IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF TENNESSEE
WESTERN DIVISION

STANDARD CONSTRUCTION CO. INC.,	)	
Plaintiff,	)	
v.	)	**No. 01-2006V**
MARYLAND CASUALTY COMPANY and NORTHERN INSURANCE COMPANY OF NEW YORK,	)	
Defendants.	)	

ORDER GRANTING IN PART PLAINTIFF'S MOTION FOR SUMMARY JUDGMENT AND DENYING DEFENDANTS' MOTION FOR SUMMARY JUDGMENT

This case involves the scope of coverage afforded under insurance policies - a comprehensive general liability (CGL) insurance policy issued to the plaintiff, Standard Construction Company, by defendant Maryland Casualty Company and an excess umbrella policy issued by defendant Northern Insurance Company. Standard brought this declaratory judgment and breach of contract action in federal court, seeking a determination that Maryland and Northern were obligated to defend Standard in a certain civil action, "the *Love* case," filed in state court against Standard and to indemnify Standard for any liability or loss sustained by Standard as a result of that civil lawsuit. Presently before the court are cross-motions for summary judgment filed by all the parties. The parties have consented to the trial of this matter

before the United States Magistrate Judge.

UNDISPUTED FACTS

The parties have agreed that the following facts are undisputed. Standard Construction Company is an asphalt paving contractor that performs governmental and private road construction and road widening jobs, among other work. (SOF 1-2). The defendant Maryland Casualty Company insured Standard from January 1, 1990 to January 1, 1993 under three successive one-year occurrence-based CGL policies. (SOF 3). The defendant Northern Insurance Company issued a series of three commercial umbrella policies to Standard effective during the same period. (SOF 9).

In March 1990, Standard entered into a contract with the state of Tennessee to perform paving and road work as part of a state road project to widen Highway 64 near Arlington, Tennessee from two lanes to five lanes. (SOF 12). Under the contract, Standard, as the general or prime contractor on the job, was responsible for "clearing and grubbing"[1] and "removal of structures and obstructions," collectively known in the industry as "dirt work," in accordance with specifications issued by the Tennessee Department of Transportation (TDOT). The TDOT specifications for clearing and grubbing required Standard to remove perishable

[1] **"Clearing" means taking down all the trees. "Grubbing" means removing the roots out of the ground.**

materials and debris and dispose of them at "locations off the project, outside the limits of view from the project during all seasons with the written permission of the property owner on whose property the materials and debris are . . . placed." (SOF 14). Similarly, the TDOT specification for removal of structures and debris required Standard to

> **raze, remove and dispose of all buildings and foundations, structures, fences, and other obstructions, any portions of which are on the rights of way . . . . All material [not designated to become the property of the Department] will become the property of the Contractor and shall be disposed of outside the limits of view from the project. If the material is disposed of on private property, the Contractor shall secure written permission from the property owner.**

(*Id.*) The TDOT specifications also included the following general provisions:

> **Section 104.11 - Final Cleanup. Before final acceptance of the Work . . . all waste areas, all areas and access roads used by the Contractor, in connection with the work, shall be cleaned of all . . . excess materials . . . rubbish, and waste, and all parts of the work shall be left in a neat and presentable condition . . . . All damage to private and public property shall be replaced, repaired, or settled for.**
>
> **Section 107.14 - Legal Responsibilities of the Contractor. In addition to specific legal responsibilities set forth . . . , the Contractor is charged with other broad legal responsibilities under these specifications. The responsibilities include but are not limited to . . . :**
>
> **(c) to conduct all operations so as to protect the members of the general public, residents near the project . . . this responsibility also extends to the protection**

of public and private property under all circumstances.

(SOF 15.) Standard hired Sammy Malloy to act as its project manager and/or superintendent. (SOF 17).

Standard subcontracted the dirt work to Ronald S. Terry Construction Company, and Terry provided a performance bond for its portion of the work. (SOF 18). In the fall of 1990, Gene A. Bobo, the superintendent for Terry, obtained the written permission of the owners of the property adjacent to Highway 64 "to dump construction debris" on their adjoining properties in order to dispose of the debris and material removed as part of the dirt work. (SOF 22). Bobo obtained the signatures of five landowners - Joseph Randolph, Louis A. Bryan, K. A. Holmes, Carolyn Fuller, and Ken Richardson - in September 1990, and a sixth landowner, M. A. Lightman, in August 1991. Bobo testified at his deposition that he also obtained the written permission of Casella Love to dump construction debris on her property at about the same time he secured the written permission of the other landowners but that he was unable to locate a copy of a 1990 or 1991 written letter agreement signed by Ms. Love. (Bobo Dep. P.10, SOF Ex. 22). At that time, Ms. Love was ninety years old. Ms. Love's property was the only property along this stretch of Highway 64 that was zoned commercial.

