CASE NO. 14-11639

IN THE
UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

HUGH A. CARITHERS and KATHERINE S. CARITHERS,

Plaintiffs/Appellees,
v.
MID-CONTINENT CASUALTY COMPANY,

Defendant/Appellant.

Appeal from the United States District Court for the Middle District of Florida
Hugh A. Carithers and Katherine S. Carithers v. Mid-Continent Casualty Company
Case No: 3:12-cv-00890-MMH-PDB

BRIEF OF APPELLANT MID-CONTINENT CASUALTY COMPANY

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CERTIFICATE OF INTERESTED PERSONS AND CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 26 of the Federal Rules of Appellate Procedure and Eleventh Circuit Rules 26.1-1 and 28-1(b), the undersigned counsel of record certifies that the following listed persons or entities have an interest in the outcome of this case. See Fed. R. App. P. 26; 11th Cir. R. 26.1-1, 26.1-3, 28-1(b).

1. Catizone, John R. – Attorney for Appellant, Mid-Continent Casualty Company.

2. Carithers, Hugh A. – Plaintiff

3. Carithers, Katherine S. - Plaintiff

4. Litchfield Cavo, LLP – Attorneys for Appellant, Mid-Continent Casualty Company

5. Mid-Continent Casualty Company – Appellant

6. Honorable Judge Magnuson – United States District Judge in the district court proceedings

7. Schottenfeld, Dara L. – Attorney for Appellant, Mid-Continent Casualty Company

8. Warren, Robert E. – Counsel for Plaintiffs

STATEMENT REGARDING ORAL ARGUMENT

Mid-Continent Casualty Company ("MCC") believes that oral argument will be helpful to the Court in deciding this appeal and therefore requests that it be granted oral argument.

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STATEMENT OF SUBJECT MATTER AND APPELLATE JURISDICTION

The district court had diversity jurisdiction by virtue of 28 U.S.C. § 1332. At all material times, MCC was a foreign corporation with its principle place of business in the state of Oklahoma. At all material times, Carithers was a citizen of Florida. In addition, the amount in controversy exceeds the sum of $75,000 exclusive of interest, attorney fees and costs.

This appeal is from a final decision of the United States District Court for the Middle District of Florida that disposed of all parties' claims. Accordingly, this Court has jurisdiction of this appeal pursuant to 28 U.S.C. § 1291.

This appeal was timely noticed by MCC. The district court entered final judgment on March 31, 2014, and MCC filed its Notice of Appeal on April 10, 2014.

STATEMENT OF THE ISSUES

I. Whether the district court erred as a matter of law in granting Carithers' motion for summary judgment and denying MCC's motion for summary judgment on the issue of the duty to defend.

II. Whether the district court erred as a matter of law in ruling that all claimed damages were for "property damage" as that term is interpreted by Florida courts.

III. Whether the district court erred as a matter of law in not allowing MCC to amend its pleadings by relying on an inapplicable statute

STATEMENT OF THE CASE

A. Course of Proceedings and Disposition

This coverage action follows an underlying action in which Carithers obtained a judgment against MCC's insured, Cronk Duch, because of construction defects. On October 28, 2011, Carithers filed a Third Amended Complaint in the underlying action. [D.E. 69-1]. Carithers specifically alleged that the construction defects at issue **were not discovered until 2010** and **could not have been discovered by a reasonable inspection before 2010**. [D.E 69-1,¶10](emphasis added). MCC refused to defend or indemnify Cronk Duch in connection with the Third Amended Complaint because its last policy expired in October 2008, long before any property damage was discovered or discoverable as alleged by Carithers. [D.E 69-8].

On May 25, 2012, Carithers and Cronk Duch entered into an Agreement for Assignment of Claim, which purported to provide for the entry of a judgment against Cronk Duch as well as an assignment of Cronk Duch's right to sue MCC in connection with the judgment amount. [D.E 69-2] Final judgment was entered in the underlying action in the amount of $91,872.00, plus prejudgment interest of $5,856.84 and costs of $524.00. [D.E. 69-3].

