THE PASCHOS LAW UPDATE NEWSLETTER
THOMAS PASCHOS & ASSOCIATES P.C. ATTORNEYS AT LAW

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I. FIRM NEWS

- Thomas Paschos will be a speaker/moderator at the PLUS 23rd Annual International Conference in November 2010, to be held in San Antonio, Texas.
- Thomas Paschos is co-Chairman of the Professional Liability Practice Group of the International Society of Primerus Law Firms. For additional information on Primerus, please visit www.Primerus.com .

II. INSURANCE COVERAGE

Commercial General Liability Insurer Has No Duty to Defend a Contractor for Faulty Workmanship

In *Specialty Surfaces Intern., Inc. v. Continental Cas. Co.,* --- F.3d ----, 2010 WL 2267197 (3d. Cir. (Pa.) June 8, 2010), appellant, Specialty Surfaces, a Pennsylvania corporation, and its subsidiary, Empire, a California corporation with a principal place of business in Pennsylvania together, doing business as Sprinturf, manufactured and sold synthetic turf for athletic playing fields. Specialty Surfaces was insured by Continental Casualty Company; Empire was named as an additional insured.

The Continental policy agreed to pay damages because of 'bodily injury' or 'property damage' to which the insurance applied. The contract of insurance applied to "'bodily injury' and 'property damage' only if ... [t]he 'bodily injury' or 'property damage' is caused by an 'occurrence'....". "Occurrence" is defined as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions."

The underlying action involved allegations against Specialty Surfaces and Empire by the Shasta Union High School District ("Shasta") arising out of the installation of Sprinturf and drainage systems on several high school football fields. Specifically, Shasta alleged that the synthetic turf systems installed on exhibited defects in materials and workmanship, which worsened over time. In addition, it was alleged that that Specialty Surfaces, doing business as Sprinturf, breached the terms of the warranties by failing "to make good the aforementioned defects in materials and workmanship in a timely fashion."

Specialty Surfaces provided Continental with notice of the lawsuit and requested coverage. Continental disclaimed coverage stating that the commercial general liability policy did not cover Shasta's claim because “[t]he allegations are solely poor workmanship and/or product” and “[a]ny damage that your company can be responsible for would be for improper installation or a defect in the product itself.”

Shasta amended the complaint to include Empire as a defendant. In addition to breach of warranty claims against Specialty Surfaces and Empire, Shasta added a claim for negligence against Empire, Trent Construction, and Airfield.

After the amended complaint was filed, Continental agreed to defend Specialty Surfaces and Empire in the California action, subject to a reservation of rights. Continental stated that it agreed to provide a defense because the amended complaint alleged that negligence resulted in damage to the base below the playing fields and the drainage system. Continental, however, continued to refuse to reimburse Sprinturf for its expenses in defending itself before Continental received notice of the amended complaint.

Sprinturf commenced this action seeking a declaratory judgment that Continental had a duty to defend and to indemnify against any liability in Shasta's suit. Both parties moved for summary judgment on the issue of when Continental was required to provide for its defense. Sprinturf argued that Continental was required to provide a defense when it received notice of Shasta's original complaint because the Shasta complaint alleged property damage to another party's work product. Continental argued that the property damage alleged in the Shasta complaints was not caused by an “occurrence” covered under the policy and, in the alternative, that policy exclusions applied to the type of damage alleged.

To start, the court analyzed whether Pennsylvania or California law applied. The court found that Pennsylvania law applied. In its choice of law analysis, the court made conclusions regarding the coverage issues presented in this case. The court addressed three Pennsylvania cases which analyzed similar coverage issues regarding faulty workmanship : *Kvaerner Metals Division of Kvaerner U.S., Inc. v. Commercial Union Ins. Co.,* 908 A.2d 888 (Pa.2006) (holding the definition of “accident” required to establish an “occurrence” cannot be satisfied by claims based upon faulty workmanship as such claims do not present the degree of fortuity contemplated by the ordinary definition of “accident”); *Millers Capital Ins. Co. v. Gambone Bros. Development Co.,*941 A.2d 706 (Pa.Super. 2007) (holding that “natural and foreseeable acts, such as rainfall, which tend to exacerbate the damage, effect, or consequences caused by faulty workmanship cannot be considered sufficiently fortuitous to constitute an ‘occurrence’ or ‘accident’ for the purposes of an occurrence based CGL policy); and *Nationwide Mutual Ins.Co. v. CPB International, Inc.,*562 F.3d 591 (3d Cir. 2009) (holding that consequential damages resulting from faulty workmanship was not an “occurrence”).

Based on *Kvaerner*, *Gambone* and *CPB International*, the Third Circuit concluded that Pennsylvania law interprets “occurrence” based coverage like that provided to Sprinturf in accordance with its literal text. In order for a claim to trigger coverage, there must be a causal nexus between the property damage and an “occurrence,” i.e., a fortuitous event. Faulty

workmanship, even when cast as a negligence claim, does not constitute such an event; nor do natural and foreseeable events like rainfall.

