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# A Study in Denial

## Comment on *California Traditions, Inc. v. Claremont Liability Insurance Company*

In today's turbulent construction market, homes are often built as one type of unit and reclassified as another during construction. For example, many towers developed as condominiums at the height of the housing market were reclassified as apartments when home prices went south. Conversely, some developers find it easier to secure permits for apartment projects which they then "convert" to condominiums after construction. When faced with the question of whether a unit is an apartment, condominium, or town home, only a subcontractor's lawyer may know for sure.

This poses a problem in determining whether coverage exists for construction of a particular unit. Commercial general liability policies often exclude coverage for one type of multi-unit home, but not another. For example, certain policies may exclude coverage for condominiums, but not for apartments or even town homes. The California Court of Appeal recently addressed the issues:

- When is a single family home really a condominium?
- When is a policyholder's expectation of coverage truly reasonable?

In the recent case of *California Traditions, Inc. v. Claremont Liability Insurance Company* (2011) (citation D057154), the Court of Appeal considered the following facts in arriving at a decision addressing these issues. Claremont Liability Insurance Company ("Claremont") issued a comprehensive general liability policy to a framer, Ja-Con Systems, Inc. ("Ja-Con"). Ja-Con subcontracted with the developer, California Traditions, Inc. ("California Traditions"), to perform framing for thirty residential units within a housing development.

After California Traditions sold the homes, a homeowner sued California Traditions alleging construction defects. As expected, California Traditions cross-complained against the framer, Ja-Con. Ja-Con then tendered its defense and indemnity to its insurer, Claremont. However, the Claremont policy contained an exclusion for the construction of multi-unit developments, specifically condominiums or town homes. Accordingly, Claremont denied coverage to Ja-Con under the exclusion. Without a defense, Ja-Con allowed California Traditions to take a default judgment against Ja-Con in excess of $2,000,000.

California Traditions initiated litigation against Claremont under Insurance Code section 11580(b)(2). That section allows a judgment creditor to litigate against a debtor's insurance carrier to recover on the judgment up to the policy limits. In response, Claremont moved for summary judgment citing its condominium exclusion. California Traditions opposed the motion

by arguing that the Claremont policy was ambiguous and citing the longstanding principle that courts must resolve any ambiguities in favor of an insured's reasonable expectation of coverage. *See, e.g., Foster-Gardner, Inc. v. National Union Fire Ins. Co.* (1998) 18 Cal.4th 857, 868. Further, California Traditions argued that the Claremont policy did not define the term "condominium" and that Ja-Con would not expect the homes at issue to qualify as condominiums because they were freestanding units similar to single family homes. Specifically, the homes were freestanding units with no shared walls roofs, halls, or plumbing or electrical lines. Accordingly, California Traditions argued that Ja-Con reasonably expected coverage for its work on these homes regardless of the condominium exclusion.

The court acknowledged that the Claremont policy failed to specifically define a "condominium." However, California courts may look beyond the "four corners" of an insurance policy in determining the meaning of policy terms. For example, courts may consider the mutual intent of the parties to the policy, the ordinary and popular meaning of terms in the policy, and the usage of those terms in the place where the policy is entered.[1] Accordingly, the *California Traditions* court looked beyond the terms of the Claremont policy and considered the Civil Code's following definition of condominiums:

> "A condominium consists of an undivided interest in common in a portion of real property coupled with a separate interested in space . . . described on a recorded final map, parcel map, or condominium plan. . . . The description of the unit may refer to. . . an entire structure containing one or more units. . . ."
> *See* Civil Code, Section 1351(f).

The court ruled that the definition of "condominium" in Civil Code, Section 1351(f) rendered the Claremont policy unambiguous. The court then ruled that because the Claremont policy was unambiguous, the insured could not have a reasonable expectation of coverage for the homes at issue.

The court also reaffirmed that insurance carriers are free to decide which risks to cover and which to exclude. The court declared that "[t]here is nothing. . . that suggests that an insurer, having deemed certain matters material to the risks it would insure, may not rely on those matters to deny coverage unless it can convince a court of the actuarial materiality of those matters."

The take-away for subcontractors is that their expectation of coverage may be overruled by the courts. What qualified for coverage in the past may be denied in the future due to changing

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[1] *See, e.g.,* California Civil Code sections 1636 (policies "must be [] interpreted to give effect to the mutual intention of the parties. . . ."), 1644 (policy terms "are to be understood in their ordinary and popular sense. . . ."), & 1646 (policy "is to be interpreted according to the law and usage of the place where it is to be performed. . . .").

policy language interpretations. If subcontractors are uncertain of the meaning of certain terms in a policy, they should consult an attorney before purchasing that policy, seek an evaluation of coverage before working on particular projects, and seek aid in tendering claims to their carriers. We find that, in many cases, even a subcontractor's broker may not fully understand the limitations in coverage purchased. Finally, we caution subcontractors to pay attention to the classification of projects in contracts and on blueprints to avoid the coverage pitfalls evidenced in this case.

The take-away for carriers is that they are entitled to choose those risks to cover, and those to exclude, so long as their policies are found unambiguous. Again, this finding is based on the court's current interpretation of terms, not necessarily on the subcontractor's understanding.

We at Braden, Hinchcliffe & Hawley are committed to helping our carrier and contractor clients navigate these issues and assuring that the coverage purchased and the coverage provided meet the needs of carriers and contractors alike.

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