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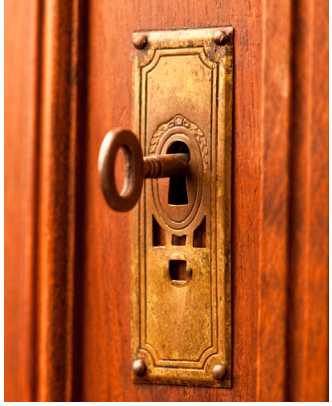

The 1st Party Report

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Georgia Supreme Court Clarifies Property Damage Caused by an Intentional "Accident" Constitutes an "Occurrence" Under a CGL Policy

By: D. Barton Black

The Georgia Supreme Court recently dealt a blow to insurers when it clarified the definition of an "accident" as it relates to an "occurrence" in construction defect cases. *See Am. Empire Surplus Lines Ins. Co. v. Hathaway Dev. Co.,* 2011 Ga. LEXIS 177 (March 7, 2011). In *Hathaway*, the Georgia Supreme Court was faced with a question that had been posed several times before to the Georgia Court of Appeals and the federal courts in Georgia: can an intentional act of workmanship, when performed negligently, constitute an "accident," and therefore an "occurrence," under a commercial general liability ("CGL") policy? *Id.* The Georgia Court of Appeals held in 2004, and again in 2010, that faulty workmanship can, in fact, constitute an "occurrence." *See QBE Ins. Co. v. Couch Pipeline & Grading*, 303 Ga. App. 196, 198 (2010); *Sawhorse, Inc. v. So. Guar. Ins. Co. of Ga.*, 269 Ga. App. 493, 498-99 (2004). However, Georgia federal courts held in 2004, and again in 2008, that because faulty workmanship is an intended act, even though damages may not have been intended or expected, such faulty workmanship is not an "accident," and therefore not an "occurrence." *See Hathaway Dev. Co., Inc. v. Ill. Union Ins. Co.*, 274 Fed. Appx. 787, 791 (11th Cir. 2008); *Owners Ins. Co. v. James*, 295 F. Supp. 2d 1354, 1363 (N.D. Ga. 2003). Therefore, this issue was ripe for resolution by the Georgia Supreme Court.

In the *Hathaway* case, a developer sued its plumbing subcontractor in the Gwinnett Superior Court for damage to neighboring property resulting from the negligent plumbing work by the subcontractor. *Hathaway*, 2011 Ga. LEXIS 177. The subcontractor failed to answer, default judgment was entered, and the developer sought payment from American Empire Surplus Lines Insurance Company ("AESLIC"), the subcontractor's insurer. *Id.* AESLIC denied liability, asserting that the developer's claim was not covered under the subcontractor's CGL policy ("the Policy") because the property damage did not arise out of an "occurrence." *Id.* The Policy defined an "occurrence" as "an accident, including continuous or repeated exposure to substantially the same, general harmful conditions"; however, as is frequently the case, the Policy did not define "accident." *Id.*

The Superior Court followed several Georgia federal district and appellate courts and ruled that there was no "occurrence," holding that "an abundance of Georgia case law holds that general liability policies simply do not cover the costs of fixing the faulty workmanship of a contractor or subcontractor because poor workmanship does not constitute an accident." *Hathaway Dev. Co. v. Am. Empire Surplus Lines Ins. Co.*, 301 Ga. App. 65, 69 (2009). On appeal, however, the Georgia Court of Appeals reversed and held that the subcontractor's actions did give rise to an "occurrence," stating that cases from the Georgia Court of Appeals took precedent over the federal cases. *Id.* at 69-70. In particular, the Georgia Court of Appeals followed the *Sawhorse* case from 2004 and held that "negligently performed faulty workmanship that damages other property may constitute an 'occurrence' under a CGL policy." *Id.* at 69 (citing *Sawhorse*, 269 Ga. App. at 498).

AESLIC then appealed the Georgia Court of Appeals decision to the Georgia Supreme Court to resolve which definition of "occurrence" should control in Georgia state courts—the definition from the Georgia Court of Appeals or the definition from the Georgia federal courts. *See Hathaway*, 2011 Ga. LEXIS 177, at *1-2. The Georgia Supreme Court ultimately adopted the definition from the Georgia Court of Appeals, holding that "an occurrence can arise where faulty workmanship causes unforeseen

or unexpected damage to other property." *Id.* In particular, the Court reasoned that a "deliberate act, performed negligently, is an accident if the effect is not the intended or expected result; that is, the result would have been different had the deliberate act been performed correctly." *Id.* (citing *Lamar Homes v. Mid-Continent Cas. Co.*, 242 S.W.3d 1, 16 (Tex. 2007)).

In light of the *Hathaway* decision, there is, unfortunately, no where for insurers to hide as Georgia federal courts are bound to apply the Georgia Supreme Court definition of "occurrence." Therefore, fewer cases can be disposed of through summary judgment by arguing that the alleged activities do not constitute an "occurrence." We will provide further updates as the issue is clarified in subsequent Georgia Supreme Court decisions.

