Case Alert

Oregon Supreme Court Confirms Broad Duty to Defend

The Supreme Court of Oregon issued a decision at the end of last year which perfectly illustrates the lengths to which a court may go to grant a contractor's claim for defense from its insurer in a construction defect suit. In *West Hills Development Co. v. Chartis Claims, Inc.,1* the Court held that a subcontractor's insurer had a duty to defend a general contractor as an additional insured because the allegations of a homeowner's association's complaint could be interpreted to fall within the ambit of coverage provided under the policy—despite the fact that the policy only provided ongoing operations coverage, and despite the fact that the subcontractor was never mentioned in the complaint. The decision is favorable to policyholders but also provides an important lesson: that contractors may avoid additional insured disputes if those contractors have solid contractual insurance requirements for both ongoing and completed operations risks.

An insurer's duty to defend is typically determined by the allegations of a complaint as compared with the language of the policy. This principle is often referred to as the "four-corners rule" in reference to the four corners of the paper the policy is written on. Some states have relaxed this rule and allow parties to introduce "extrinsic evidence"—that is, facts which are not set forth in the complaint—to establish the duty to defend.[2] Oregon, however, has consistently followed the "four-corners rule,"[3] with one notable exception: a party claiming additional insured status may introduce extrinsic evidence to prove that they are an insured on the policy.[4] In *West Hills*, the Court reiterated Oregon's stance on these issues.

West Hills Development Company ("West Hills") was a general contractor for a townhouse development in Oregon. West Hills contracted with L&T Enterprises ("L&T") as subcontractor and required that L&T obtain insurance coverage naming West Hills as an additional insured. L&T's commercial general liability policy with Oregon Automobile Insurance Company ("Oregon Auto") named West Hills as an additional insured on a standard additional insured endorsement, which insured West Hills "only with respect to liability arising out of [L&T's] ongoing operations performed for [West Hills]." There was no contractual requirement that L&T provide completed operations additional insured coverage for West Hills, nor did the Oregon Auto policy include such coverage.

Following the completion of the project, the development's homeowner's association sued West Hills for construction defects. According to the complaint, West Hills' subcontractors had negligently used improper means and methods in their construction work that resulted in defects. The association also alleged that West Hills was liable for negligence in hiring, supervising, and failing to oversee and inspect the subcontractors and their work. The Court noted that the "complaint contained very little information regarding the time when the damages allegedly occurred," although the complaint did allege that the defects already existed and had started to cause damage when the owners purchased their townhomes. Moreover, as is often the case in suits brought by project owners, the complaint did not specifically identify the allegedly negligent subcontractors by name.

West Hills tendered a claim for additional insured coverage to Oregon Auto. Oregon Auto refused to defend West Hills, arguing that: (1) the homeowner's association only alleged claims against West Hills as general contractor, not the named insured, L&T, and; (2) the claims did not arise from covered ongoing operations. Before the Oregon Supreme Court, Oregon Auto argued that the duty to defend could not be triggered merely because a complaint failed to "rule out" the possibility of coverage. Instead, it asserted that the duty to defend arises only when the complaint explicitly articulates a covered claim.

The Court rejected Oregon Auto's argument and confirmed that the legal standard was whether the allegations in the complaint, reasonably interpreted, could result in liability for an incident or injury that was covered under the four corners of the policy, regardless of any ambiguity or lack of clarity in the complaint. Specifically, the Court found that the complaint alleged claims against West Hills from which West Hills may incur liability that could be reasonably interpreted to "aris[e] out of [L&T's] ongoing operations performed for [West Hills]," as required under the additional insured endorsement. The complaint alleged that West Hills' subcontractors had used "improper construction means and methods" and that West Hills was negligent in preventing them from doing so. Thus, although L&T was not specifically named in the complaint, the Court held that the complaint could reasonably be interpreted as alleging liability for conduct covered by the policy, i.e. L&T's operations for West Hills. The Court further stated that the complaint alleged damages that occurred by the time the owners purchased their homes, making it possible that the damages occurred during L&T's "ongoing operations." In light of this analysis, the Court ruled that Oregon Auto had a duty to defend West Hills.

Thus, the *West Hills* decision confirmed Oregon's broad duty to defend standard, a favorable outcome for policyholders. It is interesting to note, however, that the case might never have come about if West Hills had required that its subcontractors provide completed-operations additional insured coverage; if L&T had both ongoing and completed operations additional insured endorsements on its policy, then Oregon Auto's duty to defend West Hills would have likely been more obvious. Upstream and downstream parties alike must consider case law such as this when developing effective risk management plans suitably tailored to their needs, and should remember to require appropriate additional insured coverage for both ongoing and completed operations from their subcontractors.

For more information about this case contact Theresa Guertin at tag@sdvlaw.com or 203-287-2119, or Tiffany Casanova at tlc@sdvlaw.com or 203-287-2108

1. 360 Or. 650 (2016).
2. For a state-by-state breakdown on the use of extrinsic evidence in the determination of the duty to defend, see SDV Law, Extrinsic Evidence State by State Survey, http://www.sdvlaw.com/wp-content/uploads/2015/11/Extrinsic-Evidence-State-by-State-Survey.pdf.
3. Ledford v. Gutoski, 877 P.2d 80, 82 (Or. 1994); Insenhart v. Gen. Cas. Co., 377 P.2d 26, 28-29 (Or. 1962).
4. Fred Shearer & Sons, Inc. v. Gemini Ins. Co., 240 P.3d 67 (Or. 2010).