Thereafter, Carithers filed this action against MCC in the same court as the underlying action, seeking to enforce the judgment. MCC removed to the Middle District of Florida. *See Notice of Removal.*

Both parties moved for summary judgment on the issue of the duty to defend. The district court denied MCC's motion and granted Carithers' motion. The case then proceeded to trial on the issue of MCC's duty to indemnify. Following a bench trial, the district court awarded Carithers all of his claimed damages, and MCC brought this appeal.

B. Statement of Facts

Carithers filed suit against Cronk Duch Miller & Associates Inc., Cronk Duch Architecture LLC, Cronk Duch Craftsmen LLC, Joseph S. Cronk, Cronk Duch Partners LLC and Cronk Duch Holdings Inc. ("Cronk Duch") in state court as a result of defective work performed by the defendants and their subcontractors at the Carithers' residence. [D.E 69-1]. Carithers allegedly contracted with the defendants for the construction of the Carithers' residence in 2003. Carithers moved into the residence in 2005. *Id.*

The complaint was amended several times in the underlying action. The third amended complaint, which was the operative complaint at the time of the underlying judgment, contained counts of professional negligence, breach of contract, breach of implied warranty, and negligence. [D.E 69-1]. The alleged

construction defects included wood rot, damaged bricks, a defective balcony, and cracked patio tiles. *Id.*.

A final judgment was entered against Cronk Duch for $98,252.84, which includes prejudgment interest of $5,856.84 and costs of $524.00. [D.E. 69-2] The judgment includes damages for the replacement of improper and inadequate mud base ($7,500.00), replacement of stone damaged as a result of the improper mud base ($50,000.00), repairs to an electrical box ($100.00), replacement and installation of appliances destroyed by electrical surges permitted by improperly installed electrical box ($13,014.00), sand blasting and repair of brick as a result of improper boral coating ($350.00), installation of protective coating on exterior porous brick ($9,425.00), repairs to structural damage to floor, ceiling and wall due to defective balcony ($3,658.00), replacement of balcony ($3,325.00), and supervision permitting, dumpster use, reports, tests and other conditions ($4,500.00). *Id.*

Carithers then brought this action against MCC to enforce the judgment. Carithers alleges that MCC had a duty to defend and indemnify Cronk Duch in the underlying action. [D.E. 1]. MCC removed the case to the United States District Court for the Middle District of Florida. *Notice of Removal*. Both parties moved for summary judgment in this matter on the duty to defend. [D.E. 69 and D.E 70]. MCC's Motion for Summary Judgment was denied as to the duty to defend, while

Carithers' Motion for Summary Judgment was granted as to the duty to defend. [D.E. 97]

A bench trial took place on February 17, 2014 wherein the only issue was whether MCC had a duty to indemnify its insured for any part of the underlying judgment. At trial, Carithers' expert Brett Newkirk testified regarding, among other things, wood rot. [Tr. at 113-14]. He testified that wood rot cannot exist in the absence of fungus. [Tr. at 113]. At the end of the trial, MCC moved to conform its pleadings to the evidence on the basis that Mr. Newkirk's previously disclosed opinions did not include any statement that wood rot cannot exist in the absence of fungus and that each of the MCC policies contained a fungus/mold exclusion. The district court denied MCC's motion to conform its pleadings to the evidence, relying on Florida's Claims Administration Act, §627.426. [Tr. at 141].

The district court issued its Order on MCC's duty to indemnify on March 11, 2014. [D.E. 126]. In that Order, the district court found that all of Carithers' alleged damages constituted "property damage" under Florida law. [D.E. 126]. The district court therefore found that MCC had a duty to indemnify Cronk Duch for all of Carithers' damages. [D.E. 126]

The MCC Policies

MCC issued the following four commercial general liability ("CGL") policies to Cronk Duch:

1. Policy number 04-GL-000594283 to Cronk Duch Miller & Associates, Inc. with policy period of March 9, 2005 through March 9, 2006; [69-4]

2. Policy number 04-GL-000623817 to Cronk Duch Miller & Associates, Inc. with policy period of March 9, 2006 through March 9, 2007;[69-5]

