CASE NO. SC05-168
L.T. CASE NO. 2D03-134

IN THE SUPREME COURT OF FLORIDA

U.S. FIRE INSURANCE COMPANY,

Petitioner,

vs.

FIRST HOMEBUILDERS OF FLORIDA,

Respondent.

ON DISCRETIONARY CONFLICT REVIEW OF A DECISION FROM THE SECOND DISTRICT COURT OF APPEAL

AMICUS BRIEF OF MID-CONTINENT CASUALTY COMPANY

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STATEMENT OF IDENTITY AND INTEREST

Mid-Continent Casualty Company ("Mid-Continent") is an insurer that sells Commercial General Liability (CGL) insurance policies throughout the United States, including Florida. Mid-Continent is also the defendant-appellee in *Lamar Homes, Inc. v. Mid-Continental Cas. Co.*, Case. No. 04-51074, where the Texas Supreme Court is presently deliberating over the question of insurance coverage for the repair and replacement of a contractor's faulty workmanship now before this Court. *As the preferred carrier for the 19,509 members of the Florida Home Builders Association*, Mid-Continent has a direct and substantial interest in the decision below, as it threatens to convert every CGL insurance policy issued in the State of Florida into a cost-free performance bond.

SUMMARY OF ARGUMENT

As one commentator aptly noted, the risks on a modern construction project are "staggering." David J. Barru, *How to Guarantee Contractor Performance on International Construction* …, 37 Geo. Wash. Int'l L. Rev. 51, 52 (2005). To list only some of the perils, there are design errors, construction negligence, weather risks, labor risks, human risks, design and technology risks, environmental risks, logistical risks, supplier and transportation difficulties, regulatory concerns, solvency risks, and even political risks. *Id.*

If the Second DCA's ruling below is not quashed, the entire range of construction costs associated with repairing and replacing a contractor's poor workmanship will be improperly foisted upon CGL insurance carriers. Unlike an insurance policy, a performance bond is specifically designed to protect against these risks. The opinion by the Second DCA effectively converts every CGL insurance policy into coverage against not only tort damages, but also contractual liability – no different than a performance bond. The Court should give meaning to a CGL policy's "occurrence" and "property damage" requirements and Florida's historical interpretation of CGL coverage, and quash the decision below.[1]

ARGUMENT

I. A PERFORMANCE BOND IS DESIGNED TO GUARANTEE THAT A PROJECT WILL BE COMPLETED ACCORDING TO CONTRACT

Surety bonds are "older than recorded history." Phillip Bruner and Patrick J. O'Connor, Jr., *Historical Development of Suretyship*, 4 Bruner & O'Connor Construction Law ("BOCL") §12:3 (2006). There are typically three parties to the bond: the Surety, the Principal, and the Obligee. The Principal has an obligation to perform under a contract with the Obligee. Occasionally the Obligee might ask for assurance that the contract will be properly performed. In order to protect the Obligee and ensure that the contract will be satisfactorily completed, the Principal

[1] The standard of review is *de novo*. *Jones v. Utica Mut. Ins. Co.*, 463 So.

purchases a bond. By issuing the bond, the Surety agrees to fully perform the Principal's obligations under the contract if the Principal cannot. Stanley P. Sklar, *The Construction Loan: Who Really Pays for the Construction?*, 525 PLI/Real 59, 70 (2006). Stated another way, the surety bond guarantees the Principal's ability to satisfactorily perform its contract.

Of the various types of bonds in a construction contract, the most common is the performance bond. Under a performance bond, the Surety guarantees the owner that it will perform the obligations of the contract if the contractor fails to perform the work according to the specifications under the contract.

A performance bond is statutorily required in certain public construction. The U.S. Supreme Court observed that the purpose of the performance bond requirement is "to protect those who have a direct contractual relationship with either the prime contractor or a subcontractor." *J.W. Bateson Co., Inc. v. U.S. ex rel. Bd. of Trustees of Nat.*, 434 U.S. 586, 586 (U.S. 1978).

