



**OVERVIEW OF COMMON ISSUES IN
CONSTRUCTION DEFECT CLAIMS**

Spring 2018 Edition

www.grayduffylaw.com

15760 Ventura Boulevard
16th Floor
Encino, California 91436
Phone (818) 907-4000
Fax (818) 783-4551

210 B Twin Dolphin Drive
Redwood City, California 94065
Phone (650) 365-7343
Fax (650) 365-6225

PREFACE

As its name implies, this book is intended to provide the user with a source for quick reference to particular issues which may arise when analyzing claims within the dynamic field of construction defect litigation. While its focus is primarily on California decisional and statutory law, many of the cases comment on out-of-state authorities dealing with the topics under consideration.

The cases cited in this source book provide a starting point for legal research on these issues. The user is cautioned that this manual is not intended to be an exhaustive treatise on or restatement of the law, or a comprehensive listing of all cases on the subject. When necessary, consultation with counsel is recommended.

INDEX OF TOPICS

A. OVERVIEW OF COMMON COVERAGE ISSUES IN CONSTRUCTION DEFECT CLAIMS

1. DISTINCTION BETWEEN “DEFECT” AND “PROPERTY DAMAGE”	22
2. THE DUTIES TO DEFEND AND INDEMNIFY.....	28
3. POLICY EXCLUSIONS	36
4. INDEMNITY AGREEMENTS.....	50
5. ADDITIONAL INSURED ENDORSEMENTS	64
6. RULES FOR ALLOCATION OF DEFENSE COSTS	67
7. DEDUCTIBLES AND SELF-INSURED RETENTIONS	74
8. DUTY TO DEFEND AS BETWEEN PRIMARY AND EXCESS INSURERS.....	79
9. TENDER AND WITHDRAWAL OF DEFENSE ISSUES	82
10. ARBITRATION AND SETTLEMENT ISSUES	86
11. “CURRENT ISSUES” REGARDING EVIDENTIARY AND PROCEDURAL MATTERS IN CONSTRUCTION DEFECT LITIGATION.....	105
12. “INTERESTING ISSUES” IN CONSTRUCTION DEFECT LITIGATION	113

B. CONSTRUCTION BASICS FROM TOP TO BOTTOM

I. CAST OF CHARACTERS 118

II. GEOTECHNICAL TERMS AND TYPICAL DEFECTS 120

III. FOUNDATION TERMS AND TYPICAL DEFECTS 126

IV. STRUCTURAL RELATED DEFECTS 129

**V. WATER INTRUSION, THE FORCE THAT DRIVES
THE INSURANCE INDUSTRY 133**

Table of Cases and Codes

1. Aas v. Superior Court (2000) 24 Cal.4th 627
2. Abaya v. Spanish Ranch I, LP (2010) 189 Cal.App.4th 1490
3. Abbott Ford, Inc. v. Superior Court (1987) 43 Cal.3d 858
4. Acceptance Ins. Co. v. Syufy Enterprises (1999) 69 Cal.App.4th 321
5. Acqua Vista Homeowners Association v. MWI, Inc. (2017) 7 Cal.App.5th 1129
6. Adolph v. Coastal Auto Sales, Inc. (2010) 184 Cal.App.4th 1443
7. Advent, Inc. v. National Union Fire Insurance Co. of Pittsburgh, PA, Topa Insurance Co. (2016) 6 Cal.App.5th 443
8. Aerojet-General Corp. v. Transport Indemnity Co. (1997) 17 Cal.4th 38
9. Aetna Cas. & Sur. Co. v. Certain Underwriters at Lloyds (1976) 56 Cal.App.3d 791
10. Aguilar v. Atlantic Richfield (2001) 25 Cal.4th 826
11. Ahdout v. Hekmatjah (2012) 213 Cal.App.4th 21
12. Air Machine Com SRL v. Superior Court (2010) 186 Cal.App.4th 414
13. AIU Ins. Co. v. Sup. Ct. (FMC) (1990) 51 Cal.3d 807
14. Alcal Roofing & Insulation v. Superior Court (1992) 8 Cal.App.4th 1121
15. Aluma Systems Concrete Construction of California v. Nibbi Bros., Inc. (2016) 2 Cal.App.5th 620

16. Ameron v. Insurance Company of the State of Pennsylvania (2010) 50 Cal.4th 1370
17. Amis v. Greenberg Traurig (2015) 2015 235 Cal.App.4th 331
18. Argonaut Ins. Co. v. Transport Indemnity Co. (1972) 6 Cal.3d 496
19. Armstrong World Industries, Inc. v. Aetna Casualty & Surety Co. (1996) 45 Cal.App.4th 1
20. Axis Surplus Insurance Co. v. Glencoe Insurance Ltd. (2012) 204 Cal.App.4th 1214
21. Baeza v. Superior Court (2011) 201 Cal.App.4th 1214
22. Bank of the West v. Sup.Ct. (Industrial Indemnity Co.) (1992) 2 Cal.4th 1254
23. Baroco West, Inc. v. Scottsdale Insurance Co. (2003) 110 Cal.App.4th 96
24. Beacon Residential Community Association v. Skidmore Owings & Merrill (2014) 59 Cal.4th 568
25. Belasco v. Wells (2015) 234 Cal.App.4th 409
26. Belz v. Clarendon American Insurance Co. (2007) 158 Cal.App.4th 615
27. Biakanja v. Irving (1958) 49 Cal.2nd 647, 650
28. Blackhawk Corp. v. Gotham Ins. Co. (1997) 54 Cal.App.4th 1090
29. Blackwell v. Visilas (2016) 244 Cal.App.4th 160
30. Blue Ridge Ins. Co. v. Jacobson (2001) 25 Cal.4th 489
31. Brisbane Lodging, L.P. v. Webcor Builders, Inc. (2013) 216 Cal.App.4th 1249

32. Bruni v. Didion (2008) 106 Cal.App.4th 1272
33. Buena Vista Mines, Inc. v. Industrial Indemnity Co. (2001) 87 Cal.App.4th 482
34. Buss v. Superior Court (1999) 16 Cal.4th 35
35. C.I. Engineers & Constructors, Inc. v. Johnson & Turner Painting Co. (1983) 140 Cal.App.3d 1011
36. Cahill v. San Diego Gas & Electric Company (2011) 194 Cal.App.4th 939
37. California Pacific Homes, Inc. v. Scottsdale Ins. Co. (1999) 69 Cal.App.4th 1448
38. California Pac. Homes, Inc. v. Scottsdale Ins. Co. (1999) 70 Cal.App.4th 1187
39. California Shoppers, Inc. v. Royal Globe Ins. Co. (1985) 175 Cal.App.3d 1
40. California Traditions v. Claremont Liability Insurance Co. (2011) 197 Cal.App.4th 410
41. Carr Business Enterprises, Inc. v. City of Chowchilla (2008) 166 Cal.App.4th 25
42. Cassel v. Superior Court (2011) 51 Cal.4th 113
43. CEG Essex Insurance Co. v. H&H Land Development Corporation (MD Georgia 2007) 525 F.Supp.2d 1344
44. Centennial Ins. Co. v. United States Fire Ins. Co. (2001) 88 Cal.App.4th 105
45. Centex Golden Construction Co. v. Dale Tile Co. (2000) 78 Cal.App.4th 992
46. Centex Homes v. St. Paul Fire & Marine Insurance Co. (2015) 237 Cal.App.4th 23
47. Centex Homes v. St. Paul Fire & Marine Insurance Co. (2018) 19 Cal.App.5th 789

48. Certain Underwriters at Lloyds, London v. Arch Specialty Insurance Company (2016) 246 Cal.App.4th 418
49. Chemstar, Inc. v. Liberty Mut. Ins. Co. (9th Cir. 1994) 41 F.3d 429
50. Chinn v. KMR Property Management (2008) 166 Cal.App.4th 366
51. Chu v. Canadian Indemnity Co. (1990) 224 Cal.App.3d 86
52. Chubb/Pacific Indem. Group v. Insurance Co. of No. America (1987) 188 Cal.App.3d 691
53. Clarendon America Insurance v. General Security Indemnity Company of Arizona (2011) 193 Cal.App.4th 1311
54. Clarendon America Ins. Co. v. North American Capacity Ins. Co. (2010) 186 Cal.App.4th 556
55. CNA Casualty of California v. Seaboard Surety Co. (1986) 176 Cal.App.3d 598
56. Continental Heller Corp. v. Amtech Mechanical Services, Inc. (1997) 53 Cal.App.4th 500
57. Crawford v. Weathershield Manufacturing, Inc. (2008) 44 Cal.4th 541
58. Crowley Maritime Corp. v. Boston Old Colony Insurance Co. (2008) 158 Cal.App.4th 1061
59. Cullen v. Corwin (2012) 206 Cal.App.4th 1074
60. Curtis Engineering Corp. v. Superior Court (2017) 16 Cal.App.5th 542
61. Darling v. Superior Court (2012) 211 Cal.App.4th 69

- 62. De Bruyn v. Farmers Group, Inc. (2008) 158 Cal.App.4th 1213
- 63. Delgadillo v. Television Center, Inc. (2018) WL 106971
- 64. DeSaulles v. Community Hospital of the Monterey Peninsula (2016) 62 Cal.4th 1140
- 65. Diamond Heights Homeowners Association v. National American Ins. Co. (1991) 227 Cal.App.3d 563
- 66. Dillingham Construction, N.A., Inc. v. Nadal Partnership, Inc. (1998) 64 Cal.App.4th 264
- 67. Duran v. U.S. Bank National Association (2012) 137 Cal.Rptr.3d 391
- 68. El Escorial Owners Association v. DLC Plastering, Inc. (2007) 154 Cal.App.4th 1337
- 69. Employers Mut. Cas. Co. v. Philadelphia Indemnity Ins. (2008) 169 Cal.App.4th 340
- 70. Employers Reinsurance Corp. v. Phoenix Ins. Co. (1986) 186 Cal.App.3d 545
- 71. Engle v. Copenbarger & Copenbarger (2007) 157 Cal.App.4th 165
- 72. EOTT Energy Corp. v. Storebrand International Ins. Co. (1996) 45 Cal.App.4th 565
- 73. Erreca's v. Superior Court (1993) 19 Cal.App.4th 1475
- 74. Espejo v. Southern California Permanente Medical Group (2016) 246 Cal.App.4th 1047
- 75. Estuary Owners Association v. Shell Oil Company (2017) 13 Cal.App.5th 889

76. Executive Risk Indemnity, Inc. v. Jones (2009) 171 Cal.App.4th 319
77. F&H Construction v. ITT Hartford Insurance Co. (2004) 118 Cal.App.4th 364
78. Fair v. Bakhtiari (2006) 40 Cal.4th 189
79. Fiorito v. Sup.Ct. (State Farm Fire & Cas. Co.) (1990) 226 Cal.App.3d 433
80. Fireman's Fund Ins. Co. v. Maryland Casualty Co. (1998) 65 Cal.App.4th 1279
81. Flores v. Nature's Best Distribution LLC (2016) 7 Cal.App.5th 1
82. Foster-Gardner, Inc. v. National Union Fire Ins. Co. (1998) 18 Cal.4th 857
83. Gaines v. Fidelity National Title Insurance Company (2016) 62 Cal.4th 1081
84. General Star Indemnity Co. v. Superior Court (Hard Rock Cafe America, L.P.) (1996) 47 Cal.App.4th 1586
85. Gloster v. Sonic Automotive, Inc. (2014) 226 Cal.App.4th 438
86. Golden Eagle Ins. Co. v. Insurance Co. of the West (2002) 99 Cal.App.4th 837
87. Golden Eagle Ins. Corp. v. Cen-Fed, Ltd. (2007) 148 Cal.App.4th 976
88. Gonzalez v. Mathis (2018) 20 Cal.App.5th 257
89. Gray v. Chiu (2013) Cal.App.4th 1355
90. Greystone Homes, Inc. v. Midtec, Inc. (2008) 168 Cal.App.4th 1194
91. Guy F. Atkinson Co. v. Schatz (1980) 102 Cal.App.3d 351
92. Hall v. Travelers Ins. Cos. (1971) 15 Cal.App.3d 304

93. Harshad & Nasira Corporation v. Global Sign Systems (2017) 14 Cal.App.5th 523
94. Hartford Acc. & Indem. Co. v. Sup.Ct. (Syntex) (1994) 23 Cal.App.4th 1774
95. Hartford Casualty Insurance Co. v. J.R. Marketing, LLC (2015) 61 Cal. 4th 988
96. Hartford Casualty Insurance Co. v. Mt. Hawley Ins. Co. (2004) 123 Cal.App.4th 278
97. Hartford Casualty Insurance Co. v. Traveler's Indemnity Co. (2003) 110 Cal.App.4th 710
98. Haskel, Inc. v. Superior Court (1995) 33 Cal.App.4th 963
99. Heppler v. J.M. Peters Co. (1999) 73 Cal.App.4th 1265
100. Hillenbrand, Inc. v. Insurance Co. of North America (2002) 104 Cal.App.4th 784
101. Ignacio v. Caracciolo (2016) 2 Cal.App.5th 81
102. Insurance Co. of North America v. National American Ins. Co. (1995) 37 Cal.App.4th 195
103. Jamestown Builders, Inc. v. General Star Indem. Co. (1999) 77 Cal.App.4th 341
104. Janopaul + Block Companies, LLC v. Superior Court (2011) 200 Cal.App.4th 1239
105. J.B.B. Investment Partners, Ltd. v. Fair (2014) 232 Cal.App.4th 974
106. Jeld-Wen v. Superior Court (2007) 146 Cal.App.4th 536
107. Johansen v. Cal State Auto Association Inter-Insurance Bureau (1975) 15 Cal.3d 9
108. Johnson v. Continental Ins. Cos. (1988) 202 Cal.App.3d 477

109. JPI West Coast Construction v. RJS & Associates (2007) 156 Cal.App.4th 1448
110. Kaufman v. Diskeeper Corporation (2014) 229 Cal.App.4th 1
111. Khosh v. Staples Construction Co., Inc. (2016) 4 Cal.App.5th 712
112. Knox v. County of Los Angeles (1980) 109 Cal.App.3d 825
113. Lazy Acres Market, Inc. v. Tseng (2007) 152 Cal.App.4th 1431
114. Leung v. Verdugo Hills Hospital (2012) 55 Cal.App.4th 291
115. Li v. Yellow Cab Co. (1975) 13 Cal.3d 804
116. Liberty Mutual Insurance Co. v. Brookfield Crystal Cove, LLC (2013) 219 Cal.App.4th 98
117. Lindemann v. Hume (2012) 204 Cal.App.4th 556
118. Litt v. Eisenhower Medical Center (2015) 237 Cal.App.4th 1217
119. Lyons v. Fire Ins. Exchange (2008) 161 Cal.App.4th 880
120. MacDonald & Kruse, Inc. v. San Jose Steel Co. (1972) 29 Cal.App.3d 413
121. Manzarek v. St. Paul Fire & Marine Ins. Co. (9th Cir. 2008) 519 F.2d 1025
122. Martin Potts & Associates, Inc. v. Consarl, LLC (2016) 244 Cal.App.4th 432
123. Martinez v. Brownco Construction Co., Inc. (2012) 203 Cal.App.4th 507
124. Maryland Casualty Co. v. Imperial Contracting Co. (1989) 212 Cal.App.3d 712
125. Maryland Casualty Co. v. National American Ins. Co. (1996) 48 Cal.App.4th 1822

126. Maryland Casualty Co. v. Nationwide Mutual Ins. Co. (2000) 81 Cal.App.4th 1082
127. Maryland Casualty Co. v. Reeder (1990) 221 Cal.App.3d 961
128. Maya v. Centex (2011) 658 F.3d 1060 (9th Cir. 2011)
129. McCrary Construction Co. v. Metal Deck Specialists, Inc. (2005) 133 Cal.App.4th 1528
130. McMillan Albany, LLC v. Superior Court (2018) WL 456728
131. McMillin Management Services, L.P. v. Financial Pacific Ins. Co. (2017) 17 Cal.App.5th 187
132. Montgomery Ward & Co., Inc. v. Imperial Casualty & Indemnity Co. (2000) 81 Cal.App.4th 356
133. Monticello Insurance Co. v. Essex Insurance Co. (2008) 162 Cal.App.4th 1376
134. Montrose Chemical Corp. v. Admiral Ins. Co. (1995) 10 Cal.4th 645
135. Montrose Chemical Corp. v. Superior Court (1993) 6 Cal.4th 287
136. Najera v. Huerta (2011) 191 Cal.App.4th 872
137. National Union Fire Ins. Co. v. Nationwide Ins. Co. (1999) 69 Cal.App.4th 70
138. Nemecek & Cole v. Horn (2012) 208 Cal.App.4th 641
139. Osborne v. Todd Farm Service (2016) 247 Cal.App.4th 43
140. Otay River Constructors v. San Diego Expressway (2008) 158 Cal.App.4th 796
141. Pacific Employers Ins. Co. v. Domino's Pizza, Inc. (9th Cir. 1998) 144 F.3d 1270

- 142. Pacific Rim Mechanical Contractors v. AON Risk Ins. Services West (2012) 203 Cal.App.4th 1278
- 143. Padilla Const. Co. v. Transportation Ins. Co. (2007) 150 Cal.App.4th 984
- 144. Pardee Construction Co. v. Ins. Co. of the West (2000) 77 Cal.App.4th 1340
- 145. Park Woods Community Association v. California Insurance Guarantee Association (2006) 141 Cal.App.4th 1362
- 146. People v. Sanchez (2016) 63 Cal.4th 664
- 147. Pepperell v. Scottsdale Ins. Co. (1998) 62 Cal.App.4th 1045
- 148. Perry v. Hawthorne (2017) WL712748
- 149. Picerne Construction Corp. v. Castellino Villas (2016) 244 Cal.App.4th 1201
- 150. Pine Terrace Apartments, L.P. v. Windscape, LLC (2009) 170 Cal.App.4th 1
- 151. Pines of LaJolla Homeowners Association v. Industrial Indemnity (1992) 5 Cal.App.4th 714
- 152. Pinnacle Museum Tower Association v. Pinnacle Market Development (2012) 55 Cal.4th 223
- 153. Presley Homes, Inc. v. American States Ins. Co. (2001) 90 Cal.App.4th 571
- 154. Prichard v. Liberty Mutual Ins. Co. (2010) 84 Cal.App.4th 890
- 155. Provost v. Regents of the University of California (2011) 201 Cal.App.4th 1289
- 156. Prudential-LMI Commercial Ins. Co. v. Reliance Ins. Co. (1994) 22 Cal.App.4th 1508

157. Puerta v. Torres (2011) 195 Cal.App.4th 1267
158. Pulte Home Corp. v. American Safety & Indemnity Co. (2017) 14 Cal.App.5th 1086
159. Qualcomm, Inc. v. Certain Underwriters at Lloyds, London (2008) 161 Cal.App.4th 184
160. Radford v. Shehorn (2010) 187 Cal.App.4th 852
161. Rael v. Davis (2008) 166 Cal.App.4th 1608
162. Rafiero v. American Employers Ins. Co. (1970) 5 Cal.App.3d 799
163. Ranchwood Communities Ltd. Partnership v. Jim Beat Construction (1996) 49 Cal.App.4th 1397
164. Ray v. Goodman (2006) 142 Cal.App.4th 83
165. Regalado v. Callaghan (2016) 3 Cal.App.5th 582
166. Regional Steel Corporation v. Liberty Surplus Insurance Corporation (2014) 226 Cal.App.4th 1377
167. Reliance Ins. Co. v. St. Paul Surplus Lines Ins. (4th Cir. 1985) 753 F.2d 1288
168. Ringler Assocs. Inc. v. Maryland Cas. Co. (2000) 80 Cal.App.4th 1165
169. Roberts v. Assurance Co. of America (2008) 163 Cal.App.4th 1398
170. Rosen v. State Farm General Insurance Co. (2003) 30 Cal.4th 1070
171. Rossmoor Sanitation, Inc. v. Pylon, Inc. (1975) 13 Cal.3d 622
172. Safari Associates v. Superior Court (2014) 231 Cal.App.4th 1400

- 173. Safeco Insurance Company of America v. Superior Court (2006) 140 Cal.App.4th 874
- 174. St. Paul Fire & Marine Insurance Co. v. American Dynasty Surplus Lines (2002) 101 Cal.App.4th 1038
- 175. St. Paul Mercury Insurance Co. v. Mountain West Farm Bureau Mutual Insurance Co. (2012) 210 Cal.App.4th 645
- 176. Sargon Enterprises, Inc. v. University of Southern California (2012) 55 Cal.4th 747
- 177. Scottsdale Insurance Company v. Essex Insurance Company (2002) 98 Cal.App.4th 86
- 178. Scottsdale Insurance Co. v. MV Transportation (2005) 36 Cal.4th 643
- 179. Select Ins. Co. v. Sup.Ct. (Custer) (1990) 226 Cal.App.3d 631
- 180. Shade Foods, Inc. v. Innovative Products Sales & Marketing (2000) 78 Cal.App.4th 847
- 181. Shell Oil Co. v. Winterthur Swiss Ins. Co. (1993) 12 Cal.App.4th 715
- 182. Signal Companies, Inc. v. Harbor Ins. Co. (1980) 27 Cal.3d 359
- 183. State of California v. Continental Insurance Company (2017) 15 Cal.App.5th 1017
- 184. State Ready Mix, Inc. v. Moffatt & Nichol (2015) 232 Cal.App.4th 1227
- 185. Stonelight Tile v. CIGA (2007) 150 Cal.App.4th 19
- 186. Stonewall Ins. Co. v. City of Palos Verdes Estates (1996) 46 Cal.App.4th 1810

187. Tidwell Enterprises, Inc. v. Financial Pacific Insurance Co. (2016) 6 Cal.App.5th 100
188. Tillman v. K. Hovnanian Communities, Inc. (2012) Cal.App. (Unpub. Lexis 5919)
189. Tiri v. Lucky Chances, Inc. (2014) 226 Cal.App.4th 231
190. Toro Enterprises, Inc. v. Pavement Recycling Systems, Inc. (2012) 205 Cal.App.4th 954
191. Transcontinental Ins. Co. v. Insurance Co. of State of Penn. (2007) 148 Cal.App.4th 1296
192. Traveler's Casualty & Surety Co. v. Transcontinental Insurance Co. (2004) 122 Cal.App.4th 949
193. Truck Ins. Exchange v. Unigard Ins. Co. (2000) 79 Cal.App.4th 966
194. UDC Development, LP v. CH2M Hill (2010) 181 Cal.App.4th 10
195. Underwriters of Interest Subscribing to Policy Number A15274001 v. ProBuilders Specialty Insurance, Co. (2015) 241 Cal.App.4th 721
196. Valley Crest Landscape Development, Inc. v. Mission Pools of Escondido, Inc. (2015) 238 Cal.App.4th 468
197. Vandenberg v. Superior Court (Centennial Ins. Co.) (1999) 21 Cal.4th 815
198. Vons Companies v. United States Fire Ins. Co. (2000) 78 Cal.App.4th 52
199. Wagner Construction v. Pacific Mechanical Corp. (2007) 41 Cal.4th 19
200. Waller v. Truck Ins. Exchange (1995) 11 Cal.4th 1
201. Watt Industries, Inc. v. Zurich American Ins. Co. (2004) 121 Cal.App.4th 1029

- 202. Wausau Underwriters Ins. Co. v. Unigard Security Ins. Co. (1998) 68 Cal.App.4th 1030
- 203. Weseloh Family Limited Partnership v. K.L. Wessel Construction (2004) 125 Cal.App.4th 152
- 204. Western Employers Ins. Co. v. Arciero & Sons (1983) 146 Cal.App.3d 1027
- 205. Zamora v. Lehman (2013) 214 Cal.App.4th 193
- 206. Ziani Homeowner's Association v. Brookfield Ziani, LLC (2015) 243 Cal.App.4th 274
- 207. CACI 1009(B)
- 208. CACI 3926
- 209. California Business & Professions Code Section 7031
- 210. California Civil Code Section 583.310
- 211. California Civil Code Section 583.340(b)
- 212. California Civil Code Section 895
- 213. California Civil Code Section 896
- 214. California Civil Code Section 897
- 215. California Civil Code Section 910
- 216. California Civil Code Section 911
- 217. California Civil Code Section 912

- 218. California Civil Code Section 914
- 219. California Civil Code Section 930
- 220. California Civil Code Section 936
- 221. California Civil Code Section 938
- 222. California Civil Code Section 1542
- 223. California Civil Code Section 1633.9(a)
- 224. California Civil Code Section 1717
- 225. California Civil Code Section 2778
- 226. California Civil Code Section 2782
- 227. California Civil Code Section 2860
- 228. California Civil Code Section 2860(c)
- 229. California Civil Code Section 3115
- 230. California Civil Code Section 3434
- 231. California Civil Code Section 8412
- 232. California Code of Civil Procedure Section 337
- 233. California Code of Civil Procedure Section 337.15
- 234. California Code of Civil Procedure Section 387

- 235. California Code of Civil Procedure Section 411.35
- 236. California Code of Civil Procedure Section 437c(c)
- 237. California Code of Civil Procedure Section 437c(d)
- 238. California Code of Civil Procedure Section 473(b)
- 239. California Code of Civil Procedure Section 664.7
- 240. California Code of Civil Procedure Section 877
- 241. California Code of Civil Procedure Section 887
- 242. California Code of Civil Procedure Section 998
- 243. California Code of Civil Procedure Section 1032
- 244. California Code of Civil Procedure Section 1033
- 245. California Code of Civil Procedure Section 1033.5
- 246. California Code of Civil Procedure Section 2034.210
- 247. California Evidence Code Section 1115
- 248. California Evidence Code Section 1119
- 249. California Evidence Code Section 1123
- 250. California Evidence Code Section 1401
- 251. California Insurance Code Section 22
- 252. California Insurance Code Section 250

- 253. California Insurance Code Section 530
- 254. California Insurance Code Section 11580
- 255. California Labor Code Section 2750
- 256. California Labor Code Section 2750.5

**OVERVIEW OF COMMON ISSUES
IN CONSTRUCTION DEFECT CLAIMS**

1. DISTINCTION BETWEEN “DEFECT” AND “PROPERTY DAMAGE”

A. In order to trigger coverage under a liability policy, an “occurrence” giving rise to “property damage” within the policy period must take place. “Property damage” has been defined as “physical injury to tangible property . . .”

B. The timing of an accident or other event causing the property damage (i.e., the negligent work of the insured) is largely immaterial to establishing coverage; it can occur before or during the policy period. Neither is the date of discovery of the property damage controlling; it might or might not be contemporaneous with the causal event. It is only the *effect* of that occurrence (i.e., the occurrence of property damage during the policy period) that triggers potential coverage.

Montrose Chemical Corp. v. Admiral Ins. Co. (1995) 10 Cal.4th 645;
Stonelight Tile v. CIGA (2007) 150 Cal.App.4th 19.

C. Continuing or progressive property damage is deemed to occur over the entire process of the continuing injury. Whether property damage is in fact “continuous” is a matter to be determined by the trier of fact.

Montrose Chemical Corp. v. Admiral Ins. Co., *supra*;
Pepperell v. Scottsdale Ins. Co. (1998) 62 Cal.App.4th 1045;
Stonelight Tile v. CIGA, *supra*.

D. The mere presence or incorporation of defective materials or “work” of the insured does not constitute “property damage” covered by policies of liability insurance issued to contractors.

Armstrong World Industries, Inc. v. Aetna Casualty & Surety Co. (1996) 45 Cal.App.4th 1;
F&H Construction v. ITT Hartford Insurance Co. (2004) 118 Cal.App.4th 364;

Watts Industries, Inc. v. Zurich American Ins. Co. (2004) 121 Cal.App.4th 1029.

E. The phrase, “legally obligated to pay damages,” as used in the policy’s grant of coverage, does not necessarily preclude coverage for losses pled as arising from breach of contract. The focus of coverage is on the nature of the property, the injury, and the risk that caused the injury, rather than the form of action pled.

Shade Foods, Inc. v. Innovative Products Sales & Marketing (2000) 78 Cal.App.4th 847;

Vandenberg v. Superior Court (Centennial Ins. Co.) (1999) 21 Cal.4th 815;

Waller v. Truck Ins. Exchange (1995) 11 Cal.4th 1.

F. A homeowner may not recover the cost of repair of, or the diminished value attributable to, proven construction defects that have not caused property damage.

Aas v. Superior Court (2000) 24 Cal.4th 627;

Rosen v. State Farm General Insurance Co. (2003) 30 Cal.4th 1070.

G. California Civil Code Section 895, et seq., (“SB 800”) the so called “fix it” law effective January 1, 2003 expressly provides that with respect to residential construction, defects are defined as set forth in Civil Code Section 896 and said defects do not require appreciable “property damage.” The holding in Aas is expressly superseded for construction completed on or after January 1, 2003.