3. Policy number 04-GL-000666145 to Cronk Duch Holdings, Inc. with policy period of March 9, 2007 through March 9, 2008; [69-6] and

4. Policy number 04-GL-000708330 to Cronk Duch Holdings, Inc. with policy period of March 9, 2008 through October 6, 2008. [69-7]

The policies provide in relevant part as follows:

SECTION I – COVERAGES

COVERAGE A. BODILY INJURY AND PROPERTY DAMAGE LIABILITY

1. Insuring Agreement

a. 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. We will have the right and duty to defend any suit seeking those damages. We may, at our discretion, investigate any occurrence and settle any claim or suit that may result. …

b. This insurance applies to "bodily injury" and "property damage" only if

(1) The "bodily injury" or "property damage" is caused by an "occurrence that takes place in the "coverage territory", and

> **(2)** The "bodily injury" or "property damage" occurs during the policy period…

The policies contain the following relevant definitions:

> **SECTION V – DEFINITIONS**
>
> **13.** "Occurrence" means an accident, including continuous or repeated exposure to substantially the same general harmful conditions. [D.E 69-4, 5, 6, 7 at V (13)].
>
> **17.** "Property damage" means:
>
> **a.** Physical injury to tangible property, including all resulting loss of use of that property. All such loss of use shall be deemed to occur at the time of the physical injury that caused it; or
>
> **b.** Loss of use of tangible property that is not physically injured. All such loss of use shall be deemed to occur at the time of the "occurrence" that caused it. [D.E. 69-4, 5, 6, 7 at V (18)].

The policies all contain a "fungus, mildew and mold" exclusion, which provides in relevant part as follows:

> This insurance does not apply to … "property damage" … **arising out of**, resulting from, caused by, **contributed to, attributed to, or in any way related to** any fungus… .

[D.E. 69-4, 5, 6, 7 at Form ML 1217(04 01)] (emphasis added).

STANDARD OF REVIEW

The District Court's grant of Carithers' motion for partial summary judgment and denial of Mid-Continent's motion for summary judgment are subject to *de novo* review. *Cagle v. Bruner,* 112 F.3d 1510, 1514 (11th Cir. 1997). Whether to grant or deny a motion for leave to amend pleadings to conform to the evidence presented at trial are within the discretion of the trial court. *Borden, Inc. v. Florida East Coast Ry. Co.*, 772 F.2d 750, 758 (11th Cir. 1985). However, the district court's denial of MCC's motion in this case was based on the court's reliance on an inapplicable statute, such that this issue also involves legal error. Where the court errs as a matter of law, the standard of review is *de novo.* Following a bench trial, a district court's legal conclusions are subject to *de novo* review. *See Mitchell v. Hillsborough County,* 468 F.3d 1276, 1282 (11th Cir.2006); *Kona Tech. Corp. v. Southern Pac. Transp. Co.,* 225 F.3d 595, 601 (5th Cir.2000) ("The standard of review for a bench trial is well established: findings of fact are reviewed for clear error and legal issues are reviewed de novo.").

SUMMARY OF THE ARGUMENT

The district court erred as a matter of law in three ways. First, the district court erred in denying MCC's summary judgment motion on the duty to defend and granting Carither's motion. Carithers specifically alleged in the Third Amended Complaint that the construction defects at issue were not discovered

until 2010 and could not have been discovered by a reasonable inspection before 2010. Because MCC's final policy expired in October 2008, Carithers' allegations eliminated any duty to defend under any of its four policies based on the majority of decisions holding that the appropriate trigger of coverage in Florida is the "manifestation" trigger. This Court should reverse the district court's ruling on the duty to defend and find that MCC had no duty to defend. Also, where there is no duty to defend, there is no duty to indemnify as a matter of law. Therefore, this Court should reverse with a direction to the district court to enter judgment in favor of MCC.

Second, the district court erred as a matter of law in finding that all of Carithers' damages were for "property damage" under an MCC CGL policy. Among other things, two elements of Carithers' damages were because of defective workmanship by subcontractors, where each subcontractor's work damaged only itself and did not damage any other subcontractor's work. Under *J.S.U.B.* and the other cases discussed herein, damages for the removal, repair or replacement of those two elements of damages do not constitute "property damage" under a CGL policy. This Court should reverse the district court's finding of coverage in that regard.