At bottom, a performance bond is the appropriate mechanism for ensuring proper completion of a construction contract, not a CGL insurance policy.

II. COURTS IN FLORIDA AND ELSEWHERE HAVE REFUSED TO CONVERT CGL INSURANCE POLICIES INTO PERFORMANCE BONDS

1153, 1157 (Fla. 1985).

In a bit of irony considering the decision below, the Second DCA has previously ruled that poor workmanship was not covered under a U.S. Fire Insurance Company ("U.S. Fire") CGL policy, because a liability policy is not a performance bond. *Hardaway Co. ex rel. Wright Contracting Co. v. U.S. Fire Ins. Co.*, 724 So.2d 588 (Fla. 2d DCA 1998). Citing to this Court's bedrock decision in *LaMarche v. Shelby Mut. Ins. Co.*, 390 So.2d 325 (Fla. 1980), the Second DCA ruled that there was no coverage under the liability policies.

> Further, after review of the Authority's third amended complaint and the insurance policies at issue, we hold that, even if there had been an occurrence that would trigger coverage, the alleged damages are excepted from coverage by the work product and business risk exclusions. These exclusions bar coverage for the cost of repair and replacement of the insured's faulty or defective workmanship or for other problems associated with the insured's business risk. … Liability insurance policies, such as the policies involved here, are not performance bonds. *See, LaMarche.*

Id. at 590.

Florida courts have consistently ruled that faulty workmanship is not covered under a CGL policy, because to find coverage would mean to convert the policy into a surety bond. *See, e.g., Hardaway Co. ex rel. Wright Contracting Co.*

v. U.S. Fire Ins. Co., 724 So.2d 588, 590 (Fla. 2d DCA 1998) ("Liability insurance policies, such as the policies involved here, are not performance bonds"); *Auto-Owners Ins. Co. v. Marvin Dev. Corp*., 805 So.2d 888, 892-93 (Fla. 2d DCA 2001) ("we also note that the Auto-Owners Insurance policies were not warranty policies providing coverage for construction deficiencies or defective workmanship"); *Auto-Owners v. Travelers*, 227 F.Supp. 1248, 1262 (M.D. Fla. 2002) ("*LaMarche* provides that a surety's liability and CGL's liability are not coextensive").

Courts across the nation have similarly reasoned that to find insurance coverage for replacing faulty workmanship is tantamount to converting a CGL policy into a performance bond.

- *Redev. Auth. of Cambria County v. Int'l Ins. Co.*, 685 A.2d 581, 592 (Pa. Super. 1996) ("The Redevelopment Authority in the instant case is similarly seeking to convert a general liability policy into a professional liability policy or a performance bond. The express provisions of the insurance contract do not provide coverage for the claims in the underlying action which arise out of and relate to the contract between the parties, and the Authority");
- *Hotel Roanoke Conference Ctr. Comm'n v. Cincinnati Ins. Co.*, 303 Fl.Supp.2d 784, 786-87 (W.D. Va. 2004) (holding poor performance on a

renovation contract could not be considered an accident or occurrence, and concluding that "[t]he insurance policy issued to the [contractors] is a general liability policy covering accidents causing bodily injury or property damage. It is not a performance bond. It does not cover poor workmanship");

- *Qualls v. Country Mut. Ins. Co.*, 462 N.E.2d 1288, 1291 (Ill. App. 1984) ("[C]omprehensive general liability policies … are intended to protect the insured from liability for injury or damage to the persons or property of others; they are not intended to pay the costs associated with repairing or replacing the insured's defective work and products, which are purely economic losses. Finding coverage for the cost of replacing or repairing defective work would transform the policy into something akin to a performance bond") (internal citations omitted);

- *Jim Johnson Homes, Inc. v. Mid-Continent Cas. Co.*, 244 F.Supp.2d 706, 715 (N.D. Tex. 2003) ("In effect, plaintiff is asking the court to give the insurance policy in question attributes of a contractor's performance bond, guaranteeing to the owner that the contractor will perform the construction agreement between the parties in a *workmanlike* manner and in accordance with the terms of the contract. None of the language of the insurance

policy suggests that the policy was intended to serve as a performance bond as well as a typical liability insurance contract … . Furthermore, the better reasoned authorities hold that claims such as the Jeters are making against plaintiff are not claims of accidental damage to property, with the consequence that the statement of such a claim does not allege an 'occurrence' within the meaning of the insurance policy.");