The Third Circuit found that Continental did not have a duty to defend Sprinturf when it received notice of the original complaint because the original complaint only alleged that Specialty Surfaces breached its contract with the school district by failing “to make good ... defects in materials and workmanship in a timely fashion.” The Court held that a breach of contract claim could not constitute an “occurrence” in a commercial general liability policy under Pennsylvania law.

The Third Circuit also held that Continental was not required to defend Sprinturf after it received notice of the amended complaint. In the amended complaint, Shasta alleged that Empire was negligent in designing, manufacturing and installing a suitable and compatible subdrain system and impermeable liner in compliance to the contract documents. As a result, Shasta alleged that there was damage to the synthetic turf, the impermeable liner, the subdrain system, and the subgrade.

The court found that the allegations of damages to Empire's own work product based on Empire's alleged negligence were claims of damage based on faulty workmanship and, therefore, not caused by an accident. Sprinturf argued that the damage to the subgrade was accidental, and therefore was a covered occurrence. The court rejected this argument citing *Gambone*, in which the Superior Court, relying on *Kvaerner*, held that damage caused by water leaks resulting from faulty workmanship was not an occurrence. The court provided:

Here, Shasta alleged that Empire installed the subdrain system, the impermeable liner, and the synthetic turf. In addition to defects in Empire's work product, Shasta alleged that “as a direct result” of the problems with the subdrain system, “water has leaked from the subdrain system into the subgrade, dirt has washed from the subgrade into the subdrain system, the subgrade has settled and subgrade soil stablilizer has remulsified. Consequently, the fields have developed depressions and unstable playing surfaces....” Thus, the amended complaint alleges that the damage to the subgrade was caused by water leaks that resulted from the faulty workmanship. But water damage to the subgrade is an entirely foreseeable, if not predictable, result of the failure to supply a “suitable” impermeable liner or properly install the drainage system. Thus, as in *Gambone*, this damage is not “sufficiently fortuitous to constitute an ‘occurrence’ or ‘accident.’

Sprinturf insisted that *Gambone* was distinguishable because the plaintiffs there did not allege damage beyond the structure of the house, which was the work product of the insured. The court found that Sprinturf’s argument ignored that the *Gambone* Court, following *Kvaerner*, clearly focused on whether the alleged damage was caused by an accident or unexpected event, or was a foreseeable result of the faulty workmanship when deciding whether the policy covered the damage. The court stated “[h]ere, water damage to the subgrade was a foreseeable result of the failure to supply a suitable liner or ‘to ensure the proper design, manufacture and installation of the synthetic turf and subdrain system.’” As such, the court held that Continental did not have a duty to defend Sprinturf in the California litigation and as such that Continental also had no duty to indemnify Sprinturf.

II. EMPLOYMENT LITIGATION

Fee Claimant Need Not Be Prevailing Party, but Must Show Some Degree of Success on the Merits to Be Eligible for Attorney Fees Under ERISA's General Fee-Shifting Statute

In *Hardt v. Reliance Standard Life Ins. Co.,* --- S.Ct. ---, 2010 WL 2025127 (U.S. May 24, 2010), petitioner Hardt filed for long-term disability benefits under her employer's long-term disability plan after she was forced to stop working due to medical problems. Upon exhausting her administrative remedies, Hardt sued Reliance, her employer's disability insurance carrier, alleging that it had violated the Employee Retirement Income Security Act of 1974 (ERISA) by wrongfully denying her benefit claim. The District Court denied Reliance's summary judgment, finding that because the carrier had acted on incomplete medical information, the benefits denial was not based on substantial evidence. While the District Court found compelling evidence that Hardt was totally disabled, it also denied her summary judgment in order to give Reliance the chance to address the deficiencies in its decision to deny Hardt's benefits claim.

The court remanded to Reliance, giving it 30 days to consider all the evidence and to act on Hardt's application, or else the court would enter judgment in Hardt's favor. Reliance did as instructed and awarded Hardt benefits. Hardt then moved for attorney's fees and costs under § 1132(g)(1). The District Court assessed her motion under the three-step framework that governed fee requests in ERISA cases under Circuit precedent. At step one of that framework, a district court asks whether the fee claimant is a "prevailing party." If the fee claimant qualifies as a prevailing party, the court proceeds to step two and determines whether an award of attorneys' fees is appropriate. Finally, if a fee award is appropriate, the court must review the attorneys' fees and costs requested and limit them to a reasonable amount.

The District Court concluded that Hardt had attained the requisite "prevailing party" status and granted the motion. The Fourth Circuit vacated the fees award, holding that Hardt had failed to establish that she qualified as a "prevailing party" under the rule set forth in *Buckhannon Board & Care Home, Inc. v. West Virginia Dept. of Health and Human Resources, 532 U.S. 598, 604, 121 S.Ct. 1835, 149 L.Ed.2d 855,* that a fee claimant is a "prevailing party" only if he has obtained an "enforceable judgmen[t] on the merits" or a "court-ordered consent decre[e]." The court reasoned that because the remand order did not require Reliance to award Hardt benefits, it did not constitute an enforceable judgment on the merits.