1. The Civil Code sections have three main impacts with respect to construction defect litigation. First, the statutes establish functionality requirements by defining what a construction defect is. The following are typical examples of the new code definitions:

(a) Foundations. Foundations will not allow water or vapor to enter the structure and damage another building component. Foundations shall be constructed to materially comply with design criteria set by applicable building codes, regulations, and ordinances for chemical deterioration or corrosion in effect at the time of the original construction.

California Civil Code Section 896(a)(7);
California Civil Code Section 896(b)(3).

(b) Framing / Structure. The building shall be constructed to materially comply with design criteria for earthquake and wind load resistance as set forth in the applicable government building codes, regulations and ordinances in effect at the time of the original construction.

California Civil Code Section 896(b)(4).

2. The statutes provide meet and confer guidelines concerning the builder's right to fix alleged defects and specifically provides time limits in which to respond to a claim (14 days) and the time allowed for inspections and the repair of the property (14 days and 30 days, respectively). Under these new statutes, the builder maintains the right to offer alternative dispute resolution options such as arbitration and judicial reference.

3. The new statutes have significant procedural and legal modifications.

(a) As the Aas decision is largely abrogated by Civil Code Section 896, there is no need to establish resulting property damage. Mere failure to comply with performance standards is enough to sustain a defect claim.

(b) The standards do not require breach of contract and may be enforced either by homeowners' associations or an individual homeowner of a single home.

(c) With respect to Statute of Limitations issues, the three-year discovery statute and four-year patent defect statute no longer apply to claims for violations of the standards. All claims must instead be brought within ten years following substantial completion unless otherwise specified. There are, however, new statutes of limitations for various "minor components" such as inner-unit noise transmission, operation of electrical systems, and the like. They are specified as one and two year statute of limitations.

California Civil Code Section 896.

H. Disclosure requirements of SB 800 do not apply to builders who opt out of SB 800's pre-litigation procedures in favor of their own procedures.

1. Plaintiff sued developer for defects arising from the construction of 32 homes. Developer sought compliance with Civil Code Section 895 et seq. and plaintiffs asserted that developer had failed to comply with the disclosure requirements of Civil Code Section 912, thereby relieving plaintiffs of the duty to comply with the Right to Repair Act. Developer opposed plaintiffs' motion on the basis that the disclosure provisions of Civil Code Section were inapplicable as the purchase and sell agreements provided for an opt out of such provisions in favor of developer's own disclosure provisions. Under Civil Code Section 914(a), a builder can opt out of the statutory procedures in favor of its own alternative procedures, as long as the builder notifies the homeowner of its intent to use alternative non-adversarial contract provisions. The Fifth District Court of Appeal held that a builder who opts out of SB 800's statutory pre-litigation procedures in favor of its own purchase and sale contractual procedures opts out of the entirety of SB 800's pre-litigation procedures, meaning that the disclosure provisions of Civil Code Section 912 do not apply to that builder. Accordingly, builder had no obligation to comply with the disclosure requirements, and plaintiffs were required to comply with the builder's remaining pre-litigation procedures before continuing to prosecute their construction defect action.

Baeza v. Superior Court (2011) 201 Cal.App.4th 1214.

2. In an unpublished decision, the Fourth Appellate District of the Court of Appeal asserted plaintiffs must comply with SB 800 pre-litigation procedures or alternative agreed upon procedures with builders before filing a lawsuit. Plaintiff homeowners filed a construction defect lawsuit against defendants. Defendants moved to dismiss the stated action on the grounds that the plaintiffs purchased their homes after January 1, 2003 and were thus subject to SB 800 procedures. Pursuant to Civil Code Section 914, defendant developers elected to use an alternative contractual non-adversarial procedure via its limited warranty, which defendants recorded and which required homeowners to provide written notice of defects, and an opportunity to repair, mediate and arbitrate. Plaintiffs challenged defendants' compliance with these pre-litigation procedures. The trial court granted the defendants' motion to dismiss without prejudice. In an unpublished decision, the court, citing Baeza v. Superior Court (2011) Cal.App.4th 1214, noted that under the Right to Repair Act, a builder has the option of contracting for an alternative contractual non-adversarial procedure in lieu of statutory

procedures. In this case, because defendants elected that contractual procedures be a warranty, plaintiffs were not entitled to the statutory procedures.

Tillman v. K. Hovnanian Communities, Inc. (EO52173) (2012 Cal.App.Unpub. Lexis 5919).

3. Builder may halt construction defect lawsuit and withhold requested documents where a homeowner failed to serve builder with pre-litigation notice of complaint.

Pursuant to a writ from the trial court, the California Court of Appeal, First Appellate District, determined the question of whether a homeowner must serve notice of a construction defect claim under Civil Code Section 910(a) for a builder to be obligated to respond to their request for documents under Civil Code Section 912(a). The court concluded that the homeowner must serve a notice of a construction defect claim under Civil Code Section 910 to commence the statutory pre-litigation procedure, and until such service, the builder has no obligation to respond to a request for documents under any other sections of the SB 800 Right to Repair Act. Typically, if the homeowner files a lawsuit before the pre-litigation procedure is completed, a builder may obtain a stay of the lawsuit pursuant to Civil Code Section 930(b). However, if that builder fails to comply with the requirements of the pre-litigation procedure, the homeowner may proceed with a lawsuit without completing the pre-litigation process pursuant to Civil Code Section 930(a) and 912(i).

Darling v. Superior Court (2012) 211 Cal.App.4th 69.

I. Homeowners may sue developers for decreased value and desirability of their homes.

The plaintiffs were homeowners who purchased homes from developers between 2004 and 2006. The plaintiffs allege that over time, the value of their homes decreased not solely because of the national housing crises, but also because developers' conduct created a negative impact upon the homeowners' neighborhoods. The plaintiff homeowners specifically contended that the developers had represented that they would sell houses to buyers who could be expected to afford them and would be stable neighbors. Plaintiffs further contended that the developers marketed the neighboring homes to unqualified buyers who posed a high risk of foreclosure and abandonment of

their homes, and they therefore misrepresented the character of the neighborhoods to the plaintiff buyers. Developers contended that the homeowners lacked standing to sue as they failed to allege concrete, particularized, and actual injury caused by developers. The U.S. District Court, Central District of California, dismissed the complaint and denied homeowners' request to amend. The Ninth Circuit Court of Appeals reversed, holding that the alleged damages were actual and concrete economic injuries, and that homeowners of large subdivisions have standing to sue developers for the decreased value and desirability of their homes.

Maya v. Centex (2011) 658 F.3d 1060 (9th Cir. 2011).

J. The California Supreme Court has concluded that SB 800 (“The Right to Repair Act”) is the only remedy for construction defect claims arising out of new residences sold after January 1, 2003.

In the very recent holding of McMillan Albany, LLC v. Superior Court (2018) WL 456728, the California Supreme Court discussed at length the legislative intent of SB 800 and the holding in the Liberty Mutual Insurance Co. v. Brookfield Crystal Cove, LLC (2013) 219 Cal.App.4th 98 case. The McMillan court expressly concluded that the legislature intended that all claims arising out of defects in residential construction, involving new residences sold on or after January 1, 2003 (Civil Code Section 938) be subject to the standards and requirements of the Act; the homeowner bringing such a claim must give notice to the builder and engage in the pre-litigation procedures in accordance with the provisions of Chapter 4 of the Act prior to filing suit in court. Where the complaint alleges deficiency in construction that constitutes violation of the standards set out in Chapter 2 of the Act, the claims are subject to the Act, and the homeowner must comply with the pre-litigation procedures, regardless whether the complaint expressly alleges a cause of action under the Act. The Act is the exclusive remedy for residential construction defect claims so plaintiffs must comply with Act’s pre-litigation notice, inspection, and repair procedures. The McMillan decision thoroughly analyzed the plain language, statutory scheme, and legislative history of the Act and reached the conclusion that Liberty Mutual misinterpreted the Act and held that where the complaint alleges deficiencies in construction that constitute violation of the standards set forth in Civil Code Sections 896-897, the claims are subject to the Act. The court concluded that for economic losses, the Legislature intended to supercede Aas, and provide a statutory basis for recovery. For personal injuries, the Legislature preserved the status quo, retaining the common law as an avenue for recovery, and for property

damage, the Legislature replaced the common law methods of recovery with the new statutory scheme. The Act, in effect, provides that construction defect claims not involving personal injury would be treated the same procedurally going forward whether or not the underlying defects gave rise to any property damage. The court expressly disapproved of the holding in Liberty Mutual Ins. Co. v. Brookfield Crystal Cove, LLC, *supra*, 219 Cal.App.4th 98.

K. The California Appellate Court (Fourth District) has held that claims against a material supplier under SB 800 (Civil Code, Sections 895 and 936) require proof that the SB 800 violation was caused by the supplier's negligence or breach of contract. In the instant case, an HOA sued MWI, a supplier of Chinese pipe used in the construction of the condominium development. The HOA's complaint asserted a single cause of action for violation of SB 800 standards, and alleged that the defective cast iron pipe was used throughout the building. After trial, the trial court entered a judgment against MWI in excess of \$23,000,000, reflecting the jury's finding that MWI was 92 percent responsible for the HOA's damages. The matter was appealed, and the Court of Appeal reversed and ordered the trial court to enter a judgment in favor of MWI. The Court of Appeal relied on the legislative history of SB 800, and Greystone Homes, Inc. v. Midtec, Inc. (2008) 168 Cal.App.4th 1194, which held that the first sentence of Civil Code Section 936 contains "an explicit adoption of a negligent standard, for SB 800 claims against product manufacturers. The Court of Appeal concluded that since Civil Code Section 936 treats product manufacturers and materials suppliers identically, the holding of Greystone was equally applied to materials suppliers.

Acqua Vista Homeowners Association v. MWI, Inc. (2017) 7 Cal.App.5th 1129.

2. THE DUTIES TO DEFEND AND INDEMNIFY

A. An insurer's duty to defend an insured is broader than its duty to indemnify for a loss, but that duty is not unlimited. It extends beyond claims that are actually covered to those that are also potentially covered, in light of facts alleged or otherwise disclosed. It arises as soon as tender is made and is discharged when the action is concluded.

Manzarek v. St. Paul Fire & Marine Ins. Co. (9th Cir. 2008) 519 F.2d 1025;

Montrose Chemical Corp. v. Superior Court (1993) 6 Cal.4th 287;
Buss v. Superior Court (1999) 16 Cal.4th 35;
Buena Vista Mines, Inc. v. Industrial Indemnity Co. (2001) 87 Cal.App.4th 482.

B. An insurer's duty to indemnify runs to claims that are actually covered, in light of facts proved, and arises only after liability is established.

Montrose Chemical Corp. v. Admiral Ins. Co., supra;
Armstrong World Industries, Inc. v. Aetna Casualty & Surety Co., supra;
Qualcomm, Inc. v. Certain Underwriters at Lloyds, London (2008) 161 Cal.App.4th 184.

C. In the California Supreme Court case of Crawford v. Weathershield Manufacturing, Inc. (2008) 44 Cal.4th 541, the court addressed the issue concerning the contractual duty to defend in a non-insurance context. In particular, the court considered whether the provisions of a pre-2006 residential construction subcontract obligated the subcontractor to defend its indemnitee - the developer-builder of the project - in lawsuits brought against both parties, based on plaintiff's complaints of alleged construction defects arising from the subcontractor's negligence. Notwithstanding the fact that the jury ultimately found that the subcontractor was not negligent, and the parties accepted an interpretation of the subcontract that gave the builder no right of indemnity unless the subcontractor was negligent, the court concluded the subcontractor still had a contractual duty to defend the developer in this context.

Crawford v. Weathershield Manufacturing, Inc. (2008) 44 Cal.4th 541.

D. After the ruling in Crawford, certain subcontractors and their insurers sought to avoid the immediate duty to defend obligation in Crawford by arguing that a showing of negligence was necessary to trigger the defense obligation. Subsequently, a California Court of Appeal decision held a duty to defend is not dependent upon an allegation or a determination of negligence to trigger the duty. In the case, developer pursued its own cross-complaint for indemnity against an engineering firm after having tendered to that firm and the tender being rejected. The developer incurred its own defense costs and settled with the plaintiff HOA. At trial, the jury found that the firm was not negligent in the provision of its services. Nonetheless, the trial court ordered the firm to reimburse the developer for its defense costs related to defense of that firm's work. The Court of Appeal affirmed and expressly stated that a duty to defend arose when the developer's

cross-complaint attributed responsibility for the plaintiff's damage to the firm's deficient provision of its services for the construction project. Specifically, the court held that if the indemnity language is clear and explicit on the point, and the appropriate tender is made, the indemnitee must either defend or proceed at its own caution within the framework of Civil Code Section 2778.

UDC Development, LP v. CH2M Hill (2010) 181 Cal.App.4th 10.

E. However, even assuming the general contractor's contractual right to indemnity from the subcontractor was triggered, the contractual indemnity clause does not control the payment obligations of the parties respective insurers. The obligations are determined by the language in the applicable policies of insurance.

JPI West Coast Construction v. RJS & Associates (2007) 156 Cal.App.4th 1448.

F. In a "mixed" action (i.e., where some of the claims are at least potentially covered and the others are not), the insurer has a duty to defend the entire action. However, an insurer may obtain reimbursement of those defense costs that can be allocated solely to the non-covered claims for which a defense was provided. To do so, it must carry the burden of proof of these costs by a preponderance of the evidence.

Buss v. Superior Court (1999) 16 Cal.4th 35;
Lyons v. Fire Ins. Exchange (2008) 161 Cal.App.4th 880.

G. Insurer has no duty to defend insured for claims for work that fails to comply with building code absent property damage. After pouring concrete for a parking garage, the city notified a developer that plaintiff, a steel subcontractor had installed defective tie hooks that did not meet the building code. The affected areas had to be demolished and repaired, resulting in a claim against plaintiff for failure to comply with the subcontract and building code when it failed to install the proper tie hooks. Plaintiff tendered a defense of the claim to defendant insurer. The Second District Court of Appeal held that defendant insurer had no duty to defend plaintiff subcontractor against claims over defective tie hooks. The court specifically concluded that the defective tie hooks did not constitute property damage for the purposes of coverage because California courts have consistently held that the coverage does not exist where the only property "damage" is

the defective construction, and no other property damage has occurred. Moreover, the Impaired Property Exclusion applied and barred the possibility of coverage.

Regional Steel Corporation v. Liberty Surplus Insurance Corporation (2014)
226 Cal.App.4th 1377

H. In order to avail itself of its right to seek reimbursement of defense costs for non-covered claims, an insurer must:

1. Specifically advise the insured, in a Reservation of Rights letter, that it reserves its right to seek reimbursement of defense expenses paid for non-covered claims; and

2. Seek recovery of those defense costs by way of an action for “Declaratory Relief and Reimbursement,” specifically alleging its “implied-in-law” rights based on a claim of “unjust enrichment.”

Buss v. Superior Court, *supra*;
Scottsdale Insurance Co. v. MV Transportation (2005) 36 Cal.4th 643.

I. An insurer who defends an insured, while reserving its right to dispute coverage, may seek reimbursement from the insured for money it paid to settle a non-covered claim, even in the absence of the insured’s consent to such settlement. It may also seek reimbursement from other insurers on various equitable grounds.

Blue Ridge Ins. Co. v. Jacobson (2001) 25 Cal.4th 489;
Hartford Cas. Ins. Co. v. Mt. Hawley Ins. Co. (2004) 123 Cal.App.4th 278.

J. In an action brought by plaintiffs for construction defects, a developer was named as an additional insured on one of its subcontractor’s policies. That insurer accepted the developer’s tender of defense subject to a reservation of rights. The developer sued the subcontractor and its insurer contending that the insurer breached its duty to defend and indemnify against homeowner claims and sought immediate declaratory relief to determine the allocation of its defense fees and costs. Developer additionally argued that the insurer had breached its duty to provide a full, conflict-free defense and asserted that pursuant to Civil Code, Section 2860, developer was entitled to independent counsel. The trial court sustained the insurer’s demurrer to the complaint

and developer appealed. The Appellate Court (Fourth District) held that the declaratory relief claim brought by the developer regarding its right to reimbursement was anticipatory and not actual or ripe, and that the developer, subcontractor, and the subcontractor's carrier did not currently have any conflict of interests which required appointment of independent counsel. Further, the Court concluded that the general reservation of rights in this case did not create a significant conflict of interest requiring independent counsel.

Centex Homes v. St. Paul Fire & Marine Insurance Co. (2015) 237 Cal.App.4th 23.

K. An insurer that properly reserved rights may later recoup defense costs if it is subsequently determined that no duty to defend arose.

Scottsdale Insurance Co. v. MV Transportation (2005) 36 Cal.4th 643.

L. In an action for equitable contribution by a settling insurer against a non-participating insurer, the settling insurer has met its burden of proof, and it makes a prima facie showing of coverage by proving that there was merely a potential for coverage (the same showing necessary to trigger the duty to defend). Upon a prima facie showing, the burden of proof shifts to the non-participating insurer to prove the absence of actual coverage.

Safeco Insurance Company of America v. Superior Court (2006) 140 Cal.App.4th 874.

M. The California Supreme Court has held that an insurer has a direct right to seek reimbursement from *Cumis* counsel rather than an insured. An insurer issued general commercial liability policies to two entities. A lawsuit was subsequently filed against said entities but the insurer rejected the insureds' tender on the ground that some of the defendants were not covered insureds and that certain acts occurred before the policies inception dates. The insureds filed a coverage action against the insurer who then agreed to defend the entities subject to a reservation of rights. A trial court found that the insurer had a duty to defend the action effective the date of the original tender and that the insurer was required to appoint *Cumis* counsel to represent its insureds. The insureds retained said counsel, who then drafted an enforcement order directing the insurer to pay all defense fee and costs but allowing the carrier to challenge by way of reimbursement unreasonable or unnecessary fees and costs upon resolution of the

underlying action. The underlying case was resolved, and the coverage action resumed. In that action, the insurer filed a cross-complaint against *Cumis* counsel asserting a direct right of action pursuant to the enforcement order. Ultimately, the California Supreme Court held that equitable principles of unjust enrichment and restitution permitted the insurer to seek recovery for unreasonable and unnecessary defense fees directly from *Cumis* counsel. In a limited holding, it found that since *Cumis* counsel's enforcement order limited its recovery to "reasonable" fees and specifically reserved the insurer's right to later obtain reimbursement of excess charges, Civil Code, Section 2860(c) did not apply, and the insurer's obligation to pay for *Cumis* counsel did not extend beyond the duty to pay reasonable fees and costs.

Hartford Casualty Insurance Co. v. J.R. Marketing, LLC (2015) 61 Cal. 4th 988.

N. Right to independent counsel under California Civil Code, Section 2860 is not applicable when there is only a potential conflict of interest rather than an actual conflict of interest. After a homeowner brought a construction defect action against developer and the subcontractor's insurance carrier agreed to defend developer as additional insured (subject to a Reservation of Rights) developer filed a cross-complaint against the subcontractor and its insurer arguing that it was entitled to independent counsel under Civil Code, Section 2860 because the insurer's Reservation of Rights created significant conflicts of interest. The insurer appointed an attorney solely to represent developer and defend against the homeowner's claims. Trial court granted insurer's motion for summary adjudication denying developer's claim for independent counsel claiming that insurer had negated the existence of a conflict by its appointment of separate counsel for developer's matters.

Centex Homes v. St. Paul Fire & Marine Insurance Co. (2018) 19 Cal.App. 5th 789.

O. A subcontractor's liability insurer is potentially liable to pay any sums the contractor was legally obligated to pay the homeowner insurer for property damage even after the relevant insurance policy period ended. In the underlying case, a subcontractor participated in the construction of a house by installing a fireplace. Twenty months after the end of the last policy period for the subcontractor's general liability coverage with the insurer, the house was damaged by fire. The subcontractor brought an action for declaratory relief against the insurer who had refused to defend the subcontractor in the

underlying action brought by the homeowner's subrogating insurer, on the grounds that the fire occurred after the policies had ended. Under the applicable policies, the insurer agreed to pay sums that the subcontractor was legally obligated to pay as damages because of property damage caused by an occurrence if the property damage occurred during the policy period. The policies defined "occurrence" as an accident, including continuous or repeated exposure to the substantially same general harmful conditions. The policies further defined property damage as physical injury to tangible property. The insurer moved for summary judgment on the ground that it had no duty to defend as there is no potential or actual coverage under its policies for the claims asserted in the action. The trial court granted summary judgment in favor of the insurer. The Court of Appeal (Third District) reversed the prior judgment granting summary judgment and held that the liability insurer had a duty to defend the subcontractor. The court indicated that the liability insurer had failed to eliminate all possibilities of coverage. For example, there was a possibility that the damages were caused due to earlier physical injury to the house for which the subcontractor was responsible, and therefore there was a possibility that the damages fell within the coverage provided by the terms of the general liability policies issued by the insurer to the subcontractor.

Tidwell Enterprises, Inc. v. Financial Pacific Insurance Co. (2016) 6 Cal.App.5th 100.

Limit on Defending Insurer Liability

P. Where liability insurer provides defense to a claim asserted against insured, and settles the case without cost to the insured, carrier has no liability to insured for attorney's fees incurred paid to private counsel hired to defend insured against claim.

Lazy Acres Market, Inc. v. Tseng (2007) 152 Cal.App.4th 1431.

Supplementary Payments

Q. Most CGL policies include a "supplementary payments" provision. The clause generally requires insurers to pay the following types of expenses as a component of their defense obligations: (1) investigation expenses incurred by the insured at the insurer's request; (2) court costs awarded against the insured; and (3) pre-judgment and post-judgment interests.

Prichard v. Liberty Mutual Ins. Co. (2010) 84 Cal.App.4th 890.

R. California courts construe the "costs taxed" language of most supplementary payments provisions to include attorneys' fees awarded to the opposing party. However, the supplementary payments provision can only be utilized to pay "costs taxed," including attorneys' fees, if the insurer actually owed a duty to defend.

Employers Mut. Cas. Co. v. Philadelphia Indemnity Ins. (2008) 169 Cal.App.4th 340;

Golden Eagle Ins. Corp. v. Cen-Fed, Ltd. (2007) 148 Cal.App.4th 976.

Broker Liability

S. Insurance brokers have no duty to inform OCIP enrollees or insurers of insurer's subsequent insolvency.

General contractor engaged an insurance broker to obtain an owner controlled insurance program ("OCIP") for construction projects in San Diego. The broker procured coverage for all OCIP enrollees from Legion Insurance Company which was solvent during construction. When Legion subsequently became insolvent, the broker informed the general contractor of the same, but did not inform any of the subcontractors who had enrolled in the OCIP. A suit for construction defects was later filed against the general contractor, who cross-complained for indemnity against all of the subcontractors. The subcontractors cross-complained against the insurance broker alleging fraudulent concealment by the broker of the insurance company's insolvency. The broker claimed that as an insurance broker, it owed no duty to inform the subcontractors of the carrier's subsequent insolvency. The Fourth District Court of Appeal held that the insurance broker had no duty to inform a subcontractor of the carrier's post-issuance insolvency because insurance brokers are limited to the duty of using reasonable care in procuring the insurance requested by an insured. However, the court did further find that the general contractor had a contractual duty to inform all parties enrolled in the OCIP of the carrier's insolvency because the general contractor had contracted with and been informed by the insurance broker of the insolvency.

Pacific Rim Mechanical Contractors v. AON Risk Ins. Services West (2012) 203 Cal.App.4th 1278.

3. POLICY EXCLUSIONS

An insured cannot avoid policy exclusions by mischaracterizing the event causing loss.

Plaintiffs purchased an undeveloped lot intending to build a home and their lender required that they first obtain a Course of Construction insurance policy. During construction, a landslide occurred causing substantial damage to the property. The carrier denied the claim because it determined that the damage was caused by earth movement which was excluded from the policy. Plaintiffs conceded the earth movement was excluded, but they argued that the developer had negligently concealed evidence of a potential landslide and that this act of development negligence was covered. The court rejected the argument finding that the concealment by the developer was not a separate cause for the loss, but merely a separate explanation for the single cause of loss, i.e., earth movement.

Roberts v. Assurance Co. of America (2008) 163 Cal.App.4th 1398.

The following exclusions are those typically considered when determining whether an insurer has a duty to indemnify for a loss.

The “Loss In Progress” Exclusion

A. The “Loss In Progress” or “Known Loss” exclusion is in reality a rule which holds that once an insured becomes aware of damages which form the basis of a claim, that loss is no longer “fortuitous” and the damages not “unexpected.”

B. However, application of the “Loss In Progress” rule in third-party liability claims has been criticized and narrowly enforced.

1. For example, a developer’s knowledge of one defect or set of defects (plumbing leaks, cracks in unit slabs, and window leaks) in units of a development prior to sale was held not equivalent to knowledge of other, distinct defects discovered after sale of the units (slope and drainage problems, decaying stucco, and problems with exterior plumbing).

Chu v. Canadian Indemnity Co. (1990) 224 Cal.App.3d 86;

Pines of LaJolla Homeowner's Association v. Industrial Indemnity (1992) 51 Cal.App.4th 714 (reversed on other grounds).

C. However, standard “known loss” provisions have not proven particularly helpful in construction defect actions, particularly given the broad duty to defend. Furthermore, in these types of actions, when the damage is “known” will not be clear as of the date of the tender, such that the “known loss” provisions are generally left to matters involving reservation of rights.

D. There is no published authority in California that interprets and applies the standard ISO “known loss” provisions. In certain out-of-state decisions addressing the scope and application of the “known loss provisions” the United States District Court in applying Florida and Georgia law has essentially stated that language of the known loss must be applied to each specific aspect of “property damage” and doesn’t generally encompass the global concept, i.e., based on individual defects “known” to the insured.

CEG Essex Insurance Co. v. H&H Land Development Corporation (MD Georgia 2007) 525 F.Supp.2d 1344.

The “Work Performed” and “Product” Exclusions

A. These two exclusions, commonly combined and referred to as the “work-product” exclusion, eliminate coverage for property damage to the insured’s own work or product, but will not preclude coverage for damage caused by the negligence of other subcontractors, or to other property not the work or product of the insured.

Hillenbrand, Inc. v. Insurance Co. of North America (2002) 104 Cal.App.4th 784;

Western Employers Ins. Co. v. Arciero & Sons (1983) 146 Cal.App.3d 1027;

Insurance Co. of North America v. National American Ins. Co. (1995) 37 Cal.App.4th 195.

1. Deficiencies in roofing, drainage systems, structural elements, water leaks, and inadequate foundations have been held to comprise part of the “work-product” of a developer and general contractor, thus precluding coverage for damages arising from those defects.

Diamond Heights Homeowners Association v. National American Ins. Co. (1991) 227 Cal.App.3d 563;

Baroco West, Inc. v. Scottsdale Insurance Co. (2003) 110 Cal.App.4th 96.

2. Coverage for a general contractor who built an apartment building and furnished and installed allegedly defective roofs, hot water and electrical heaters, and windows, did not apply because the damage was due to “. . . work completed by or for the named insured, out of which the accident arises . . .”

Rafiero v. American Employers Ins. Co. (1970) 5 Cal.App.3d 799.

3. Allegations of inadequate structural design, defective soils beneath structures, defective doors, roofs and ceilings, and defective wall systems did not give rise to coverage for a developer/general contractor for “(o) . . . property damage to work performed by or on behalf of the named insured arising out [of] the work or any portion thereof, or out of materials, parts or equipment furnished in connection therewith . . .”

Maryland Casualty Co. v. Imperial Contracting Co. (1989) 212 Cal.App.3d 712.

B. Whereas the usual Completed Operations coverage, with no Broad Form Property Damage endorsement attached, flatly excludes property damage to work performed *by or on behalf of the named insured* arising out of the work, the Broad Form Property Damage endorsement only excludes coverage for work performed *by the named insured*. In such cases, damages arising out of work performed on behalf of the named insured would be covered. Thus, where the named insured is the developer or general contractor who hires the subcontractors, and the subcontractors’ work causes damage, the named insured would be covered for the work performed on its behalf by its subcontractors.

Blackhawk Corp. v. Gotham Ins. Co. (1997) 54 Cal.App.4th 1090;

Maryland Casualty Co. v. Reeder (1990) 221 Cal.App.3d 961;

Prudential-LMI Commercial Ins. v. Reliance Ins. Co. (1994) 22 Cal.App.4th 1508.

C. The question whether a policy contains “Broad Form” coverage appears largely moot under policies comprised of the Commercial General Liability Coverage

Form issued by the Insurance Services Office (ISO) after November, 1985, as amended. Standard Policy Form No. CG 00 01 01 04 states that the policy does not apply to:

* * *

“Property damage” to “your work” arising out of it or any part of it and included in the “products-completed operations hazard.” *This exclusion does not apply if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor.* (Emphasis added)

The “Impaired Property” Exclusion

A. The current ISO CGL form contains an exclusion for “. . . ‘property damage’ to the ‘impaired property’ or property that has not been physically injured, arising out of a defect, deficiency, inadequacy, or dangerous condition in your ‘product’ or ‘your work.’”

1. For example, if the insured installed stucco (its “product”) that cracked and flaked off, and which did not cause or contribute to other damage to the structure, coverage would be precluded under this type of exclusion.