Believing that it had Ms. Love's written permission, Terry deposited construction debris, including trees, corrugated metal pipe, concrete chunks with exposed steel, and asphalt, on Ms. Love's property. (SOF 26-27). At that time, Ms. Love's property was the subject of a condemnation suit initiated against her by the state for the widening of Highway 64. William H. Fisher, the attorney representing Ms. Love's interest in the condemnation proceedings, retained an engineer to inspect the Love property. (SOF 28). The engineer reported that the waste material deposited on the land consisted of fallen trees, corrugated metal piping, large chunks of concrete with exposed reinforcing steel, broken asphalt, rubber tires and other deleterious materials not suitable for embankment construction for land development, covered by a thin layer of soil. After receiving the engineer's report, Mr. Fisher, by letter dated May 22, 1992, demanded that Standard cease dumping on Ms. Love's property, he revoked any authority which Standard may have had to do "fill" work on Ms. Love's property, and he requested Standard to remove the waste material and recompact the fill. (SOF 30). The letter also pointed out that Ms. Love was suffering from senile dementia and her ability to enter a binding contract was questionable. (*Id.*)

Upon receiving the letter, Standard contacted Malloy, its project manager, to make sure that Ms. Love had signed an agreement

permitting Standard to dump debris on her property. (SOF 32). When Standard could not locate the agreement, Bobo, the Terry supervisor, obtained Ms. Love's signature on another letter agreement. (Bobo Dep. p. 19, SOF Ex. 23). This agreement was dated June 17, 1992. Interlineated on the agreement was the following: "Agree to asp. driveway and dump 2 loads of dirt in front yard." Neither Terry nor Standard removed any construction debris from Ms. Love's property at this point in time, but Standard did in fact pave Ms. Love's driveway. In addition, Standard, through Terry, spread additional dirt on and leveled off the portion of Ms. Love's land on which the debris had been dumped. Standard accepted the work of its subcontractor Terry in October or early November 1992, paid Terry in full and released Terry's performance bond. (SOF 34).

Nearly two years later, on November 22, 1994, Ms. Love, by and through her daughter Louise Poole as next friend, commenced a lawsuit against Standard, Terry, Bobo, and the state of Tennessee in Tennessee state court in which she asserted various claims for damage to her real property arising out of Standard's and Terry's work on the Highway 64 project. The complaint included three separate counts. (SOF 36). In Count I, Ms. Love pled alternative theories of trespass and breach of the disposal contract between Terry and Ms. Love. In Count II, Ms. Love alleged that the

defendants violated the Tennessee Solid Waste Disposal Act which violations were wilful and/or constituted negligence per se. Count III claimed a violation of the Tennessee Consumer Protection Act. The complaint sought damages for: (1) the costs to remove and dispose of the impure "waste" fill; (2) the costs of recompacting the dirt fill; (3) impairment in the value of her property: (4) exposure to civil nuisance liability; and (5) loss of use of her property. (SOF 37-39). The complaint also alleged that Ms. Love was ninety-two years old and at all times pertinent was *non compos mentis.*

Standard was served with the original complaint in the *Love* lawsuit on December 1, 1994, and tendered it to its insurance broker. (SOF 40). Following tender of the defense of the *Love* lawsuit to Maryland and Northern, Maryland and Northern by letter dated January 17, 1995, denied coverage on the basis of the pollution exclusion. On February 6, 1995, Maryland and Northern supplemented their earlier denial of coverage by adding several additional grounds, including absence of an occurrence and property damage as defined in the policy as well as the impaired property exclusion. (SOF 41).

Nearly three years later, in October of 1997, Ms. Love amended her complaint. (SOF 42). In her amended complaint, Ms. Love pled four counts. In Count I, entitled "Intentional Misconduct of the

Defendants," Ms. Love pled trespass, nuisance, and intentional tort causes of action. In Count II, styled " Breaches of Contract by the Defendants," Ms Love alleged that the defendants breached the construction contract with the state of Tennessee of which she claimed to be a third party beneficiary. Count III alleged that the defendants violated the Tennessee Solid Waste Disposal Act and regulations promulgated by the Tennessee Department of Environment and Conservation governing the disposal of solid waste which violations were wilful and/or constituted negligence per se. Count IV set forth a cause of action for simple and gross negligence. (SOF 43-46). The amended complaint alleged Ms. Love was ninety-five years old and *non compos mentis* at all pertinent times.

On November 16, 2000, approximately three years after the amended complaint was filed, Standard tendered it to Maryland and Northern along with a request that Maryland and Northern reconsider and reverse their earlier decision to deny coverage. (SOF 47-48). Shortly thereafter, Standard filed the present coverage action on January 5, 2001, to force its insurers to honor their alleged policy obligation to defend Standard in the *Love* action and pay any liability on behalf of Standard. (SOF 49).

