RIVKIN RADLER
ATTORNEYS AT LAW

May 2025 | Insurance Update | WWW.RIVKINRADLER.COM

Supreme Court of Oregon Holds That Faulty Workmanship May Be Covered Even Where Claimant Only Sues for Breach of Contract

Courts generally recognize that damages arising solely from breach of contract are not caused by an "occurrence," and thus do not qualify for coverage under a commercial general liability policy. But when the facts support both a tort and contract claim, decisions are mixed on whether there is coverage where the only claim against the insured is for breach of contract.

In this case, a general contractor (GC) built plaintiffs' house but didn't level the garage floor properly. The GC and plaintiffs entered into a Repair Agreement to fix the garage floor. As part of the repair work, the GC hired a subcontractor to install a concrete overlay known as "Ardex." But against the manufacturer's instructions, the subcontractor covered up the construction joints when applying the Ardex coating, resulting in cracking. The garage floor repairs had to be redone.

Plaintiffs commenced arbitration alleging that the GC breached its obligations under the Repair Agreement. Plaintiffs prevailed but could not collect from the contractor. So, they pursued the contractor's commercial general liability insurer, Admiral.

Admiral denied coverage. It cited Oregon Supreme Court authority that liability imposed by law – a requirement of the CGL policy – occurs only if property damage results from a tort. Admiral argued that there was no "property damage" caused by an "occurrence" (defined as an "accident") because the only damages the arbitrator awarded were for breach of contract.

Plaintiffs, for their part, argued that there is no "occurrence" only when there is a complete failure to perform the contract. A mistake that results in accidental property damage, according to plaintiffs, is an "occurrence." Plaintiffs argued that cracks in the garage floor resulted from the subcontractor's mistake in covering up the construction joints.

Admiral won at the trial and the intermediate appellate courts. But the Oregon Supreme Court reversed.

The Oregon high court acknowledged that damages arising solely from a breach of contract do not qualify as having been caused by an "accident" under a CGL policy. But focusing on the facts and not the legal labels, the court said this was not dispositive.

The mere fact that an insured was in a contractual relationship with a plaintiff did not foreclose the possibility of liability to that plaintiff in tort. Where a party is held to a standard of care independent of those imposed by contract, then property damage resulting from a breach of that standard may be recovered in tort.

For insurance purposes, the court distinguished between nonperformance and negligent performance. Nonperformance isn't the result of an accident, but negligent performance may be accidental. The court held that plaintiffs' decision to pursue only a breach of contract claim did not affect recovery under the CGL policy.

This issue was before the court on the Admiral's summary judgment motion. The court found a genuine issue of fact remained over whether the subcontractor, by failing to follow the manufacturer's explicit installation instructions, unreasonably created a foreseeable risk of harm to plaintiffs and that plaintiffs had incurred damages as a result. In other words, there was a possibility that plaintiffs had a tort remedy independent of the contract remedy.

Thus, the Oregon Supreme Court held that the trial court erred in awarding summary judgment because Admiral showed only that plaintiffs pursued a contract remedy; Admiral did not show there was no basis for tort recovery.

The case is *Twigg v. Admiral ins. Co.,* No. SC S070191 (Ore. Apr. 17, 2025).

NOTE: The Oregon Supreme Court did not address whether the damages awarded to plaintiffs in the arbitration proceeding were in fact for “property damage” under either the insurance policy or Oregon’s tort law. Most jurisdictions adhere to the economic loss rule: a party suffering only economic loss from the breach of an express or implied contractual duty may not assert a tort claim for such a breach absent an independent duty of care under tort law.

Last month, the Colorado Supreme Court considered the contours of that doctrine. In *Mid-Century Insurance Co. v. HIVE Construction, Inc.*, No. 23SC267 (Apr. 21, 2025), the court held that no exception to the economic loss rule exists for alleged willful and wanton conduct. Although the economic loss rule generally does not apply to intentional torts that also breach a contractual obligation, the court distinguished willful and wanton conduct (acting purposefully without regard to the consequences) from intentional torts (acting purposefully and intending the result or knowing the conduct is likely to bring about that result).