2. The exclusion does not apply where other property has been physically injured.

Watt Industries, Inc. v. Zurich American Ins. Co. (2004) Cal.App.4th 1029.

B. A condominium project has been held not to be the “product” of the developer of the project, thus making the exclusion inapplicable where the insured was the developer or builder.

Maryland Casualty Co. v. Reeder, *supra*.

The “Incorrectly Performed Work” Exclusion

A. Under this exclusion, the policy does not provide coverage for property damage to “[t]hat particular part of any property that must be restored, repaired or replaced because ‘your work’ was incorrectly performed on it . . .”

1. For example, when a subcontractor returns to the project to perform repairs to or service on his prior work, damage caused by this subsequent work to the prior work would be excluded.

B. This exclusion is the successor to the “faulty workmanship” exclusion and differs from its predecessor in two important aspects:

1. First, the new exclusion applies to work being performed either *on or off* the insured’s premises, whereas the old exclusion applied only to property *away from* the premises owned by or rented to the insured;

2. Second, the new exclusion makes clear it does not apply to property damage within the “products-completed operations hazard,” whereas it was unclear whether the “faulty workmanship” exclusion did or did not apply to the insured’s completed operations.

The “Owned Property” Exclusion

A. This exclusion precludes coverage for “. . . ‘property damage’ to . . . property you own . . .”

B. This exclusion is rarely applicable in construction defect cases, since a contractor does not usually “own” the property in question, and “ownership” of materials used or furnished by the contractor are generally transferred to the owner upon completion of the contractor’s work.

C. However, the exclusion may preclude coverage for a developer who “owned” the property if damage occurs before its sale to others. The exclusion has been upheld in cases involving pollution and environmental contamination issues.

D. No California case has interpreted the “Owned Property” exclusion in the context of a construction defect case.

E. The “owned property” exclusion comes up more frequently in the environmental claims area.

Shell Oil Co. v. Winterthur Swiss Ins. Co. (1993) 12 Cal.App.4th 715.

The “Alienated Premises” Exclusion

A. Standard general liability policies contain exclusions for property damage to “. . . premises alienated by the named insured arising out of such premises or any part thereof,” or, in later policies, property damage to “. . . [p]remises you sell, give away or abandon, if the ‘property damage’ arises out of any part of those premises. . . . This exclusion does not apply if the premises are ‘your work’ and were never occupied, rented, or held for rental by you.”

B. As the exclusion makes clear, where an insured is not an owner of the property, the exclusion does not apply. Moreover, under the later exclusionary language, it does not apply to the typical completed operations of an insured developer or contractor, as those operations would qualify as the insured’s “work,” and the property was never intended to be “occupied, rented, or held for rental” by the insured, but was built for resale.

Prudential-LMI Commercial Ins. v. Reliance Ins. Co. (1994) 22 Cal.App.4th 1508.

The “Contractual Liability” Exclusion

A. The 1988 standard ISO CGL policy’s contractual liability exclusion provides that coverage will not apply to property damage “. . . for which the insured is obligated to pay as damages by reason of the assumption of liability in a contract or agreement.” However, the exclusion then states it does not apply to damages “(1) [a]ssumed in a contract or agreement that is an ‘insured contract’ . . .”

B. The term “insured contract” has been defined to include “. . . [t]hat part of any contract or agreement pertaining to your business . . . under which you assume the tort liability of another to pay for . . . ‘property damage’ to a third person or organization. . . . Tort liability means a liability that would be imposed by law in the absence of any contract or agreement.” This would include a construction subcontract which obligates

the subcontractor to indemnify, defend and hold harmless the general contractor and/or owner.

C. A California Supreme Court case has held that the phrase, “legally obligated to pay damages,” found in the insuring agreement of a CGL policy, provides coverage for damages arising from breach of contract, not just for damages based on tort.

Golden Eagle Ins. Co. v. Insurance Co. of the West (2002) 99 Cal.App.4th 837;

Vandenberg v. Superior Court (Centennial Ins. Co.) (1999) 21 Cal.4th 815;

The “Joint Venture” Exclusion

A. This exclusion, usually contained in the policy’s definition of, “Who Is An Insured,” provides that coverage does not apply to property damage “. . . arising out of the conduct of any partnership or joint venture of which the insured is a partner or member and which is not designated in this policy as a named insured.”

B. There is scant California decisional authority on the application and interpretation of the “joint venture exclusion.” In one case, the court found that whether the insured built the condominium project as a joint venture which was not listed as such on the policy was a matter to be determined by the trier of fact.

Maryland Casualty Co. v. Reeder (1990) 221 Cal.App.3d 961;

The “Subsidence” Exclusion

A. Neither the 1986 or later standard ISO CGL policies contain earth movement and/or subsidence exclusions, which are usually endorsed to the policy by way of manuscript language.

B. An endorsement which precluded coverage for property damage “. . . caused by, resulting from, contributed to or aggravated by ‘subsidence’ and arising out of or attributable to any ‘operations’ of the insured . . .” was upheld as eliminating coverage for a developer who constructed and graded unimproved lots which were later sold to building contractors. Subsidence was defined to include “earth movement, including but not limited to . . . earth sinking, earth rising or earth shifting.” The term “operations” was defined as “any act, error or omission on the part of the insured, including but not limited to improper grading or site preparation, error in design, faulty materials or faulty workmanship.”

The exclusion applies to damage attributable to any “operations” of the insured. This is broad enough to include work by the insured’s subcontractors as well as its own employees. Thus, the independent contractors’ negligence in performing the grading operations for the developer were thus acts or omissions “on the part of the insured.”

Blackhawk Corp. v. Gotham Ins. Co. (1997) 54 Cal.App.4th 1090.

The “Montrose” Exclusion

A. In response to the California Supreme Court’s decision of Montrose Chemical Corporation v. Admiral Ins. Co., *supra.*, insurers have attempted to preclude coverage for damages commencing prior to the inception of a policy but arguably continuing through the policy period. Such exclusions are commonly known as “Montrose” exclusions.

B. Whether coverage exists for losses commencing before the current policy period and continuing into the policy period is subject to interpretation of the “Loss in progress” rules. California Insurance Code §§ 22 and 250 provide that only “contingent or unknown” risks are insurable. This phrase was interpreted by the Montrose Court to mean that insurance cannot be obtained for a known liability, but liability coverage may

exist where there is uncertainty about the imposition of liability and no legal obligation to pay has yet been established.

C. Under the current CGL form, there is no coverage for bodily injury or property damage beginning before the policy period if “known to the insured,” even if such injury or damage continues during the policy period (e.g., pollution claims). [CG 00 01 12 04, Sec. I, Coverage A, ¶ 1.b.(3)] Bodily injury or property damage is “known” to the insured if the insured or any agent or employee *authorized* to give or receive notice of a claim:

1. Reports the injury or damage to an insurer; or (2) receives a written or verbal demand or claim for damages because of bodily injury or property damage; or becomes aware by any other means that bodily injury or property damage has occurred or has begun to occur. [CG 00 01 12 04, Sec. I, Coverage A, ¶ 1.d.] This language does not appear in pre-2001 CGL forms.

D. For example, one endorsement entitled, “Pre-Existing Damage Exclusion,” eliminates coverage for “. . . [a]ny damages arising out of or related to . . . ‘property damage’ . . . [¶] (a) which first occurred prior to the inception date of this policy . . . ; or [¶] (b) which is, or is alleged to be, in the process of occurring as of the inception date of this policy . . . even if the ‘occurrence’ continues during this policy period. . .”

E. The current CGL provision redefines the “known loss rule” to exclude coverage for losses which existed before the policy period even if no liability or obligation to pay had yet been imposed. Policyholders may argue that Montrose cannot be avoided in California by a CGL policy provision because Montrose is an interpretation of California statutes (Ins. C. §§ 22, 250) defining the “known loss rule.” Courts have previously held that Policy provisions contrary to California statutes have been unenforceable. The more convincing argument is that insurers are free to limit coverage in any way they choose as long as the limitation satisfies the plain, clear and conspicuous standard under California law.

F. Another example of an attempted “Montrose” exclusion precludes coverage for “property damage” that was “. . . known to **you**, any additional insured, or anyone working on **your** behalf; and/or [¶] reported to **you**, any additional insured, or anyone working on **your** behalf, before the inception date of this policy . . .”

G. California courts have yet to determine the application and viability of any “Montrose” exclusion.

“Ongoing Operations” Limitation of Additional Insured Endorsement

The Additional Insured Endorsement Form promulgated by the Insurance Services Office, Inc. (“ISO”) 2004 Edition states in pertinent part as follows:

“A. Section II -- Who Is An Insured is amended to include as an additional insured the person(s) or organization(s) shown in the Schedule [or to whom the named insured agrees in a written contract to include as an additional insured], but only with respect to liability for “bodily injury”, “property damage” or “personal and advertising injury” caused, in whole or in part, by:

1. Your acts or omissions; or
2. The acts or omissions of those acting on your behalf;

in the performance of your ongoing operations for the additional insured(s) at the location(s) designated above.

B. With respect to the insurance afforded to these additional insureds, the following additional exclusions apply:

This insurance does not apply to “bodily injury” or “property damage” occurring after:

1. All work, including materials, parts, or equipment furnished in connection with such work, on the project (other than service, maintenance or repairs) to be performed by or on behalf of the additional insured(s) at the location of the covered operations has been completed; or
2. That portion of “your work” out of which the injury or damage arises has been put to its intended use by any person or organization other than another contractor or subcontractor

engaged in performing operations for a principal as a part of the same project.”

Prior to the 2004 Edition, there was an ambiguity in the interpretation of “arising out of” the named insured's operations since that language had been interpreted broadly by various courts to require only a minimal causal connection. The 2004 revised endorsement provided coverage to the additional insured only when injury or damage is “caused, in whole or in part, by” the named insured and, thus, eliminates claims caused by the sole negligence of the additional insured.

In April 2013, ISO made several substantive changes to the 2013 AI Forms significantly narrowing the scope of coverage under those forms. In addition, it was made clear that separate endorsements are required for ongoing operations as well as completed operations. Generally, the changes to the 2013 AI Forms amount to the following three changes: (1) limiting coverage to the additional insured “only to the extent permitted by law”; (2) providing that coverage to the additional insured will not be broader than that which the named insured is required by the contract or agreement to provide; and (3) limiting the amount the insurer is required to pay out to the amount of insurance (a) required by the contract or (b) available under the applicable limits of insurance, whichever is less.

ISO added the following language in the 2013 AI Forms:

“[t]he insurance afforded to such additional insured only applies to the extent permitted by law.”

The intent of this language is to act as a “savings clause” in states that have enacted “anti-indemnity” statutes, where the statutes extend to naming a party as an additional insured in addition to preventing or otherwise limiting the extent to which an indemnitor may be required to indemnify an indemnitee from the indemnitee’s own negligence. For example, these statutes typically prevent a party from being named as an additional insured to the extent doing so would provide coverage to the additional insured for damage caused by the additional insured’s own negligence. This new change by ISO appears to be an attempt to ensure that the additional insured endorsement forms will not be determined to run afoul of those types of anti-indemnity statutes.

ISO also added the following language in the 2013 AI Forms:

“[i]f coverage provided to the additional insured is required by a contract or agreement, the insurance afforded to such additional insured will not be broader than that which you [the insured] are required by the contract or agreement to provide for such additional insured.”

Based on this language, if the contract between a contractor and an owner, as an additional insured, requires the contractor to maintain insurance coverage that is narrower in scope than what the contractor actually carries, the owner, as an additional insured, will be limited to what is actually required by the contract. In other words, it is possible there could be a scenario where the contractor’s insurance might have been broad enough to cover a claim in whole, but because the contract between the contractor and the owner required less coverage, the owner only would be entitled to collect part of the total amount of that claim. Therefore, if the 2013 AI Forms are utilized, the parties will need to be extremely careful when negotiating and drafting the terms and conditions of the insurance requirements to ensure they fully and accurately reflect the bargained-for coverage.

The final change to the 2013 AI Forms by ISO was to add a new provision that modifies the limits of insurance as follows:

“If coverage to the additional insured is required by a contract or agreement, the most [the insurer] will pay on behalf of the additional insured is the amount of insurance:

1. Required by the contract or agreement; or
2. Available under the applicable Limits of Insurance shown in the Declarations: whichever is less.

This endorsement shall not increase the applicable Limits of Insurance shown in the Declarations.”

Because not all additional insured endorsements are created equal, requiring the appropriate additional insured endorsement from the named insured is critical. Although it likely will take some time before the new 2013 AI Forms make their way into the marketplace, eventually parties will begin utilizing these forms when requested to name another party as an additional insured. If the party to be named as an additional insured

agrees to utilize the new 2013 AI Forms, it will be more important than ever to carefully draft the insurance requirements within the contract to reflect the full and accurate coverage and limits intended by the parties.

Nonstandard Exclusions and Limitations

Mold Exclusion:

Excludes coverage for bodily injury or property damage “caused by the invasions or existence of water or moisture including but not limited to mold, mildew, rot and deterioration of property.”

A. Mold exclusion applies to sudden and accidental release of water. When a homeowner filed a claim for water related damage for a home which had become contaminated with mold, the insurer denied the mold claim based upon the terms of the policy, specifically, the mold exclusion. The plaintiff homeowner asserted that the insurer could not rely on the mold exclusion in light of Insurance Code Section 530 which provides that an insurer is liable for losses proximately caused by insured risks, and sudden and accidental discharge of water was an insured risk. The Court of Appeal held the clear language of the mold exclusion applied.

De Bruyn v. Farmers Group, Inc. (2008) 158 Cal.App.4th 1213.

Specified Projects or Operations Exclusion

1. Tract Housing/Condos/Townhomes Exclusion:

A. Excludes coverage “for any apartments, condominiums or townhomes or attached homes . . . ”

B. Condominium Exclusion upheld while criticizing court's own prior decision.

A developer of a residential housing development hired a subcontractor to perform rough framing work. Homeowner sued the developer for defective construction, and the developer cross-complained against the subcontractor for indemnity. Subcontractor tendered to its CGL insurer, who disclaimed coverage based on a Manuscript Condominium Exclusion. After obtaining a judgment on its cross-complaint against the

subcontractor, the developer filed an Insurance Code Section 11580 action directly against the insurer seeking to satisfy its judgment. The developer conceded the project was recorded legally to qualify as a "condominium project," but contended that the project actually consisted of single family homes, and therefore the exclusion did not apply. Alternatively, the developer argued that coverage should nonetheless extend to the homes as the project constituted "condominiums" but did not materially alter the risk the insurer agreed to undertake. The developer relied upon Scottsdale Insurance Company v. Essex Insurance Company (2002) 98 Cal.App.4th 86 in which the court refused to enforce a Joint Venture Exclusion on the basis that the capacity under which the insured performed its work did not adversely impact the insurer's underwriting intent. The Fourth District Court of Appeal held that the term "condominium" was statutorily defined and upheld the exclusion. With respect to the developer's additional argument that the project did not materially alter the insurer's risk, the court refused to follow the Scottsdale case (even though it came out of the same division) and the justice who wrote the Scottsdale case concurred with the court's opinion in the current case. The court concluded that the Scottsdale holding that a court may invalidate an exclusionary clause based on the lack of material impact upon insurer's underwriting intent was not a valid basis for such exclusion.

California Traditions v. Claremont Liability Insurance Co. (2011) 197 Cal.App.4th 410.

2. Exclusion for Size of Project or Limitation to Single Family Homes:

Excludes coverage for “any apartment or condominium or any single-family or tract homes where the total project or development exceeds ____ homes and/or units.”

3. Exclusion for Work or Operations Prior to Policy Period:

Excludes coverage for “ ‘your work’ . . . prior to the policy period” or for “any pre-existing construction or preparation for construction . . . ”

4. INDEMNITY AGREEMENTS

A. A named insured's assumption of another's liability under a hold harmless or indemnity provision within an "insured contract" is considered "derivative liability" and is covered under the policy's "contractual liability coverage/exclusion."

Insurance Co. of North America v. National American Ins. Co. (1995) 37 Cal.App.4th 195.

1. An indemnity agreement which expressly and unequivocally provides that the indemnitor will indemnify the indemnitee for the indemnitee's negligence, regardless if that negligence is active or passive, is considered a "Type I" indemnity agreement. (Formerly typical agreement between subcontractor contractor. See below)

MacDonald & Kruse, Inc. v. San Jose Steel Co. (1972) 29 Cal.App.3d 413.

2. An indemnity agreement which provides that the indemnitor will indemnify the indemnitee for the indemnitee's own acts of passive negligence, is considered a "Type II" indemnity agreement. An indemnitee's active negligence is a bar to recovery under this form of indemnity agreement.

C.I. Engineers & Constructors, Inc. v. Johnson & Turner Painting Co. (1983) 140 Cal.App.3d 1011;

Guy F. Atkinson Co. v. Schatz (1980) 102 Cal.App.3d 351.

3. An indemnity agreement which provides that the indemnitor will indemnify the indemnitee for the indemnitor's negligence only is considered "Type III" indemnity agreement. Any negligence on the part of the indemnitee or others will bar enforcement of the agreement. This agreement is rare.

MacDonald & Kruse, Inc. v. San Jose Steel Co., (1972) 29 Cal.App.3d 413.

B. The question of whether an Indemnity Agreement covers a given case turns primarily on contractual interpretation, and it is the intent of the parties that is expressed in the Agreement that should control. This requires an inquiry under the circumstances of the damage or injury in the language of the contract.

Rossmoor Sanitation, Inc. v. Pylon, Inc. (1975) 13 Cal.3d 622, 633.

C. California courts, when interpreting express indemnity agreements, generally have employed a three-type analysis, originally set forth in MacDonald & Kruse, Inc. v. San Jose Steel Co., which focus on the indemnitees' active or passive negligence.

MacDonald & Kruse, Inc. v. San Jose Steel Co., *supra*.

D. Given the establishment of the Type I indemnity, the critical inquiry is whether or not the indemnity provisions at issue apply absent proof by the developer that subcontractor was at fault. Stated differently, the question to be decided is whether or not the indemnity provisions require the establishment of subcontractor fault (negligence plus causation) as a prerequisite to triggering the contractual obligations to indemnify under the subcontractor agreement.

1. An indemnity agreement in a commercial setting which provided that the indemnitor/subcontractor would indemnify the indemnitee/general contractor for a loss which “. . . arises out of or is in any way connected with” the subcontractor's performance of its work under the contract, and “. . . shall apply to any acts or omissions, willful misconduct or negligent misconduct, whether active or passive, on the part of the Subcontractor . . .”, did not require a showing of fault on the part of the subcontractor by the general contractor to enforce indemnification.

Continental Heller Corp. v. Amtech Mechanical Services, Inc. (1997) 53 Cal.App.4th 500;

McCrary Construction Co. v. Metal Deck Specialists, Inc. (2005) 133 Cal.App.4th 1528.

2. In contrast, an indemnity provision (in a standard multiple party construction defect action) which provided that the subcontractor would indemnify the owner for “. . . damage to property arising out of or in connection with Subcontractor's . . . performance of the Work and for any breach or default of the Subcontractor in the performance of its obligations . . .” required the developer to prove negligence on the part of the subcontractor to trigger its indemnity obligation to the developer.

Heppler v. J.M. Peters Co. (1999) 73 Cal.App.4th 1265.

3. An indemnity agreement which provided that all work performed by the subcontractor “shall be at the risk of [the subcontractor] exclusively,” and that the subcontractor would indemnify and hold harmless the general contractor from any claim or loss “resulting from [the general contractor’s] alleged or actual negligent act or omission, regardless of whether such act or omission is active or passive . . .,” did not require the general contractor to prove negligence on the part of the subcontractor to obtain indemnity.

Centex Golden Construction Company v. Dale Tile Co. (2000) 78 Cal.App.4th 992.

E. Major Changes Have Been Undertaken to the California Indemnity Statutes as They Relate to Construction Contracts.

1. The indemnity statutes delineate between residential construction and non-residential construction. Specifically, in 2008, the California Legislature amended Civil Code Section 2782 in an attempt to limit the applicability of Type I indemnity for construction defect claims in residential construction projects. The statute specifically indicates that for contracts entered into on or after January 1, 2009, it invalidates provisions that purport to require subcontractors to indemnify certain indemnitees (including builders, developers, and general contractors) against liability for construction defect claims on residential projects to the extent that such claims arise out of, pertain to, or relate to the negligence of such purported indemnitee(s). This means that each party will be held liable to the respective degree to which it is found to be at fault. There is no indemnity for construction defects for either active or passive negligence of a general contractor developer. There are limitations to the limitation on indemnity. First, the limitation of the indemnity applies only to construction defects claims. This means that a Type I indemnity provision is not invalid with respect to a bodily injury or wrongful death claim.

2. Civil Code Section 2782(d) addresses defense obligations and the timing thereof. In an attempt to correlate with SB 800 protocols (The Right to Repair Act), the obligation to defend begins with a written tender of the claim regardless if formal litigation has been commenced. If an indemnitee tenders a claim to a subcontractor, the subcontractor must, within specified deadlines, agree to defend the

claim except to the extent it results from the scope of work, actions, or omissions of the indemnitee or any other party. Alternatively, the subcontractor must pay "on an ongoing basis" during the pendency of the claim "no more than a reasonable allocated share" of the indemnitee's defense fees and costs. Such payments are subject to later re-allocation, and all party's rights to seek equitable indemnity are preserved.

California Civil Code Section 2782.

F. Civil Code Section 2782.05 Extends the Provisions of California Civil Code Section 2782 to Any Construction Contract (Non-Residential) Entered Into on or After January 1, 2013.

In Civil Code Section 2782.05(a), the Legislature provides that any indemnification provisions "that purport to insure or indemnify, . . . against liability . . . are void and unenforceable to the extent the claims arise out of, pertain to, or relate to the active negligence or willful misconduct of that general contractor, construction manager, or other subcontractor, or their other agents, other servants, or other independent contractors who are responsible to the general contractor, construction manager, or other subcontractor." The Legislature further codifies that no party may waive or modify these provisions by contract. However, the Legislature does provide that "contractual provisions, clauses, covenants, or agreements not expressly prohibited herein are reserved to the agreement of the parties." Essentially, the Legislature is providing that the parties may enter into certain types of agreements, as long as the indemnitee cannot avoid its obligations for its active negligence or willful misconduct.

Civil Code Section 2782.05(b) sets forth 13 different scenarios to which the statute does not apply. Specifically, the Legislature indicates that Civil Code Section 2782.05 does not apply to WRAP or OCIP policies.

Under Section 2782.05, the Legislature created a mechanism to trigger the obligations of the parties subject to an indemnification agreement. In Civil Code Section 2782.05(e), the Legislature sets forth the basis upon which the indemnity provision shall be applicable to the indemnitor. Civil Code Section 2782.05(e) provides that "Subdivision (a) does not prohibit a subcontractor and a general contractor or construction manager from mutually agreeing to the timing or immediacy of the defense. . . ."

The Legislature placed the onus on the party seeking indemnification to notify the indemnitor of their demand for indemnity. Civil Code Section 2782.05 provides that the subcontractor has no obligation to defend or indemnify the general contractor or construction manager until the general contractor or construction manager provides a written tender of the claim. This written tender requires information regarding the claims by the claimants implicating the subcontractor's scope of work.

The Legislature has also placed another burden on the general contractor or construction manager in the submission of their written tender of the claim to a subcontractor. The general contractor or construction manager must present a reasonable allocation of fees and costs. The general contractor or construction manager has the burden of providing, in writing, how the allocated share of fees and costs was determined. This requirement makes the general contractor or construction manager put forth the basis for each subcontractor's involvement in the litigation and how much exposure the general contractor or construction manager believes each subcontractor should be allocated.

Without some type of agreement as to the timing of the triggering of the obligation under the indemnification provision, Civil Code Section 2782.05 provides the mechanism for the subcontractor to respond to an indemnification tender. The subcontractor has two choices under the statute. The subcontractor may defend the claim with counsel of its choice and thereby maintain control of the defense. However, the statute also makes it clear that the defense by the subcontractor shall be a complete defense of the claims against the subcontractor's scope of work including claims of vicarious liability resulting from the subcontractor's scope of work. The statute also makes it clear that the subcontractor is not responsible for defending claims against the scope of work of any other party, including the general contractor or construction manager.

Civil Code Section 2782.05 also gives the subcontractor the ability to prove, to the satisfaction of the general contractor or construction manager, that the subcontractor's scope of work is not implicated or, at the very least, is a small portion of the claim. As such, it is of benefit to both the subcontractor by giving it the opportunity to set forth evidence showing it is not at fault and the general contractor or construction manager by obtaining information to help it defend against such allegations. Both sides have a vested interest in doing the work necessary to show that the scope of work of the subcontractor was implicated unjustly.

California Civil Code Section 2782.05.

G. The California Supreme Court in Crawford v. Weathershield, supra, has clarified any issues with respect to defense obligations and indemnity agreements.

1. In Crawford, the California Supreme Court considered whether a pre-2006 residential construction subcontract required the subcontractor to defend the indemnitee developer-builder in suits brought against both parties where the plaintiffs' complaints alleged construction defects arising from the subcontractor's negligence even though (1) a jury ultimately found that the subcontractor was not negligent, and (2) the subcontract gave the builder no right of indemnity unless the subcontractor was negligent. The court concluded that the subcontractor had such a duty, determining that pursuant to the subcontract language, subcontractor had agreed to "defend" any suit or action, against the developer "founded upon" any claim "growing out of the execution of the work." The court found that the duty to defend was clear from the contract and reasoned that a contractual promise to "defend" another against specified claims clearly meant an immediate and active obligation for the promisee's defense to provide a defense on the promisee's behalf as soon as such claims are made against the promisee and until they were resolved. The duty to defend was determined by the court to attach to indemnity claims which, at the time of tender, alleged facts that would give rise to a duty to indemnify.

Similarly, in UDC-Universal Development, LP v. CH2M Hill (2010) 181 Cal.App.4th 10, the Court of Appeal found that a "duty to defend" arises out of an indemnity obligation as soon as the litigation commences and regardless of whether the indemnitor is ultimately found negligent. In UDC, the contract's indemnity provision did not state that there must be an underlying claim of negligence specifically against the subcontractor to trigger the subcontractor's defense obligation. Rather, the court determined that the subcontract agreement called for indemnification when claims against UDC "arise out of or are any way connected with" a negligent act or omission by the subcontractor. The court determined the duty to defend applied to any "suit or action" brought against the developer on any claim or demand covered. The court determined that an indemnitee "should not have to rely on the plaintiff to name a particular subcontractor in order to obtain a promised defense by the one that the indemnitee believed was responsible for the plaintiff's damages."

Crawford v. Weathershield Manufacturing, supra.;
UDC Development, LP v. CH2M Hill (2010) 181 Cal.App.4th 10.

H. An insurer notified of the underlying claim against its insured and given the opportunity to protect its interests is bound by any resulting judgment whether or not its refusal to participate in the underlying proceeding is legally justified.

Executive Risk Indemnity, Inc. v. Jones (2009) 171 Cal.App.4th 319.

I. The timing and nature of an SIR payment does not defeat equitable contribution claims against a co-insurer. The HOA sued developer, Pacifica, for construction defects related to a condominium conversion project. Pacifica tendered its defense to two carriers. Axis (Carrier I) agreed to defend, but Carrier II declined because developer had not yet satisfied its self-insured retention (“SIR”). Ultimately, the case settled for \$1,000,000 and Carrier II refused to fund the settlement, but agreed that developer's \$250,000 settlement contribution would apply toward satisfaction of its SIR. Axis paid the remaining \$750,000, then filed suit against Carrier II for equitable contribution. The Court of Appeal held that the timing of the developer's payment of the SIR did not prevent Axis from establishing Carrier II's legal obligation to cover the underlying claim. The court found that the settlement was presumptive evidence of the insurer's liability in the amount of liability. Because the settlement included developer's payment of the SIR, the same presumption applied and Axis was not required to prove that the SIR applied only to covered property damage.

Axis Surplus Insurance Co. v. Glencoe Insurance Ltd. (2012) 204 Cal.App.4th 1214.

J. Subcontractor's insurer's settlement contribution does not relieve its obligation to defend its additional insured. In an underlying construction defect action, a hotel sued the general contractor for defective construction. The general contractor, through its insurer, tendered its defense to various subcontractors including a framing subcontractor insured by Mountain West. The Mountain West policy contained an additional insured endorsement naming the general contractor as an additional insured. Mountain West admitted it owed a duty to defend the general contractor but refused to accept the carrier's tendered defense, claiming instead that its contribution to a portion of the settlement on behalf of its insured was sufficient. The general contractor's carrier (St. Paul) thereafter brought an action for equitable contribution against Mountain West contending that the shifting burdens doctrine set forth in Safeco Insurance of America v. Superior Court (2006) 140 Cal.App.4th 874 should apply. Under the shifting burdens

doctrine, St. Paul had the burden to prove the potential for coverage under Mountain West's policy and Mountain West had the burden to prove that the absence of actual coverage as an affirmative defense. The Court of Appeal held that Mountain West was a non-participating co-insurer, and that as a result, the Safeco burden shifting applied. Mountain West could not defeat equitable contribution by merely contributing to a portion of the settlement on behalf of its named insured but failing to contribute to its additional insured's defense. Since the settlement agreement did not release Mountain West, it remained liable for its defense obligation.