Around the same time Standard tendered the amended complaint to its insurers, settlement discussions began among the parties to the *Love* action. (SOF 52). From November 2000 through April 2001,

Standard's attorneys kept Maryland apprised of the status of the negotiations. (SOF 53-56). The parties to the *Love* action then agreed to mediate their dispute, and at a mediation conducted by Wyeth Chandler on April 14, 2001, an agreement to settle the *Love* lawsuit was reached. The agreement was memorialized in a letter dated May 4, 2001. It provided that Ms. Love would receive a lump sum cash payment of $900,000 of which Standard would pay $200,000. It further provided that Standard and Terry would be "jointly obligated to remove the unsuitable fill from the Love property, dispose of it, replace it with suitable all dirt fill, and grade and recompact the fill to an agreed upon elevation." Terry agreed to perform the actual remediation work. According to the agreement, if Terry fails to perform the work in one year, Standard is obligated to do the work, but whoever performs the work will received a lien on Ms. Love's property for its actual costs up to $650,000 to be paid at the time of sale of the property. (SOF 57).

ANALYSIS

I. Legal Standard

A. Summary Judgment Standard

Under Rule 56(c) of the Federal Rules of Civil Procedure, summary judgment is proper "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any

material fact and that the moving party is entitled to a judgment as a matter of law." *LaPointe v. United Autoworkers Local 600*, 8 F.3d 376, 378 (6th Cir. 1993); *see also Osborn v. Ashland County Bd. of Alcohol, Drug Addiction and Mental Health Servs.*, 979 F.2d 1131, 1133 (6th Cir. 1992) (per curiam). The party moving for summary judgment has the burden of showing that there are no genuine issues of material fact at issue in the case. *LaPointe*, 8 F.3d at 378. This may be accomplished by demonstrating to the court that the nonmoving party lacks evidence to support an essential element of its case. *Barnhart v. Pickrel, Schaeffer & Ebeling Co.*, 12 F.3d 1382, 1389 (6th Cir. 1993).

In response, the nonmoving party must present "significant probative evidence" to demonstrate that "there is [more than] some metaphysical doubt as to the material facts." *Moore v. Phillip Morris Co.*, 8 F.3d 335, 339-40 (6th Cir. 1993). When a summary judgment motion has been properly made and supported, "an adverse party may not rest upon the mere allegations or denials of the adverse party's pleading, but . . . by affidavits or as otherwise provided in this rule, must set forth specific facts showing that there is a genuine issue for trial." Fed. R. Civ. P. 56(e). "[T]he mere existence of some alleged factual dispute between the parties will not defeat an otherwise properly supported motion for summary judgment; the requirement is that there be no genuine issue

of material fact." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 247-48 (1986).

In deciding a motion for summary judgment, "this court must determine whether 'the evidence presents a sufficient disagreement to require submission to a jury or whether it is so one-sided that one party must prevail as a matter of law.'" *Patton v. Bearden*, 8 F.3d 343, 346 (6th Cir. 1993) (quoting *Anderson*, 477 U.S. at 251-52). The evidence, all facts, and any inferences that permissibly may be drawn from the facts must be viewed in the light most favorable to the nonmoving party. *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986). However, "[t]he mere existence of a scintilla of evidence in support of the plaintiff's position will be insufficient; there must be evidence on which the jury could reasonably find for plaintiff." *Anderson*, 477 U.S. at 252.

B. Choice of Law

Because jurisdiction is based on diversity, the court, as a preliminary matter, must decide which state's substantive law applies. To determine which law applies, this court applies the choice of law rules of the forum state. In insurance coverage cases, Tennessee courts apply the substantive law of the state in which the insurance policy was issued and delivered if there is no choice of law clause in the policy. *Standard Fire Ins. Co. v.*

***Chester-O'Donley & Assocs., Inc.*, 972 S.W.2d 1 (Tenn. App. 1998)(citing *Ohio Cas. Ins. Co. v. Travelers Indem. Co.*, 493 S.W.2d 465, 467 (Tenn. 1973)). Neither side has pointed to any choice of law clause in the policy and the court assumes the policies were delivered in Tennessee. In the absence of any information to the contrary, the court will apply the substantive law of Tennessee.**

C. <u>The Insurer's Duty to Defend</u>

Issues as to scope of coverage and insurer's duty to defend are legal rather than factual issues. *Chester-O'Donley*, 972 S.W.2d at 5-6 (citing *Pile v. Carpenter*, 99 S.W. 360, 362 (Tenn. 1907)). As such, they are appropriate for resolution by summary judgment if the relevant facts are not in dispute. *Id.* (citing *St. Paul Fire & Marine Ins. Co. v. Torpoco*, 879 S.W.2d 831, 834 (Tenn. 1994).

