The Tenth Circuit Holds That New York Court of Appeals Likely To Allow Coverage For Claims Arising Out of a Subcontractors' Faulty Workmanship

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The United States Court of Appeals for the Tenth Circuit recently rendered a decision that may impact New York law regarding the rights of general contractors to obtain insurance coverage for damages resulting from a subcontractor's faulty work. In Black & Veatch Corp. v. Aspen Ins. (UK) Ltd., 2018 U.S. App. LEXIS 3342, Case No. 16-3359 (February 13, 2018), the Tenth Circuit held that the New York Court of Appeals would likely conclude that a subcontractor's shoddy work is a covered occurrence under a general liability policy should the issue come before New York's highest court. The New York Court of Appeals has yet to address the issue, although New York's intermediate appellate courts remain divided on the issue.

Black & Veatch arose from an insurance coverage dispute in which the general contractor sought to be reimbursed by its insurer for costs incurred due to damaged equipment that its subcontractor constructed at power plants in Ohio and Indiana. The insured contracted to engineer, procure and construct several "jet bubbling reactors," which purportedly eliminate contaminants from the exhaust emitted by coal-fired power plants. The insured subcontracted the engineering and construction of "internal components" which were found to be deformed and cracked as a result of a subcontractor's work. The policy excluded coverage for "Your Work", which was defined as "work operations performed by you or on your behalf" by a subcontractor. The "Your Work" exclusion, however, was subject to a subcontractor exception, which stated that the exclusion did not apply "if the damaged work or the work out of which the damage arises was performed on [the insured's] behalf by a subcontractor." The Court commented on this exclusion by stating that "[i]n other words, the Policy does not cover property damage to [the insured's] own completed work unless the damage arises from faulty construction performed by a subcontractor."

Since the insurer's policy was governed by New York law, the Tenth Circuit was asked on appeal to address a single issue – whether the New York Court of Appeals would decide that the damages sustained were "occurrences." The Tenth Circuit answered that question in the affirmative, holding that New York would follow the trend adopted by a number of other state supreme courts that damages connected to a subcontractor's faulty work can constitute an occurrence.

The Court concluded that the property damage at issue was an occurrence because the insured did not expect or intend its subcontractors to perform faulty work, and that a third party had asserted the property damage claims against the insured. In reaching this determination, the Tenth Circuit examined several New York intermediate appellate decisions rejecting coverage for faulty subcontractor workmanship — including the decision in *George A. Fuller Co. v. USF&G*, 200 A.D.2d 255 (1st Dep't 1994) — and concluded that those decisions would not provide adequate guidance to the Court of Appeals because they focused on policies – drafted before ISO's 1986 changes – that did not contain the subcontractor exception.

The Black & Veatch decision is noteworthy because it is a well-respected court and may sway other

courts, in addition to the New York Court of Appeals, on the question of whether a subcontractor’s shoddy work is an “occurrence” and the application of the “Your Work” exclusion in a CGL policy.