

The staff of HIO hopes you enjoy the 4th of July holiday. We will return with another edition of HIO on July 12th.

IF YOU HAVE QUESTIONS REGARDING
THIS MATTER, PLEASE CONTACT:



Katherine T. Garber
Partner, Houston
1401 McKinney Street, Suite 2200
Houston, Texas 77010.4035
713.951.5665
Kathy.Garber@strasburger.com

EDITORS

Kathy Darling & David Bain

HEALTHCARE GROUP

David Andrew Bain
Virginia A. Barry
Debra W. Biehle
Thomas W. Burton
Renee Chafitz
Merritt M. Clements
Joseph F. Coniglio
Kathryn Midboe Darling
William Duane Darling
Rebecca L. Davis
R. Bradley Fletcher*
Brian G. Hamilton
John R. Lowry
Bryan J. Maedgen
Cynthia Schafer Marietta
Stuart Miller
David G. Moore
Craig H. Myers
C. Scott Nichols
Laura Reilly O'Hara
Jeffrey S. Osgood
David L. Ovard
Donald Patrick Owens
Paul W. Sheldon
Layne Thompson
Joseph A. Turano
Melissa Webb
Carol D. Williamson
Ivan Wood
Kevin M. Wood

*Not licensed to practice in the state of Texas.

BEWARE THE USE OF RESIDENTIAL CONSTRUCTION EXCLUSIONS IN CGL POLICIES

Virtually all contracts for the construction, renovation and/or repair of health care facilities include a requirement that the contractor provide commercial general liability ("CGL") insurance to protect both the owner and the contractor in the event of a claim for bodily injury or property damage during or as a result of construction activity. Proof that the requested insurance has been procured is usually provided via a certificate of insurance issued by the contractor's insurance agent. However, an owner rarely requests a copy of the actual insurance policy or an opportunity to review the entire policy wording. The failure to take this extra step may leave the owner in a precarious situation in the event of a future claim.

In the last few years, concern regarding the rise in construction defect litigation has led to the insurance industry's increased use of certain restrictive endorsements in CGL policies.¹ One such endorsement is the residential construction exclusion, which "removes coverage with respect to any operations in connection with property intended for habitation."² To date, various insurance companies have filed a total of twenty-nine (29) residential construction exclusions with the Texas Department of Insurance.³ The wording of a residential construction exclusion varies from policy to policy, and from insurer to insurer. Although some versions of the exclusion clearly state that they apply only to the construction of multifamily housing, such as apartments, town homes, and condominiums, some refer more generally to "any operations in connection with property intended for habitation."⁴ Broad exclusions defining "residential" as "structures with beds" or "occupancy" potentially exclude buildings not typically considered "residential" in nature, such as hospitals, skilled nursing facilities and the like.

Notably, the trend to exclude coverage for residential construction does not appear to be restricted to contractors who apply for CGL policies for the first time. Contractors who are currently covered have reason to be concerned, as nothing precludes an insurer from adding a residential construction exclusion to a renewal policy.⁵ Contractors renewing their CGL policies may be likely to

assume they are getting the same coverage as before, instead of carefully reading the policy and requesting that their health care facility construction work be excepted from the exclusion.

Ultimately, whether a certain construction project is covered under a contractor's CGL policy will depend upon the wording of the residential construction exclusion's language. In construing disputed terms in insurance contracts, Texas courts favor the insured's interpretation when the policy language can be interpreted in more than one way. Texas courts hold firmly to the rationale that because insurance companies choose the language in the policy, the wording will be construed in favor of providing coverage to the insured, as long as the insured's interpretation is reasonable.⁶ This is true "even if the construction urged by the insurer appears to be more reasonable or a more accurate reflection of the parties' intent."⁷ Thus, if an insurance company denies coverage to a contractor and/or owner based on a residential construction exclusion, it may be possible to successfully challenge the applicability of the exclusion via the litigation process. The better practice, however, is for the owner to examine the contractor's CGL policy to ensure the construction project is covered before the work begins. If coverage is uncertain, the owner can request clarification from the insurance company or, alternatively, require the deletion of the endorsement before allowing the contractor to proceed with the work.

¹ Ann Rudd Hickman, *Construction Defect Crisis Produces Coverage-Restricting Endorsements*, Int'l Risk Mgmt Inst. (August 2003), at <http://www.irmi.com/expert/Articles/2003/Hickman08.aspx>.

² *Id.*

³ This information was obtained on June 13, 2006 in response to Open Records Request #53055 directed to the Texas Department of Insurance.

⁴ Kevin B. O'Reilly, *New Specialty Trades Program Looks to Exploit Market Opportunity*, Ins. J. (July 19, 2004), at <http://www.insurancejournal.com/magazines/west/2004/07/19/features/44736.htm>; see also Merriam Webster Online Dictionary available at <http://www.m-b.com> (defining "habitation" as "occupancy" or "residence").

⁵ Steven Davis, *Emerging Trends in Construction Insurance*, Construction Fin. Mgmt. Ass'n. (Nov. – Dec. 2005), at <http://www.cfma.org/pubs/docs/ND05-Davis.pdf>.

⁶ *Barnett v. Aetna Life Ins. Co.*, 723 S.W.2d 663, 666 (Tex. 1987).

⁷ *Id.*