In *Mid-Century*, a general contractor was hired to build a kitchen for a restaurant. The plans called for two layers of drywall to be installed between the kitchen and the dining area for fire resistance. But the contractor installed only one layer of drywall, and a fire eventually started in the wall.

The restaurant’s insurer filed a subrogation action against the contractor, alleging the contractor’s actions were willful and wanton. But the Colorado Supreme Court held that the insurer was barred from pursuing a negligence claim that arose from a contractual duty. The contractor’s alleged willful and wanton conduct created no exception. That’s because there was no duty in tort independent of the contractual duty. The duty of care that the contractor allegedly breached did not differ from its contractual duty to follow the design plans.

In both the Oregon and Colorado cases, the contractor was liable for failing to follow instructions, and the Colorado Supreme Court found that whether that breach was willful or not didn’t prevent the economic loss rule from applying. The Colorado case was not an insurance coverage case. But as these two cases illustrate, the economic loss rule and the coverage issue are intertwined.

Sixth Circuit Holds That Settlement Demand Letter to CGL Insurer Was not a "Claim" for Bad Faith under Insurer's E&O Policy

The Waves motel bought a $1 million primary general liability policy from State Automobile Mutual Insurance Company. In April 2016, a motel guest was murdered at the motel and her estate sued the motel for wrongful death. State Auto defended the Waves in the lawsuit.

A few months later, the estate sent a letter to the Waves demanding that it settle for $1 million. It included State Auto on the letter and stated that State Auto would be acting in bad faith if it did not accept the settlement offer. State Auto declined the offer.

In 2017, the estate sent a second letter, this time demanding $5 million to settle. The demand letter emphasized State Auto's alleged bad faith for not having accepted the earlier $1 million settlement demand. State Auto rejected the estate's offer and the case went to trial. The jury awarded the estate $12 million, finding the Waves fully at fault for the incident.

State Auto then notified its own errors and omissions insurers, Columbia Casualty and ACE, of the excess verdict. Both insurers told State Auto that they would treat the jury's verdict against Waves as a "notice of circumstances."

Waves appealed the verdict but lost. State Auto paid the estate $13.3 million, including post-judgment interest.

State Auto next sought coverage from its E&O insurers, but they denied because no "claim" had been made against State Auto under the policy. The coverage dispute was litigated and the trial court ruled for the E&O insurers. State Auto appealed to the Sixth Circuit.

State Auto argued that the 2017 demand letter asserted a "claim" for bad faith for refusing to settle the estate's suit. The E&O policies defined "claim" as including "a written demand for monetary damages or non-monetary relief."

The Sixth Circuit, applying Ohio law, acknowledged that the demand letter was a written demand for monetary damages. But it was only a demand to settle claims the estate had against the Waves, not against State Auto. The court found that even though the letter was addressed to State Auto, that did not transform it into a "claim" against State Auto. The letter was directed at the Waves for its liability. It did not assert a claim for bad faith against State Auto.

The court next found that the 2017 demand letter could not state a bad faith claim because there was no final judgment against the insured in excess of the policy limits until April 2020. Thus, there was no legal basis for bad faith against State Auto in 2017.

State Auto argued that the 2017 demand letter asserted a conditional claim that ripened into an actual claim once the excess judgment was rendered. The court was skeptical that Ohio law even recognized conditional claims but found that any such conditional claim would have expired before the judgment. Because the settlement offer expired before the contingency (an excess-of-limits judgment) was met, so too did the conditional claim.

The Sixth Circuit also equated the bad faith reference in the 2017 letter with posturing. State Auto's conduct may have given the estate leverage to argue that it was in State Auto's best interest to settle for an amount above the $1 million policy limit. But that did not transform the estate's demand into a bad faith claim against State Auto. Alleging that State Auto acted in bad faith, the court reasoned, is not the same as seeking payment from State Auto on account of its alleged bad faith conduct.