Third, almost all other elements of damages were because of consequential damage, i.e., "property damage" to subcontractors' work caused by the defective

workmanship of different subcontractors. That damage, however, was because of wood rot. At trial, a Carithers expert testified for the first time that wood rot cannot exist in the absence of fungi. Therefore, before concluding its case in chief MCC moved for leave to amend the pleadings to assert as an affirmative defense its "fungus, mold, mildew" exclusion based on that new testimony. Given the very liberal rules regarding amendments, the district court should have allowed the amendment, and should have found that all of the damages awarded because of wood rot were excluded. But the district court erred as a matter of law by concluding that the exclusion would not apply and by ruling that MCC was precluded from asserting that defense by Florida Statutes, §627.426. The court erred as a matter of law in relying on that statute because the Supreme Court of Florida has made it clear that the statute applies only to "coverage defenses," i.e., defenses based on policy conditions such as late notice, and not to exclusions. This Court should reverse the district court's denial of the motion for leave to amend, permit the amendment, and find that all damages related to wood rot are excluded.

ARGUMENT

A. THE DISTRICT COURT ERRED AS A MATTER OF LAW IN DENYING MID-CONTINENT'S MOTION FOR SUMMARY JUDGMENT ON THE DUTY TO DEFEND

Summary judgment is appropriate where "there is no genuine issue as to any material fact and the moving party is entitled to a judgment as a matter of law." *See* Fed. R. Civ. P. 56(c); *Celotex Corp. v. Catrett*, 477 U.S. 317 (1986); *Gas Kwick, Inc. v. United Pacific Ins. Co.*, 58 F.3d 1536 (11th Cir. 1995). The existence of some factual disputes will not defeat an otherwise properly supported motion for summary judgment. "The requirement is that there be a genuine issue of material fact." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986).

Summary judgment is particularly appropriate to resolve questions of insurance coverage, since the interpretation of a written contract is a matter of law to be determined by the court. *Technical Coating Applicators, Inc. v. U.S. Fidelity and Guar. Co.*, 157 F.3d 843 (11th Cir. 1998); *DEC Electric, Inc. v. Raphael Construction Corp.*, 558 So.2d 427 (Fla. 1990); *Jones v. Utica Mutual Ins. Co.*, 463 So.2d 1153 (Fla. 1985).

In this case, MCC was entitled to summary judgment based on the plain meaning and legal effect of its policy, which requires that "property damage" occur during a policy period. [D.E. 69-4, 5, 6, 7 at I(1)(b)(2)]. Although Florida's state appellate courts have not addressed the issue, the majority of Florida's federal

courts have concluded that damage "occurs" when it is "manifest." MCC had no duty to defend Cronk Duch in the underlying action because Carithers sought damages for alleged defects which, according to the express allegations of the Third Amended Complaint, were not discovered and could not have been discovered by a reasonable inspection prior to 2010. [D.E.69-1 at ¶ 10]. Because no MCC policy was in effect after October 6, 2008, the allegations of the underlying complaint negated any duty to defend under an MCC policy. The court should have granted MCC's Motion for Summary Judgment on the duty to defend, which as a matter of law would also be conclusive as to the duty to indemnify, and the court should have denied Carithers' Motion for Summary Judgment on the Duty to Defend [D.E. 70] .

1. An Insurer's Duty to Defend is Determined Solely by the Allegations of the Underlying Complaint.

It is well settled that a determination regarding a liability insurer's duty to defend depends solely upon the allegations contained within the four corners of the complaint against the insured. *Jones v. Florida Ins. Guar. Assoc., Inc.*, 908 So.2d 435 (Fla. 2005); *National Union Fire Ins. Co. v. Lenox Liquors Inc.*, 358 So.2d 533 (Fla. 1977). In determining whether an obligation to defend exists, a court may not consider evidence or testimony outside the four corners of the complaint. *Wackenhut*, 15 F. Supp.2d, at 1322; *State Farm Fire and Cas. Co. v. Edgecumbe*,

471 So.2d 209, 210 (Fla. 1st DCA 1985); *Baron Oil Co. v. Nationwide Mutual Ins. Co.*, 470 So.2d 810, 814 (Fla. 1st DCA 1985).

