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Contractors, beware: General liability insurers wrongfully denying claims for damage by defective subcontractor work - by Eric Eisenberg and Robert Ferguson

March 22, 2024 - Construction Design & Engineering

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As a contractor, you are familiar with working together with subcontractors – delegating project scope as part of the overall job. However, when a subcontractor's work is defective, who is liable for the damage?

This is not an unfamiliar issue to contractors – more than likely, you have responded to one or more claims that a subcontractor's work was defective and that the defective work damaged other non-defective project work. For example, a scenario you may encounter could include damage to interior electrical, ?ooring, painting and/or drywall work as a result of work completed by roo?ng or building envelope subcontractors. Other claims include alleged damage to window units caused by painting subcontractors, or allegations that work completed by ?reproo?ng subcontractors has damaged the non-defective HVAC and cabling work of other subcontractors. Courts across the United States are grappling with whether standard insurance policies, known as Comprehensive General Liability (CGL) policies cover such claims for damage caused by subcontractors.

In most states, courts have ruled that there is coverage for these types of claims under the Insurance Services Organization (ISO) standard form CGL policy. However, the situation in Massachusetts is less clear, as the state's highest courts have not recently addressed this issue. Recent events suggest clarity might come soon making it imperative to push back on carrier denials of these subcontractor work claims, until this issue is settled.

On November 30, 2023, the Supreme Court of Illinois ruled unanimously that defective work can be a covered accident under Illinois law for purposes of CGL policies. While the decision is limited to Illinois law, it is consistent with the national trend, which overwhelmingly holds that defective subcontractor work can be a covered occurrence under CGL policies. In so ruling, the Illinois court also rejected the insurers' argument that there was no coverage for non-defective project work – even if it was damaged by subcontractor negligence – because the entire project was the general contractor's "work."

There are numerous sound reasons that support the Illinois court's determination. However, not all courts have reached the same result. In fact, in mid-2022, the United States District Court for Massachusetts ruled that there is no coverage under CGL policies for damage to non-defective portions of a project caused by defective subcontractor work. This ruling goes against the majority of cases nationally (29 states to 5 states) and is currently under appeal. Hinckley Allen, representing the Associated General Contractors of Massachusetts and of America, submitted an amicus brief urging the first circuit court to follow the "majority" approach and recognize coverage for damage caused by or damage to subcontractors' work. We are awaiting the first circuit's decision.

In the meantime – seemingly as a result of the Massachusetts District Court's "No Coverage" ruling, and notwithstanding the national trend, including the recent Illinois decision, we are seeing carriers deny coverage for claims by construction clients for damage allegedly caused by defective subcontractor work. Typically, carriers have been asserting that such defective subcontractor work is not an "occurrence" under the CGL policy and/or that the entire project was, they argue, the work of the insured/general contractor (and that damage to the insured's own work is therefore not covered under CGL policies).

For projects in Massachusetts, these types of "no coverage" determinations are, at best, premature, in that neither the first circuit, nor the Massachusetts Supreme Judicial Court have yet to uphold/approve of the District Court's decision. We are, on behalf of our construction contractor clients, disputing insurance coverage denials that contradict the national weight of authority. Construction companies receiving such denials are advised to have experienced coverage counsel evaluate such denials and, if appropriate, dispute them, at least until the First Circuit or Supreme Judicial Court rule on this issue. In arguing for coverage, contractors should explain how non-defective project work was damaged by subcontractor negligence and/or how defective work caused damage to non-defective project work. While each case rises and falls on its own facts, an insurer denial of coverage letter may not be the final word on coverage.

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