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Client Alert

Indiana Supreme Court Hears Oral Argument in Construction Defect Coverage Case

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On January 14, 2010, the Indiana Supreme Court heard oral argument on the policyholder's petition to transfer in *Sheehan Construction Company, Inc. v. Continental Casualty Company*. This is an important case to watch for companies in the construction business and owners of real property. The recent argument has been posted on, and can be viewed by the public using, the Indiana Supreme Court's website, www.in.gov/judiciary/webcast.

In June, 2009, the Indiana Court of Appeals held that there was no coverage under a home builder's general liability policy for liability that arose from water damage caused by construction defects in the homes in a subdivision in Indianapolis that the home builder had constructed. The Court of Appeals held that the facts presented did not constitute "property damage" under the language of the home builder's policy. The Court of Appeals did not quote or examine the policy's definition of "property damage." It relied, instead, on general statements in prior Indiana decisions' regarding the purpose of liability insurance in the construction context.

The home builder argued, to the Indiana Supreme Court, that the actual words of the policy cannot be ignored in a determination of whether coverage is available for a liability claim. At the January 14, 2010 argument, the policy's definition of "occurrence" was a focal point of discussion. As in many liability insurance policies, "occurrence" is defined by the home builder's policy as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions" The "subcontractor" exception to the "damage to your work" exclusion was another issue addressed by the lawyers' arguments and the questions from the bench. This exception restores coverage for liability claims arising from damage to the policyholder's work when the work is performed by a subcontractor.

The home builder's lawyer argued that the policy's definitions of "occurrence" and "property damage" clearly were satisfied by the damage to homes and their contents that was caused by periodic water intrusion that had accidentally resulted from the way that a subcontractor had constructed the exterior walls of homes. The home builder's lawyer argued that there would be no point in having this exception in the policy if there was no possibility of coverage for damage to the work because the threshold conditions of an "occurrence" or "property damage" can not exist as a matter of law. The insurer's lawyer urged the Supreme Court to put aside the policy language and decide the case on other grounds.

Many companies in the construction business believe that liability insurance will protect them from claims that arise when a subcontractor's negligence results in damage to the constructed building. Owners of real property that has been damaged by such construction defects likewise believe that the liability insurance of the builder or general contractor will respond to their liability claims. The Court of Appeals decision in *Sheehan Construction* conflicts with these positions and is out of step with insurance coverage decisions from other states. This coverage issue has wide impact on Indiana businesses and property owners.