Hardt filed a petition for a writ of certiorari seeking review of the Court of Appeals' judgment. The Court held that a fee claimant need not be a "prevailing party" to be eligible for an attorney's fees award under § 1132(g)(1). This is based on the Court's interpretation of § 1132(g)(1)'s plain text which expressly grants district courts "discretion" to award attorney's fees "to either party." However, the court held that a fees claimant must show "some degree of success on the merits" before a court may award attorney's fees under § 1132(g)(1) and that Hardt satisfied this standard. The Court noted that though Hardt failed to win summary judgment on her benefits claim, the District Court nevertheless found compelling evidence that she is totally disabled and

stated that it was inclined to rule in her favor. She also obtained the remand order, after which Reliance conducted the court-ordered review, reversed its decision, and awarded the benefits she sought. As such the Court found that the District Court properly exercised its discretion to award Hardt attorney's fees.

A Plaintiff Who Does Not File a Timely Charge Challenging the Adoption of a Practice May Assert a Disparate-Impact Claim in a Timely Charge Challenging the Employer's Later Application of that Practice

In *Lewis v. City of Chicago, Illinois,* --- S.Ct. ---, 2010 WL 2025206 (U.S. May 24, 2010), African-American applicants for city firefighter jobs brought a Title VII action, alleging that a written test required by city had disparate impact on African-American applicants. The written examination was given in 1995 by the City of Chicago to applicants seeking firefighter positions. In January 1996, the City announced it would draw candidates randomly from a list of applicants who scored at least 89 out of 100 points ("well qualified") on the examination. It informed those who scored below 65 that they had failed and would not be considered further. It informed applicants who scored between 65 and 88 ("qualified") that it was unlikely they would be called for further processing but that the City would keep them on the eligibility list for as long as that list was used.

In May of 1996, the City selected its first class of applicants to advance, and it repeated this process multiple times over the next six years. Beginning in March 1997, petitioners, several African-American applicants who scored in the "qualified" range but had not been hired, filed discrimination charges with the EEOC and received right-to-sue letters. They then filed suit, alleging that the City's practice of selecting only applicants who scored 89 or above had a disparate impact on African-Americans in violation of Title VII. The District Court denied the City's summary judgment motion, rejecting its claim that petitioners had failed to file EEOC charges within 300 days "after the unlawful employment practice occurred," and held that the City's "ongoing reliance" on the 1995 test results constituted a continuing Title VII violation. The litigation then proceeded, and petitioners prevailed on the merits. The Seventh Circuit reversed the judgment in their favor, holding that the suit was untimely because the earliest EEOC charge was filed more than 300 days after the only discriminatory act-sorting the scores into the "well qualified," "qualified," and "not qualified" categories. The later hiring decisions, the Seventh Circuit held, were an automatic consequence of the test scores, not new discriminatory acts. The Supreme Court granted certiorari.

In order to determine whether petitioners' charges were timely required identifying the 'unlawful employment practice.' Petitioners challenged the City's practice of picking only those who had scored 89 or above on the 1995 examination when it later chose applicants to advance. With the exception of the first selection round, all agreed that the challenged practice - the City's selection of firefighter hires on the basis announced in 1996 - occurred within the charging period. As such, the court provided that the real question was not whether a claim based on that conduct is timely, but whether the practice can be the basis for a disparate-impact claim. The court held that the

unlawful practice in this matter could be the basis for a disparate-impact claim. The court explained that a Title VII plaintiff establishes a prima facie claim by showing that the employer "uses a particular employment practice that causes a disparate impact." "Employment practice" clearly encompasses the conduct at issue: exclusion of passing applicants who scored below 89 when selecting those who would advance. The City "use[d]" that practice each time it filled a new class of firefighters, and petitioners allege that doing so caused a disparate impact.

The Court addressed the City's argument that the only actionable discrimination occurred in 1996 when it used the test results to create the hiring list, which it concedes was unlawful. The Court provided:

It may be true that the City's adoption in 1996 of the cutoff score gave rise to a freestanding disparate-impact claim. If so, because no timely charge was filed, the City is now "entitled to treat that past act as lawful," But it does not follow that no new violation occurred-and no new claims could arise-when the City later implemented the 1996 decision. (citations omitted).

Based on the above, the Court held that a plaintiff who does not file a timely charge challenging the adoption of a practice may assert a disparate-impact claim in a timely charge challenging the employer's later application of that practice as long as he alleges each of the elements of a disparate-impact claim.

Copies of the full text of any of the cases discussed in this Newsletter may be obtained by calling our office. The articles contained in this Newsletter are for informational purposes only and do not constitute legal advice.