

CONSTRUCTION

ARIZONA COURT OF APPEALS RULES THAT COVERAGE FOR AN ADDITIONAL INSURED IS NO GREATER THAN COVERAGE AFFORDED A NAMED INSURED -- INTERPRETATION OF THE "YOUR WORK" EXCLUSION.

by J. Gregory Cahill

In a matter of first impression, the Arizona Court of Appeals recently ruled that the "Your Work Exclusion" in a Commercial General Liability ("CGL") insurance policy bars coverage for an additional insured when the only claimed damage was to the named insured's own work.

This exclusion is standard in most CGL policies. The theory behind the exclusion is that the purpose of a CGL policy is to compensate for property damage, not to warrant the quality of an insured's work. For example, if a roofing subcontractor defectively installs a roof and the only damage is to the roof itself, the exclusion bars coverage. However, if damage occurs to other property as well, then coverage to repair the "other" damage will typically exist. Thus, if the roofer's defective work also leads to water intrusion which damages the interior of a building (e.g., drywall or framing damage), the exclusion will not bar coverage for the interior property damage.

This exclusion is typically coupled with a "Subcontractor Exception," which provides that the exclusion does not apply if the damage to *Your Work* . . . "arises from work performed on Your behalf by a subcontractor." The term "Your" is typically defined as the named insured.

Until recently it was unclear whether the exception would permit coverage for an additional insured (general contractor) even though the only damage was to a named insured's (subcontractor) work. That was the issue before the Arizona Court of Appeals in *Double AA Builders, Inc. v. Preferred Contractors Insurance Company, LLC*.¹

In 2007, Harkins Theaters hired Double AA to serve as a general contractor for the construction of a theater complex. Double AA, in turn, hired Anchor Roofing to install the roof. Double AA's subcontract with Anchor required Anchor to have Double AA named as an additional insured under any CGL policies that would apply to the work. Anchor obtained a CGL policy from Preferred Contractors Insurance Company in which Anchor was the named insured and Double AA an additional insured.

Shortly after the project was completed the roof began to leak. At Harkin's request Double AA replaced the roof. Double AA then sued Anchor, Preferred, and its own insurance carrier. Notably, the only damage claimed by Double AA was the cost to replace the roof.

Double AA settled with its carrier and obtained a default judgment against Anchor. Preferred answered the complaint and it and Double AA filed cross-motions on whether the "Your Work" exclusion barred coverage for the cost to replace the roof. The trial court ruled in favor of Double AA and Preferred appealed.

In reversing the trial court's ruling the Court of Appeals held that, under an additional insured endorsement, the coverage afforded an additional insured can be no greater than the coverage afforded a named insured. The Court explained that, since the term "Your" was defined as the named insured, the Subcontractor Exception only applied if the damage was to the work of Anchor's subcontractor. The fact that Anchor was Double AA's subcontractor was irrelevant. The court found that if an additional insured was allowed to take advantage of the "Subcontractor Exception" where the named insured could not, the carrier's risk would be increased without a corresponding increase in premiums. The Court directed the trial court to enter judgment in favor of Preferred.

The Court's opinion did clarify an important point. It made clear that its holding was dictated by the nature of the claimed damages, that is, Double AA only sought recovery of the cost to replace Anchor's defective work. Had Double AA sought recovery for damage to other property, the result would likely have been different.

¹ No. 1 CA-CV 15-0375 (December 30, 2016).

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