St. Paul Mercury Insurance Co. v. Mountain West Farm Bureau Mutual Insurance Co. (2012) 210 Cal.App.4th 645.

K. “Indemnity” for Attorney’s Fees

1. Under standard subcontract agreements, general contractors assert entitlement to indemnity based on, among other theories, a contractual indemnity agreement. Contracts have “prevailing party” clauses entitling a prevailing party to its attorney’s fees. Fees under such a contractual clause are allowable as costs under Code of Civil Procedure §§ 1032 and 1033.5. Such costs would normally fall within the Supplementary Payments provision.

2. Agreements between contractors and owners which have attorney fee provisions, but not indemnity provisions, do not necessarily allow recoverable attorney’s fees under the policy based on the fact the owner/contractor agreement is not an “insured agreement.” This could impact settlement issues in these types of cases.

3. General contractor can be liable for attorney's fees to a subcontractor after an unsuccessful indemnity action. A motorist sued a general contractor after an auto accident near a roadway construction project. The general contractor filed a cross-complaint against the subcontractor for defense and indemnity based on a provision in the subcontract. The subcontractor in turn filed its own cross-complaint against the general contractor. The trial court granted summary judgment for the subcontractor on the complaint and on the general contractor's cross-complaint, and found the subcontractor to be the prevailing party. The Court of Appeal held that the subcontractor is entitled to attorney's fees because of the subcontract authorized fees to the prevailing party in “any dispute resolution” arising “under or relating to . . . the Subcontract.” The court therefore found that the attorney's fees provision controlled the matter and under it,

the subcontractor, as the prevailing party in the general contractor's indemnity enforcement action, was owed attorney's fees.

Toro Enterprises, Inc. v. Pavement Recycling Systems, Inc. (2012) 205 Cal.App.4th 954.

4. Prevailing party is not entitled to attorney's fees where it failed to comply with contractual requirement to mediate. Plaintiffs allege that defendants failed to disclose garage roof defects when they sold a vacation home to plaintiffs. The purchase agreement provided that a party who failed to attempt to mediate prior to the suit was not entitled to attorney's fees. After filing the lawsuit, plaintiffs requested mediation twice but defendants refused. Trial court ultimately granted defendants' motion for summary judgment and awarded attorney's fees to defendants. The Court of Appeal conclusively established that defendants were not entitled to recover legal fees as their motion for summary judgment did not excuse the contractual requirement of participating in mediation.

Cullen v. Corwin (2012) 206 Cal.App.4th 1074.

L. “Horizontal Exhaustion Rule” Trumps Indemnity Agreement Between Insured Parties

RJS was a subcontractor on an apartment construction project and carried primary liability insurance with Lloyds of London (\$1,000,000). It also carried excess coverage with Great American Insurance. JPI was the general contractor on the project and carried primary insurance with Transcontinental Insurance (\$1,000,000). The terms of the subcontract included a Type II indemnity agreement which extended indemnity by RJS to JPI for any claims arising out of RJS' work. In this action, Great American sought to recover from Transcontinental the amount it had paid out in settlement in settling the claim against JPI. Transcontinental argued that the indemnity agreement between the parties required under the principles articulated in Rossmor Sanitation, that the entire burden should fall on RJS' insurers and therefore it owed nothing. Great American, on the other hand, argued that, as an excess insurer, it had no liability until all of the primary insurance had been exhausted (the “Horizontal Exhaustion Rule”). The trial court agreed with Great American and entered judgment in its favor establishing that while an indemnity provision can impact the rights of the insurers of both the indemnitee and

indemnitor, it will not be controlling in cases involving insurers that have different levels of exposure (primary versus excess).

JPI West Coast Construction, Inc. v. RJS & Associates, Inc. (2007) 156 Cal.App.4th 1448.

M. Ten-Year Statute of Limitations Applies to Cross-Complaints for Indemnity

Plaintiff, the buyer of an apartment complex, sued defendant developer-sellers after discovering that all of the windows of the complex lacked flashing which led to water damage. Developers filed a cross-complaint for indemnification against the cross-defendant subcontractors. The subcontractors moved for summary judgment on the grounds that the cross-complaint was barred by the statute of limitations and failed to allege a specific claim. The Court of Appeal held that the cross-complaint that asserted a theory of recovery was not barred under Code of Civil Procedure Section 337.15, and found that the exemption under 337.15(f) for actions based on willful misconduct applied to the cross-complaints for indemnity.

Pine Terrace Apartments, L.P. v. Windscape, LLC (2009) 170 Cal.App.4th 1.

N. Statute of Limitations Periods May be Contractually Shortened, Provided It Would Not Prevent the Effective Pursuit of a Judicial Remedy

Defendants, corporate executives, signed employment agreements with a corporation providing that a party's claims were barred if not presented to the other party in writing within a year of the time the claiming party knew, or should have known, the facts giving rise to the claim. After the corporation filed bankruptcy, the bankruptcy trustee filed an action against the executives for breach of fiduciary duty. Defendants asserted they had never received notice of the claim and filed a motion for summary judgment on the basis that the claim was time barred by the one-year notice provision. The Court of Appeal held that the statute of limitations on the claim had expired and reasoned that the plaintiff and defendants could lawfully require one year's notice of the claim shortening the statute of limitations, because California courts generally accord contracting parties substantial freedom to modify statute of limitations periods unless otherwise provided by statute.

Zamora v. Lehman (2013) 214 Cal.App.4th 193.

The California Court of Appeal has further extended this logical reasoning concerning the ability to contract for a shortened statute of limitations. The Court of Appeal recently upheld and enforced standard AIA contract language which effectively shortened to four years the 10-year statute of limitations for bringing claims for latent construction defects. The court held that a waiver of the delayed discovery rule and the shortening of the statute of limitations is permitted where there are two sophisticated parties in a commercial context that occupy equal bargaining positions. In the case, the parties entered into a contract for the construction of a commercial hotel. Eight years after substantial completion of the project, the owner discovered a latent defect and sued the general contractor for breach of contract. The general contractor asserted the contractual provisions of the AIA agreement which limited the statute of limitations to four years. While the Court of Appeal found that the enforceability of this clause was an issue of first impression in California, it looked to the decisions of many other states which had enforced the same provision. The Court of Appeal also focused heavily on the party's freedom of contract and the sophistication of the parties. The fact that both parties were represented by counsel in negotiations and drafting of the contract, and that each side had submitted proposed revisions and comments to the agreement was persuasive. The court affirmed the AIA contract provision limiting and shortening the statute of limitations.

Brisbane Lodging, L.P. v. Webcor Builders, Inc. (2013) 216 Cal.App.4th 1249.

O. The Four-Year Statute of Limitations Does Not Apply to Express Indemnity Claims or an Insurer's Equitable Subrogation Claims Which Arise as a Result

A construction defect action was commenced against a general contractor and a subcontractor. The general contractor filed a cross-complaint alleging express indemnity based upon the subcontract agreement. After all defendants had settled with plaintiff, the general contractor's insurer intervened in the cross-complaint against the subcontractor to recover attorney's fees and costs incurred pursuant to its insurance policy under a theory of equitable subrogation. The subcontractor argued that the cross-complaints were time barred under the four-year statute of limitations (California Code of Civil Procedure, Section 337.1). The California Court of Appeal held that Code of Civil Procedure, Section 337.1 did not apply to the general contractor's claim for express

indemnity nor to its insurer's claim for equitable subrogation. The ten-year statute (California Code of Civil Procedure, Section 337.15) specifies that the term "action" includes an action for indemnity while Code of Civil Procedure, Section 337.1 does not include the same provision. The court therefore concluded that Code of Civil Procedure, Section 337.1 did not apply to contractual indemnity claims, but the longer statute of limitations applied.

Valley Crest Landscape Development, Inc. v. Mission Pools of Escondido, Inc. (2015) 238 Cal.App.4th 468.

P. Ten-Year Statute of Repose Does Not Apply to Property Contamination Claims When the Claim is Not Based on Defective Work

EOA, the condominium owners association, sued various project developers, design professionals, and prior land owners including Shell Oil, alleging construction defect and contamination of ground water and soil on the condominium site. The site was previously owned by Shell and was used as a distribution terminal until approximately 1980. In 2002, the California Regional Water Quality Control Board discovered that leaks from the fuel storage had contaminated the soil and ground water. Various measures were undertaken to clean up the site including installation of ground water monitoring wells. In 2003, the property was purchased and condominiums were constructed. In or about 2010, EOA filed a lawsuit alleging defendants knew about the contaminated soil and ground water and failed to properly clean up the site. Defendant Shell moved for summary judgment against EOA on the grounds that the cause of action was barred by the ten-year Statute of Limitations for Construction Defects pursuant to California Code of Civil Procedure, Section 337.15 and that all of the other causes of action were barred by the three-year Statute of Limitations for Real Property Damage. The trial court granted a summary judgment and EOA appealed. The Court of Appeal determined that California Code of Civil Procedure, Section 337.15 only applied to construction defect claims and, therefore, cannot be used as a basis to grant Shell's summary judgment motion because such claims against Shell pertain to contamination of the site due to Shell's negligence during its operations on the property. However, the Court of Appeal found that with regards to the Statute of Limitations for Real Property Damage, the actual and constructive knowledge of prior landowners was imputed to future owners, and the three-year Statute of Limitations for Real Property Damage applied.

Estuary Owners Association v. Shell Oil Company (2017) 13 Cal.App.5th 889.

Q. The “Relation-Back” Doctrine Does Not Apply to Allow Belated Filing of A Certificate of Merit with an Amended Complaint

A crane operator brought a professional negligence action against an engineering corporation arising out of injuries sustained when one of its cranes tipped over. Plaintiff’s First Amended Complaint was identical to its original complaint except that a Certificate of Merit was now attached to the Amended Complaint. The defendant demurred to the First Amended Complaint on the grounds that a Certificate of Merit as required by California Code of Civil Procedure, Section 411.35 was not filed within the statute of limitations, because one was not filed with the original complaint or within sixty (60) days thereafter. The trial court denied the demurrer concluding that the Amended Complaint related back to the filing date of the original complaint. The Court of Appeal reversed stating that the plain language of Code of Civil Procedure, Section 411.35 does not allow the application of the Relation-Back Doctrine.

Curtis Engineering Corp. v. Superior Court (2017) 16 Cal.App.5th 542.

R. Third-Party Allocations in an Underlying Lawsuit Are Not Determinative of Liability for Purposes of Duty to Defend

A deck shoring subcontractor entered into a contract with a general contractor to design and supply the materials for all formwork and deck shoring at the general contractor’s construction site. The subcontract agreement provided an indemnity provision which indicated that the general contractor was to defend, indemnify and hold harmless subcontractor against any and all claims or actions specifically relating to personal injuries except to the extent such claims were caused by the acts or omissions of subcontractor. The subcontractor was later sued by a number of general contractor’s employees for injuries sustained when a shoring system collapsed. Subcontractor asserted, as an affirmative defense, that the employees’ injuries were proximately caused by the negligence of the general contractor and on that basis tendered the defense and indemnity of the personal injury lawsuits to the general contractor based upon the contract’s indemnity provision. When the general contractor failed to acknowledge the tender, the subcontractor sued the general contractor for indemnification. The general contractor demurred to the subcontractor’s cross-complaint and the trial court sustained

the demurrer without leave to amend. The Court of Appeal reversed the trial court's decision holding that the allegations in the personal injury employee suits were not determinative of the subcontractor's claim for indemnity. As part of their holding, the court reasoned that the subcontractor reasonably interpreted the indemnification provision as providing proportionate liability such that the general contractor must indemnify the subcontractor for any portion of the economic damages attributable to the negligence of general contractor, but is not obligated to indemnify the subcontractor for any portion of the damages attributable to the subcontractor's negligence.

Aluma Systems Concrete Construction of California v. Nibbi Bros., Inc.
(2016) 2 Cal.App.5th 620.

S. A Standard Indemnity Clause Does Not Create a Reciprocal Right to Attorney's Fees

The City of Chowchilla contracted with Carr Business Enterprises to do improvement work on city streets. A series of problems arose delaying the work which caused Carr to incur additional costs. Carr sued Chowchilla for those extra costs and later moved for an award of attorney's fees arguing that the indemnity provisions included in the contract authorized the award of attorney's fees because the language in the provisions included within their scope of actions arising out of the performance of the work provided in the contracts. The Appellate Court disagreed and interpreted the provisions as standard indemnity provisions applicable only to third party claims. The court found that there was no express language authorizing recovery of fees in an action to enforce the contracts.

Carr Business Enterprises, Inc. v. City of Chowchilla (2008) 166
Cal.App.4th 25.

5. ADDITIONAL INSURED ENDORSEMENTS

A. Coverage may also be afforded by virtue of an “additional insured” endorsement. The three most common types of endorsements are as follows:

1. ISO CG 20 09

This standard endorsement, commonly referred to as a “20 09,” is also known as the “long form” or “Form A,” and grants coverage to the additional insured “. . . but only with respect to liability arising out of : [¶] A. [The named insured’s] ongoing operations performed for the additional insured(s) at the location designated above; or [¶] B. Acts or omissions of the additional insured(s) in connection with their general supervision of such operations.”

This form is the most limited, covering only the ongoing or current operations of the named insured, and does not confer “additional insured” status once the named insured’s work at the project has been completed.

The term “ongoing operations” in the endorsement is not defined and thus subject to interpretation. Many independent acts of the additional insured could reasonably fall within the scope of that term, such as coordination and scheduling of a subcontractor’s work, inspection of the work, or ordering changes to its subcontractor’s work.

2. ISO CG 20 10

The “20 10” endorsement, also known as “Form B,” confers additional insured status, but only with respect to “liability arising out of . . . ‘your work’ for that [additional] insured by or for you” (1985 version) or “. . . your ongoing operations performed for that [additional] insured.” (1993 version).

Pursuant to the 1993 version, the “Who Is An Insured” section of the CGL policy was amended to include an insured as “a person or organization shown on the Schedule, but only with respect to liability arising out of your ongoing operations performed for that insured.” This language effectively cut off additional insured status at the completion of the insured’s ongoing operations.

a. Acceptance Ins. Co. v. Syufy Enterprises (1999) 69 Cal.App.4th 321 (coverage for the additional insured/developer was found where an employee of the insured/subcontractor was injured on the job site, even though the employee's injuries were not directly caused by the "work" of the subcontractor, since the injury "arose from" work he was performing on the building owned by the additional insured/developer).

b. Pardee Construction Co. v. Ins. Co. of the West (2000) 77 Cal.App.4th 1340 (a pre-1993 20 10 endorsement provided the additional insured general contractor with coverage for liability arising from the named insured subcontractor's work even after the work had been completed, since coverage was afforded based on the named insured's "work" or "product," rather than its "ongoing operations" or "work in progress.")

c. St. Paul Fire & Marine Insurance Co. v. American Dynasty Surplus Lines (2002) 101 Cal.App.4th 1038 (subcontract did not require electrical subcontractor to indemnify general contractor for liability to subcontractor's employee who was injured by explosion of pipe during pressure testing by general contractor; the subcontract required indemnity for liability attributable to bodily injury arising out of or resulting from the performance of the work that was the subject of the subcontract, if the liability arose from any act or omission of the subcontractor, but the employee's mere presence at the job site was not a sufficient act or omission by the subcontractor, and the subcontractor performed no act or omission.

d. Hartford Casualty Insurance Co. v. Traveler's Indemnity Co. (2003) 110 Cal.App.4th 710 (coverage under tenant's commercial general liability insurance policy was not limited to liability directly caused by tenant and related to subjects much broader than mere operations or use of the interior of leased premises, including liabilities potentially imposed on landlord that were related to tenant's business presence in landlord's facilities, as well as specific events occurring during the actual performance of tenant's own work or operations).

e. No coverage for claim unrelated to named insured's work. Does not provide coverage for homeowner's claims against developer for negligent misrepresentation in its sales literature or breach of fiduciary duty.

Transcontinental Ins. Co. v. Insurance Co. of State of Penn. (2007) 148 Cal.App.4th 1296.

3. **ISO CG 2037**

In 2001, ISO again modified the CG 20 10 creating the CG 20 10 10 01 in order to reinstate coverage to the additional insured with respect to the completed operations excluded in CGO 20 10 10 93, and because that “completed operations” exclusion was carried forward into the CG 20 10 10 01, ISO introduced a new additional insured endorsement, CG 2037 creating in 2001 the CG 20 37 10 01. This endorsement provided additional insured status only with respect to the completed operations of the named insured’s work by amending the “Who Is An Insured” section of the CGL policy to include as an insured the following: “[the identified persons or organizations] but only with respect to liability arising out of ‘your work’ at the location designated and described in the [endorsement] performed for that insured and included in the ‘products-completed operations hazard.’” In 2004, ISO narrowed the coverage afforded by the “arising out of” language under both CG 20 10 and the CG 2037 by eliminating the coverage under those forms to liability at least caused in whole or in part by the named insured (i.e., limiting coverage for the additional insured’s sole negligence.) As set forth in Section 3 above, the endorsements have been further narrowed by the addition of language in the 2013 ongoing operations (CG 20 10) and completed operations (CG 2037) endorsements.

4. **ISO CG 7634**

Finally, this form provides slightly modified “Type I” coverage for the additional insured, and covers liability “arising out of” the named insured’s work, and liability “arising from” its supervision of the named insured, but excludes coverage for damages “arising out of the sole negligence or willful misconduct of, or for defects in design furnished by, [the additional insured].”

a. National Union Fire Ins. Co. v. Nationwide Ins. Co. (1999) 69 Cal.App.4th 70 (general contractor’s inadequate remedial measures to address hazards of ponding rain water and failure to properly coordinate its subcontractors’ work schedules were held to constitute its “sole negligence,” thus precluding the insurer’s duty to indemnify).

b. An additional insured endorsement in a policy issued to a subcontractor, which amended the policy to add the general contractor as an insured “. . . but only with respect to liability arising out of ‘your work’ for that insured by or for you,” required the insurer to provide the additional insured with a *full* defense, not just for the claims related to the subcontractor’s work.

Presley Homes, Inc. v. American States Ins. Co. (2001) 90 Cal.App.4th 571.

6. RULES FOR ALLOCATION OF DEFENSE COSTS

A. In general, once coverage of a policy potentially has been triggered, an insurer has an indivisible obligation to defend its insured, even if other insurers also cover the claim. The allocation of that burden is to be determined at a later date.

Aerojet-General Corp. v. Transport Indemnity Co. (1997) 17 Cal.4th 38;
Haskel, Inc. v. Superior Court (1995) 33 Cal.App.3d 963, 976, fn.9.

1. Where several liability insurers cover the same risk, each insurer's duty to defend must be assessed independently “since the duty of each is independent of whatever duty another might have.”

Wausau Underwriters Ins. Co. v. Unigard Security Ins. Co. (1998) 68 Cal.App.4th 1030, 1033, 80 Cal.Rptr.2d 688, 689.

B. There are no hard and fast rules which govern the allocation of defense costs among multiple insurers who have a duty to defend an insured. Costs of defense must be apportioned on the basis of *equitable considerations* not found in the contracts of insurance since insurers who share the burden have no contractual agreement among themselves.

1. Where several insurers jointly cover the same risk, they must share defense costs. Even in the absence of a prior agreement to do so, the court will apportion costs “on the basis of equitable considerations ... which depend on the particular policies of insurance, the nature of the claim made, and the relation of the insured to the insurers.”

Centennial Ins. Co. v. United States Fire Ins. Co. (2001) 88 Cal.App.4th 105, 115–116, 105 Cal.Rptr.2d 559, 565–566.

2. Each of the insurers “on the risk” has a duty to defend the action in its entirety and the duty is separate and independent from the other insurers, each also has “a corresponding right” of some sort to require the others to share in discharging the duty or at least contribute to its costs.

Aerojet-General Corp. v. Transport Indem. Co. (1997) 17 Cal.4th 38, 70, 70 Cal.Rptr.2d 118, 138;

CNA Casualty of California v. Seaboard Surety Co. (1986) 176 Cal.App.3d 598;

Signal Companies, Inc. v. Harbor Ins. Co. (1980) 27 Cal.3d 359;

Centennial Ins.Co. v. United States Fire Ins. Co. (2001) 88 Cal.App.4th 105.

C. Courts have addressed and approved various ways to allocate indemnity payments, as well as defense costs, among multiple insurers for the same loss, given the specific facts and “equities” of each case:

1. Absent other considerations, where several insurers cover the same risk, “defense costs” must also be shared between them pro rata *in proportion to the respective coverage* afforded by them to the insurance.

CNA Cas. of Calif. v. Seaboard Sur. Co., *supra*.

2. If one of the insurers on the risk has defenses the others lack (e.g., fraudulent misrepresentations by the insured in applying for coverage), to avoid its obligation to share defense costs, that insurer must establish there is no potential for coverage under its policy by obtaining an *adjudication of its coverage defense*.

Maryland Cas. Co. v. National American Ins. Co. of Calif. (1996) 48 Cal.App.4th 1822, 1831–1832, 56 Cal.Rptr.2d 498.

3. Because the duty to defend is determined at the time of tender a subsequent judicial determination that the claim was not covered under any of the several policies involved does not preclude a finding that there was a *potential* for coverage—hence, a duty to defend—when the claim was tendered. In that event, nondefending

insurers who owe no duty to indemnify must nevertheless contribute to defense costs paid by the defending insurer.

Wausau Underwriters Ins. Co. v. Unigard Security Ins. Co., supra.

4. Apportionment based on relative policy limits (the “policy limits” method). (CNA Casualty of Calif., supra; Employers Reinsurance Corp. v. Phoenix 8Ins. Co. (1986) 186 Cal.App.3d 545); Argonaut Ins. Co. v. Transport Indemnity Co. (1972) 6 Cal.3d 496.

5. The “Loss in progress” rule applies to render each insurer providing occurrence-type liability coverage liable for all damages attributable to underlying defect manifested during policy period, though damage may have become progressively worse during other insurer’s tenure. (Pines of La Jolla Homeowners Association v. Industrial Indemnity (1992) 5 Cal.App.4th 714).

6. Apportionment based on the relative duration of each primary policy as compared with the overall period during which the “occurrences” “occurred” (the “time on the risk” method). (Stonewall Ins. Co. v. City of Palos Verdes Estates (1996) 46 Cal.App.4th 1810; Centennial Ins. Co. v. United States Fire Ins. Co., supra); and

7. “Equal Shares” approach. Reliance Ins. Co. v. St. Paul Surplus Lines Ins. (4th Cir. 1985) 753 F.2d 1288.

8. Apportionment based on relative duration of each policy multiplied by the amount of the respective limits (the “qualified time on the risk” method).

Armstrong World Industries, supra.

9. There is no contribution from self-insured parties. Insurers that pay defense costs may seek contribution only from other *insurers*. They cannot obtain contribution from codefendants or other parties who are uninsured (self-insured) Equitable contribution applies *only* between insurers and has no place between insurer and insured, nor between insurer and uninsured or self-insured party.

Aerojet-General Corp. v. Transport Inc., supra.

D. Where multiple insurers share the same level of liability on the same risk for the same insured, the doctrine of *equitable contribution*, rather than equitable subrogation, will apply to apportion defense costs among equally responsible insurers.

Fireman's Fund Insurance Company v. Maryland Casualty Company (1998) 65 Cal.App.4th 1279;

Hartford Casualty Insurance Company v. Travelers Indemnity Company (2003) 110 Cal.App.4th 710.

E. Escape clauses are generally unenforceable among co-primary insurers. In general, insurers are permitted to limit the risks that they assume through explicit policy provisions. Many policies seek to preclude coverage in instances where another insurance policy providing for the defense is available to them. California courts have routinely disfavored these types of “escape clauses” based on public policy concerns. Two recent California Court of Appeal cases, confirmed the unenforceability of such escape clauses.

Underwriters of Interest Subscribing to Policy Number A15274001 v. ProBuilders Specialty Insurance, Co. (2015) 241 Cal.App.4th 721.

Certain Underwriters at Lloyds, London v. Arch Specialty Insurance Company (2016) 246 Cal.App.4th 418.

F. In contrast, an insurer, who had an obligation to defend its insured, the general contractor, for the general contractor's own independent acts of negligence, was not entitled to seek *equitable subrogation* for defense costs from other carriers who insured the general contractor as an “additional insured” for derivative liability, arising out of the acts or omissions of the general contractor's subcontractors.

Maryland Casualty Company v. Nationwide Mutual Insurance Company (2000) 81 Cal.App.4th 1082.

G. A secondary insurer's coverage is triggered when the applicable limit of underlying insurance has been exhausted by payment of claims and only arises when neither the specifically identified underlying primary policy nor other insurance applies. Horizontal exhaustion of all triggered primary policies is required before the secondary insurer could owe a duty to defend.

Traveler’s Casualty & Surety Co. v. Transcontinental Ins. Co. (2004) 122 Cal.App.4th 949;

Padilla Const. Co. v. Transportation Ins. Co. (2007) 150 Cal.App.4th 984.

H. The specific language of an excess insurance policy is highly relevant to the determination of coverage. In an underlying construction site action, plaintiff was an employee of a subcontractor. The plaintiff fell down an unguarded stairway shaft sustaining serious injuries. The plaintiff sued the general contractor (“Advent”) and a subcontractor (“Pacific”). Advent had primary insurance with Landmark, and an excess insurance with Topa. The plaintiff’s employer (“Johnson”) had primary and excess policies with National Union. Advent sought coverage as an additional insured under Johnson’s National Union primary and excess policies. The matter was ultimately settled and funded by National Union’s primary policy, Landmark and Topa. National Union excess did not contribute. Advent sued National Union seeking a declaration that it was an additional insured under the excess policy. Topa intervened in the action and also sought declaratory relief, equitable contribution and subrogation as against National Union Excess. The trial court granted National Union’s motion for summary judgment finding that Topa was not entitled to contribution from National Union because Topa’s excess policy provided coverage upon exhaustion of the underlying Landmark policy, and National Union’s excess policy contained specific policy language which indicated that it was “only triggered upon exhaustion of all other insurance.” The Court of Appeal (Sixth District) affirmed the trial court’s ruling. The court held that because plaintiff’s employer did not cause the accident, no indemnity coverage was triggered. It further found that Topa had not demonstrated that its policy afforded the same excess coverage as the National Union policy which specifically set forth that coverage would only apply after exhaustion of all other insurance.

Advent, Inc. v. National Union Fire Insurance Co. of Pittsburgh, PA, Topa Insurance Co. (2016) 6 Cal.App.5th 443.

I. A duty to defend owed to an additional insured under an ongoing operations policy, after work complete, exists where homeowner’s claim “arises out of” work performed by named insured. Developer McMillin hired numerous subcontractors to build the residential development. Certain insurance carriers provided policies to subcontractors naming McMillan as an additional insured. After the construction was completed, several homeowners filed construction defect claims against McMillin who

then brought claims directly against the AI insurers alleging they had breached their contractual obligation to defend McMillin in the underlying action. The carriers asserted by summary judgment motion they did not owe McMillin a duty to defend because their AI endorsements made it clear that McMillin was only afforded ongoing operations coverage, and since there was no homeowners during the time that the insureds performed their work and the homeowners are alleging damages sustained after the project was completed, there could be no potential coverage. Trial court granted summary judgment for the defendants. The Court of Appeal reversed the trial court's entry of summary judgment finding that under at least one policy there was a duty to defend McMillin. Pursuant to that policy (Lexington Insurance) the court indicated that the policy would provide coverage to McMillin for liability "arising out of" such ongoing operations. As the phrase has been given broad interpretation, the policy provided only that McMillin's liability had to be "linked" through a minimal causal connection. The court further concluded that a homeowner's construction defect claim is not necessarily one brought to recover under the "Products-Completed" coverage of a named insured subcontractor's policy. Therefore, they determined a duty to defend was owed by the subcontractors' carriers to McMillin.

McMillin Management Services, L.P. v. Financial Pacific Ins. Co. (2017) 17 Cal.App.5th 187.

J. When certain insurance clauses were not specific to other lower-layer insurance and the policies did not require exhaustion of any of the other insurance, vertical exhaustion applied for continuous loss. The State of California sued various carriers to recover the cost of remediation of a hazardous waste site. One of the carriers (Continental) was an insurer who had issued the State policies of insurance that were excess to retained limits. Various parties filed summary judgment motions to determine whether Continental's policies attached immediately upon exhaustion of the specific retention or upon exhaustion of all of the retentions across all policy periods.

State of California v. Continental Insurance Company (2017) 15 Cal.App.5th 1017.

K. Insurer's denial of coverage for completed operations is based on the inclusion of the phrase "ongoing operations" in an additional insured endorsement was improper.

