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What Happens Next after Cypress

The New Jersey Supreme Court in Cypress Point Condominium Association, Inc. v. Adria Towers, LLC., et al. (A-13/14-15)(076348) finally put to rest (in New Jersey) an issue that has been haunting general contractors and developers since 1979. That is the year when Justice Clifford penned Weedo v. Stone-E-Brick, 81 N.J. 233 (1979), denying a faulty workmanship claim, under products-completed operations coverage, based on two specific business risk exclusions that have not existed in liability policies since 1986. The issue decided by Cypress is whether faulty workmanship claims constitute "property damage" caused by an "occurrence." This is a threshold issue to come within the insuring agreement of liability policies that provide for "products-completed operations" coverage.

The unanimous Cypress Court found (as have the majority of the courts in the country) that consequential water damage caused by a subcontractor's (not the named insured's) faulty workmanship constitutes property damage caused by an occurrence. The Cypress Court did so primarily as a result of the subcontractor's exception to one of the business risk exclusions added to liability policies in 1986. That exception arose as a direct result of the marketplace demanding the availability of coverage for faulty workmanship claims.

As of August 4, 2016, carriers in New Jersey can no longer deny coverage for "consequential damages" arising out of faulty workmanship of a subcontractor of the named insured, barring the application of other exclusions.

The more interesting issues, not addressed by the Cypress Court since they were not before it for consideration, are (a) whether repair and replacement (or "rip" and "tear") costs are also covered; (b) if these rip and tear costs are covered for additional insureds, whether or not the named insured can recoup them; and (c) how do named insureds and additional insureds obtain the broadest possible coverage?

The fiction that only consequential damages are covered by liability policies does not arise from the insuring agreement or any other language taken from these standard liability policies. It springs from the notion, espoused in Weedo by Justice Clifford, that one cannot buy insurance to fix work one does badly. The retort to this is: why not? People commit negligent acts all the time, and if that negligence results in injury or damage then the injured victim should be able to collect for all costs associated with remedying the results of that negligence. (How do lawyers and doctors, after all, obtain malpractice insurance?) There is an argument that if the poorly performed work needs to be replaced in order to fix the resulting problem (the consequential damages), it should be covered despite the policy exclusion (in which the subcontractor exception appears) for damage to "your" work.

The New Jersey Supreme Court has not squarely addressed whether any damages other than consequential damages are recoverable for faulty workmanship, but this issue is certain to arise in a future case since consequential damages are often only a small percentage of the costs incurred to fix poorly performed construction work.

Second, what happens if your claim for coverage arises because you are an additional insured under a policy that provides for products-completed operations coverage? Is the scope of available products-completed operations coverage different than it is for a named insured? The Appellate Division in East Coast Residential Associates v. Builders Firstsource Notheast, 2012 WL 75146 (N.J Super App. Div. 2012) said "yes" to this question. The scope of coverage for additional insureds arises out of the policy endorsement (if there is one) providing for that additional insured coverage. Whether and to what extent any of the other policy language applies (including the business risk exclusions discussed in Cypress) should depend upon what the endorsement says.

Finally, it is paramount that any insured obtaining products-completed operations coverage (either as a named insured or an additional insured) make certain prior to commencing construction that (a) it is obtaining both "on-going" and "completed" operations coverage and that (b) it understands precisely what will and will not be covered if either the named insured or one of its subcontractors performs the work negligently, causing consequential damages to the structure in question. It is too late to undertake this review once the negligent work is performed and the claim arises.

This *Insurance Law Alert* was written by **Margaret Raymond-Flood, Esq.**, and **Martha N. Donovan, Esq.**, Members of **Norris McLaughlin & Marcus, P.A.** If you have any questions about the information contained in this alert or any other questions related to insurance law, please feel free to contact Margaret or Martha, at **mrflood@nmmlaw.com**, **mndonovan@nmmlaw.com**, respectively.