The court also observed that the policies' notice requirements distinguished between circumstances that may reasonably be expected to give rise to a claim and an actual claim. Because the policy distinguished between actual and potential claims, it would not make sense to find that a mere intention to hold the insured responsible was the same as an actual claim.

In short, the Sixth Circuit held that the 2017 demand letter sought payment from the motel for its negligence, not State Auto's bad faith. The letter thus did not assert a triggering claim.

The case is *Columbia Cas. Co. v. State Auto Mut. Ins. Co.*, No. 24-3338 (6th Cir. Apr. 10, 2025).

Texas Court of Appeals Reverses $25M Judgment Favoring Exxon, Finds That Employer's Liability Exclusion Applies

In this case, payments under an owner-controlled insurance program (OCIP) affected a premises owner's recovery as an additional insured under its contractor's insurance policy. As a statutory employer of workers injured on a job site, the premises owner was subject to the insurance policy's employer's liability exclusion.

Exxon Mobil retained Brock services to provide scaffolding services at an Exxon refinery. The parties' contract stated that Brock and its employees were independent contractors. Brock was required under the contract to obtain commercial general liability coverage naming Exxon as an additional insured. Exxon provided workers' compensation coverage to Brock through an OCIP.

An explosion at the refinery injured several Brock employees. After receiving workers' compensation benefits provided through the OCIP, the injured workers sued Exxon.

Exxon sought defense and indemnity under Brock's umbrella policy with Lexington. Lexington disputed coverage. A Texas trial court affirmed an arbitrator's finding that Exxon was an additional insured under the Lexington umbrella policy and held that Exxon was entitled to the full $25 million limits of that policy. (Exxon settled the Brock employees' claims for $35 million). Lexington appealed.

The issue boiled down to whether the Employer's Liability exclusion applied. That exclusion stated:

> [t]his insurance does not apply to ... "[b]odily injury" to an "employee" of the "Insured" arising out of and in the course of (a) [e]mployment by the 'Insured'; or (b) [p]erforming duties related to the conduct of the "Insureds" business and applies [w]hether the "Insured" may be liable as an employer or in any other capacity ....

Lexington argued that the Exxon became the employer of the injured Brock workers by its participation in the OCIP. Under the Texas Labor Code, because Exxon procured workers' compensation coverage for Brock's employees under the OCIP, it was treated as their employer (but only for purposes of the state's workers' compensation laws). An employer who does not provide workers' compensation insurance for its employees remains liable in tort. But an employer that provides such insurance is shielded from liability to its employees for tort suits. So, Lexington argued that Exxon had no liability to the injured Brock workers and was considered an employer by statute. The employer's liability exclusion would thus apply.

For its part, Exxon argued that in determining whether the employer's liability exclusion applies, the court should look to the defined terms in the insurance policy. Exxon emphasized that the Brock workers were not Exxon employees under the common law, nor under the parties' contract, which identified Brock as an independent contractor. That they were statutory employees under the workers' compensation act did not change their status under the insurance policy.

The Texas Court of Appeals disagreed and sided with Lexington. It found that the Texas Supreme Court recognizes that Exxon would be a statutory employer of the Brock workers and was entitled to invoke the exclusive remedy defense of the workers' compensation statute. And all parties knew they were participating in an OCIP program, which provided that employees of a subcontractor would be considered employees of the general contractor in the event of a workplace accident. As Exxon was the statutory employer of the injured Brock workers, the employer's liability exclusion in the Lexington policy applied. Lexington had no duty to defend or indemnify Exxon in the Brock workers' suit.

The case is *Lexington Ins. Co. v. Exxon Mobil Corp.*, No. 09-22-00174-CV (Tex. Ct. App. Apr. 3, 2025).

Tenth Circuit Confirms That New Mexico Does Not Follow Indiana Policyholder-Friendly Approach to Pollution Exclusions

The City of Las Cruces and the County of Doña Ana, New Mexico, sued Chisholm's Village Plaza, LLC for cost recovery and contribution as part of a decades-long effort to respond to a two-mile-long chemical plume in Las Cruces. The underlying suit was brought under the Comprehensive Environmental Response, Compensation, and Liability Act ("CERCLA"). Chisholm's sought coverage from its insurer, Fidelity and Guaranty Insurance Underwriters ("Fidelity"). Fidelity denied coverage based on absolute pollution exclusions which barred coverage arising from the alleged release of a "contaminant." Chisolm's filed a coverage suit in federal court.