1. Pulte, a general contractor, entered into subcontracts requiring subcontractors to name it as an additional insured on their policies for completed operations. One of the carriers, American Safety, issued three AI endorsements with similar language. The first endorsement provided coverage for liability arising out of the subcontractor's work which was ongoing. The second and third policies provided language for liability arising out of subcontractor's work. Various lawsuits were filed against Pulte by homeowners and Pulte tendered the defense to American Safety, who denied the tenders on the basis the coverage was limited to ongoing operations. The trial court held that the denial of the tender was improper and the additional insured endorsements reference to ongoing operations was ambiguous given that they did not effectively exclude coverage for completed operations. The Court of Appeal affirmed the trial court's ruling regarding that the additional insured endorsements were ambiguous because they combined coverage for ongoing and completed operations in one clause, and failed to limit coverage to the time of the subcontractor's ongoing operations.

Pulte Home Corp. v. American Safety & Indemnity Co. (2017) 14 Cal.App.5th 1086.

Equitable Contribution

L. Where subcontractor's policy did not provide coverage for the "additional insured" general contractor, subcontractor's insurer had no liability for equitable contribution to the general contractor's insurer.

Monticello Insurance Co. v. Essex Insurance Co. (2008) 162 Cal.App.4th 1376.

M. Where insurer's policy period began after termination of the insurance contract, subsequent insurer has no duty to defend. Plaintiffs contracted with Hilmore Development to build its home. Insurer A insured the property for one year. Insurer B insured the property in the subsequent year. During Insurer B's policy period and prior to the completion of the home, plaintiffs terminated their contract with the insured/developer. Plaintiff subsequently filed an action alleging construction defects. Insurer A settled with plaintiffs and brought this action against Insurer B for equitable contribution. The Second District Court of Appeal held that Insurer B was not liable for

equitable contribution as the policy excluded coverage for work that had not been completed, or abandoned, during its policy period.

Clarendon America Insurance v. General Security Indemnity Company of Arizona (2011) 193 Cal.App.4th 1311.

7. DEDUCTIBLES AND SELF-INSURED RETENTIONS

A. In general, a deductible provision in a policy acts as a partial offset of an insurer's indemnity obligation after the resolution of a claim. It may apply on a "per claim" or "per occurrence" basis, and an insurer's defense duties and other obligations are usually unaffected whether it is paid or not.

B. In contrast, the existence of a self-insured retention (SIR) endorsement operates to limit an insurer's obligations to the insured (i.e., defense and indemnity) until the insured has satisfied a previously-agreed upon limit of liability (called the "retained limit").

C. A number of cases have held that SIRs are equivalent to "primary coverage," and policies subject to SIRs are thus "excess policies" with no duty to defend or indemnify until the SIR is exhausted.

Pacific Employers Ins. Co. v. Domino's Pizza, Inc. (9th Cir. 1998) 144 F.3d 1270;

Padilla Construction v. Transportation Ins. Co., supra.

D. The absence of an "aggregate" retained limit in a SIR does not transform the SIR into a deductible, but requires application of the retained limit to each new claim before an insurer's duties arise.

General Star Indemnity Co. v. Superior Court (Hard Rock Cafe America, L.P.) (1996) 47 Cal.App.4th 1586.

1. Some policies provide that a separate deductible applies to each "occurrence," "accident" or "claim" made against the insured. Where numerous claims or claimants are involved, the number of **deductibles** chargeable to the insured depends

on interpretation of the terms “occurrence,” “accident” or “claim.” Where the policy provides a deductible for each “claim” made, separate claims may result in separate **deductibles**, even though all claims arise out of the same “occurrence.” To have this effect, however, the wording of the deductible must be clear and unambiguous.

2. To the extent that there is any ambiguity in the policy language, the California Supreme Court has required that any ambiguity should be resolved according to the insured's objectively reasonable expectations.

AIU Ins. Co. v. Sup. Ct. (FMC) (1990) 51 Cal.3d 807;
Bank of the West v. Sup. Ct. (Industrial Indemnity Co.) (1992) 2 Cal.4th 1254.

3. Any ambiguity as to the term "claim" is construed strictly against the carrier. Two insurance companies insured a developer under separate and consecutive General Commercial Liability policies. When the insured was sued for construction defects it tendered its defense to both carriers. The first carrier defended the insured under a Reservation of Rights, eventually settling the case. The second carrier, North American Capacity ("NAC"), argued that its duty to defend never arose because the insured never paid a self-insured retention for each home involved in the action. NAC argued that "claim" referred to each separate house. Insurer No. 1 argued that the SIR in North American Capacity's policy applied to the underlying action as a whole, not to each of the allegedly defective homes. The Fourth District Court of Appeal agreed and held that as the term "claim" was susceptible to both parties' proffered meanings, NAC had the burden of establishing "claim" existed on a per house basis and failed to meet that burden.

Clarendon America Ins. Co. v. North American Capacity Ins. Co.
(2010) 186 Cal.App.4th 556.

E. Absent further definition, the term “occurrence,” as used in a deductible clause, has been interpreted to mean a loss, and all claims due to the same *cause* were considered a single *loss* to which a single deductible and policy limit applied.

1. EOTT Energy Corp. v. Storebrand International Ins. Co. (1996) 45 Cal.App.4th 565 (where policy did not define the term “occurrence,” the court held that 635 separate thefts of diesel fuel over an 11-month period were a series of *related* acts

attributable to a *single* cause or *occurrence* (i.e., a systematic, organized scheme to steal fuel.))

2. Where a deductible is stated in terms of “per occurrence,” the term “occurrence” is subject to the same causation analysis as is applied to determine the “per occurrence” policy limits, i.e., it means the *underlying cause* of injury, rather than the injury or claim itself.

Chemstar, Inc. v. Liberty Mut. Ins. Co. (9th Cir. 1994) 41 F.3d 429, 433 (applying Calif. law).

(Plaster manufacturer (Insured) was sued for defective plaster walls in 28 different homes. Although multiple claimants were involved, the damage suffered by each resulted from the same cause. There was a single “occurrence” subject to only one deductible.)

3. Where the insured makes a claim under a single policy with adequate coverage limits, the insurer paying the loss *cannot* reduce its liability by “stacking” deductibles under other policies “triggered” by the continuing injury. The court’s rationale was that because the deductible is stated in terms of “occurrence” (cause of injury), and there is only a single occurrence, only a single deductible is chargeable to the insured.

California Pac. Homes, Inc. v. Scottsdale Ins. Co. (1999) 70 Cal.App.4th 1187.

Aggregate retention:

Under the provision quoted above, a separate SIR amount applies to *each* “occurrence.” But other policy forms may contain an *aggregate* retained limit amount (usually, at an additional cost). Such a provision *limits the insured’s risk* in the event of *several* covered claims: i.e., payments made by the insured are aggregated until the aggregate limit is exhausted; thereafter, the insurance company must cover any additional claims from the first dollar.

General Star Indem. Co. v. Sup. Ct. (Hard Rock Cafe America), *supra*, 47 Cal.App.4th at 1594, 55 Cal.Rptr.2d at 326.

The effect of a policy provision requiring the insured to retain the first portion of a loss is that the insurer is essentially providing *excess insurance*: i.e., no coverage attaches unless and until the insured becomes legally obligated for a loss in excess of the SIR. Until then, the insurer has *no duty to defend or indemnify*.

General Star Indem. Co. v. Sup. Ct. (Hard Rock Cafe America), *supra*, 47 Cal.App.4th at 1593, 55 Cal.Rptr.2d at 325;
Vons Cos., Inc. v. United States Fire Ins. Co., *supra*, 78 Cal.App.4th at 63–64, 92 Cal.Rptr.2d at 605.

F. In one case, in which five consecutive policies each contained an SIR endorsement with a retained limit of \$250,000 for any one occurrence, the court held that the insured need satisfy the SIR only once, where the damage constituted a single occurrence of continuous and progressive injury during all policy years.

California Pacific Homes, Inc. v. Scottsdale Ins. Co. (1999) 69 Cal.App.4th 1448. (“CPH”)

G. The CPH decision may be limited to its facts for a number of reasons:

1. First of all, the language of the policies in question was important to the court’s ruling. There, the policies did not contain “all sums” language, but instead required Scottsdale to pay the “. . . ultimate net loss [of any one occurrence] in excess of the retained limit . . . [for] which the Insured shall become legally obligated to pay as damages . . .;”

2. In footnote 3 of the decision, there is an inference the insured itself did not actually pay the retained limit (and was probably not obligated to do so, given the absence of such a specific requirement). Rather, that limit was deducted from the carriers’ agreed-upon contribution;

3. The parties had stipulated that the underlying claim against the insured arose from a single occurrence involving continuous or progressive property damage; and

4. The case involved an “insured vs. insurer” dispute, rather than one among the carriers themselves, and the issue of allocation for the loss among the insurers was therefore not before the court.

H Further, the court has recently held that self-insured retention limits are not “primary policies,” and the principle of “horizontal exhaustion” did not apply to require that SIRs be exhausted before a number of “excess” insurers incurred obligations under their respective policies.

Montgomery Ward & Co., Inc., v. Imperial Casualty & Indemnity Co.
(2000) 81 Cal.App.4th 356.

I. Where an SIR endorsement did not expressly require the insured to satisfy the retained limits, and the endorsement’s language made it “subject to” all of the policy’s other terms and conditions, including the “other insurance” clause, the court held payment of the SIR by other insurance was permitted. Had the carrier wanted to limit satisfaction of the SIR by payment from the insured only, it could have used specific language to that effect.

The Vons Companies, Inc. v. United States Fire Ins. Co. (2000) 78
Cal.App.4th 52.

1. Where a loss commences during one policy period and continues through several others (e.g., environmental pollution), coverage is triggered under all liability policies in effect during those periods. Unless the policies provide otherwise, each insurer is liable up to its policy limits upon exhaustion of the SIR in its own policy.

J. Under policies containing a covenant to pay for “all sums for which the insured shall become liable to pay as damages . . . ” (emphasis added), where any portion of the continuing and progressive damage occurs within any of the policies, the insured may select one of those policies triggered by the loss to fully respond to the claim. Subsequent allocation of the loss among the insurers is subject to principles of contract law, the express terms and limitations of the policies on the risk, and equitable considerations.

Armstrong World Industries, Inc., supra.

K. An insurer providing a defense to an insured must “promptly” notify other non-defending insurers of its intention to seek contribution for indemnity and defense costs paid, or otherwise it may be later barred from obtaining contribution against those non-defending carriers.

Truck Insurance Exchange v. Unigard Insurance Company (2000) 79 Cal.App.4th 966.

8. DUTY TO DEFEND AS BETWEEN PRIMARY AND EXCESS INSURERS

A. The primary insurer owes the exclusive duty to defend (and the corollary right to control the defense) even where the third party claim against the insured is for more than the amount of primary coverage, i.e., the fact that the claim *may* invade the overlying excess coverage does *not* shift the duty to defend. The same principle applies where there is a *self-insured retention*. The liability insurer is treated as an excess insurer and has no duty to defend until the self-insured retention has been exhausted by defense costs or settlements.

General Star Indem. Co. v. Sup.Ct. (Hard Rock Cafe America) (1996) 47 Cal.App.4th 1586, 1593, 55 Cal.Rptr.2d 322, 325;
Signal Cos., Inc. v. Harbor Ins. Co. (1980) 27 Cal.3d 359, 368, 165 Cal.Rptr. 799, 804.

B. No reimbursement for defense costs. The primary insurer, being obligated to defend, may not seek contribution from the excess carrier even where its successful settlement or defense relieves the excess insurer from indemnifying the injured party.

Signal Cos., Inc. v. Harbor Ins. Co., *supra*,

C. Duty to defend shifts upon exhaustion of primary coverage. Once the primary limits are exhausted, the defense burden shifts to the excess carrier. This is true even if the excess policy does not expressly provide for a defense. The obligation to defend is *implied* from the obligation to indemnify the insured after the primary insurance is exhausted. However, if there is a dispute as to whether the primary coverage is exhausted, the primary insurer must continue to defend until a judicial determination is obtained.

Aetna Cas. & Sur. Co. v. Certain Underwriters at Lloyds (1976) 56 Cal.App.3d 791, 804, 129 Cal.Rptr. 47, 55.

1. The primary insurer *cannot* avoid its duty to defend before coverage is exhausted by tendering its policy limits to the excess insurer to settle the case.

Chubb/Pacific Indem. Group v. Insurance Co. of No. America (1987) 188 Cal.App.3d 691, 698, 233 Cal.Rptr. 539, 543.

2. The excess policy may specifically exclude any obligation to furnish a defense; e.g., provisions incorporating all terms of the primary coverage “except ... the obligation to investigate and defend”; or requiring the excess insurer’s “written consent before it shall be liable for defense costs.” To have this effect, the exclusion must be clear and specific. Doubts will be resolved against the excess insurer.

3. Even if the excess policy specifically excludes the duty to defend, there may be cases in which the excess insurer is *equitably* obligated to share defense costs with the primary insurer. If there is a risk that the insured would be left without a defense, “compelling equitable principles” may require the excess insurer to reimburse the primary insurer for defense costs, even in contravention of its policy provisions.

Signal Cos., Inc. v. Harbor Ins. Co. (1980) 27 Cal.3d 359, 165 Cal.Rptr. 799.

4. The insurer’s duty to defend continues until the third party litigation ends “unless the insurer sooner proves, by facts subsequently developed, that the potential for coverage which previously appeared *cannot possibly materialize*, or no longer exists.”

Scottsdale Ins. Co. v. MV Transp. (2005) 36 Cal.4th 643, 657, 31 Cal.Rptr.3d 147, 156.

D. Exhaustion of policy limits by payment of a settlement or judgment against the insured may terminate any further defense duty. Whether payment of policy limits to one of several claimants terminates the insurer’s duty to defend is unsettled. However, if the insurer pays its policy limits to one of several claimants in the same

lawsuit, the insurer owes no further duty to defend the other claims against the insured in that lawsuit.

Johnson v. Continental Ins. Cos. (1988) 202 Cal.App.3d 477.

1. Where the policy limits are “self-consuming” (i.e., reduced by defense costs), the insurer's duty to defend terminates when it has paid out the full limits in defense even if no settlement or judgment has been reached. However, if a dispute arises over exhaustion of policy limits, the insurer must continue the defense until it obtains a judicial determination that it has exhausted its policy limits.

Hartford Acc. & Indem. Co. v. Sup. Ct. (Syntex) (1994) 23 Cal.App.4th 1774, 1778, 29 Cal.Rptr.2d 32, 36;

Aerojet-General Corp. v. Transport Indem. Co. (1997) 17 Cal.4th 38, 77, 70 Cal.Rptr.2d 118, 142.

E. CIGA is not required to assume liability if unexhausted excess insurance coverage exists to cover the claim. In an action brought by a homeowners association against the developer and subcontractors, the California Insurance Guarantee Association (“CIGA”) agreed to defend the subcontractors. The developer settled by exhausting its primary policy and a contribution by the excess insurer that did not exhaust the excess policy. CIGA took the position that the developer’s remaining excess policy constituted “other insurance” available to the HOA which must necessarily be exhausted before CIGA can be compelled to pay any settlements or judgments. The Court of Appeal held that the HOA’s claim was not “a covered claim” within the meaning of the CIGA statutes because there was other insurance available, namely the remaining limits of the developer’s excess policy. The case raises an important point that a claimant cannot “bootstrap” its claim against CIGA by releasing its right to recover under an available policy and then claim that there is no other insurance.

Park Woods Community Association v. California Insurance Guarantee Association (2006) 141 Cal.App.4th 1362.

9. TENDER AND WITHDRAWAL OF DEFENSE ISSUES

A. The duty to defend arises when the insured tenders defense of the third party lawsuit to the insurer: “Imposition of an immediate duty to defend is necessary to afford the insured what it is entitled to: the full protection of a defense on its behalf.”

Montrose Chem. Corp. v. Sup. Ct., supra.

B. The duty to defend is separate from the duty to indemnify. The insurer must pay defense costs before liability is established and apart therefrom; the insurer is “responsible for those costs whether or not there is ultimately any duty to indemnify the insured for the claim.”

Montgomery Ward & Co., Inc. v. Imperial Cas. & Indem. Co. (2000) 81 Cal.App.4th 356, 373, 97 Cal.Rptr.2d 44, 55.

C. A tender by the insured creates a duty to defend where the following conditions are met: (1) there is a policy in effect and if “Suit” has been filed against the insured: CGL policies typically provide that the insurer shall have the “right and duty to defend any *suit* against the insured ... and *may* make such investigation and settlement of any *claim* or *suit* as it deems expedient.” Current CGL policies define suit to include arbitrations, alternative dispute resolution proceedings [CG 00 01 12 04, Sec. V, ¶ 18] and administrative hearings.

Foster-Gardner, Inc. v. National Union Fire Ins. Co. (1998) 18 Cal.4th 857, 863, 77 Cal.Rptr.2d 107, 111.

1. Even though there is no duty to defend, insurers are authorized to “investigate and settle” pre-lawsuit “claims.” It is often in the insurer's interest to assist its insured in administrative proceedings that could lead to an award of damages in subsequent civil proceedings which they will ultimately have to indemnify. “(H)owever, this is a judgment call left solely to the insurer.”

Foster-Gardner, Inc. v. National Union Fire Ins. Co., supra, 18 Cal.4th at 883, 77 Cal.Rptr.2d at 125.

2. A tender of a claim simply requires the insured to provide some notice of the claim to the insurer in order to trigger its duty to defend the insured. No formal request that the insurer undertake the defense is required. The tender can either be formal

or constructive. A defense is owed if the insurer has “constructive” notice of the tender, i.e., notice of facts that would put a reasonable person on inquiry. If the insurer fails to make inquiry in the face of such facts, and thus erroneously fails to defend, it will be liable for breach of contract.

California Shoppers, Inc. v. Royal Globe Ins. Co. (1985) 175 Cal.App.3d 1; Truck Ins. Exch. v. Unigard Ins. Co. (2000) 79 Cal.App.4th 966, 979, 94 Cal.Rptr.2d 516.

3. Prejudicial delay by the insured in tendering the claim may excuse the insurer from liability on the claim (i.e., it may excuse not only the duty to defend but also the duty to indemnify). “(I)f successful, the insurers’ notice defense could prevent any recovery under the policy.” However, The *insurer* bears the burden of proving it was substantially prejudiced by the delay.

Select Ins. Co. v. Sup.Ct. (Custer) (1990) 226 Cal.App.3d 631, 639, 276 Cal.Rptr. 598, 603.

4. Similarly, an insurer must suffer actual and substantial prejudice to avoid default judgment following lack of notice from insured. Plaintiff filed an action against a general contractor (insured) for water leaks relating to the building, alleging causes of action for negligence and breach of contract. The insured did not tender the defense to the insurer and a default judgment was taken against the insured. The insurer denied coverage based on the failure of the insured to notify and failure to cooperate with the investigation. Plaintiff homeowner brought suit against the insurance carrier to recover the amount of the default judgment. The Court of Appeal held that when a default judgment results from lack of notice by the insured, the insurer is liable unless it suffered actual and substantial prejudice. The inability to investigate the claim or present a defense in the underlying suit does not satisfy the prejudice requirement. To demonstrate substantial prejudice, the insurer must show at the very least that if the notice clause had not been breached, there was a substantial likelihood that the insurer would have received a favorable judgment, settled the claim for less, or been able to reduce the insured’s liability.

Belz v. Clarendon American Insurance Co. (2007) 158 Cal.App.4th 615.

D. An insured may incur investigation or legal expenses in connection with a third party lawsuit before tendering defense to the insurer. Whether the insured is entitled to recover such expenses from the insurer depends on the terms of the policy. Liability policies usually prohibit “voluntary” payments by the insured. For example: “No insured will, except at that insured's own cost, voluntarily make a payment, assume any obligation, or incur any expense, other than for first aid, without our consent.” [CG 00 01 12 04, Sec. IV, ¶ 2.d.]

1. Courts disagree whether liability insurers must reimburse an insured for investigation or legal expenses voluntarily incurred by the insured before tendering defense to the insurer. Several cases hold the insurer owes no duty to reimburse the insured for pre-tender expenses because it owed *no duty to defend* the insured until the defense was tendered. For example, a Developer (Insured) spent more than \$1.4 million to repair water intrusion defects in a residential development *before notifying* its liability insurer. The insurer had no duty to reimburse the insured for the costs incurred.

Jamestown Builders, Inc. v. General Star Indem. Co. (1999) 77 Cal.App.4th 341.

2. Other cases treat the matter as unsettled. “The (no voluntary payments) provision does not specifically refer to the costs of defense and there is a *question what a reasonable insured would understand* reading the provision.”

Fiorito v. Sup.Ct. (State Farm Fire & Cas. Co.) (1990) 226 Cal.App.3d 433.

E. Recent cases have defined the concept of “suit” for defense purposes.

1. A homeowner's association has served a developer with a Notice of Commencement of Proceedings pursuant to the Calderon Act. Developer sued its additional insurers for defense costs. The insurers contended that the Calderon process did not constitute a “suit” within the meaning of the defense agreement in its CGL policies. The Fourth District Court of Appeal held that the Calderon process is an integral part of construction defect litigation and therefore the carriers must provide a defense.

2. The California Supreme Court recently held that the definition of “suit” is a broad definition. The United States Department of Interior contracted with a general contractor to supply siphons for an aqueduct. The general contractor contracted

part of the job to a subcontractor. The Department of Interior ultimately determined that the siphons were defective and the matter was settled through a payment of \$10,000,000. The subcontractor insurers refused to defend and indemnify the general contractor and subcontractor. The California Supreme Court held that a reasonable policyholder would believe that a policy providing coverage for a "suit" would provide coverage for Department of Interior proceedings. The Supreme Court defined the term "suit" in a comprehensive general liability insurance policy as a core proceeding initiated by the filing of a complaint, and held that the IBCA proceeding was a suit for the purposes of the duty to defend and the potential coverage, thus broadening the definition of "suit."

Ameron v. Insurance Company of the State of Pennsylvania (2010) 50 Cal.4th 1370.

F. Withdrawal.

1. If the insurer is defending under a reservation of rights and subsequently determines there is in fact *no potential* for coverage, it may withdraw by notifying the insured that it will no longer furnish a defense in the action. An insurer may "withdraw from defending a claim once it is able to demonstrate, by reference to *undisputed* facts, that the claim *cannot* be covered." If the termination is challenged by the insured, the insurer bears the burden of proving the absence of any potential for coverage.

Ringler Assocs. Inc. v. Maryland Cas. Co. (2000) 80 Cal.App.4th. 1165.

2. One of the more interesting issues regarding withdrawal is based on the insured's failure to cooperate. Such withdrawal is justified; however, only if the insured's conduct has *substantially prejudiced* the insurer's ability to conduct the defense. "Substantially prejudiced" has not been defined by the courts in this context.

Hall v. Travelers Ins. Cos. (1971) 15 Cal.App.3d 304.

10. ARBITRATION AND SETTLEMENT ISSUES

A. Arbitration.

As noted above, under the new “fix it” law, arbitration is available to builders to resolve claims of homeowners. Similarly, arbitration is available in the commercial context with respect to construction issues. This presents several issues.

1. The law is well settled that a party to a contract which contains an arbitration provision cannot compel a non-party to arbitrate. The courts have repeatedly held that arbitration is consensual in nature and that a contract agreement between two parties cannot bind a non-party to the contract and, therefore, an insurer cannot be bound by that agreement.

Crowley Maritime Corp. v. Boston Old Colony Insurance Co. (2008) 158 Cal.App.4th 1061.

2. This comes up more frequently in the situations where a general contractor will have an arbitration provision in an agreement with an owner, but has no similar provisions in its subcontract agreements with the subcontractors. Under that scenario, the general contractor is left to defend the arbitration and has to bring a companion civil litigation against the non-arbitrating subcontractors. This can result in an additional time and expense in defense, and potentially inconsistent rulings. Where this matter routinely comes into play is cases involving pool contractors who generally have arbitration provisions in their agreements but have no subcontract agreements with their “long time” subcontractors such as the gunite supplier or deck coating subcontractors.

3. Plaintiffs have the right to have a statute of limitations issue heard before an arbitrator, and a trial court has no authority to decide that issue. The California Supreme Court recently ruled that an arbitration agreement obligates the parties to resolve their controversies, including disputes about the viability of potentially time-barred claims, before an arbitrator rather than a court.

Wagner Construction v. Pacific Mechanical Corp. (2007) 41 Cal.4th 19.

4. However, the question of whether or not a plaintiff has agreed to arbitrate its claims must be heard before the court who has the authority to determine the enforceability of the provision. In a recent Court of Appeal decision, the court noted that a party cannot be forced to arbitrate anything, including the arbitability of the claim until

a court has made a threshold determination that the party did agree to arbitrate “the claim.”

Bruni v. Didion (2008) 106 Cal.App.4th 1272.

5. A party who obtains an order denying a petition to compel arbitration is a “prevailing party” in an action on the contract when this is the only issue before the court even though the merits of the underlying contractual dispute have not been resolved.

Otay River Constructors v. San Diego Expressway (2008) 158 Cal.App.4th 796.

6. Arbitration provisions that risk conflicting rulings on common issues are not enforceable. In a case brought by mobile home residents against a mobile home park owner for alleged failure to maintain the park's facilities, some of the leases, but not all of them, contained an alternative dispute resolution provision. The mobile home park owner sought to enforce the arbitration provision. The court ultimately determined that there was a possibility that resolution of some of the common questions in different forums (i.e., arbitration or superior court) presented the possibility that inconsistent rulings might occur, and pursuant to California Code of Civil Procedure Section 1281.2 (c) the court did not enforce the arbitration provision.

Abaya v. Spanish Ranch I, LP (2010) 189 Cal.App.4th 1490.

7. Arbitration provision is unenforceable in a lawsuit that arises from related transactions. Developer built and sold a home to a famous actor, who subsequently sold it to plaintiff. Plaintiff's purchase agreement with the actor contained an arbitration clause. Plaintiff later sued the developer for alleged construction defects and sued the actor for failure to disclose the defects. The actor sought to compel plaintiff to arbitrate his claims against it pursuant to the arbitration clause, contending that plaintiff's claims against it were only tangentially related to its construction defect related claims against the developer. The trial court denied the actor's motion, finding that there was a possibility of conflicting rulings on common issues of law and fact. The Court of Appeal held that the trial court did not abuse its discretion in denying the actor's motion to compel arbitration against the plaintiff. The claims arose out of a series of related transactions which is a proper basis for a denial pursuant to California Code of Civil

Procedure Section 1281.2(c). It was reasonable for the trial court to conclude that the entire case should be resolved in a single litigation.

Lindemann v. Hume (2012) 204 Cal.App.4th 556.

8. Unreasonable delay in seeking arbitration can result in waiving the right to arbitrate. Plaintiff brought a Superior Court action against defendant for claims relating to the sale of a vehicle. Defendant proceeded to litigate the matter in Superior Court, including filing demurrers and engaging in the discovery process. On the eve of trial, defendant sought to compel arbitration. The Court of Appeal held that the defendant had waived its right to arbitrate by using the court proceedings for its own purposes, and therefore the public policy argument for seeking arbitration (to take advantage of the efficiencies of arbitration) was frustrated, and therefore arbitration was denied.

Adolph v. Coastal Auto Sales, Inc. (2010) 184 Cal.App.4th 1443.

9. Arbitration clauses in homeowner's association's CC&Rs which seek to have home buyers give up their rights to a jury trial are enforceable. Plaintiff HOA filed a construction defect action against developer. The developer filed a motion to compel arbitration based upon an arbitration clause in the recorded CC&Rs. The trial court held that the arbitration agreement was unconscionable and therefore unenforceable. The Court of Appeal affirmed, finding that the clause did not constitute an agreement sufficient to waive the plaintiff's right to a jury trial for construction defect claims. However, the California Supreme Court recently held that the arbitration provision was enforceable against the plaintiff, consistent with the provisions of the Davis-Stirling Act and was not unconscionable.

Pinnacle Museum Tower Association v. Pinnacle Market Development (2012) 55 Cal.App.4th 223.

10. Bad faith issues are to be addressed before arbitration of Civil Code Section 2860 fee dispute issues. Plaintiff HOA filed a construction defect suit against the developer, who in turn filed a cross-complaint against the general contractor. The developer tendered its defense to general contractor's insurer who had issued several CGL policies. The insurer immediately acknowledged the tender, but stated it was investigating the claim, and proceeded to investigate the claim (for the next two years). As a result of the delay in determining its investigation, the developer advised insurer of

its intent to file a bad faith complaint if the insurer did not respond meaningfully within 30 days. The insurer then agreed to defend the developer under Reservation of Rights and then acknowledged a *Cumis* obligation to provide separate counsel pursuant to Civil Code Section 2860. The insurer later disputed the fees submitted by Cumis counsel and asked the developer to submit the billing issues to arbitration. The developer refused to arbitrate, and the insurer invoked its right to arbitration under Section 2860 and filed a petition to compel arbitration, which the developer sought to dismiss. The Court of Appeal acknowledged the insurer's right to arbitration pursuant to Civil Code Section 2860, but held that the parties should first proceed with developer's bad faith lawsuit which would allow the parties to address threshold issues such as the duty to defend, any breach, waiver and/or bad faith.