For more information on this topic, contact Barton Black at barton.black@swiftcurrie.com or 404.888.6149. ■

Diminution in Value — Not for Commercial Claims Anymore

By: Melissa A. Segel

As his first Directive since taking office, Insurance and Safety Fire Commissioner Ralph T. Hudgens withdrew former Commissioner Oxendine's controversial April 21, 2010 Directive which had applied diminution in value to commercial property claims. Commissioner Hudgens' Directive is succinct: "Directive 10-EX-1, dated April 21, 2010, related to diminution of value, is hereby withdrawn." *Directive 11-EX-1.*

In application, this Directive will likely not change the way insurance carriers settle commercial property claims, as Georgia courts had previously rejected diminution in value as a method of assessing damages in the context of commercial property when a plain reading of the policy language indicates otherwise. *See e.g. Royal Capital Development, LLC v. Md. Cas. Co.*, 2010 U.S. Dist. LEXIS 133911 (N.D. Ga. Dec. 2, 2010).

Diminution in value first found traction in the state of Georgia in *State Farm Mutual Ins. Co. v. Mabry*, 274 Ga. 498, 556 (2001). In *Mabry,* the Supreme Court of Georgia affirmed that diminution in value must be assessed as an element of damages in a first party automobile claim. On the heals of *Mabry*, former Commissioner Oxendine issued a directive requiring all insurance carriers to assess diminution in value along with the elements of physical damage when a policyholder makes a general claim of loss. *Directive 01-P&C-1.* Courts have grappled very little with *Mabry* and it has remained good law with regard to automobiles, obligating insurers to compensate their policyholders for the loss in value if the repair of physical damage from a covered event returned the vehicles to their pre-loss condition in terms of appearance and function without returning the vehicles to their pre-loss value. However, there have been some distinctions outside automobile damage.

In *City of Atlanta v. Broadnax,* 285 Ga. App. 430 (2007), the Court of Appeals of Georgia held that in a nuisance action, homeowners could not recover for both the diminution in the value of their property and the costs of repair, as it would constitute a double recovery of damages. While not specifically addressing diminution in value, in *AFLAC Inv. v. Chubb & Sons, Inc.,* 260 Ga. App. 306

Spoliation

By: Thomas B. Ward

Swift Currie attorneys recently obtained a favorable ruling in a case pending in Fulton State Court that continued Georgia's apparent trend of restricting application of the spoliation doctrine. Spoliation refers to the destruction of evidence that is necessary to contemplated or pending litigation. When the destruction of evidence would result in prejudice to the opposing side at trial, the court has considerable leeway in determining how to best undo the prejudice. The remedies available to the court range from instructing the jury to presume the party destroyed evidence because it was harmful, to excluding any testimony about the destroyed evidence, to, in extreme cases, deciding liability against the spoliating party.

In the personal injury case *Wright v. YKK AP America*, Ms. Wright was driving her car in defendant's parking lot when she was struck in the side by a forklift. Ms. Wright claimed that five surveillance cameras would have captured the collision, but the defendant had destroyed the footage before the lawsuit was filed. When the defendant did not produce video footage in discovery, Ms Wright filed a motion to find that spoliation occurred. The court declined to rule that spoliation had occurred for three reasons.

(2003), the Court of Appeals of Georgia held that a policy providing coverage for "direct physical loss or damage to covered property" did not cover economic losses, making it clear that parties to an insurance policy could limit damages by the terms of the contract.

Former Commissioner Oxendine's Directive attempting to apply diminution in value to commercial property claims was considered controversial when enacted in April of 2010. At the time, the owners of Royal Capital Development, donors to Oxendine's gubernatorial campaign, were involved in a multimillion dollar dispute with their insurance carrier over coverage for damage to their building caused by construction of The Streets of Buckhead development. Oxendine's Directive applying diminution in value to commercial property claims was issued just six days after Royal Capital Development filed suit. The *Atlanta Journal Constitution* linked the campaign contributions by the owners of Royal Capital Development to their request that Oxendine make *Directive 10-EX-1. See http://www.ajc.com/news/georgia-politics-elections/oxendine-donors-deny-link-571811.html.*

In the end, the Directive did not change the outcome of that lawsuit. Federal District Court Judge Robert L. Vining rejected Royal Capital Development's commercial property claim for diminution in value to damaged floor tiles caused by construction at an adjoining property, holding that the matter "boils down to simple policy interpretation." *Royal Capital Development, LLC v. Md. Cas. Co.*, 2010 U.S. Dist. LEXIS 133911 (N.D. Ga. Dec. 2, 2010). "Because the parties limited the defendant's liability by the terms of their policy and because a plain reading of the policy shows that 'diminution of value damages' are not meant to be included in the [cost of repairing or replacing the lost or damaged property], the defendant is entitled to summary judgment." *Id.* at *7. While this order left open the possibility that diminution in value damages may be recoverable under another option of the payment option provision, it weakened the possibility of a policyholder's claim and rendered former Commissioner Oxendine's Directive 10-EX-1 mostly ineffective. Commissioner Hudgens' new Directive has now shut the door - diminution in value is no longer applicable as a method of assessing damages in commercial property claims in Georgia.