- *ACS Const. Co., Inc. v. Bituminous Fire and Marine Ins. Co.*, 621 S.E.2d 33, 37 (S.C. 2005) ("Accordingly, we hold that the damage in the present case did not constitute an 'occurrence.' If we were to hold otherwise, the CGL policy would be more like a performance bond, which guarantees the work, rather than like an insurance policy, which is intended to insure against accidents").

Under the Second DCA's decision, a general contractor in Florida now has a choice. Rather than pay a 1-3% premium, per construction project, the contractor can simply pay a nominal amount for a blanket CGL policy and be covered for all of its construction activities, as if it had multiple performance bonds for each of its contracts. A CGL insurer has no right to reimbursement if the contractor elects to use cheap materials and inexperienced labor in order to maximize its profits. This Court should give meaning to the language of the CGL policy and preserve the fundamental differences between a surety bond and in insurance policy.

III. FAULTY WORKMANSHIP THAT CAUSES NO BODILY INJURY AND NO DAMAGE TO OTHER PROPERTY IS NOT AN "OCCURRENCE" CAUSING "PROPERTY DAMAGE" UNDER A CGL POLICY

Under a CGL insurance policy, the "occurrence" and "property damage" requirements in the insuring agreement are not satisfied by a claim against a contractor for contractual liability for failing to properly build a home as specified in a contract. Stated another way, faulty workmanship is not covered under the terms of a CGL insurance policy.

A. Faulty Workmanship is Not an "Occurrence"

In pertinent part, the U.S. Fire policy defines an "occurrence" as an "accident," which suggests a fortuitous event that is beyond the insured's control. *Webster's Third New International Dictionary of the English Language* 11 (2002) (an "accident" is "an event or condition occurring by chance or arising from unknown or remote causes"). This Court has also ruled that an "occurrence" includes "injuries or damage neither expected nor intended from the standpoint of the insured." *State Farm Fire & Cas. Co. v. CTC Dev. Corp.*, 720 So.2d 1072, 1076 (Fla. 1998). Damages arising out of the insured's contractual liability, unlike tort damages, are not covered under a CGL policy, as they are by law foreseeable damages arising out of the insured's failure to perform its contract. *LaMarche v.*

Shelby Mut. Ins. Co., 390 So.2d 325 (Fla. 1980); *Tucker Constr. Co. v. Michigan Mut. Ins. Co.*, 423 So.2d 525 (Fla. 5th DCA 1982).

Prior to the decision below, Florida courts have consistently ruled that the cost of repairing and replacing a contractor's faulty workmanship is not an "occurrence" or "accident" under a CGL policy. *See, e.g., Home Owners Warranty Corp. v. Hanover Ins. Co.*, 683 So.2d 527 (Fla. 3d DCA 1996) (no coverage for faulty workmanship since no damages outside of the contract alleged); *Lassiter Constr. Co., Inc. v. Amn. States Ins. Co.*, 699 So.2d 768 (Fla. 4th DCA 1997) (no coverage for breach of contract as the result of poor construction); *Centex Homes Corp. v. Pre-Stress Systems, Inc.*, 444 So.2d 66, 67 (Fla. 3d DCA 1984) ("purpose of comprehensive liability insurance coverage is to provide protection for personal injury or property damage caused by the product only and not for the replacement or repair of the product."); *U.S. Fire Ins. Co. v. Meridian of Palm Beach*, 700 So.2d 161, 162 (Fla. 4th DCA 1997) (no coverage for defective workmanship under CGL policy); *Aetna Cas. & Sur. Co. of Am. v. Deluxe Sys., Inc.*, 711 So.2d 1293 (4th DCA 1998) (the "your work" exclusion barred coverage for insured's liability for cost of purchasing and installing replacement shelving, whether insured's work was its product or advice in selecting the shelves); *Keller Indus., Inc. v. Employers Mutual Liability Ins. Co.*, 429 So.2d 779, 780 (Fla. 3d DCA 1983) (no coverage for cost of repairing and replacing defective products and