The district court awarded Chisolm's summary judgment, finding that absolute pollution exclusions were ambiguous under New Mexico law. It found that the insurers owed Chisholm's a duty to defend. In reaching that conclusion, the court predicted that the New Mexico Supreme Court would adopt an interpretive approach to pollution exclusions taken only in Indiana that requires the policy to specify the exact type of pollutant by name. The insurers appealed.

The Tenth Circuit reversed. The court said no New Mexico case law required an insurer to list the exact pollutant in an exclusion for the exclusion to be deemed clear. Rather, the New Mexico Supreme Court has held that a pollution exclusion need only include a term that encompasses noncovered activities among the itemized list of excluded things. Thus, there was no reason to believe that New Mexico would follow Indiana's maverick approach.

The Tenth Circuit held the terms "pollutant" and "contaminant" were unambiguous on their face and unambiguously precluded coverage for the CERCLA suit. Fidelity did not have to defend Chisholm.

The case is *Chisholm's-Vill. Plaza LLC v. Cincinnati Ins. Co.*, No. 23-3122 (10th Cir. Apr. 23, 2025).

Ninth Circuit Holds Care, Custody, or Control Exclusion Bars Coverage for Damage to Aircraft in Hangar

In June 2017, Richard Harris executed a lease for a North Las Vegas aircraft hangar. The hangar was to house Richard Harris' aircraft, which was for the use of his law firm, the Harris Law Firm, LLP and its principals. Harris later formed 702PC LLC and purchased a Pilatus Aircraft.

The Harris Law Firm and 702PC entered into an agreement by which 702PC agreed to provide air transportation services for the law firm employees. Although 702PC paid for a hangar, the Harris Law firm and 702PC each used the space. 702PC's use of the hangar was limited to aircraft-related activities, while Harris's use was limited to file storage. No physical barriers restricted a party's access to areas within the hangar or property stored, and each had the ability to access the hangar as needed for the items they stored in the space. According to Harris, although there was no written rule about the law firm and its employees' interactions with the aircraft, there was an understanding that the law firm and its employees would have nothing to do with the plane.

In November 2018, two law firm employees had to remove their stored files from the hangar. The plane was in the way. Although not authorized to remove or otherwise touch the aircraft, they used a powered wheel-dolly to move the aircraft under the hangar door, and then briefly exited the hangar. Shortly after they left, the hangar door closed on the aircraft (through unknown circumstances), seriously damaging the plane.

702PCrepaired the aircraft. 702PC demanded coverage from State Farm. State Farm denied coverage and filed a declaratory judgment suit against the Harris law firm. The district court granted State Farm summary judgment, applying the policy's exclusion for property damage to personal property in the "care, custody, or control" of the insured. Applying Nevada law, the court held it did not matter that the law firm's employees assumed control over the property without the owner's permission. It was undisputed that they had access to the property and knowingly assumed physical control over it. The court also held that the possessory control here was exclusive even if it was a short duration and no other person exercised any physical control over the aircraft during the incident. The Harris law firm appealed.

The Ninth Circuit affirmed. The court held that even though the law firm did not own the aircraft, its employees controlled the aircraft at the time of the incident when they physically maneuvered the aircraft to sit under the open hangar door, where it was ultimately damaged. The court further held that legal control was not required for the exclusion to apply, especially because legal control for liability coverage was a concept found elsewhere in the policy but not in the care, custody, or control exclusion.

The case is *State Farm Fire & Cas. Co. v. Richard Harris Law Firm*, 24-2047 (9th Cir. Apr. 1, 2025).

RIVKIN RADLER
ATTORNEYS AT LAW

Rivkin Radler LLP
926 RXR Plaza, Uniondale NY 11556
www.rivkinradler.com