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Federal Diversity Jurisdiction: Ensure the Amount in Controversy Does Not Fall a Penny Short Before Removing a Case to Federal Court

By: Brooke N. Williams

In a recent decision from the United States Court of Appeals for the Sixth Circuit, the Court noted that the penny is easily the most neglected piece of U.S. currency. *Freeland v. Liberty Mutual Fire Insurance Co.*, No. 10-3038 (6th Circuit, February 4, 2011). The Court pointed out that pennies often lie at the bottom of change jars and that most people will not even bend over to pick up a penny off the ground, deeming the reward not worth the effort. However, a penny can be the deciding factor when it comes to diversity jurisdiction. The appeals court

First, the Court found the defendant did not know that litigation was contemplated or pending when it destroyed the footage. Under recent decisions, the simple fact that someone was injured, without more, is not notice that the injured party is contemplating litigation. Further, even though Ms. Wright's counsel demanded insurance information from the defendant's insurer, there was no evidence that the defendant ever received a copy of that letter or knew that Ms. Wright had obtained counsel.

Second, it was apparent from recent camera images that the destroyed video footage would not have revealed any material information about the collision. The poor camera angles, coupled with testimony that the cameras only record video footage when triggered, made it highly unlikely that relevant video footage ever existed.

Third, the Court ruled that Ms. Wright had not shown prejudice because such video footage, had it existed, would not be a critical piece of evidence anyway. According to the court, other well-documented and more reliable methods exist for establishing speed in a collision. Because Ms. Wright could not demonstrate prejudice, the Court had no basis for fashioning a spoliation remedy.

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found that the amount in controversy in *Freeland* was exactly one penny short of the jurisdictional minimum of the federal courts, and remanded the case to state court for lack of subject matter jurisdiction.

The *Freeland* case involved an insurance coverage issue which arose out of a motor vehicle accident. A declaratory judgment action was filed in order to clarify a dispute between the insurance company and an insured over the uninsured motorist limits of an automobile policy. The insurance company argued that there was only $25,000 in coverage based on the uninsured motorist limit selected by the insured. The insured argued that the coverage selection form did not contain certain required disclosures and, therefore, the uninsured motorist coverage should have been $100,000, the same as the policy's liability limit.

The insurance company removed the case to federal court pursuant to 28 U.S.C. § 1441(a), which allows removal of civil actions "of which the district courts of the United States have original jurisdiction." Because the case presented no federal question, the insurance company invoked the district court's diversity jurisdiction. Article III of the Constitution authorizes federal jurisdiction in all controversies where the parties are "citizens of different states." U.S. Const, Art. III, § 2. But Congress has always limited this grant of jurisdiction by also requiring that cases satisfy a minimum amount in controversy requirement. *See Snyder v. Harris*, 394 U.S. 332, 334 (1969). The matter in controversy must exceed the sum or value of $75,000, exclusive of interest and costs. 28 U.S.C. § 1332.

"In actions seeking declaratory or injunctive relief, it is well established that the amount in controversy is measured by the value of the object of the litigation." *Hunt v. Wash. State Apple Adver. Comm'n*, 432 U.S. 333, 347 (1977). Applying this principle, courts have held that the amount in controversy is not necessarily the money judgment sought or recovered, but the value of the consequences which may result from the litigation. *See Freeland*, *supra*. If the Freelands prevailed in the declaratory judgment action, they would have received a declaration that their policy provided up to $100,000 in uninsured motorist coverage. If they did not prevail, they would have only $25,000 in coverage. The difference was exactly $75,000. Pursuant to 28 U.S.C. § 1332, the Freelands' demand for interest and costs in their complaint did not increase the amount to more than $75,000. The Court found that it simply had no choice but to remand the case back to state court for lack of federal jurisdiction.

Note that a court has "an independent obligation to determine whether subject matter jurisdiction exists, even in the absence of a challenge from any party." *Arbaugh v. Y&H Corp.*, 546 U.S. 500, 514 (2006). Accordingly, parties should ensure that the amount in controversy exceeds $75,000 prior to removing a case to federal court based on diversity jurisdiction. Otherwise, substantial resources can be expended only to learn that the case must start anew in state court if the amount in controversy falls just a penny short of the jurisdictional minimum.

For more information on this topic, contact Brooke Williams at brooke.williams@swiftcurrie.com or 404.888.6183. ■

Events

Atlanta Claims Association Reception
Thursday, April 14, 2011
5:00 - 7:00 pm
Gwinnett Center - Duluth, GA

Joint Litigation Luncheon with McAngus Goudelock and Courie
Wednesday, April 27, 2011
11:30 am - 2:00 pm
Maggiano's Buckhead - Atlanta, GA

"Settling Your CAT Claim"
Wednesday, May 4, 2011
11:00 am - 1:30 pm
Villa Christina - Atlanta, GA

For more information on these programs or to RSVP, visit www.swiftcurrie.com/events.

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