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WHEN YOUR BOAT SPRINGS A LEAK: COVERAGE IN CONSTRUCTION DEFECT CASES – CONTRIBUTION, INDEMNITY AND ADDITIONAL INSURED ISSUES

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When your Boat Springs a Leak: Coverage in Construction Defect Cases – Contribution, Indemnity and Additional Insured Issues

In virtually every jurisdiction in the country, general contractors are being sued by large numbers of homeowners because of defects in a number of homes within a subdivision. The defects include sub-surface subsidence, roof leaks, plumbing problems and a myriad of other defects. General contractors normally attempt to shift the burden of the defense of these suits to their subcontractors and their carriers, because of indemnity and additional insured provisions in the contracts with the subcontractors. This panel will engage in small group discussions on the issues arising from these suits and practical methods of resolving the coverage disputes to focus on the defense of the homeowners’ claims.
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Hypothetical Case for Discussion


Background facts:

XYZ Construction Company is a large national homebuilder, who built a 2000 home subdivision in the State of Jefferson. The architect and designer of the subdivision was Samuel Architect. XYZ did not do any of the construction work itself, but instead contracted all of the work to various subcontractors. XYZ did market the homes and sold the homes to the homeowners.

Shortly after the completion of the subdivision, 200 of the homes began experiencing distress. 100 of the homes experienced subsidence of the soils under the homes, and suffered cracks of the floors, walls and ceilings. 50 homes experienced roof leaks, causing damage to the interior of the homes. 25 homes experienced plumbing leaks and sustained damage to the interior of the homes as a result of those leaks. 25 homes had allegedly defective windows, which caused rainwater to leak into the homes, causing property damage.

The 200 homeowners filed suit against XYZ and Architect, alleging property damage caused by negligent design and construction. The Complaint also alleges fraud and unfair trade practices against XYZ for misrepresentations made during the sales of the homes.

XYZ had a contract with Architect for design of the subdivision, including research to determine the sufficiency of the soils in the area for a subdivision. Architect was also required to design all the homes and supervise the construction. There were no indemnity or insurance provisions in this contract.

XYZ had contracts with the dirt moving contractor, the plumber, the roofer and the window installer. These contracts obligated the subcontractor to indemnify and defend XYZ for property damage caused by the subcontractor, and obligated the subcontractors to name XYZ as an additional insured under their CGL.

XYZ has made demand on the 4 subcontractors and their general liability carriers to defend XYZ and agree to indemnification. XYZ is self-insured up to 10 million dollars. The excess carrier for XYZ has no duty to defend.
Questions Presented by Hypothetical Case

The laws of the 50 states vary with regard to the enforceability of indemnity and insurance agreements in the construction industry. Thus, it is probably not helpful to focus on any individual state or any particular statute. However, the issues in the hypothetical are common to all states, and the panel hopes to draw upon the experience of all attendees to this program to develop practical and common sense approaches to the coverage issues associated with this litigation, so the focus can be shifted from the coverage issues to the defense of the underlying litigation.

The panel presents the following questions to be discussed by individual groups.

1. How are the coverage issues associated with the hypothetical case resolved short of litigation? Pro rata sharing of defense costs based on policy limits? Pro rata sharing of defense costs based on number of houses allegedly damaged by the acts of each subcontractor? Pro rata sharing of defense costs based on alleged damages? Separate defense provided by each carrier for only the homes alleged to have sustained property damage because of their insured’s faulty work?

2. How does the group of insurers deal with a recalcitrant insurer who refuses to participate in the defense? Mediation? Intercompany arbitration? Lawsuit initiated by XYZ and all participating insurers?

3. What role does Architect play in this process? Is he left out of the whole process, or can he assist in the resolution of the various coverage issues?

4. How do the separate allegations of fraud and unfair trade practices against XYZ affect the defense of the case? Should XYZ be asked to pay a portion of the defense costs associated with the defense of XYZ?

5. Can a separate mediation between XYZ and the various AI carriers, without the participation of the homeowners, be an effective method of resolving any disputes with regard to defense and indemnity?

6. Without an agreement between the carriers and XYZ on indemnity, can one attorney/law firm represent XYZ, or is there an inherent conflict of interest?