workmanship); *Auto-Owners Ins. Co. v. Marvin Dev. Corp*., 805 So.2d 888 (Fla. 2d DCA 2001) (business risk exclusions precluded coverage for contractor who built home on construction site which was improperly prepared); *Sekura v. Granada Ins. Co.*, 896 So.2d 861 (Fla. 3d DCA 2005) (no coverage for repairing and replacing faulty construction since policy protects against property damage caused by the completed work – not the defective work itself); *Auto-Owners Ins. Co. v. Tripp Constr., Inc.*, 821 So.2d 1157 (Fla. 3d DCA 2002) (same).

B. Faulty Workmanship is Not "Property Damage"

In pertinent part, the U.S. Fire policy defines "property damage" as: "physical injury … or … [l]oss of use of tangible property." *Black's Law Dictionary* (8th ed. 2004) defines "tangible," in pertinent part, as: "1. Having or possessing physical form; CORPOREAL. 2. Capable of being touched and seen; perceptible to the touch." On the other hand, "intangible" is defined as: "Something that lacks a physical form; an abstraction, such as responsibility; esp., an asset that is not corporeal, such as intellectual property." (8th ed. 2004). For these reasons, economic losses from breach of contract cannot constitute property damage caused by an occurrence. *Lazzara Oil Co. v. Columbia Cas. Co.*, 683 F.Supp. 777, 780-91 (M.D. Fla. 1988) (allegations of price fixing were for economic damages not "damage or injury to tangible property … Such pure economic losses do not constitute damage or injury to tangible property"); Steven

Plitt, Daniel Maldonado, and Joshua D. Rogers, *Overview of Commercial General Liability Policies*, 9A Couch on Ins. §129:1 (3d ed. 2005) ("a commercial general liability insurance policy is generally designed to provide coverage for tort liability for physical damages to others and not for contractual liability of the insured for economic loss because the product or work is not that for which the damaged person bargained.").

Florida courts have consistently found that the cost of repairing and replacing a contractor's faulty workmanship is not "property damage" under a CGL policy. For example, in *West Orange Lumber Co., Inc. v. Indiana Lumbermens Mut. Ins. Co.*, 898 So.2d 1147 (Fla. 5th DCA 2005), a lumber company contracted to provide specified cedar. It was learned later learned that incorrect cedar was supplied by the contractor. On appeal, the Fifth DCA ruled that there was no coverage because the failure to act according to the contract was not property damage:

> Failure to supply a product specified in a contract is a business risk not covered by the liability policy issued by Indiana. ... [T]he allegations in the complaint show the owner or general contractor's property suffered no damage from the failure to supply the correct quality of lumber. The only damage alleged was the cost

> or expense to the vendor to remove the defective product and supply an acceptable substitute.

Id. at 1148.

CONCLUSION

The Second DCA's decision ignores the fundamental differences between a liability policy and a performance bond by forcing CGL insurers to cover contractual liability. This Court should prevent the inevitable insurance crisis and accordingly quash the decision below. The insurance industry cannot provide performance bond coverage for the price of a basic CGL policy.

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the amicus brief of Mid-Continent Casualty Company was served on June 8, 2006 by FedEx, upon: Counsel for Petitioner, Ronald L. Kammer, Esq., Hinshaw & Culbertson LLP, 9155 S. Dadeland Blvd., Suite 1600, Miami, Florida 33156, and Counsel for Respondent, Mark A. Boyle, Esq., Fink & Boyle, P.A., 2030 McGregor Blvd., Fort Myers, Florida 33902.

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CERTIFICATE OF COMPLIANCE

The undersigned counsel hereby certifies that this amicus brief complies with Rule 9.210, Fla.R.App.P., and is typed in Times New Roman 14-point font.

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