

No Coverage for Tearing Down Barn Apartment that Violated Building Code

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The South Carolina Court of Appeals recently held that a general liability policy excluded coverage for the homeowners' claim that they lost the use of property when they had to remove an apartment built on top of a barn because it violated zoning ordinances. *William and Frances Walde, as Assignees of Johnson Construction Co. of Aiken, Inc. v. Assoc'n Insurance Co.*, (S.C. Ct. App. Op. No. 5061, Dec. 2012).

The Waldes, (homeowners) wanted to build a barn with an upstairs apartment on their property in Aiken. They hired Johnson Construction to obtain the necessary variances from city building ordinances. The homeowners then contracted with Johnson to construct the barn and apartment. Eighty percent of the work had been completed when the building inspector notified Johnson that the barn did not comply with the variance or the special exception. The city ultimately allowed the barn to remain if the apartment was removed to lower the barn's roof.

The homeowners filed an arbitration claim against Johnson, who tendered it to his insurer, Association Insurance Company (AIC). AIC denied coverage. Johnson and the homeowners settled their dispute prior to arbitration. The settlement included an assignment to the homeowners of Johnson's rights against AIC. The homeowners filed suit against AIC, alleging breach of duty to defend and indemnify. The trial court granted the homeowners' motion for partial summary judgment, holding AIC was obligated to defend Johnson, that the policy provided coverage, and that AIC was liable for fees and costs.

Property Damage – The homeowners claimed they suffered “physical injury” to property when the barn was partially demolished. The Court of Appeals rejected that argument holding that although “physical injury” was not defined by the policy, injury is generally considered the violation of another's legal right. Using this definition, the court ruled that the partial tearing down of the barn's second story did not constitute an injury because the removal was a remedial measure to fix the injury caused to the homeowners when the construction put them in violation of the City's ordinances. However, the court also held the homeowners' allegations raised the possibility of loss of use of tangible property that had not been physically injured, because the homeowners could not fully use the property after they were informed of the barn's noncompliance. The court rejected AIC's argument that the homeowners failed to allege property damage because the physical injury to the barn resulted from faulty or defective workmanship, as faulty workmanship was only relevant to the policy's exclusions, not the definition of property damage.

Occurrence – The court next concluded the homeowners' allegations in the arbitration demand established the possibility of an occurrence. The demand claimed that Johnson's advice was “wrongful”. AIC argued the use of “wrongful” meant the claims were not based on an accident that would give rise to an occurrence. The court

rejected the argument, holding the allegation that Johnson “wrongly” said its plans complied with the variance and exception could be construed as alleging Johnson was mistaken or acting without due care. The opinion noted that the court must look beyond the labels describing the acts and allegation and look to the acts themselves which formed the basis of the complaint.

Accordingly, regardless of whether the claim was for negligence, negligent misrepresentation, or breach of fiduciary duty, the allegation of erroneous representations and provision of information was unintentional, and therefore, potential acts within the terms of the policy.

Exclusion – The court concluded, however, the “your work” exclusion applied and excluded coverage. That exclusion excludes coverage for property damage to that particular part of any property that must be restored, repaired, or replaced because the party’s work was incorrectly performed on it. The exception to that part of the Damage to Property exclusion provides the section does not apply to property damage included in the products-completed operation hazard. The court agreed with AIC that the homeowners’ alleged property damage was not included in the products-completed operations hazard coverage. Regardless of whether the contract was complete (or terminated) when the homeowners lost the use of the property, the policy deems all loss of use unaccompanied by physical injury to have occurred at the time of the occurrence.

The homeowners claimed the loss of use of property arose out of Johnson incorrectly advising them and obtaining the necessary approval from the City. Therefore, the loss of use was deemed to have happened at the time of those incorrect performances, and before Johnson’s work was complete. The homeowners alleged the loss of use of the barn while they were required to tear down and build a new roof; they alleged property damage to that particular part of property that must be replaced because Johnson’s permit work was incorrectly performed.

The court rejected the homeowners’ argument that their claims were not excluded because the defective work occurred before the zoning authority rather than the construction of the barn. The argument that their claims involved a permitting defect, not a construction defect, did not allow it to escape the damage to property exclusion.

About Pete Dworjanyn

Pete Dworjanyn is a shareholder and chair of Collins & Lacy’s Insurance Coverage Practice Group and founding author of the South Carolina Insurance Law Blog. Following law school, Pete served as a law clerk for the Honorable Julius H. Baggett, Eleventh Judicial Circuit and as Assistant Solicitor in the Eleventh Circuit Solicitor’s Office. Prior to joining Collins & Lacy in 1999, Pete was in private practice, focusing on civil litigation. Pete’s reputation has earned him a BV rating by Martindale-Hubbell. He also is one of the Best Lawyers in America, the oldest and most respected peer-review publication in the legal profession.

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