<u>_____</u>The duty to defend is broader than duty to indemnify. *Drexel Chem. Co. v. Bituminous Ins. Co.*, 933 S.W.2d 471, 480 (Tenn. App. 1996). It logically follows therefore that if there is no duty to defend, there is no duty to indemnify. An insurer's duty to defend is determined by comparing the allegations of the complaint filed against the insured with the terms of the insurance policy. *Id.* at 480. If any one claim can possibly or potentially be covered, there is a duty to defend, regardless if other claims may be excluded by the policy. *Id.* The test for determining the duty to defend is "based exclusively on the facts as alleged rather than on

the facts as they actually are . . . ." *Id*. Once a duty to defend is triggered, it continues "until the facts and the law establish that the claimed loss is not covered." *Chester-O'Donley,* 972 S.W.2d at 11 (citing *James Graham Brown Found., Inc. v. St. Paul Fire & Marine Ins. Co.*, 814 S.W.2d 273, 279 (Ky. 1991)).

II. <u>The Insuring Agreement</u>

The insuring agreement establishes the outer limits of an insurer's contractual liability. *Chester O'Donley*, 972 S.W.2d at 7. Exclusions in the policy decrease coverage once coverage is found. *Id.* "If coverage cannot be found in the insuring agreement, it will not be found elsewhere in the policy." *Id.* Thus, in analyzing coverage disputes, the starting point is the insuring agreement.

The insuring agreement in Maryland's policy[2] uses the standard ISO language for CGL policies as amended in 1986. It provides:

> **We will pay those sums that the insured becomes legally obligated to pay as damages because of "bodily injury" or "property damage" to which this insurance applies . . . This insurance applies only to "bodily injury" and "property damage" which occurs during the policy period. The "bodily injury" or "property damage" must be caused by "an occurrence." The "occurrence" must take place in the "coverage territory."**

There is no dispute that Ms. Love's claim arose during the policy period and is within the coverage territory. As concerns the

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[2] **Because Northern's excess policies follow form, the court will analyze these issues only under Maryland's policies.**

insuring agreement, the issues then are whether there was an "occurrence" which caused "property damage" as both those terms are defined in the policy.

A. <u>Was there an "occurrence"?</u>

The CGL policy defines an "occurrence" as an "accident" including "continuous or repeated exposure to substantially the same general harmful conditions." "Accident" is not defined in the policy. Courts have construed the term "accident" broadly to encompass "not only 'accidental events,' but also injuries or damage neither expected nor intended from the standpoint of the insured." *State Farm & Cas. Co. v. CTC Development Corp.*, 720 So. 2d 1072, 1076 (1998). In other words, "if the resulting damages are unintended, the resulting damage is 'accidental even though the original acts were intentional.'" *Id.* at 1075 (citing John Alan Appleman & Walter F. Berdal, *Insurance law and Practice § 4492.02*, at 33 (rev. ed. 1979)). "Coverage under this definition would be provided not only for an accidental event, but also for the unexpected injury or damage resulting from the insured's intentional actions." *Id. See also Hartford Cas. Co. v. Cruse*, 938 F.2d 601, 605 (5th Cir. 1991)(holding that an occurrence within the meaning of a CGL policy takes place where the resulting injury or damage was unexpected and unintended, regardless of whether the insured's acts were intentional).

The *CTC* case from Florida is factually similar to the present case. In *CTC*, a builder sued its liability insurer to recover damages for breach of its contractual duty to defend and indemnify after the builder settled claims arising out of his mistaken construction of a residence beyond the setback lines on the side of the property. *CTC,* 720 So. 2d at 1073. When the construction was approximately 60% complete, the neighboring property owners filed suit against the builder and the homeowner for the encroachment. *Id.* at 1073. The builder tendered the defense of the lawsuit to his insurer, State Farm, who denied coverage and refused to defend. The builder settled with the neighbors then brought a coverage suit against his insurer. After adopting the definition of accident set forth above, the Supreme Court of Florida determined as a matter of law that the builder did not expect or intend damages to result from his actions of building the house where he did. *Id.* at 1076. The builder mistakenly believed that he had received a variance from the setback line; thus his actions were accidental, and coverage existed under the policy for the "occurrence."

This definition of occurrence adopted by the Florida Supreme Court in *CTC* is consistent with the Tennessee Supreme Court's treatment of the exclusion in liability insurance policies for

property damage "expected and intended" by the insured.[3] In *Tennessee Farmers Mut. Ins. Co. v. Evans*, 814 S.W.2d 49 (Tenn. 1991), the Tennessee Supreme Court held that for the intended and expected acts exclusion to apply, "it must be established that the insured intended the act *and also* intended or expected that injury would result." *Id.* at 55 (emphasis added).

> These are separate and distinct inquiries because many intentional acts produce unexpected results and comprehensive liability insurance would be somewhat pointless if protection were precluded if, for example, the intent to cause harm was not an essential (and required) showing. See 7A J. Appleman, *Insurance Law and Practice* § 4501.09 at 263 ((1979).

Id. While exclusions cannot grant coverage, the exclusions must be construed *in para mutua* with the insuring agreement to determine the coverage under the policy.