Janopaul + Block Companies, LLC v. Superior Court (2011) Cal.App.4th 1239.

11. An arbitration award must be vacated if the arbitrator fails to disclose a conflict of interest. The Court of Appeal held that the California Arbitration Act and California Ethics Standards for Neutral Arbitrators in Contractual Arbitrations require a neutral arbitrator to disclose that a lawyer in the arbitration is a member of the administering dispute provider resolution organization, and non-compliance requires a trial court to vacate the arbitration award.

Gray v. Chiu (2013) 22 Cal.App.4th 1355.

12. Arbitrators' "insubstantial" professional relationships need not be disclosed to parties and is not sufficient to overturn an arbitration award. After a matter was submitted to arbitration, plaintiffs hired a private investigator to determine whether there were any undisclosed relationships between the arbitrator and the defendant. The investigator found that the arbitrator and the head of defendant's appellant department were members of the L.A. County Bar's Executive Committee Section. The plaintiff petitioned to vacate the arbitration award based upon this failure to disclose this relationship by the arbitrator. The Appellate Court held that an arbitrator must only disclose relationships that are substantial and involve financial considerations that create an impression of possible bias not those that are slight or insubstantial as in the present case.

Nemecek & Cole v. Horn (2012) 208 Cal.App.4th 641.

13. An arbitrator's findings are not binding upon a trial court where arbitrator's findings expressly contravene the legislature's clear expression of public policy. In a construction action, the plaintiff asserted that defendant was an unlicensed contractor. Defendant asserted claims for certain monies. The arbitrator only made minor adjustments to the profit sharing percentages denying defendant's claims regarding the unlicensed contractor status. The Court of Appeal held that the arbitrator's decision regarding the application of Business & Professions Code Section 7031 (regarding unlicensed contractors) exceeded the arbitrator's powers as it enforced an illegal contract, and was in violation of the clear expression of the legislature with respect to the public policy concerning the licensing of contractors.

Ahdout v. Hekmatjah (2012) 213 Cal.App.4th 21.

14. In awarding attorney's fees, an arbitrator can disregard the agreement and rely on Civil Code Section 1717. In the underlying case, the Fourth District Court of Appeal held that arbitrators are allowed to render decisions that are within the scope of the controversy submitted to them, and any related error would constitute a legal error which is not subject to correction. The arbitrator found that the prevailing party definition in the arbitration agreement violated California law, and instead applied the definition in Civil Code Section 1717. The court held that was a proper use of the arbitrator's powers.

Safari Associates v. Superior Court (2014) 231 Cal.App.4th 1400.

15. The arbitrator has sole authority to decide whether an arbitration agreement delegating resolution of enforceability issues to an arbitrator is unconscionable or enforceable. The First District Court of Appeal held that the trial court lacked the authority to rule on whether the arbitration agreement was unconscionable or enforceable. The parties' delegation of authority to an arbitrator to decide these issues was clear and unambiguous and was not revocable under state law.

Tiri v. Lucky Chances, Inc. (2014) 226 Cal.App.4th 231.

16. Defendants did not waive their right to compel arbitration by waiting a year to do so because the delay was not unreasonable and prejudicial. Plaintiff filed a wrongful termination suit against defendant. Defendant repeatedly informed plaintiff's counsel that plaintiff had agreed to arbitrate any dispute and threatened to claim he had

waived his right to file the suit if he did not commence arbitration. Defendant did not immediately take action to enforce arbitration after plaintiff filed the lawsuit. The First District Court of Appeal held that defendant not waive its right to compel arbitration by waiting a year or so to do so, because it did not unreasonably delay invoking its right, as defendant had consistently declared its intention to arbitrate even before plaintiff filed suit.

Gloster v. Sonic Automotive, Inc. (2014) 226 Cal.App.4th 438.

17. Ambiguous agreements for alternative dispute resolution are unenforceable. The plaintiff filed an action for wrongful termination and other related claims against her former employer. Defendants filed a petition to compel arbitration based on evidence that plaintiff signed an agreement for alternative dispute resolution. The trial court denied the petition on the grounds that defendants had failed to prove that plaintiff had agreed to submit her claims to final and binding arbitration. The California Court of Appeal (Fourth District) held that the agreement was unenforceable because it was ambiguous regarding which disputes would be subject to arbitration and which would be subject to mediation with a grievance and arbitration procedure contained in a collective bargaining agreement.

Flores v. Nature's Best Distribution LLC (2016) 7 Cal.App.5th 1.

18. A declaration supporting a petition to compel arbitration sufficiently authenticated an employee's electronic signature. The plaintiff sued defendant and others claiming wrongful termination and whistleblower retaliation. Defendants filed a petition to compel arbitration. In support of its petition, defendants filed a declaration by their systems consultant indicating that plaintiff had electronically executed certain agreements including an employment agreement and the Dispute Resolution Procedure. The trial court denied the petition to compel arbitration on the grounds that defendants had not provided evidence to authenticate the Dispute Resolution Procedure and therefore did not establish the existence of an enforceable arbitration agreement between the parties. The Court of Appeal (Second District) reversed the trial court's decision holding that the initial declaration established the existence of an agreement to arbitrate between the parties bearing plaintiff's electronic signature. Therefore, defendants had met their burden in seeking to compel arbitration by sufficiently authenticating plaintiff's electronic signature under California Evidence Code Section 1401 and California Civil Code Section 1633.9(a) of the Uniform Electronic Transactions Act.

Espejo v. Southern California Permanente Medical Group (2016) 246 Cal.App.4th 1047.

19. Plaintiffs sued defendant for \$100,000 in unpaid invoices. The parties agreed to arbitrate the dispute of the unpaid invoices and the agreement specified the arbitrator must provide a written decision with findings of fact, including California law, as if he were a Superior Court judge. The arbitration agreement also provided for full judicial review of the arbitration award as if it were decided by a court. After the arbitrator ruled, trial court affirmed the award against the defendant but vacated the award against the defendant's affiliates, who had been added to the arbitration (during the course of arbitration). Trial court also denied all parties' requests for post-award attorney's fees but held such fees could be awarded in the discretion of the arbitrator. Both parties appealed. The Court of Appeal reversed the judgment in favor of the plaintiff and affirmed the order granting the defendant's affiliates' motion to vacate the arbitrator's award. The appellate court held that the trial court prejudicially erred by failing to apply the correct standards in reviewing the arbitrator's award, holding that the trial court should have reviewed the arbitrator's decision under the appellate review standards of a court's judgment. The Court of Appeal held on the merits that substantial evidence did not support the arbitration award and that it alleged that certain contracts violated the Statute of Frauds. Given that the defendant did not agree to submit to arbitration any claim for lost profits, the arbitrator had no right to award damages in such a claim.

Harshad & Nasira Corporation v. Global Sign Systems (2017) 14 Cal.App.5th 523.

B. Settlement Related Issues.

1. The "cooperation" action and "voluntary" payments clauses in liability policies generally, as a preliminary matter, allow an insurer to control a settlement of a claim, and courts have recognized an insurer's right to settle a claim over an insured's objections.

Maryland Casualty v. Imperial Contracting Co. (1989) 212 Cal.App.3d 712, 720-721.

2. While an insured has general discretion to control settlement decisions, evaluating a settlement demand, an insurer may not consider its own coverage beliefs. An insurer must act as if it alone were liable for the entire amount of any judgment or settlement.

Johansen v. Cal State Auto Association Inter-Insurance Bureau (1975) 15 Cal.3d 9.

3. Common law release will no longer discharge a non-settling defendant from liability when plaintiff and co-defendant enter into a settlement that is not in good faith. The plaintiff brought a negligence action against his doctor and the hospital. The doctor settled with the plaintiff for \$1,000,000 in exchange for a Release of All Claims. At trial the jury found both the doctor and the hospital liable for plaintiff's damages. The hospital contended that under the common law "release rule," plaintiff's settlement and release of the doctor also released the non-settling hospital from liability. The California Supreme Court held that the release rule would no longer be followed in California because it yields inequitable results. When a settlement does not satisfy the court's "good faith" statutory requirement, liability will be apportioned under the "setoff-with-contribution" approach.

Leung v. Verdugo Hills Hospital (2012) 55 Cal.App.4th 291.

4. Cash settlement where the plaintiff releases and waives all claims against the builder precludes plaintiff from filing a subsequent lawsuit. Plaintiff purchased a newly constructed residence built by a licensed general contractor. After escrow closed, plaintiff filed a complaint with the Contractors State License Board against the contractor for construction defects. During arbitration, the contractor agreed to settle the dispute for \$25,000, the settlement agreement included a general Release of All Claims of all known and unknown claims and a Civil Code Section 1542 waiver. Subsequently, the plaintiff filed an action against the contractor and its surety based on an alleged defect in the roof that was later discovered. The Second District Court of Appeal held that the Release of All Claims was enforceable against plaintiff and precluded the subsequent lawsuit. The Right to Repair Act (Civil Code Section 895 et seq.) authorizes cash settlements and permits the builder to negotiate a reasonable release in exchange for cash payment.

Belasco v. Wells (2015) 234 Cal.App.4th 409.

5. Typed name at the end of an e-mail is not, by itself, an “electronic signature” under California Uniform Electronic Transactions Act. Plaintiff and defendant attempted to negotiate a settlement of a business dispute via e-mail communications. At the end of the series of exchanges, plaintiff sent defendant an e-mail of the terms of their final settlement offer. They stated that if defendant agreed to the terms, plaintiffs would get the “formal” settlement paperwork finalized. Subsequently, plaintiffs contended that defendant’s e-mail was a signed agreement legally binding him to the settlement terms proposed in the final offer e-mail. The First District Court of Appeal held that defendant’s printed name at the end of his e-mail was not an electronic signature under California’s Uniform Electronic Transactions Act (“UETA”) and did not legally bind him to the settlement agreement. The court found that while the exchange of e-mail showed that the parties agreed to negotiate the terms of the settlement by e-mail, the plaintiff did not show that the parties ever agreed to conduct transactions by electronic means or that defendant intended his typed name to electronically sign the settlement agreement.

J.B.B. Investment Partners, Ltd. v. Fair (2014) 232 Cal.App.4th 974.

6. Plaintiff who dismisses action after settling is prevailing party for cause purposes. The plaintiff sued the defendant for wrongful termination. Before the jury was impaneled, the parties agreed to settle the case with said settlement to be paid by defendant. Following plaintiff’s request for dismissal, the trial court entered an amended judgment which failed to mention that plaintiff was paid monies in exchange for a dismissal of the party. Each party claimed to be the prevailing party entitled to recovery of costs. The California Supreme Court held that when a defendant pays money to a plaintiff in order to settle a case, the plaintiff obtains a net monetary recovery, and is thus a prevailing party for the purpose of costs under Code of Civil Procedure Section 1032(a)(4). Code of Civil Procedure Section 1032(b) states that the prevailing party is entitled as a matter of right to recover costs in any action or a proceeding. The court further concluded that the definition of a “prevailing party” as “a defendant in whose favor a dismissal is entered” was not intended to include defendants that entered into monetary settlement in exchange for a dismissal. The court expressly disapproved the holding in Chinn v. KMR Property Management (2008) 166 Cal.App.4th 175.

DeSaulles v. Community Hospital of the Monterey Peninsula (2016) 62 Cal.4th 1140.

7. A release submitted as part of a settlement offer is invalid for cost shifting purposes if it is contingent upon plaintiff executing a general release. A pedestrian sued a motorist alleging negligence after an “auto versus pedestrian” accident where plaintiff was struck by the car. Defendant issued a statutory Offer to Compromise pursuant to California Code of Civil Procedure Section 998. The plaintiff did not accept the offer and the matter proceeded to trial. The ultimate jury award (including allocations) resulted in a judgment in plaintiff’s favor, but less than the statutory offer. Defendant sought to recover costs under the cost shifting provisions of Code of Civil Procedure Section 998. Plaintiff asserts that the statutory offer was invalid and that she was entitled to her costs as the prevailing party. The trial court ultimately made a determination that the defendant’s settlement offer was invalid under Code of Civil Procedure Section 998 as it was over broad and sought a release of all claims in a dismissal as opposed to just those claims set forth in the litigation. The court denied the defendant’s motion to tax costs. The Court of Appeal (Second District) affirmed the trial court’s order holding that under Code of Civil Procedure Section 998 a general release beyond the claims asserted in the litigation renders a settlement offer invalid. The court specifically held that the language releasing liability from “any and all claims” including a Civil Code Section 1542 waiver, without limitation to the claims arising out of the subject accident was overly broad and therefore the statutory Offer to Compromise was invalid.

Ignacio v. Caracciolo (2016) 2 Cal.App.5th 81.

C. Mediation.

In a case which has major implications for construction defect actions, a recent California Court of Appeal decision held that trial courts do not have the authority to order parties in a complex civil action to attend and pay for private mediation. The court ruled that the participation in the mediation is completely voluntary and the mediator must refrain from coercing any party into participating. Compulsory payment and attendance is not authorized by the mediation program and is contrary to the voluntary nature of mediation. The case cited can be used for the proposition that a mediator cannot require the personal appearance of an adjustor unless the settlement conference is being held as a mandatory settlement conference. Under the California Rules of Court, there can be only one mandatory settlement conference in a case.

Jeld-Wen v. Superior Court (2007) 146 Cal.App.4th 536.

1. A settlement agreement prepared during mediation is not enforceable unless it states that it is intended to be enforceable. In a matter being mediated under Judicial Arbitration Mediation Services, the parties entered into an agreement which indicated that the document comprised the “settlement terms.” The parties were unable to finalize the settlement, and the plaintiff petitioned to compel arbitration pursuant to the JAMS rules. The California Supreme Court held that the settlement document was not admissible as it did not reflect an agreement. California Evidence Code Section 1123 provides that a settlement agreement prepared in the course of mediation is admissible if the agreement provides that it is admissible or enforceable or “words to that effect.” The court ruled that parties express such an intent only through a direct statement of intention to be bound by the signed document.

Fair v. Bakhtiari (2006) 40 Cal.4th 189.

2. Plaintiff, a beneficiary of her deceased husband, brought a claim alleging breach of contract against the executor of the decedent’s estate. Plaintiff, along with two of the decedent’s children, had executed a settlement agreement during the course of mediation. One of the decedent’s children was not present at the mediation and did not sign the settlement agreement. At trial, plaintiff sought to introduce the settlement agreement and enforce its provisions. The court held that a mediation settlement agreement was inadmissible, and before an agreement can be enforced, it must first be admissible. The document prepared for purposes of mediation was inadmissible under Evidence Code Section 1119.

Rael v. Davis (2008) 166 Cal.App.4th 1608.

3. A stipulated written settlement created at mediation was enforceable even though not signed by defendant's officer, and mediation privilege barred evidence of coercion and duress.

The defendant medical center terminated the plaintiff's employment as an Anesthesiologist. The plaintiff filed suit under the California Whistleblower Protection Act alleging that he was wrongfully terminated for reporting alleged illegal conduct of the defendant. The parties attended a mediation, and as a result thereof, executed a stipulated settlement. After the parties had approved the agreement but before they executed it, the plaintiff indicated that he would not sign it, alleging that the defendant

did not properly execute it because the signatory was not an officer of defendant, and that among other things, the agreement did not contain all material terms, and that it was obtained by duress and coercion. The Court of Appeal held that the plaintiff failed to meet his burden of proof on any of the allegations, and therefore the settlement was enforceable. The court further concluded that the defendant's authorized representative's signature was sufficient for an enforceable settlement in accordance with California Code of Civil Procedure Section 664.7. The court further found that the mediation confidentiality provisions of Evidence Code Section 1119 barred evidence of alleged coercion or duress.

Provost v. Regents of the University of California (2011) 201Cal.App.4th 1289.

4. Section 998 Offer to Compromise must be interpreted as a contract and silence on an issue does not preclude its recovery.

Chinn v. KMR Property Management (2008) 166 Cal.App.4th 366.

5. Mediation related communications between attorneys and their clients are confidential and are not admissible in a legal malpractice action. The California Supreme Court has recently held that all attorney-client communications throughout mediation, including pre-mediation, is protected speech and not admissible in legal malpractice actions.

Cassel v. Superior Court (2011) 51 Cal.4th 113.

6. Mediation privilege prohibits mediator from testifying to anything about a settlement agreement, including its number of pages. The Second District Court of Appeal recently held that mediation confidentiality statutes prohibit a mediator from discussing anything about the agreement including who executed the agreement, the number of pages and the like.

Radford v. Shehorn (2010) 187 Cal.App.4th 852.

7. A party may not circumvent mediation confidentiality by advancing inferences about the mediation communication. A former client filed a malpractice suit against its counsel alleging that the attorney failed to properly advise of the risk of

personal liability posed by the settlement agreement. The plaintiff conceded that the damages in the matter arose entirely from entering into the settlement agreement, with all of the various communications with counsel concerning the settlement agreement occurring during mediation. The Second District Court of Appeal held that plaintiff could not rely on inferences of what may have happened during a mediation to prove a case of legal malpractice. The court expressly noted that Evidence Code Section 1115 prohibits plaintiff from directly or indirectly relying upon communications made in the course of mediation, and that no statutory exception allows the attorney to rebut the charges against it with evidence of advice it gave plaintiff during mediation.

Amis v. Greenberg Traurig (2015) 2015 WL 1245902.

8. A party seeking contractual attorney's fees subject to Civil Code Section 1717 is not required to file a Memorandum of Costs. This case arises out of a settlement agreement that contained several substantive provisions and procedural provisions, including an arbitration provision that awarded attorney's fees to the prevailing party. After the arbitrator issued an award in defendant's favor, defendant filed a motion for award of attorney's fees and costs relying on Civil Code Section 1717 and Code of Civil Procedure Section 1033.5. Plaintiffs opposed the motion arguing that California Rule of Court 3.1700 required defendant to file a Memorandum of Costs. The Second District Court of Appeal held that pursuant to Code of Civil Procedure Section 1033.5, the proper method for recovering contractual attorney's fees is an item of costs awarded upon notice of motion. The court concluded that a party seeking attorney's fees incurred before judgment under Civil Code Section 1717 is not required to file a Memorandum of Costs, in addition to filing a fee motion in compliance with California Rule of Court 3.1702.

Kaufman v. Diskeeper Corporation (2014) 229 Cal.App.4th 1.

9. A trial court "stay order" to allow mediation and completion of discovery does not toll five-year statute. After approximately five and a half years, defendants brought a motion to dismiss for failure to bring the action to trial within the five year time frame as required by Civil Code Section 583.310. Plaintiff's claim that the five-year statute had been tolled several times. In computing the period of the pendency of the action, the trial court did not exclude time during which it had vacated the party's trial date and ordered a 120-day stay of proceedings to allow the parties to participate in mediation. California Supreme Court held that the trial court was within its discretion to

compute the time attributable to partial stay proceedings but did not qualify for tolling the five-year period. The California Supreme Court stated that the prosecution of an action is stayed under Civil Code Section 583.340(b), only when the stay encompasses all proceedings in the action, thus preventing the prosecution of the action altogether. Here, the Supreme Court found that the stay did not apply to all proceedings but only actions, since the trial court's order required parties to continue any outstanding discovery and to participate in mediation. The court found that no circumstances of impracticability had been created by the trial court's stay, so the five-year period had not been tolled.

Gaines v. Fidelity National Title Insurance Company (2016) 62 Cal.4th 1081.

D. Statutory Offers to Compromise.

Pre-judgment interest accrues from the date of the first rejected 998 settlement offer. In a situation where a plaintiff provided subsequent settlement offers (reducing the settlement demand) and obtains a jury verdict in excess of the settlement offer, pre-judgment interest runs from plaintiff's first settlement offer.

Ray v. Goodman (2006) 142 Cal.App.4th 83.

1. A party who accepts a Section 998 offer is entitled to costs and fees unless they are specifically excluded in the offer. A recent Court of Appeal decision held that despite broad release language in a settlement offer, the rule is that a Section 998 Offer to Compromise excludes fees only if it says so expressly.

Engle v. Copenbarger & Copenbarger (2007) 157 Cal.App.4th 165.

2. California Code of Civil Procedure Section 998 offer does not constitute general appearance under code. Plaintiff filed a complaint against two foreign defendants. The defendants filed motions to quash due to lack of personal jurisdiction, and shortly thereafter served plaintiff with a California Code of Civil Procedure Section 998 settlement offer. Plaintiff contended that service of the offer constituted a general appearance and that defendants waived their right to contest personal jurisdiction. The Fourth District Court of Appeal held that the "act" of serving the Section 998 Offer did not constitute a general appearance.

Air Machine Com SRL v. Superior Court (2010) 186 Cal.App.4th 414.

3. Costs under California Code of Civil Procedure Section 998 denied where early settlement offer precludes reasonable opportunity to evaluate the offer. In a personal injury action, the jury found defendant was the sole cause of the accident. Plaintiff claimed entitlement to expert fees and pre-judgment interest because defendant had allegedly failed to accept plaintiff's California Code of Civil Procedure Section 998 offer settlement which was served concurrently with the summons and complaint. The Fifth District Court of Appeal held that plaintiff's Section 998 offer was not reasonable or made in good faith because there was no special circumstance present to show that at the early juncture in the case defendant's counsel had access to information or a reasonable opportunity to evaluate the plaintiff's offer within the 30 day statutory acceptance.

Najera v. Huerta (2011) 191 Cal.App.4th 872.

4. A California Code of Civil Procedure Section 998 statutory Offer to Compromise must contain a provision stating that the recipient can accept the offer by signing a statement that the offer is accepted. Plaintiff, acting as his own attorney, sued defendant as a result of a car accident. Defendant made a pre-trial settlement offer under Code of Civil Procedure Section 998 to waive costs in exchange for a dismissal. Plaintiff did not accept the offer, and after a one day trial, the court found in the defendant's favor. Defendant then filed a Memorandum of Costs and the court subsequently ordered his costs. The plaintiff appealed the decision and argued that the pre-trial settlement offer did not comply with the strict language of the code. The Fourth District Court of Appeal held that, pursuant to Code of Civil Procedure 998(b) a pre-trial settlement offer must include a provision that allows the accepting party to indicate acceptance of the offer. The statute's language had been amended to eliminate any uncertainty by removing the possibility that an oral acceptance might be valid. The Appellate Court then found that the prior Code of Civil Procedure Section 998 offer was invalid.

Puerta v. Torres (2011) 195 Cal.App.4th 1267.

5. Subsequent offers of judgment do not extinguish earlier offers of judgment. When the plaintiff was injured in an electrical accident at work, the plaintiff sued the company who had performed demolition at that job site. The plaintiff and his wife subsequently made two separate offers of compromise. Defendant rejected both

offers. After a jury trial, plaintiffs were awarded damages, and the wife' award was equal to the first offer of judgment. Based upon said award, plaintiffs sought over \$500,000 of itemized costs incurred after the first Code of Civil Procedure Section 998 offer. Defendant filed a motion to tax certain costs incurred between the first and second offers contending that the second offer of judgment operated to extinguish the first offer of judgment. The Second District Court of Appeal held that since the second offer was made after the initial offer statutorily lapsed, each offer remained valid and enforceable. The second offer did not operate to extinguish the earlier offer.

Martinez v. Brownco Construction Co., Inc. (2012) 203 Cal.App.4th 507.

6. Co-defendant's statutory offer is not assigned to defendant assuming co-defendant's defense to determine prevailing party, and defendant can recover costs paid by a third party. The plaintiff brought a negligence action against a medical center. The medical center served a California Code of Civil Procedure Section 998 settlement offer which expired. The plaintiff subsequently named an additional party as a defendant. That party never served a 998 offer on plaintiff. The third party defended the medical center pursuant to an indemnity provision. All parties stipulated in court that for the purposes of trial, the medical center and the third party would be "treated as one." The jury returned a verdict for plaintiff for less than defendant's statutory offer. After trial, the defendant and third party jointly requested costs and expert's fees pursuant to California Code of Civil Procedure Section 998. The plaintiff specifically argued that the third party had not made its own Code of Civil Procedure Section 998 offer, and therefore was not a prevailing party for purposes of the statute. The Court of Appeal (Fourth District) held that the third party was not automatically assigned the defendant's Code of Civil Procedure 998 offer, but that the defendant may recover costs paid by the third party pursuant to the indemnity agreement. The court separately analyzed the defendants to determine prevailing party status. The court concluded that despite the stipulation to treat the two defendants as one, plaintiff was the prevailing party as to the third party because the third party never made a Code of Civil Procedure Section 998 offer to plaintiff. However, the court further found that the Code of Civil Procedure does not require the requesting party to "personally" incur the fees, rather it is sufficient that the requesting party "actually" incurred legal liability to pay litigation costs.

Litt v. Eisenhower Medical Center (2015) 237 Cal.App.4th 1217.

E. Set-offs and Settlement Allocation.

In construction defect actions, subcontractors are entitled to an offset based on the pre-trial settlement by the defendants including the developer and other subcontractors. The right of offset is provided by statute under California Code of Civil Procedure Section 877 which expressly provides that settlement “is given in good faith before verdict or judgment to one or more of a number of tortfeasors claiming to be liable for the same tort . . . , it shall reduce the claims against the others in the amount stipulated by the . . .” settlement. Practically speaking, the issues of offsets and deductions are not determined by the jury, but determined by the trial court after an award of damages has been rendered to the plaintiff.

CACI 3926.

F. Good Faith Settlements.

Most construction defect actions, in terms of separate settlements, are undertaken subject to California Code of Civil Procedure Sections 664.7 and 887.6 involving the application of good faith settlement. The California Supreme Court has held that “while a good faith settlement cuts off the rights of other defendants to seek contribution or comparative indemnity from the settling defendant, the non-settling defendants obtain in return a reduction in their ultimate liability to the plaintiff.”

Abbott Ford, Inc. v. Superior Court (1987) 43 Cal.3d 858.

1. For the purposes of computing the setoff, California Code of Civil Procedure Section 887 does not require any defendant to prove that the settling co-defendants were in fact liable, only that they were “claimed to be liable” for the same tort.

Knox v. County of Los Angeles (1980) 109 Cal.App.3d 825.

2. In multiple party, multiple issue, cases such as construction defect actions, the settling parties are obligated to specify under the settlement agreement the allocation of settlement among parties and issues. However, the agreement of the settling parties is not necessarily dispositive of the issue of the offset to which the non-settling parties are entitled.

Erreca's v. Superior Court (1993) 19 Cal.App.4th 1475.

3. When the settling parties have not stipulated to an allocation as part of their settlement agreement, the trial court must allocate in a manner which is most advantageous to the non-settling party.

Dillingham Construction, N.A., Inc. v. Nadal Partnership, Inc. (1998) 64 Cal.App.4th 264.

4. The trial court has the latitude to adjust good faith settlement allocations among joint tortfeasors. Where multiple defendants cause indivisible damage, their joint tortfeasors are entitled to reduce liability through credits from settling defendant's payments. This ensures that plaintiffs do not receive double recovery and that defendants do not bear a disproportionate share of liability. Particularly in multi-party construction defect litigation cases, the court must adjust credits as evidence is adduced at trial to ensure fairness to the parties.

El Escorial Owners Association v. DLC Plastering, Inc. (2007) 154 Cal.App.4th 1337.

5. The amount of the setoff is not just inclusive of the cash consideration, but also includes a non-cash component of such consideration such as an assignment of rights. If a settling defendant assigns indemnity rights to the plaintiff, the assignment may constitute valuable additional consideration for settlement and this added value would then be included in any offset to any judgment against a non-settling party.

Alcal Roofing & Insulation v. Superior Court (1992) 8 Cal.App.4th 1121.

6. Determination of good faith settlement by a trial court can rely on factors such as potential liability, reasonableness and lack of intent to injure other tortfeasors. Plaintiff suffered severe burns when his window washing pole made contact with the power company's 12,000 volt electrical line located adjacent to the property. The plaintiff filed a personal injury action against the power company, but not the owners of the property, and subsequently settled with the owners for \$25,000 in exchange for the release of all claims. The power company filed a cross-complaint against the owners for apportionment of fault and equitable indemnification, but the trial court found that the prior settlement between the owners of the property and the plaintiffs was in good faith

and dismissed the cross-complaint. The Court of Appeal held that the trial court did not abuse its discretion in determining that the settlement between the property owners and the plaintiff was made in good faith within the meaning of California Code of Civil Procedure Section 887.6.

Cahill v. San Diego Gas & Electric Company (2011) 194 Cal.App.4th 939.

G. Equitable Indemnity Versus Contractual Indemnity.

In certain situations, developer may elect to assign to the plaintiff their equitable causes of action as part of any settlement. If there is a contractual indemnity claim which exists, the cases have uniformly held that the doctrine of equitable indemnity does not apply as the contractual indemnity clause is preemptive. Therefore, the assignment of such equitable indemnity rights has no value.

Rossmoor Sanitation, Inc. v. Pylon, Inc. (1975) 13 Cal.3d 622.

1. There can be no equitable indemnity absent apportionment of fault. The doctrine of equitable indemnity flows from the doctrine of comparative fault and therefore any such indemnity award must be based upon a finding by a trier of fact of a proportion of fault attributable to each tortfeasor, several tortfeasor or obligor.

