts and allegations of the underlying actions, such efforts are designed to obscure the impact of a decision holding that faulty workmanship claims do under some circumstances constitute coverage-triggering occurrences.

In fact, the *Indalex* decision signals an effort by the Superior Court to define the limitations of the *Kvaerner*, *Gambone* and *Abbott* holdings, while also firing a warning shot against insurance companies' efforts to expand the holdings in those cases beyond their actual or intended scope. The Superior Court could have simply distinguished *Indalex* from *Kvaerner* and reversed the trial court. Instead, it engaged in a painstaking and thorough analysis of each chapter of the *Kvaerner* triology, and not only distinguished *Indalex*, but also defined the reach of each previous decision.

Although the *Indalex* ruling cannot, and likely will not, prevent overzealous insurance companies from continually seeking to advance overbroad interpretations of *Kvaerner* and its progeny, the decision provides lower courts with guidance on the limitations of those rulings. Moreover, the decision provides policyholders with a sorely needed weapon of their own to combat overextension of *Kvaerner*, *Gambone* and *Abbott*, particularly in the context of the duty to defend.