Here, Terry and Bobo believed up to May 22, 1992, the date of Mr. Fisher's letter, that they had the permission of Ms. Love to dump construction debris on her property. Indeed, they believed that she had given her written permission. At no point did any of the defendants intend to cause harm to Ms. Love's property. There

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[3] Before 1985, the words "neither expected nor intended" were included in the definition of occurrence. In 1985, the Insurance Services Office (ISO), the organization responsible for drafting policy in the insurance industry, moved this language out of the insuring agreement into the exclusion section. *See* Emily Poulad Grotell, *Understanding the Basics of Commercial General Liability Policies*, in INSURANCE LAW; UNDERSTANDING THE ABCS 2001, Pub. L. Inst. Order No. H0-00AW, *71 (New York City, April 23-24, 2001).

is no evidence whatsoever that any of the defendants knew that Ms. Love's property was zoned commercial and that the construction debris would therefore impair the value of her property for future use as commercial property by rendering it unsuitable for commercial improvement.

Terry either breached a contract with Ms. Love or committed trespass. If Terry did not have permission to come upon Ms. Love's property and dump construction debris as he believed he did, then he would have committed trespass. The trespass, however, would have been the result of a mistake or misunderstanding between Ms. Love and Terry. Based on the foregoing analysis, the court finds as a matter of law that Terry's alleged trespass is an "occurrence" as defined under the policy for which the insurer would owe coverage provided property damage resulted.

B. <u>Was there "property damage"?</u>

The second prong of the inquiry under the insuring agreement is whether the "occurrence" caused "property damage." "Property damage" is defined in the policy as:

> **(a) Physical injury to tangible property, including all resulting loss of use of the property; or**
> **(b) Loss of use of tangible property that is not physically injured.**

Maryland and Northern insist that the damages to Ms. Love's property consisted only of faulty workmanship and economic loss, neither of which constitute property damage under the policy.

Relying on *Vernon Williams & Son Constr., Inc., v. Continental Ins. Co.*, 591 S.W.2d 760, 763 (Tenn. 1979) and *Standard Fire Ins. Co. v. Chester-O'Donley & Assocs., Inc.*, 972 S.W.2d 1 (Tenn. App. 1998), Maryland and Northern point out that "a claim limited to remedying faulty workmanship or materials does not constitute injury to or destruction of tangible property." *Id.*

In *Vernon*, a construction contractor, Vernon Williams and Sons Construction Company, filed a coverage lawsuit against its insurer, Continental Insurance Company, for failure to defend Williams in a prior lawsuit. *Vernon*, 591 S.W.2d at 761. In the prior lawsuit, Williams was sued by Mitchell Steel Company for failure to perform its construction contract for an addition to Mitchell's warehouse in a workmanlike manner. Mitchell alleged breach of contract and faulty workmanship for improper design of the concrete work and insufficient warehouse slabs, among other things. In the earlier lawsuit, the trial court ruled in favor of Mitchell, finding that Williams Company had breached its contract causing the south wall and portions of the floor to crack and rendering the building unusable. *Id.* In the coverage lawsuit, the Tennessee Supreme Court, ruling in favor of the insurance company, held that "the standard comprehensive general liability policy does not provide coverage to an insured for a breach of contract action grounded upon faulty workmanship of materials, where the damages claimed are

the cost of correcting the work itself." *Id.* at 765. Quoting extensively from *Weedo v. Stone-E-Brick, Inc.*, 155 N.J. 233, 405 A.2d 788 (1979), the court pointed out that the "risk intended to be insured by a comprehensive general liability policy is faulty workmanship and material which cause a tort liability to persons other than those to whom contractual obligation of workmanlike performance is due." *Id.* at 763. "The coverage is for tort liability for physical damages to others and not for contractual liability of the insured for economic loss because the product or completed work is not that for which the damaged person bargained." *Id.* at 764.

Similarly, *Chester-O'Donley* involved a lawsuit by a builder, Highland Rim Constructors, Inc., who had subcontracted out to Chester-O'Donley the mechanical portion of a construction contract with the state for a new music building on Austin Peay's campus in Clarksville, Tennessee. *Chester-O'Donley*, 972 S.W.2d at 4. Chester-O'Donley in turn subcontracted out the installation of ductwork for the heating, ventilation and air condition system to H & R Mechanical Specialities, Inc. After the new music building was completed and occupied, problems developed with the heating and air conditioning system. *Id.* It was determined that the problems were caused by defects in the ductwork. To correct the problem, it was necessary to remove the HVAC system. In doing so, there was

some indication that there was inconsequential damage to the walls and ceilings.

Highland Rim sued Chester-O'Donley alleging defective work, and sought recovery for the liquidated damages it was required to pay to the State, the additional damages for delay, and damages to its business reputation, as well as the damages to replace the system. Chester-O'Donley called upon its insurer, Standard Fire, to defend, and Standard Fire refused. *Id.* After carefully analyzing the applicable policy provisions, the court of appeals held that because these were economic losses stemming from Chester O'Donley's breach of contract which did not involve physical injury to tangible property other than Chester-O'Donley's work, the policy did not cover the damages sought by Highland Rim, with one exception. *Id.* at 12. Any damage to the walls and ceiling was covered because that was not part of Chester-O'Donley's work and therefore was not excluded by the impaired property exclusion. *Id.*

Maryland and Northern also rely heavily on the fact that there was no physical damage Ms. Love's property. They base this assertion on the deposition testimony of Cliff Hunt who said that the problems caused to Ms. Love's property could be corrected by merely removing the construction debris and replacing it with dirt fill.