Li v. Yellow Cab Co. (1975) 13 Cal.3d 804.

2. When a supplier breaches its contract by providing defective materials, it is barred from bringing a cross-complaint for equitable indemnity. Plaintiff general contractor sued defendant concrete supplier alleging breach of contract to recoup the costs of replacing defective concrete used in constructing a pier. The concrete supplier failed to comply with its mix design which had been reviewed by a civil engineer. The concrete supplier cross-complained against the civil engineer for equitable indemnity and contribution claiming that the civil engineer failed to use reasonable care when it approved the concrete mix design. The Second District Court of Appeal held that the concrete supplier could not seek equitable indemnity and contribution for damages caused by its breach of its own contract. The economic loss doctrine barred the concrete supplier's cross-complaint for equitable indemnity and contribution because the civil engineer had no contractual relationship with the general contractor or concrete supplier and that concrete did not injure anyone or damage other property.

State Ready Mix, Inc. v. Moffatt & Nichol (2015) 232 Cal.App.4th 1227.

11. “CURRENT ISSUES” REGARDING EVIDENTIARY AND PROCEDURAL MATTERS IN CONSTRUCTION DEFECT LITIGATION

A. Privette Doctrine

1. A general contractor can be held liable for subcontractor’s employee’s injuries if the general contractor is negligent and its negligence substantially contributed to the employee’s injuries. Plaintiff was an employee of a landscape and pool subcontractor who filed suit against the homeowner for premises liability and negligence. The plaintiff contended that the homeowner had negligently installed an underground vault with an unventilated propane heater which were both used in connection with the construction of the homeowners pool and spa. Defendant homeowner was a licensed concrete subcontractor by trade and had decided to serve as the owner/builder (a role similar to a general contractor) for the job. Defendant had obtained a building permit, completed the concrete work himself and hired subcontractors for the other work. He personally supervised the progress of the construction daily and verified completion of construction projects for the subcontractors. After the original construction by the homeowner, plaintiff’s employer undertook to do certain improvements. Plaintiff, as an employee of the pool contractor, entered the underground vault and was subsequently injured when an explosion occurred in the pool’s propane heater. The plaintiff sued the homeowner for negligence and premises liability alleging that the homeowner had negligently installed the vault and unventilated propane heater. At trial plaintiff argued the homeowner was liable as he retained control of the project by submitting plans and undertaking construction activities. The parties agreed that the court could instruct the jury with a modified version of CACI 1009(B) “Liability to Employees of Independent Contractors for Unsafe Conditions – Retain Control.” Defendant argued that there should be an additional instruction and an order defining and finding why he must have “affirmatively contributed” to the plaintiff’s injury. The trial court refused to give the order noting that the jury instruction required the jury to find that defendant “negligently exercised his retained control” which required affirmative conduct. The jury ruled in favor of the plaintiff, and the defendant appealed the jury award. The Court of Appeal affirmed the trial court’s ruling that CACI 1009(B) adequately covered the “affirmative contribution” requirement pertaining to the Privette Doctrine.

Regalado v. Callaghan (2016) 3 Cal.App.5th 582.

2. The Privette Doctrine is upheld by the Court of Appeal in a construction related accident. Plaintiff sued general contractor for general negligence pertaining to injuries suffered while performing electrical work at a Cal State University project. Plaintiff's employer, subcontractor Myers, informed Staples that it needed to completely shut down the electrical system in order to perform the electrical work required of it and the work would take three days. The university scheduled the electrical shutdown but plaintiff arrived at the project site two and a half days prior to the scheduled shutdown time. The university's project manager escorted plaintiff into the substation which housed the electrical subgear. No employees of Staples were present. The plaintiff began performing the work approximately 30 minutes before the scheduled shutdown, an electrical flash occurred causing plaintiff to sustain severe injuries. The trial court granted Staples' motion for summary judgment based on the Privette Doctrine barring plaintiff's claim. The Privette Doctrine generally prohibits an independent contractor's employee from suing the contractor's hirer for work-related injuries. The insured employee is limited to Workers' Compensation remedies from his employer. The Court of Appeal affirmed, holding that neither exception to the Privette Doctrine that was asserted by plaintiff applied to the case. The plaintiff argued that his claim was not barred because two exceptions to the Privette Doctrine applied: the Retained Control Exception and the Non-Delegable Duty Exception. The court indicated that the Retained Control Exception requires the worker to present evidence that the hirer retained control over the work, negligently exercised the control, and thus contributed to the worker's injuries. While the court found that the plaintiff presented evidence that Staples controlled the work, it indicated that plaintiff represented no evidence that Staples' control contributed to his injuries. As to the Non-Delegable Duty Exception, the court stated that the duty of workplace safety is presumptively delegated to an independent contractor when it is hired to perform the work, and this presumptive delegation includes the duty to comply with statutory and regulatory safety requirements.

Khosh v. Staples Construction Co., Inc. (2016) 4 Cal.App.5th 712.

3. An unlicensed independent contractor will be viewed as an employee for liability purposes. Independent contractor Blackwell sued property owner ("Owner") for general negligence after sustaining an injury while completing a construction project, on his property. The Owner was not a contractor, but he hired Blackwell to perform rain

gutter work and a second independent contractor (Gomez) to perform stucco work. Blackwell accessed the building's roof to install a gutter, and when he reached the area covered by Gomez' scaffold, he rested the ladder against the scaffold to obtain access. After stepping onto the scaffold, it collapsed and Blackwell fell approximately ten feet, suffering injuries. The plaintiff filed against the Owner, and Owner filed a cross-complaint against Gomez for contribution and indemnity. The Owner further argued that he had no duty to Blackwell as he had no knowledge of the scaffold's safety, and no duty to warn Blackwell. In relying upon Labor Code Section 2750.5, Blackwell argued that Gomez was Owner's employee since he was an unlicensed contractor, and therefore Owner was liable to Blackwell for the breach of the duty of care under the doctrine of respondeat superior. The trial court granted Owner's summary judgment motion. The Court of Appeal reversed holding that the trial court mis-applied Labor Code Section 2750 and indicated that Owner met the common law factors established by Aguilar v. Atlantic Richfield (2001) 25 Cal.4th 826, and he failed to meet the statutory standard codified within Labor Code Section 2750.5 which requires that a contractor either be licensed or has performed work that does not require a license in order to be classified as an independent contractor. The Owner provided no evidence of the licensure of Gomez and failed to establish that Gomez was an independent contractor. Thus, the court ruled in favor of Blackwell.

Blackwell v. Visilas (2016) 244 Cal.App.4th 160.

4. A sub-contractor window-washer ("Plaintiff") brought suit against defendant homeowner where Plaintiff was performing work at defendant's home and fell off the roof. Plaintiff alleged that there were various dangerous conditions on the roof that had caused him to fall. The trial court granted summary judgment for defendant homeowner on Plaintiff's claims indicating they were barred by the Privette Doctrine which generally prohibits an independent contractor or his employees from suing the hirer of the contractor for workplace injuries. The only exceptions to the Privette Doctrine are where a hirer retains and negligently accepts and tries to control in a manner that affirmatively contributes to an employee's injury, or conceals known hazards, or there is a known or open hazard that cannot be practically avoided, through reasonable safety precautions.

The Court of Appeal upheld that the Plaintiff had failed to present evidence showing a triable issue of fact as to the retained control exception of Privette but reversed as to the second exception to Privette and held that defendant failed to establish there was

no triable issue as to whether Plaintiff qualified for the failure to warn exception. The court held that the failure to warn exception applies not only to concealed conditions, but also to open or known hazardous conditions that cannot be established by application of reasonable safety precautions.

Gonzalez v. Mathis (2018) 20 Cal.App.5th 257.

5. The Privette Doctrine was expanded to bar liability for injury to independent contractor's employee where hirer breached statutory duties. Decedent was an employee of a window washing subcontractor ("Subcontractor"). While washing windows on defendant's third floor building, decedent attempted to rappel off the building using anchor points, but there was no structural roof anchors and decedent fell to his death. The trial court affirmed summary judgment for defendant building owner holding that the Plaintiff's suit was barred by Privette on the "Doctrine of Peculiar Risk." The Court of Appeal affirmed the trial court's summary judgment holding and indicated that the defendant's port duty as a property owner to decedent to provide a safe workplace was delegated to the window washing Subcontractor. The court noted that by hiring an independent contractor, a hirer implicitly delegates to the contractor the port law duty the hirer owed to the contractor's employee to comply with applicable statutory regulatory safety requirements. Mere failure to provide safety equipment by defendant property owner did not constitute an "affirmative contribution" to an injury that displays negligence in the exercise of retained control.

Delgadillo v. Television Center, Inc. (2018) WL 106971.

B. Current Evidentiary Issues

1. Ignoring Evidentiary Rulings Can Lead to Terminating Sanctions.

Plaintiff sued defendant, Todd, a farm services company, and defendant, Barrington ("Barrington") for severe injuries sustained when a bale of hay gave way causing her to fall eleven feet to the ground. Plaintiff's complaint alleged Barrington manufactured the bale involved in the injury. The documents Todd produced failed to establish Barrington as the manufacturer of the bale. In fact, Todd contended that it purchased hay bale from several suppliers and did not segregate the bales by supplier. The plaintiff failed to make a timely expert witness designation and intended to supply a supplemental expert witness designation after the respondent's supplied their expert

witness list. Barrington filed a motion to strike plaintiff's supplemental expert witness designation which the court granted and the plaintiff did not challenge. During trial, the trial court granted motions in limine that were requested regarding exclusion of the plaintiff's opinion testimony, hearsay testimony surrounding statements made by an unnamed Todd employee. Despite the trial court's order, plaintiff's counsel repeatedly mentioned specifically excluded matters and asked the plaintiff questions relating to the excluded evidence. At request of defendants for terminating sanctions, the trial court dismissed the case with prejudice against all defendants. The Court of Appeal (Second District) affirmed the trial court's order of dismissal indicating it was applying an abuse of discretion standard in its determination of whether the trial court properly excluded opinion testimony and hearsay testimony in its determination of whether the terminating sanctions were proper. It determined that the opinion testimony was properly excluded because the plaintiffs failed to designate an expert in time and that lay person opinion testimony was not admissible expert testimony. The Court of Appeal found that the trial court did not abuse its discretion in imposing terminating sanctions as plaintiffs continually ignored evidentiary rulings and in limine orders which were unduly prejudicial to both defendants.

Osborne v. Todd Farm Service (2016) 247 Cal.App.4th 43.

2. The California Supreme Court Refines the Rules Related to Hearsay Testimony of Expert Witnesses.

In a criminal possession case issues arose in connection with the testimony offered by a police gang expert. The jury convicted the defendant of all charges, and the Court of Appeal affirmed most of the trial court's ruling. The California Supreme Court affirmed the overall conviction, but focused its attention on the nature of the expert witnesses' testimony. The court held that an expert's testimony is inadmissible hearsay if "case-specific out-of-court statements" were relied on by the expert and presented to the jury as an accurate and true basis to support the expert's opinion without the required independent proof. Additionally, the court found that an expert witness cannot relate testimonial hearsay unless (1) unavailability can be shown and (2) the defendant had the opportunity to cross-examine or forfeited its right. The Supreme Court determined that most of the evidence presented by the gang expert was considered testimonial hearsay of case-specific statements concerning the defendant's familiarization with the gang.

People v. Sanchez (2016) 63 Cal.4th 664.

3. Expert Opinion Properly Excluded for Failure to Designate.

When trial court determined an expert opinion was inadmissible because disclosure requirements were not met, the opinion was properly excluded from consideration at summary judgment where an objection was raised. The plaintiff sued Hawthorne, LLC and Chase Bank claiming he was injured in a fall on property owned by Hawthorne and leased by Chase. Chase demanded an exchange of expert witness information but plaintiff failed to disclose the information. However, in response to Hawthorne's motion for summary judgment, plaintiff submitted the declarations of two experts pronouncing that the stairs on which he fell were in disrepair and out of compliance with the Building Code. After setting a trial date, Code of Civil Procedure Section 2034.210 states that a party may demand a simultaneous exchange of expert witness information by all parties. If there is an unreasonable failure to respond, the non-compliant party's expert opinion becomes inadmissible, unless relief is granted by the court. Code of Civil Procedure Section 437c(d) requires that affidavits and declarations presented in summary judgment proceedings set forth admissible evidence. Code of Civil Procedure Section 437c(c) further states the party may not raise a triable issue of fact at summary judgment by relying on evidence that will not be admissible at trial. The court sustained Hawthorne's objection to plaintiff's expert testimony because plaintiff unreasonably failed to disclose the information. Summary judgment was therefore granted and plaintiff moved for reconsideration. The Court of Appeal (Second District) affirmed the judgment in favor of Hawthorne holding that the time for exchanging expert witness information had expired before the summary judgment was made. The California Supreme Court upheld the lower court's ruling properly granting summary judgment as a result of plaintiff's failure to properly designate experts.

Perry v. Hawthorne (2017) WL712748.

C. Current Procedural Issues

1. An attorney need not disclose reasons behind mistake, inadvertence, surprise or neglect when filing a motion to set aside default. Upon receiving plaintiff's complaint and other filings, defendants' managing partner forwarded documents to defense counsel. Although the counsel received the documents, he took no action with respect to the lawsuit and trial court entered defendants' default. Defendants subsequently moved to set aside a default and default judgment pursuant to Code of Civil

Procedure Section 473(b) which states that a trial court is required to vacate a default, default judgment or dismissal that is caused by an attorney's mistake, inadvertence, surprise or neglect if an attorney files a sworn affidavit attesting to the same. There was an attorney affidavit regarding the default but did not disclose the reasons for the failure to act. The Court of Appeal (Second District) held that an attorney affidavit of fault under the mandatory relief provisions of Code of Civil Procedure Section 473(b) does not require an explanation of the reasons for the attorney's mistake.

Martin Potts & Associates, Inc. v. Consarl, LLC (2016) 244 Cal.App.4th 432.

2. Timeliness of a motion to intervene is determined based on the date the intervenor knew or should have known its interests were not being adequately represented. In 2012, an HOA sued a developer and others alleging construction defects. The complaint was brought in the name of the HOA on behalf of all individual unit owners and the HOA and its attorneys represented to the owners that the HOA would not settle the case unless it obtained a full recovery to pay for the necessary repairs to both the common areas and individual units. The HOA agreed to settle the lawsuit, shortly thereafter advising the owners that the settlement covered all of the necessary repairs. However, the HOA subsequently advised the owners that the settlement would not reimburse those owners who had already paid to repair the plumbing defects in their units. Thereafter, a number of owners moved to intervene under Code of Civil Procedure Section 387 assuming that the HOA was no longer adequately representing their interests in the litigation. The trial court denied the motion on the basis of the proposed intervenor's application was untimely because they knew or should have known about the litigation in July 2012 when the complaint was filed. The Court of Appeal (Fourth District) held that the timeliness of a motion to intervene under Code of Civil Procedure Section 387 is determined based on the date that the proposed intervenors knew or should have known their interests in litigation were not being adequately represented. Based on the foregoing, the Court of Appeal denied the motion to intervene.

Ziani Homeowner's Association v. Brookfield Ziani, LLC (2015) 243 Cal.App.4th 274.

3. For Mechanic's Lien purposes, the date of completion extends to the date that work is completed even where a Certificate of Occupancy was issued before completion. Plaintiff Picerne agreed to build an apartment complex for defendant which

consisted of eleven apartment buildings. A single Certificate of Occupancy was issued in July 2006. The owner's representative signed a document accepting some of the apartment buildings in August 2006 and created a punch list of work to be completed. However, until mid-September, the roofing subcontractor continued work that was within the original subcontractor's contract and an installer worked to install stair treads that were required in the project plans. Defendant began renting the apartments in October 2006 at which point Picerne requested the release of the project retention proceeds. Picerne recorded a Mechanic's Lien on November 28, 2006 and filed a complaint to foreclose its lien on December 29, 2006. After arbitration in conjunction with bankruptcy proceedings, the trial court entered judgment and a decree in favor of the lien foreclosure. Defendants appealed. The Court of Appeal (Third District) held that the Mechanic's Lien was valid as it was recorded within 90 days "after the completion of work of improvement" as required under former Civil Code Section 3115 (now Civil Code Section 8412). Because the Mechanic's Lien was recorded within 90 days of the date the defendant accepted the project and within 90 days of the date of the stairway and roofing subcontractors completing the work under their contracts, date of completion was later than the date of the Certificate of Occupancy was issued and it was deemed the Mechanic's Lien was timely.

Picerne Construction Corp. v. Castellino Villas (2016) 244 Cal.App.4th 1201.

12. "INTERESTING ISSUES" IN CONSTRUCTION DEFECT LITIGATION

Several trends have recently developed with respect to construction defect litigation for which there has been no definitive answer, but these issues bear further scrutiny.

A. Speculative Nature of Plaintiff's Extrapolation in Construction Defect Actions.

In a recent trial involving construction defects, the trial judge made specific reference to non-construction defect cases involving expert testimony and extrapolation. In particular, the trial court referenced the case of Duran v. U.S. Bank National Association (2012) 137 Cal.Rptr. 3d 391 for the proposition "courts are generally skeptical of the use of representative sampling to determine liability, even in cases in

which plaintiffs have proposed using expert testimony and statistical calculations as the foundations for setting the sample size.” (Duran at 427). The court further discussed the case of Sargon Enterprises, Inc. v. University of Southern California (2012) 55 Cal.4th 747. In that case, the Supreme Court concluded that trial courts have a duty to act as a “gatekeeper” to exclude speculative expert testimony and concluded that the trial court in that case properly excluded expert testimony and that the expert's methodology was too speculative for the evidence to be admissible.

B. Potential Liability of Construction Lenders.

The law has been well-settled in California that a lender who makes a loan of money, the proceeds of which are used or may be used by the borrower to finance the design, manufacture, construction, repair, modification or improvement of real property for sale . . . to others, shall not be liable to third parties for any loss or damage occasioned by any defect in the real property (California Civil Code Section 3434). Said code section provides protection to a lender “unless such loss or damage is a result of an act of the lender acting outside the scope of the activities of a lender of money” This section does not specify when a lender/bank's activities are outside the scope of a lender of money. Whether or not a lender is engaging in activities “outside the scope” of the lender is a fact-sensitive analysis and will most likely be analyzed on a continuum rather than bright line test.

The question arises as to whether there is an open issue with the advent of SB 800 on a lender's exposure for construction defects. “Builder” is defined in California Civil Code Section 911 as follows:

“Builder” means any entity or individual, including but not limited to a builder, developer, general contractor, contractor, or *original seller*, who, at the time of sale, was also in the business of selling residential units to the public for the property that is the subject of the homeowner's claim or was in the business of building, developing, or constructing residential units for public purchase for the property that is the subject of the homeowner's claim.

Essentially, SB 800 has no limitation on who is a “builder” which presents a problem for lenders who acquire newly constructed residences as the successor to the original developer. SB 800 applies to a party who sells just one home or many, and defines a “builder” to include “an original seller who, at the time of the sale, was also in

the business of selling residential units to the public of the property that is the subject of the homeowner's claim.” California Civil Code Section 911(a).

C. Can An Unlicensed Contractor Enforce Its Contracts and Collect *Crawford* Damages?

1. There is a current split in California appellate authority in the ability of an unlicensed general contractor to enforce its contractual indemnity and *Crawford* rights against its subcontractors in construction defect actions. In the seminal case of Ranchwood Communities Ltd. Partnership v. Jim Beat Construction (1996) 49 Cal.App.4th 1397, the court held that an unlicensed general contractor who is liable for construction defects cannot enforce indemnification agreements with its subcontractors pursuant to Business and Professions Code Section 7031.

Ranchwood was criticized by a different appellate district in the decision of UDC-Universal Development v. CH2M Hill (2010) 181 Cal.App.4th 10. The court in UDC held that enforcement of express indemnity clauses in a subcontract is not the “collection and compensation” for contractor services which is what is expressly barred by Business and Professions Code Section 7031. The court concluded that an unlicensed contractor simply enforcing an indemnity agreement is seeking indemnity for damages it has to pay plaintiff due to alleged defects within the subcontractor's scope of work.

Typically, those who assert that Ranchwood is the compelling case assert that public policy arguments behind the intent of Business and Professions Code Section 7031 specifically prohibit any unlicensed contractor from benefitting under any contract. Arguments are further asserted that the holding in UDC-Universal was mere dicta and not binding upon the court as the discussion in UDC was set forth in Footnote 5 stating “We depart from the Ranchwood majority's suggestion that a claim based on contractual indemnity necessarily implies illegality if brought by an unlicensed contractor.” The discussion of Ranchwood was not essential for the Appellate Court to uphold the denial of the summary judgment motion in the UDC matter and as such it has been argued that it is mere dicta and not the express holding of the court.

Conversely, developer's counsel typically asserts that pursuant to the UDC case, Business and Professions Code Section 7031(a) only bars an action for compensation for work performed by an unlicensed contractor. The term compensation as used in the statute “denotes sums claimed as an agreed price, fee, or percentage earned by

performance, and also some claimed as part of the reasonable value of work done under an implied contract.” Actions that do not seek compensation are outside the scope of Business and Professions Code Section 7031(a). The UDC court expressly found that UDC was not seeking compensation in the traditional sense of the word, either directly or indirectly, such that its contractual claims were not barred.

2. Business and Professions Code Section 7031 does not preclude a contractor’s recovery when the license status changed from personal to corporate during construction. During the course of constructing a home for defendants, plaintiff incorporated his sole proprietorship. Prior to the expiration of his license, plaintiff obtained a re-issue of his general contracting license through the corporation. Plaintiff sued defendant for unpaid fees alleging quantum meruit. Defendants contend that plaintiff was not licensed at all times during the performance of the contract, thus Business and Professions Code Section 7031 served as a complete bar to plaintiff’s quantum meruit claim. The Fifth District Court of Appeal held that Business and Professions Code Section 7031 did not preclude plaintiff from recovering quantum meruit damages when plaintiff changed business entities status. The court found that the plaintiff’s license did not lapse during the duration of construction on the defendant’s home since the license was issued to the sole proprietorship and transferred to the corporation. The court held that Business and Professions Code Section 7031 did not bar recovery based on this unique set of facts.

D. Liability of Architects.

1. Principal architects owe a duty of care to third-party homeowners even when they do not actually build or exercise control over construction. Defendants were the architects on a condominium project and provided both architectural and engineering services, and played an active role throughout the construction process, coordinating the design and construction team, including conducting weekly site visits and inspections and recommending design revisions as needed, along with monitoring compliance with the plans. Defendants did not make final decisions on construction. Plaintiff homeowners association sued several parties including defendants alleging negligent architectural design work resulting in defects. Defendants contended they owed no duty of care to the HOA as they were third parties to defendant’s contracts with the owner.



The Supreme Court of California held that an architect owes a duty of care to future homeowners in the design of a residential building where the architect is a principal architect on the project, i.e., the architect is not subordinate to other design professionals. Moreover, this duty of care extends as such architects even when they do not actually build the project or exercise ultimate control over the construction. The court analyzed the factors in the leading case of Biakanja v. Irving (1958) 49 Cal.2nd 647, 650 and determined that a duty of care does exist between plaintiff HOA and defendant architect in the absence of privity. The court distinguished in the case of Weseloh Family Limited Partnership v. K.L. Wessel Construction (2004) 125 Cal.App.4th 152 on the grounds that the design professionals in Weseloh were subordinate to other professionals and were not the principal designers. The court found that the allegations in plaintiff's complaint herein, if proven, were sufficient to establish that defendants owed a duty of care to the homeowners.

Beacon Residential Community Association v. Skidmore Owings & Merrill
(2014) 59 Cal.4th 568.

CONSTRUCTION BASICS FROM TOP TO BOTTOM

General Overview of Construction Terms and Typical Defects

I. Cast of Characters:

Typically, a construction project, whether it's a large scale development or a single family remodel, utilizes many distinct disciplines to complete the construction activities. We provide a brief summary description of each “unique” construction expert.

A. Architect:

Prepares the project plans and specifications (the “Bible”) upon which the other construction professionals will rely in constructing the buildings. The Architect generally submits the project plans to governing agencies to show compliance with codes and standards of the industry and obtains approval for construction. In large scale developments, the Architect simply provides plans for the construction of various residences and serves in more of a clerical role, and overall management of the project is handled by the Developer. In commercial and smaller scale projects, the architect prepares a bid package for construction of the project and solicits bids from various general contractors to obtain reasonable construction costs. The architect may then oversee the construction of the project and processes documentation to insure timely and adequate completion of the construction by the general contractor for the owner.

B. Engineers:

1. **Geotechnical (Soil) Engineer:** Generally deals with site specific soils and soil features that affect the construction of buildings and foundation systems adjacent to and within soils. For multi-residential projects, a geotechnical engineer would study the topography of the land, the nature and type of soil, its composition and properties (i.e., highly expansive soil), and establish specific soil parameters to be used in the design of the construction components that interface with soils. These parameters would include the design of the foundation system, retaining walls and other

structural systems, in conjunction with the structural engineer. Typical soil issues would involve analysis of expansive capability of the soil, whether the soil is “cut” or “compacted fill” and whether there was the existence of any landslides.

2. Civil Engineer: The civil engineer prepares the tract map, which legally describes a project’s land and any easements thereon. The civil engineer also prepares the grading plan, which considers the topography of the land including site development of slopes, drainage systems, streets, water supply and waste systems and roadway design.
3. Structural Engineer: Designs the building and its foundation to the architectural requirements, including calculations for loads, including sheer and seismic requirements. The structural engineer works with the soils engineer with respect to foundation systems.
4. A mechanical engineer designs the heating and ventilation system and the insulation components of a building.
5. The Electrical Engineer designs the electrical needs for mechanical systems and occupant needs of a building.

C. Contractors

1. General Contractor: Typically oversees management of the project, coordinates with all subcontractors to ensure proper sequencing of the project, and interfaces with the owner. In large scale projects the general contractor, does not do any “construction work,” the general contractor simply manages subcontractors. In smaller jobs, the general contractor may do some of the work themselves (i.e., framing) pursuant to a B-1 license which allows the general contractor to do all construction activities, whether qualified or not.
2. Subcontractor: Engages in specific aspects of the construction, such as stucco, roofing or plumbing. The subcontractor has the responsibility to

interface with other scopes of work which “touch” their work (i.e., framing and roofing) but has no responsibility for overall management. Generally subcontractors have C specialty licenses (i.e., concrete). Problems can arise when the general contractor, without specific expertise, orders the subcontractor to undertake construction in a manner not consistent with good construction principles.

II. Geotechnical Terms and Typical Defects

Soils related claims present unique issues, not the least of which is determining the value of such claims in light of standard soil subsidence exclusions in general liability insurance policies. Homeowner’s counsel always attempt to establish soils claims as it “maximizes” the defects. For example, if a stucco crack can be tied to expansive soil or an issue with a cut/fill transition, then the repair is not only to fix the stucco crack, but also to stabilize the soil, which generally involves considerable expense and necessitates relocation of the homeowners. Soil claims can be broken down into discrete categories, but to understand the issues, one needs to examine the specific soil related activities which take place during construction.

A. Grading of Soils

In large development projects, raw land is ultimately converted to level pads for constructing houses. This involves mass grading, which is the term usually applied to grading which modifies existing landforms into engineered building lots and streets, including slopes. This can involve cutting hillsides to create level areas or alternatively filling in large canyons and valleys to create level areas. Both processes are fraught with potential problems.

After mass grading, rough grading is undertaken to establish finish grade elevations to within one-tenth of a foot for street elevations, lot drainage patterns, building pads and slopes. Finally, finish grading takes place and provides certified elevations for building construction, street improvements, hardscape, landscape and drainage patterns.

B. Typical Soils Issues

The issues which routinely arise in construction defect actions involving soils are related to cut/fill transitions, compaction problems, expansive soils conditions, and to some extent, landslides and slope creep. It should be noted that almost all of these conditions are caused by or exacerbated by the introduction of water, either through rain or irrigation. Different soils have different combinations of soil particles of varying sizes, from microscopic particles to larger aggregates. Soil is essentially composed of three discrete materials: soil particles, air and water. By the nature of the soil structure there are “voids” in the soil which allow the transmission of water and air. When water is added past the optimum water content of the soil, the soil becomes highly plastic with a quick loss of strength. Additional water causes the bond of adjacent soil particles to be “broken”, which causes a loss of friction between the particles, allowing slippage or movement of the soil and corresponding loss of strength. Controlling water by proper grading and drainage dramatically impacts the soil related issues.

