Case Alert

May 2019

Construction Defect Dispute Governed by Contract Disputes Act not yet Suited to being a "Suit"

The Southern District of California recently held that a series of demands for a general contractor to investigate and repair several construction defects at a U.S. Army facility did not constitute a "suit" within the meaning of the general contractor's commercial general liability ("CGL") policy.

In *Harper Construction Co., Inc. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.,* the U.S. Government hired Harper Construction Company ("Harper") to construct a U.S. Army training facility for the Patriot Missile System in Fort Sill, Oklahoma. No. 18-cv-00471-BAS-NLS (S.D. Cal. Mar. 28, 2019). During the project, Harper hired Harper Mechanical Contractors ("Harper Mechanical"), an independent company, as a subcontractor "to perform demolition, grading, and other work at the Project."

After Harper completed the project, the government informed Harper of property damage at the project, "including, but not limited to, gypsum wallboard cracks and binding doors." Harper attempted to repair the issues, but the problems continued. The issues were apparently the result of Harper Mechanical's grading work.

Subsequently, the government sent two letters requesting an investigation and asking Harper to "propose a plan to correct the issues." As Harper undertook an investigation spanning multiple years, the government became increasingly frustrated with the delays. The government threatened to initiate "formal administrative recourse" and to demolish the project, forcing Harper to re-build from the ground up. It also sent Harper another letter requesting Harper submit a formal proposal to correct the issues.

Harper's general liability carrier was National Union Fire Insurance Company of Pittsburgh, PA ("National Union"). Harper Mechanical was listed as an additional insured on Harper's policy. Four years after the government's first notification to Harper of the issues with the project, Harper's broker submitted a claim to National Union. The broker noted that Harper was seeking additional insured coverage for Harper Mechanical under Harper's own policy for investigation and repair costs resulting from Harper Mechanical's work.

National Union issued a reservation of rights letter and sought more information from Harper. The parties corresponded for the next year and half, until National Union issued a denial letter indicating that there was not a "suit" against Harper seeking damages because of "property damage," based on the policy's definition of "suit."

The policy contained the standard ISO CGL definition of "suit," which is defined, in pertinent part, as "a civil proceeding in which damages because of … 'property damage' to which this insurance applies are alleged. 'Suit' includes: … b. Any other alternative dispute resolution proceeding in which such damages are claimed and to which the insured submits with our consent."

Harper sued National Union. National Union moved for summary judgment. In opposition, Harper argued that the government's demand constituted a "suit" because the demand falls within the Contract Disputes Act ("CDA"), which includes administrative and court proceedings and qualifies as "any other alternative dispute resolution proceeding" under the policy definition. The CDA applies to "contracts made by an executive agency for, among other things, the procurement of construction … of real property."

The court acknowledged that the CDA applied to the contract, given the Army's status as an executive agency. However, the CDA does not automatically consider all disputes to constitute a "claim." A dispute does not become a "claim" unless one of the contracting parties issues a "[w]ritten demand or written assertion … seeking … the payment of money in a sum certain," at which point "each claim by the Federal Government against a contractor relating to a contract shall be the subject of a written decision by the contracting officer." Without the claim being "submitted for a written decision by the contracting officer, which is the first step in the dispute resolution process under the CDA," the court determined that there was "no evidence that Harper was faced with a "civil proceeding in which damages … are alleged" or "any other alternative dispute resolution proceeding," as required by the policy's definition of "suit." The court also noted that there was no evidence that National Union had consented to any of the processes involved in the dispute, which is a further requirement of the definition of "suit."

The court granted summary judgment for National Union based on the conclusion that the CDA demands did not constitute a "suit." This case is an unfortunate example of what can happen when a contractor does not consider coverage when making strategic decisions throughout the process of investigating and repairing construction defects. The result could potentially have been favorable for Harper had it notified National Union early (and often) of the issues, involved coverage counsel to work with its defense and/or general counsel to strategize about how to cast the proceedings as a "suit" under the CDA, and followed the proper channels under the CDA to solidify its position that the parties were involved in ADR proceedings under existing California law.

For more information contact William Bennett at 951.365.3148 or wsb@sdvlaw.com.