Maryland and Northern's reliance on *Vernon* and *Chester-*

O'Donley **is somewhat misplaced. Neither is exactly on point. Both** ***Vernon*** **and** ***Chester-O'Donley*** **arose out of claims against an insured builder by a dissatisfied customer or property owner who had contracted with an insured builder. In both cases, the customers or property owsner suffered damages because the work performed by the contractor was not of the quality for which they had bargained.**

In the present case, if Terry had a contract with Ms. Love to dump "fill" on her property, then the Love property would be considered "the work" bargained for in the Terry/Love contract. In that event, the damage would not be covered under the CGL policy issued by Maryland and Northern because it would have been the result of a breach of contract due to faulty workmanship. On the other hand, if Terry did not have a contract with Ms. Love, then any faulty work on her property would not be considered part of Terry's work required by a contract, but would instead be the result of tort liability.

Maryland and Northern argue, however, that the court should consider the work performed on Love's property to be contractually bargained for under Standard's contract with the state of Tennessee. Under this theory, Maryland and Northern insist that Ms. Love is a third-party beneficiary of the Standard/state of Tennessee contract and the ***Love*** **lawsuit is merely a breach of contract claim.**

This argument, however, stretches the concept of third-party beneficiary too far. Tennessee law recognizes two kinds of third-party beneficiaries - intended and incidental. *Davidson & Jones Development Co.v. Elmore Development Co., Inc.*, 921 F.2d 1343, 1356 (6th Cir. 1991). An intended third party beneficiary exists only when 1) there is a valid contract between the principal parties and 2) the "clear intent of the contract is to benefit [the alleged third-party beneficiary]." *United American Bank v. Gardner*, 706 S.W.2d 639, 641 (Tenn. Ct. App. 1985). Only an intended, not an incidental, beneficiary may maintain a claim for breach of contract. *Moore Const. Co., Inc. v. Clarksville Dept. of Elec.*, 707 S.W.2d 1 (Tenn. Ct. App. 1985). There is a presumption that a contract is executed solely for the benefit of the parties to the contract. *Id.* at 9.

In the contract between the state of Tennessee and Standard, the clear intent of the contract is to expand Highway 64. The State's main objective was removal of debris and widening the highway. To protect itself from tort liability to third persons, the State included a provision in the contract requiring Standard to the obtain written permission of surrounding landowners to dispose of construction debris on private property:

> **201.04 - Disposal of Debris . . . may be removed . . . and disposed of . . . with the written permission of the property owner on whose property the materials are to be placed.**

> **The Contractor [Standard] shall make all necessary arrangements with property owners for obtaining suitable disposal locations. . . .**

(Def.'s Mem. of Law in Supp. of its Mot. for Sum. Judg., p.7.) Plainly, the provision was intended to protect the State from third-party tort liability; there is no indication in the State/Standard contract that it was intended to benefit Ms. Love by protecting her property from harm or that the State owed Ms. Love a duty to protect her property. Ms. Love was therefore not an intended third-party beneficiary to the State/Standard contract, and the damage to her property is not economic loss resulting from poor performance by a party to a contract intended to benefit her or with whom she had a contract.

As a result of Standard's conduct through Terry, Ms. Love suffered a loss of use of her property and the damage, whether contractual or tortious in nature, is the same. The original and amended complaints in the *Love* case alleged alternative theories of both trespass and breach of contract. Because the *Love* case was settled, there was never a determination of whether Standard breached a contract or committed trespass. If there was no contract between Ms. Love and Standard then there was "property damage," as defined in the insurance policy, and because the court has determined that there was an "occurrence" as defined in the policy, there is potential coverage for the claims alleged in the

original and amended *Love* complaints. In sum, Maryland and Northern had a duty to defend Standard unless an exclusion to coverage applies.

III. Do Any Exclusions Apply?

Having determined that the *Love* claim potentially falls within the parameters of the insuring agreement, the court must next consider whether any exclusions limit the scope of coverage or exclude coverage. The burden is on the insurer to establish an exclusion applies. *Chester-O'Donley*, 972 S.W.2d at 8. Maryland and Northern rely primarily on two exclusions to bar coverage - the impaired property exclusion (2m) and the business risk exclusion (2j5).