1. Cut/Fill Issues: Most large scale developments have had some type of soil work done, either the soil is removed (cut) or soil is added (fill) to balance for the grading. If this process is not properly monitored and tested for compaction, the soil may fail with consequential land subsidence. “Cut” is the term used to describe the removal of existing landforms (i.e., hills) in order to create a building pad or other designed improvement. “Fill” is the term used to describe the installation of native or other soils to raise the grade elevation (i.e. fill in valleys) to accommodate construction of a building pad or other improvement. If either of the soil methods are done incorrectly, there is a high probability that the soil will not be compacted properly and will suffer reduced strength and subsidence. If this occurs, the residence will likely evidence cracks in stucco, drywall, tile floors, concrete flatwork, and there may be interior distress to doors and windows which will cause them to be difficult to open. It is difficult to determine the exact cause of such distress without resorting to the testing methodologies discussed below. Cracking may also be indicative of structural problems, concrete problems, or a defect in the product itself (i.e., stucco).
2. Compaction Principles

Fundamentally, the point of properly preparing the soil is to provide a competent surface or “platform” for the construction of the building. The soil needs to be able to withstand the weight and loads of the building, as well as any influences from the environment, such as rain. The key is to have proper compaction of the soil with relevant design criteria for soil influences such as expansive soil conditions.

Competent soil is soil that is able to safely support the weight of the structure to be built with little compression of the soil material. Generally this is done through the placement of certified fill, which is placed in layers, and compacted to a specific relative compaction. Certified fill is soil. Competent soil can either be certified fill or natural soil of uniform soil properties and strength. Often times, in order to establish grades for level lots, fill is needed.

Developers and graders many times simply use “dirt” which was lying on site (generally from cutting of hills) to serve as fill. This creates two problems. Uncertified fill refers to native soil or soil placed and not compacted to a specific relative compaction density. Since the fill density is not controlled, the soil strength is not uniform and probably of low value. Second, fill is often placed to remedy expansive soil conditions (i.e., placement of three feet of fill over natural soil to mitigate expansive conditions). When “dirt” is used, this soil is also expansive which does not alleviate the condition, but in fact exacerbates the problem.

From a compaction standpoint, a soil’s maximum strength is directly proportional to its density and a function of the optimum water content at a specific dry density. The makeup of the size of the particles, their uniformity and shape factor and their percentage of the soil mass, determines the maximum dry weight for any particular soil and indirectly impacts the soil’s strength. A compaction test measures the moisture content of the soil and indirectly, the soil strength and the state of added water within the soil matrix. The optimum moisture content is determined in the soil laboratory for the determination of the maximum soil strength.

The engineer advises during grading whether the appropriate determination of relative compaction has been reached, which is usually 90% relative compaction.

3. Expansive Soil

This is a significant issue, particularly in Southern California where most of the soil has a significant clay component. Clay tends to hold in water, which causes the soil to swell in an upward direction when excess water is present. When the water is removed (through normal drying processes) the soil “shrinks” back to its original volume. The continued movement of the soil causes significant movement in the building structure which is evident in cracks in the rigid building structure.

Soils engineers can undertake a swell test or an expansion index test which can tell them the expansive characteristics of the soil. General precautions can be taken such as to remove a certain amount of the expansive soil near the surface (three to five feet) and replace that soil with soil material which has a low expansion index. The foundations can also be designed to be post tension slabs which can handle vertical movement without showing deflection. Finally, systems to mitigate water from near the foundation, such as French drains, can be added.

4. Landslides

Landslides typically are caused by a slide plane that is created when the mechanics of dissimilar soils (such as a sandy soil layer over a clay layer) are modified through seismic trauma or saturation, with a resultant loss in friction and cohesion. In essence, one type of soil is moving on top of another type of soil, sliding along a crack. Again, such movement generally does not occur unless water has reached this slide plane causing a loss in the friction of the soil materials. Landslides typically are referred as ancient landslides, which have existed for hundreds if not thousands of years. During grading, they are often completely removed, but they can be left in place and “buttressed” with appropriate design parameters. Usually, these

left in place slides are the ones which fail. This is a dramatic event but not particularly common in terms of defect actions.

5. Slope Creep

More common is the phenomena of slope creep, which is the almost imperceptible movement of a slope in a downward direction. The movement is measured in terms of hundredths of an inch. Usually there is no evidence of slope creep other than the block fences and walls showing rotation or movement down slope. Depending on where the slope creep is manifesting (bottom of slope or near top of slope with pool), the repair may be as simple as replacing the wall or might entail the placement of soldier piles (24 inch diameter pilings) placed deep into bedrock to stabilize the slope.

6. Soil Testing Methodologies

Popular testing methods for soils include *inclinometers*, *manometers*, *borings and corings*, and *piezometers*. The methods of use for each of these and determinations that can be made for each method are described below.

- a. Inclinometers. This instrument is used to investigate the stability of a slope over a period or increment of time by monitoring its movement. Inclinometers are instruments inserted into a drilled vertical shaft in the soil that measure any tilting of the drilled shaft or subsequent lateral movement within the soil profile. By drilling the shaft into competent stable bedrock, the movement of a slide and the depth of the sliding plane can be determined. Periodic measurements will indicate if a slope is moving and the rate of movement. This allows the engineer to determine the extent and location of any localized soil movement. It is typically used to monitor landslide or slope creep movements.
- b. Manometers. This instrument is used to measure the relative flatness of a foundation slab. Manometers measure the vertical offset or the

“ups” and “downs” within a plane by comparing the local elevation to a reference datum point. Manometers are used to determine if there are soil influences affecting the “levelness” of the slabs, which occurs with expansive soil or subsidence, due to improper compaction.

- c. **Borings and Corings.** Borings refer to holes drilled into the soil to explore either the soil’s properties or the profile of a soil. Corings refer to holes drilled into concrete to either create an opening in the concrete or to obtain a sample for laboratory analysis. Borings generally allow a soil engineer to “go down” hole (24 inches in diameter) to sample the soil for further laboratory analysis, and determine the visual characteristics of the soil. This visual analysis is somewhat subjective and leads to much debate among experts (i.e., clayey sandy soil vs. sandy clayey soil). The cores taken are generally tested for compressive strength (by breaking the core under pressure) which provides information as to the relative strength of the concrete, which is usually specified in the plans and specifications. The cores can also be examined under microscopes to determine whether the concrete has any voids or is being chemically attacked (the dreaded “sulfate attack”).
- d. **Piezometers.** Piezometers are instruments which measure the depth to an underground water level. Piezometers are inserted into a shaft in the ground similar to an inclinometer. Subsequent monitoring of a piezometer will show the time dependent change of the water level, which allows the engineer to determine if there are water influences affecting the soil.
- e. **Laboratory Tests:** Tests undertaken include compaction testing to determine appropriateness of grading, swell tests and expansion index tests to determine expansive characteristics of soil, as well as shear tests to determine the ability of the soil to withstand sheering or slide forces.

III. Foundation Terms and Typical Defects

Concrete foundations are the building component which is placed immediately on top of the prepared soil surface. Residential foundations are generally one of two types, either Slab-on-grade or a Post-Tension Slab.

A. Slab-On-Grade

A slab-on-grade foundation is a conventional concrete foundation slab that is poured or placed against the earth. This type of slab may be either plain concrete or reinforced concrete. Plain concrete is concrete that contains (pursuant to the Uniform Building Code) a minimum amount of steel and supports only vertical (gravity generated) bearing loads. Reinforced concrete slabs contain more steel or rebar reinforcement and are engineered to support both vertical and shear (lateral) loads. Conventional slabs are usually constructed on a flat uniform soil and are not engineered beyond the minimum requirements of the Uniform Building Code, except for determining the required depth or width of the footing.

B. Post-Tension Slab

Post-tension slabs are usually utilized where there are expansive soils conditions, or where additional stability of the slab is required to account for non-uniform foundation loads. Post-tension slabs are engineered slabs that are poured utilizing shielded tendons, which are essentially a braided wire rope covered with a lubricant such as grease. The tendon is placed at both ends of the concrete slab. After the concrete is poured and has obtained a certified minimum compressive strength, the tendons are tightened to a desired tension similar to tightening a guitar string. The difference between the two types of slabs is relatively simple. Conventionally constructed slabs cost less, but permit only certain sections of the concrete to be able to withstand upward or tensile pressures, while post-tensioned concrete costs more, but allows the entire slab to move in a monolithic fashion with less evident stresses to the concrete.

C. Concrete Footings

The other component of the foundation system besides the slab is the Concrete footings. Footings are typically the concrete placed along the outside edge of the concrete

slabs. They provide perimeter support for the slabs and vertical load bearing support for interior bearing walls (walls which are supporting the roof structure). A typical single-story residence with a standard truss roof usually only requires perimeter footings around the residence and garage. In normal soils conditions, a footing for a one-story residence would be 12 inches wide by 12 inches thick (measured from adjacent finish grade to bottom of the footing) with two steel re-bars placed in the footing. A typical two-story residence would contain perimeter footings, as well as interior bearing footings, to transfer vertical and lateral load from the second floor. A typical two-story footing would be 18 inches wide by 18 to 24 inches deep. Variations in footing size and reinforcement are based on structural or soils related issues. (i.e., footings that support shear walls usually require additional steel reinforcement).

D. Building a Slab

Regardless of the type of slab, construction of the foundation generally follows the same construction “blueprint.” (1) After the soil is fine graded, several inches of clean sand are placed to provide a uniform and consolidated bedding for the concrete slab. Sand allows water to migrate through without any expansive action and consolidates or compresses better than soil so there is no “flex” in the concrete. (2) After the first layer of sand is placed, a layer of Visqueen (polyethylene sheathing or a heavy plastic sheet) is laid down. In foundation construction, the primary purpose of visqueen is to act as a vapor barrier in order to prevent moisture and/or chemical salts such as sulfates from penetrating the concrete. Typically, visqueen is sandwiched between layers of clean sand. (3) The layering of visqueen and sand depends on the soil conditions, but normally two inches of sand is placed over the finish grade surface, followed by a layer of visqueen, followed by two more inches of sand. (4) Concrete is poured and allowed to “cure” for a specified number of days.

E. Typical Concrete Defects

The nature and type of defects generally correspond to each phase of the construction of the slab. Similar to soil defects, Plaintiff's counsel like to allege these type of defects as they know there is "more bang for the buck." For example, if it is alleged that the slab has a deformity (i.e., curling or edge lift), the typical repair is to remove all floor finishes on the first floor, remove drywall up to 18 inches on the wall, and saw cut out all the concrete, which is removed and replaced at a cost of approximately \$100,000 per residence. Defects are either defects in the concrete itself, or have caused other damage to the residence.

1. Defects in Concrete

Generally speaking, these defects primarily consist of claims that the concrete as placed is sufficiently "weaker" than intended. For example, claims have been made that concrete placed in a highly corrosive soil environment (i.e., sulfate) is chemically attacked by the sulfate salts which leads to a disintegration of the cement paste, which creates voids in the concrete, substantially weakening the slab. This particular defect has "morphed" into an argument that sulfate attack increases vapor transmission through the slab which causes mold in the areas of the building in contact with the concrete. The recommended Plaintiff "fix" is as noted above. A defense fix would be to remove the cabinets etc. in contact with the concrete and apply a topical sealer to the concrete preventing any further vapor transmission.

Other defects asserted relate to the lack of compressive strength of the concrete (tested by coring), and the novel concept that the rebar placed in the concrete is too low (or too high) which has impacted the strength of the slab (all, of course, requiring replacement of the slab).

2. Concrete causing damage to other property

These defects are intimately tied to the soils issues, particularly subsidence and expansive soil. If the concrete is not strong enough to withstand the soil influences, you get the effect of an edge lift, where the edges of the slab are higher than the middle. If the phenomena continues, eventually you achieve a doming situation where the center of the floor is higher than the edges. In either instance, there is generally corresponding damage to floor finishes, concrete cracking, an additional manifestation of cracked stucco, and visual observation that doors and windows are out of alignment.

IV. Structural Related Defects

Of all the areas of construction, structural issues are the most esoteric and confusing. We have found that juries (and mediators) usually don't understand the issues, and this gives plaintiffs' counsel another avenue to try to "maximize" their damage claims. While the concepts are confusing, we will try to simplify the issues to the basic "nuts and bolts."

A. Structural Basics

From a structural engineering standpoint, a building or structure must safely transmit the effect of all "loads" from the roof through the building components (i.e., walls) to the foundation, through what is called the "load path." Any design calculations must also take into consideration the relationship of all of the building's structural elements to form a stable and safe structure.

The goal of structural engineering is to transfer the "loads" or forces on the building into the ground (i.e., grounding the building). Any building must transmit two types of loads to its foundation: vertical loads and lateral loads. Vertical loads are simply the effect of gravity upon a building which have the effect of trying to compress or "push down" lower supporting building components. Laterals loads are the effect of either wind or seismic activity upon a building, and have the effect of trying to push (horizontally), lift, and overturn the building.

For example, a vertical load on a building begins at the roof. The vertical load then gets transferred from the roof into the walls below and ultimately to the foundation. In a normal bearing wall system of framing for a building, loads are transmitted through shear walls to the foundation.

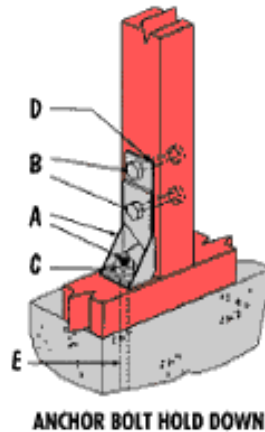
B. Specific Structural Elements

While vertical and lateral loads are transferred from the top down, for ease of convenience, we will sequentially deal with the structural components from the concrete slab up.

1. Anchor Bolts and Hold Downs

Anchor bolts connect the building's walls to the concrete foundation. A typical installation of anchor bolts is to place a threaded "L"-shaped rod into the newly poured concrete before it sets. After the concrete cures, a pre-framed wall with holes drilled into the sill plate (piece of wood which forms bottom of wall) can then be set down over the anchor bolts and attached with a washer and nut. Anchor bolts provide only a lateral shear resistance (i.e., resist overturning) to lateral loads placed upon the concrete foundation. Type, location and quantity of anchor bolts is specified by the Uniform Building Code, and is specifically indicated on the architectural plans. For example, each separate sill plate must contain at least two anchor bolts, one at each end within 12-inches.

As more fully discussed below, Shear walls are specially constructed walls that provide resistance to lateral shear forces and can provide resistance to uplift. A hold down is a special metal connector that provides uplift resistance for a shear wall, and is typically attached to the end wall stud with machine bolts and is also connected to an embedded anchor bolt cast into the foundation slab (See Figure 1)



(Figure 1)

2. Shear walls

Shear walls are typically plywood sheathing on the frame of the building which are placed pursuant to specific structural requirements. The nailing of the shear wall is done pursuant to specific requirements of the building code and includes nature and type of nail, location of the nail in the outside of the shear wall, as well as the nail “schedule” or nailing on the interior of the plywood sheet. Typically shear walls are stacked on top of one another on successive floor levels and multiple story units. Shear walls are generally designed to collect lateral loads from above and transmit them through the story level to the next level below, and so on. Similarly, plywood shear walls transfer loads from the horizontal diaphragm. The horizontal diaphragm is typically understood to be the roof and floor systems with any building.

Generally, the “load path” that is followed has loads transmitted from the diaphragm through nails which have been inserted into blocking or roof rafters or floor joists. The load is then transmitted from roof to the top of the wall (known as top wall plates) usually by the use of manufactured metal anchorage such as Simpson A 35 framing anchors. The load then

travels from the top plate into the shear wall through the nails. The nails then transmit the load from the plywood shear wall into the bottom plate at the upper stories or the steel plate (bottom of the wall) at the foundation.

In essence, all of the wood frame members work in concert, with the shear walls providing strength both from a vertical and horizontal standpoint.

The bottom line with respect to the shear walls and other structural components is that they are highly specified by the code as to the location, nature, extent and type of components that may be used. Plaintiffs' experts typically like to determine that shear walls were improperly nailed (i.e., not enough nails in the perimeter of the shear walls) or the wrong nails were used or otherwise. They use this argument to assert that the structural integrity of the building has been compromised such that the shear walls must be entirely replaced (which necessarily would require a removal of exterior and/or interior finishes greatly increasing the cost of repair). One of the issues which arises is whether or not the particular defect, (i.e., lack of nailing of the shear wall or missing anchor bolts), for example, actually has impacted to a significant extent the structural integrity of the building. Typically, structural engineers "over design" the buildings with relatively high margins of safety. Rather than simply assert that a particular component is defective and must be replaced, generally the better reasoned approach is to analyze the structural integrity of the building in total "as built," and determine whether there is any requirement for modification and repair of the particular component.

In terms of manifestations of damages, it is generally asserted that the improper structural elements have caused or contributed to excessive movement in the building so as to cause cracks in the exterior stucco or interior drywall thereby providing "property damage." A limited list of "plaintiffs' defects" would include the following: Improper sole plate anchorage (undersized or missing anchor bolts), improper nailing of plywood, missing or inadequate top plate straps, missing hold downs,

undersized hold downs, improper location of hold downs and anchor bolts etc., again, with the potential damage of there being cracked finishes.

V. Water Intrusion, the force that drives the Insurance Industry

As is evident in the industry, predominant claimed defects in any construction scenario always relate to water intrusion issues which have occurred in the building structure. While it is possible that water intrusion could manifest through the actual physical plane of the building (i.e., stucco), the predominant sources of and/or locations of water intrusions are generally related to openings such as doors and windows, and roof penetrations. We will deal with each of these sequentially.

A. Windows

Generally speaking two separate issues arise with respect to the installation of windows in a residence. Either the windows themselves have been manufactured defectively so as to allow window leaks, or the actual installation of the window and associated “flashings” have caused the problem. Window manufacturing defects generally manifest themselves in frame corner leaks, and unless the window is completely out of square, this repair generally involves a caulking repair to the frame corner.

More significant, both in terms of time and costs, are repairs associated with window installation.

1. Window Installation Basics

While windows may be manufactured from a variety of components including wood, vinyl, aluminum, or steel (with the predominant windows now being vinyl windows in tract residences) the installation of the windows is essentially the same. The framers have generally framed out a rough window opening to a specific window frame size. The window frame (with complete window assembly) is usually attached to the rough framed opening with fasteners applied through a nail fin on the window frame. Typically, prior to installation of the window ledge frame, flashing paper (a water protective fiber reinforced heavy duty paper) usually referred to as

sisalkraft, is placed around the perimeter of the rough opening at the window jambs (sides of window) and sill (bottom of window) in a specified method and procedure generally referred to as “shingling.” This paper overlaps at the various intersecting corners with the intention of shedding water away from the window. After installation of the frame itself, an additional piece of flashing paper is applied over the nailing fin at the top or head of the window. The nailing fin sticks out approximately an inch and a half to two inches from the opening of the window and allows the window to be securely attached to the building. Corners and intersections are then corresponding overlapped with the flashing paper.

Following the installation of this window flashing, a different type of flashing paper known as building paper, (generally the black asphalt paper you see wrapped around a building after framing) is again installed in a shingled fashion and tied into the window flashing paper. The entire assembly which has been put together is the primary means of protection from water intrusion into the building structure at the window location.

Generally, the window installation is undertaken by the framer and that is one of the sources of recovery to the extent there are window installation leaks. Often when these windows are deconstructed during litigation, it is determined that the method of placing the building paper or “lathing” the paper, has in fact been reversed by the workers in the field, causing water to migrate into the residence. This is particularly true in the situations where there is wind driven rain which is essentially applying water at a 90 degree angle to the window, and thus able to find any minute entry points for the water to penetrate the structure.

One of the ways that windows are tested to see if there are window installation issues, is to use a spray rack test under ASTM guidelines. This test is done under specific controlled environment and applies a certain pressurized spray of water pursuant to a rack 18 inches away from the window at a specified interval. The problem with this “standardized test” is that the amount of water applied pursuant to a spray rack test far exceeds any natural water which could ever be placed upon the window. Therefore, there are often times artificial readings that the window is defective when in fact there has been no physical observable evidence (i.e., any stains in the wall cavity or on the drywall) at the window location. These are issues which the defense experts have to deal with on a routine basis.

In addition to windows, homes typically have sliding glass doors as well. Sliding glass doors are manufactured with the same type of material as windows, and usually the design matches the window type. However, sliding glass doors are installed differently. A typical window frame is a one piece manufactured unit which is simply placed at the location. Sliding glass doors are usually frames which must be assembled at the location and include a separate jamb (side) head (top) and threshold (bottom edge) components. Like windows, paper perimeter flashings are installed at the jams and the head in a similar fashion. Typically, there are less leaks at sliding glass doors than windows, except that a number of leaks generally occur at the thresholds of the doors at the lower level, sometimes due to the fact that the thresholds are set “below grade” from the exterior of the residence, thus allowing water to migrate at that level.

B. Stucco

One of the tie-ins to the window installation flashing is the interface with stucco. Typically, in California stucco is the primary exterior product applied to a residence. Stucco is nothing more than a cementitious product containing cement, sand and water. In Southern California in particular, most stucco applications are known as a three coat plastering system. Prior to the initial application of any plaster or stucco, the entire exterior surface of the building is covered in building paper similar to the installation identified above under the window installation. The building paper is weather resistive and is again installed in a shingled fashion and tied into other paper flashing components and sheet metals. (See discussion below.) All the stucco must necessarily end or terminate into a joint or device, be it a door frame, window frame, sheet metal flashing, screed, wood stop or trim. The stucco simply can’t end in a vacuum, it must have a termination point.

In terms of the installation stucco, wire lath (sometimes referred to as chicken wire) is installed over the building paper. The first coat of plaster which is then applied is referred to as the scratch coat and it is usually 3/8th to 1/2 inch thick and is installed over the lath. This coat has a rough texture to allow for adhesion of the subsequent applications. After the appropriate drying time, a second or brown coat of stucco is then placed. This coat is smooth in texture and usually brings the total thickness of stucco to approximately 3/4 of an inch. The third coat of plaster is referred to as the color coat and primarily consists of cement with

color integrated into it. This is material that is generally trolled over the brown coat and provides the final color and texture for the plastered finish.

The issue with water intrusion arises in connection with the building paper placed by the stucco subcontractor as it ties into window and door openings. Typically the building paper and the window flashing paper must be integrated so that there are no open avenues for water to enter. In any given situation involving membrane issues with windows, both the framers (windows and doors) and the stucco subcontractors are generally implicated in any water intrusion issues due to their joint involvement in the construction at or near the window and door locations.

C. Roofs

Other than windows, the single biggest water intrusion area in a residence is the roof and its associated penetrations and accessories.

1. Types

There are generally two types of roofs, flat roof and pitched roofs. Flat roofs generally involve having a built up roofing material consisting of multiple layers of sheet membranes or asphalt related products. The layers are installed with a hot tar, a technique known as hot mopping which covers the joints and seams. Built up roofing may have a finished surface known as a “cap sheet.” Typically, flat roofs are more of a commercial design such as low story commercial buildings and apartment buildings. Flat roofs by their very nature have limited slope and thus, do not allow water to run off as readily as on a pitched roof. Under the Uniform Building Code, such roofing systems require the roofs to be sloped at a minimum of 1/4 inch per every 12 inches of positive drainage, and most manufacturers require the roofs to be free of ponding water 48 hours after rainfall. Water can not drain over the roof edge (in the situation where the roof walls are slightly higher than the roof itself) (again, apartment design.) The roofs are required to have roof drains and an overflow drain at the low point in the roofs. The asphaltic material generally must turn up the walls from the roof deck to allow for a continuous transition of roofing materials.

One of the issues which generally arises is that, the sloped wall must have a proper top to it or cap so that water does not come down into the structure. Properly sloped sheet metal coping or a piece at the top of the parapet wall will reduce the potential for water intrusion and will eliminate staining from the top of the wall runoff. Stucco capped parapet walls require a higher level of care and design and construction, as stucco itself is not waterproof.

Typically the problems you see with flat roofs are the fact that water is not drained properly and sits on the roof. The water then finds a seam which has separated and allows water to travel or migrate into the interior building units.

2. Pitched Roofs

Pitched roofs generally have two types of products. They either have shingle products which top nail the shingle to the underlayment into the roof sheathing, or they have a concrete tile which is typically nailed through a hole in the top of the tile and then through the underlayment and into the sheathing. Concrete tiles have been the predominant roofing tile in more recent construction.

Contrary to what most people think, the tile itself is not the waterproofing component of the roof. That component is referred to as the underlayment.

D. Underlayment

Underlayment is usually an asphalt sheet product that provides a weather resistant barrier for the roof sheathing and framing components. Underlayment is usually referred to in pounds per 100 square feet, therefore a 30 pound underlayment is material that would weigh 30 pounds per 100 square foot. Underlayment is placed directly over the roof substrate such as plywood sheathing or framing components. It may be installed in single or multiple layers. In any case, the underlayment is always installed in a “shingled” fashion, one layer laying on top of another layer to allow appropriate water runoff. The shingle fashion begins at the lower edge of roof eave and extends up to the top most termination referred to as the ridge. In some high slope conditions with concrete tile, the underlayment is the entire waterproofing element, and the roof tile is simply a decorative covering.

E. Sheet metal

Sheet metal is an intricate part of preventing water intrusion. Frankly, if there were no penetrations through the roof and it was simply a solid surface with underlayment and tile, there would be very few roof leaks. However, penetrations for plumbing vents, electrical vents and the like are required to be placed through the roof and such penetrations must be properly “roofed in” to protect against the elements.

Sheet metal provides most of the finish material interfaces and terminations for the roofing material. Most of the sheet metal is preformed into specific shapes for intended uses. Typical examples are bird stops, valley flashing, eave flashing, tile pan flashing, and wall flashing. Bird stops are a pre-formed metal flashing that fits under and between concrete clay or tile to prevent intrusion by bird or rodents. Valley flashing is a piece of flat metal with a raised center used to cover the intersecting roof planes at valley conditions. This is essentially a piece of sheet metal that sits in the valley where the water flows, to keep the water flowing in a specific direction and away from the underlayment. Eave flashing is an L shaped metal with a bent drip edge which is placed at the edge of the roof along the eave lines. There is also specific sheet metal flashing, such as Z-bar flashing, which is utilized for siding or stucco termination.

Two specific types of sheet metal are crickets and saddles. A cricket is a formed piece of sheet metal that diverts water flow to a path that leads either to the roof edge or to a roof drain. The cricket may be a small piece of sheet metal behind a corner of a chimney on a sloped roof or could be a large piece of metal on a flat roof. A saddle is a custom piece of sheet metal that is typically found at the intersection of the sloping roof in the back of a chimney. This allows the water to flow in two directions but not into the chimney surface.

In discussing any “roof leaks,” one must necessarily consider the scope of work of each of the subcontractors involved. Sometimes the roofer installs all of the sheet metal pursuant to its subcontract. In other situations a separate sheet metal subcontractor fabricates the sheet metal and places it on site for final installation by the roofer. A third situation is where the sheet metal subcontractor actually places and installs the sheet metal. The determination of how this sheet metal work is actually undertaken is critical to an understanding of any roof issues, as typically any roof leaks generally manifest themselves in sheet metal/roofing

transitions. Very rarely do you simply find a roof leak in the field of the roof through the underlayment unless there was a complete tear in the underlayment during construction. More likely than not, the leaks are manifesting themselves at sheet metal intersection locations or vent locations which required a sheet metal component which was not properly “roofed in.”

Typical plaintiff allegations regarding roof leaks are that there is improper and incomplete sheet metal flashing, there is missing or short cut roof underlayment felts, improper use of materials, improper slope to drain, and lack of gutters. With respect to the short roof underlayment felt, the underlayment generally needs to turn down from the roof a specified distance onto the eaves so that there is no possibility that water could land on the roof and “get under” the roof felt. Often, to save time, the roofer will cut the felt rather than turn it down the eave, creating this problem.

F. Balcony/Decks

A subset of the roofing/sheet metal issues is a balcony or a deck generally found on second story houses, or apartments or condos. A deck typically is constructed off of a sliding glass door. The decks are generally constructed with frame members or plywood, over which an elastomeric type coating is placed (this is similar to an asphalt built up roof). It has been our experience that decks tend to generally be a problematic area, as they are constructed relatively quickly, and simple construction points are overlooked. If, for example there are a number of units with decks and each deck has been constructed improperly, the magnitude of the claimed repair can be significant.

Typically speaking, deck leaks occur for the following reasons: improper flashing, the threshold of the sliding glass door is not higher than the deck to prevent water intrusion, there is an improper deck to wall transition, there is improper slope drainage to drain (i.e., reverse drainage towards the house instead of away from the house), improper deck finishing or coatings, and/or improper installation of deck scupper drains. We have observed all of these conditions on a routine basis in connection with decks or balconies. The manifestation of damages can run the gamut from deck structural failure, to dry rot, to interior leaks and/or stucco staining and cracking as a result of water intrusion at the wall/door threshold. One of the most obvious defects generally observed is that the waterproofing material in the deck



does not in fact extend up the vertical surface of the walls by any appreciable amount (i.e., ideally 1½ to 2 inches) to create a continuous waterproof membrane along the balcony sides. While the membrane may exist on the balcony “floor”, any water at the transition of the wall to the deck has not been waterproofed such that water is allowed to migrate into the interior wall spaces.

These are a few summary observations and analysis of common construction defects. For more detailed information or answers to specific questions, please don’t hesitate to contact the firm at (818) 907-4000 or info@grayduffylaw.com.