A. Exclusion 2m - Impaired Property Exclusion

The impaired property exclusion states as follows:

> **Coverage does not apply to "Property Damage" to "impaired property" arising out of: (1) A defect, deficiency, inadequacy or dangerous condition in . . . "your work" or (2) A delay or failure by you or anyone acting on your behalf to perform a contract or agreement in accordance with its terms.**

(Def.'s Mem. in Supp. of its Mot. for Sum. Judg., p. 32.) The impaired property exclusion is a business risk exclusion. The exclusion makes certain that the policy operates to insure against damages to third parties rather than the risk of faulty workmanship by a party to the contract. *Chester-O'Donley*, 972 S.W.2d at 7.

The nature of the relationship between Ms. Love and Standard is crucial to determining the applicability of the exclusion. If, as discussed previously, there was no contract between Ms. Love and Standard and/or Terry when Terry dumped construction debris on Ms. Love's property, then any damage that occurred to Ms. Love's property was not Standard's contractually bargained-for work, i.e. "your work," as defined in the policy, and part (1) of the exclusion would not apply. If, on the other hand, there was a binding contract with Ms. Love when the construction debris was deposited on Ms. Love's property, then Standard's actions would be considered "your work," causing the exclusion to be triggered. In that event, there would be no coverage. As previously determined, based on the facts alleged in the original and amended complaints, there is potentially a trespass claim which would be covered under the policy. Because there is a potential that no contract existed and thus Standard's actions were trespass as alleged in the complaints, the impaired property exclusion does not apply to preclude a defense obligation.

B. <u>Exclusion 2j(5)</u>

This exclusion provides that property damage to the following will not be covered:

> **That particular part of real property on which you or any contractors or subcontractors working directly or indirectly on your behalf are performing operations, if the "property**

damage" arises out of those operations.

Exclusion j(5) is also a business risk exclusion. Its purpose is to exclude liability under the policy for damages caused to the particular piece of property upon which the insured was hired to perform work or operations.

In support of their respective positions, both parties cite to *Vinsant v. Elec. Contractors, Inc. v. Aetna Cas. & Sur. Co.*, 530 S.W.2d 76 (Tenn. 1975), as one example of relevant precedent. In *Vinsant*, a contractor was hired to install circuit breakers on a switchboard in a shopping mall. One of its employees dropped a wrench, causing a short-out of the entire switchboard. The contract between the parties contained the same j(5) "business risk" exclusion as in the present case. The insurance company denied coverage, as the employee was "performing operations" within the confines of the agreement. The Supreme Court of Tennessee agreed and affirmed the holding of the Court of Appeals, stating that the switchboard was a "single, self-contained item of property." *Id*. at 77.

Similarly, in an unpublished Sixth Circuit opinion cited by Maryland and Northern, a contractor was hired to install a water pumping station which required blasting out a hole in a rock. *Haren Constr. Co. v. Continental Ins. Co.*, 2000 U.S. App. LEXIS 28061 (6th Cir. 2000). Too much rock was blasted out, and

consequently the hole created was too large, causing damage to third parties' property. The contract between the parties also contained the j(5) exclusion, and the insurance company denied coverage based on this fact. The Sixth Circuit affirmed, stating that the property to be worked on in the contract was one piece of property, a "homogenous rock mass," and the claim was excluded under the policy by the j(5) exclusion. *Haren*, 2000 U.S. App. LEXIS 28061 at *6.

These cases do little to augment Maryland and Northern's position that the j(5) exclusion applies in Ms. Love's situation. Both *Vinsant* and *Haren* involve damage to property that was covered in the contract as the property upon which "performing operations" were to occur. The reason the exclusion applied in both cases involved the homogenous nature of the property upon which the work was performed.

In the present case, the contract between the State and Standard involved the widening of Highway 64 and the removal of waste and excess dirt at the project site. The contract provided specifically that additional agreements had to be reached with landowners to dispose of the excess debris. The contract between Standard and the State did not require Standard to perform any work on Ms. Love's property in connection with the expansion of the highway. Rather, work on Ms. Love's property was an additional

duty or task that Standard was to undertake through additional contracts with adjacent landowners. Nor was Ms. Love's property one unified, homogenous piece of property with the highway as were the properties at issue in *Vinsant* and *Haren*.

Only if Standard had contracted directly with Ms. Love would the j(5) exclusion be triggered. Here, it is uncertain whether a contract existed which gave Standard the right to dump the road debris onto Ms. Love's property. Because the original and amended complaints allege that Ms. Love was incapable of entering a binding contract, there is a very strong potential that no contract existed, and therefore exclusion j(5) would not apply. *See Glens Falls Ins. Co. v. Donmac Golf Shaping Co.*, 417 S.E.2d 197 (Ga. App. 1992)(holding exclusion j(5) did not bar coverage for the insured's negligent construction of a golf course on federally protected wetlands, as the damage caused went beyond the scope of the contract and hence was no longer excluded as a "business risk"). Because the potential exists for coverage under the policy, the duty to defend is triggered.

In summary, there are claims alleged in the original and amended complaints that fall "potentially within" coverage of the policy, and no exclusion operates to conclusively bar coverage. Maryland and Northern therefore had a duty to defend Standard, and the duty continued until it was conclusively established that there

was no potential for recovery under the policy. As the *Love* claim was settled before trial, it is still unclear whether there was tort or contractual liability on the part of Standard; thus, the duty to defend did not end. As such, Maryland and Northern's motion for summary judgment as to the duty to defend is denied, and Standard's motion as to the duty to defend is granted.

IV. <u>The Duty to Indemnify</u>

To determine whether there is a duty to indemnify, the true facts, rather than the facts as they are alleged in the complaint, must be ascertained. *St. Paul Fire & Marine*, 879 S.W.2d at 834-35. (quoting *American Policyholders' Ins. Co. v. Cumberland Cold Storage Co.*, 373 A.2d 247 (Me. 1977)). In other words, an insurer's duty to indemnify is established after determining the true facts of the case. Here, whether a contract existed between Ms. Love and Standard through Terry must be determined in order to decide whether Maryland and Northern have a duty to indemnify. The existence of a contract is crucial. As stated earlier, the Love case settled before it was ever determined if Ms. Love and Standard entered into a binding contract. Given Ms. Love's questionable mental capacity to enter into a contract at all times pertinent, this court cannot determine as a matter of law whether a contract existed and whether the business risk exclusions then apply to bar coverage. Plus, if there is a binding agreement between Ms. Love

and Standard, there is a question of fact as to whether any harmful dumping occurred on Ms. Love's property after she allegedly granted written permission to deposit debris on her property or whether the dumping occurred prior to the time she granted permission. The duty to indemnify, therefore, presents genuine issues of material fact and cannot be decided on a motion for summary judgment. *St. Paul Fire & Marine*, 879 S.W.2d at 834-35. Thus, Standard's motion for summary judgment on the indemnification issue and Maryland and Northern's motion for summary judgment on the indemnification issue are denied.

V. <u>Did Standard Give Timely Notice?</u>

Lastly, Maryland argues that Standard's failure to give timely notice voids coverage. Maryland insists that it should have been put on notice of a possible claim when Standard first received Ms. Love's attorney's letter of May 22, 1992, demanding that Standard cease dumping fill on her land. To its credit, Terry looked for a contract to ascertain Ms. Love's consent for the dumping. After it could not locate the contract, Terry had Ms. Love sign another contract on June 17, 1992, allowing them to dump two more loads of fill in her yard and asphalting her driveway in return. Nevertheless, Standard did not notify its insurers at this time. Standard waited until Ms. Love filed her complaint, two and a half years after the demand letter was mailed, to advise Maryland and

Northern's insurance brokers of the situation. Maryland argues that it was prejudiced by Standard's two-year delay in notifying it regarding the Love situation.

According to Tennessee law, the insurer must be prejudiced by the delay to claim untimely notice under the policy and deny coverage. *Alcazar v. Hayes*, 982 S.W.2d 845, 856 (Tenn. 1998). If an insured has breached the notice provision, a rebuttable presumption is established that the lack of timely notice prejudiced the insurer. *Alcazar*, 982 S.W.2d at 856; *American Justice Ins. Reciprocal v. Hutchison*, 15 S.W.3d 811, 813 (Tenn. 2000). Summary judgment may be appropriate to determine whether the insurer was prejudiced by the delay. *Alcazar*, 982 S.W.2d at 856.

In response, Standard argues that Maryland was put on notice immediately upon Standard being served with the complaint, and Maryland chose shortly thereafter to deny coverage. Subsequently, Ms. Love did not amend the complaint for two years. All other witnesses to the claim were and still are available, aside from Ms. Love herself, who died a few years ago. At the time of the lawsuit, however, and for an undetermined period prior to the lawsuit, Ms. Love was allegedly *non compos mentis.* The original complaint was filed in state court by her daughter Louis Poole, then later amended and filed by conservator Ed Milliken. Based on

Ms. Love's mental state, her testimony likely would have been unhelpful to the case.

Further, discovery was taken in the *Love* case which preserved testimony and memory. Pictures of Ms. Love's property were taken in February of 1992, long before the original complaint was filed and before Ms. Love's attorney sent the demand letter to Standard and Terry. (Std. Dep., pp. 43-44, Ex. 5). During settlement negotiations, Maryland was made aware of the status of the situation and could have participated in settlement negotiations but chose not to do so.

Based on the above facts, this court determines that Standard has rebutted the presumption that prejudice resulted from its notice in December of 1994 to its insurers. The issue of timeliness of the notice, therefore, shall not serve to bar coverage in this matter.

CONCLUSION

For the reasons set forth above, summary judgment is granted in favor of Standard on Maryland and Northern's duty to defend but denied as to indemnity. Summary judgment is denied as to Maryland and Northern on both the issues of duty to defend and duty to indemnify.

IT IS SO ORDERED May 15, 2002.

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DIANE K. VESCOVO

UNITED STATES MAGISTRATE JUDGE