Where the complaint alleges any facts which fall within the scope of coverage, the insurer is required to afford a defense. *MCO Environmental Inc. vs. Agricultural Excess & Surplus Ins. Co.*, 689 So.2d 1114 (Fla. 3d DCA 1997); *Sunshine Birds & Supplies Inc. vs. U.S.F.&G.*, 696 So.2d 907 (Fla. 3d DCA 1997). On the other hand, if the complaint does not allege any damages which are potentially within the policy's coverage, no duty to defend the insured arises. *Wackenhut Services, Inc., v. National Union Fire Ins. Co.,* 15 F. Supp.2d 1314 (S.D. Fla. 1998); *Allstate Ins. Co. v. Myers*, 951 F. Supp. 1014 (M.D. Fla. 1996).

Because the duty to defend is broader than the duty to indemnify, a determination that there is no duty to defend logically requires a finding that there is also no duty to indemnify. *Allstate Ins. Co. v. Safer,* 317 F. Supp.2d 1345 (M.D. Fla. 2004); *Council v. Paradigm Ins. Co.,* 133 F. Supp.2d 1339 (M.D. Fla. 2001).

2. "Manifestation" Is the Applicable Trigger of Coverage

In order for there to be coverage under a CGL policy, the property damage must "occur" during the policy period. There are four "trigger of coverage" legal theories which have been applied by courts in various jurisdictions to determine when property damage "occurs" under a CGL policy: (1) exposure;

(2) manifestation; (3) continuous trigger; and (4) injury in fact. *See Auto Owners Ins. Co. v. Travelers Cas. & Sur. Co.,* 227 F.Supp.2d 1248 (M.D. Fla. 2002).

In this action, the district court concluded that the "injury in fact" trigger of coverage is the appropriate trigger of coverage in Florida. As explained herein, the district court was incorrect in its decision. Although there is no Florida state court appellate decision discussing which trigger of coverage is to be applied, the majority of federal courts in Florida have stated that the applicable trigger of coverage in Florida is the "manifestation" trigger. Thus, a CGL policy is triggered when the property damage "manifests" itself, not when the negligent act or omission giving rise to the damage occurs. *See, e.g., Auto Owners,* 227 F.Supp.2d at 1266 (the general rule is that the time of occurrence within the meaning of an "occurrence" policy is the time at which the injury first manifests itself); *Amerisure Ins. Co. v. Albanese Popkin the Oats Dev. Group, L.P.*, 2010 WL 4942972 (S.D. Fla. Nov. 30, 2010)(no coverage where the underlying complaint alleged that plaintiffs first noticed the damage prior to the policy period, even though plaintiffs argued that the damage was continuous); *Assurance Co. of Am. v. Lucas Waterproofing Co., Inc.* 581 F. Supp.2d 1201 (S.D. Fla. 2008); *Essex Builders Group, Inc., v. Amerisure Ins. Co.*, 485 F. Supp.2d 1302 (M.D. Fla. 2006); *Mid-Continent Cas.Co. v. Frank Casserino Constr., Inc.*, 721 F.Supp.2d 1209 (M.D. Fla. 2010); *United Nat'l Ins. Co. v. Best Truss Co.*, 2010 WL 5014012

(S.D. Fla. 2010); *Mid-Continent Cas. Co. v. Siena Home Corp.*, 2011 WL 2784200 (M.D. Fla. 2011); *Contra, Axis Surplus Ins. Co. v. Contravest Constr. Co.*, 2012 WL 2048303 (M.D. Fla.).

Until 2010, no court had explained what exactly is meant by the term "manifestation." It is MCC's position that property damage "manifests" when it is discovered, because any dictionary meaning of the term "manifest" clearly requires such an interpretation. MCC litigated that issue in *Mid-Continent Cas.Co. v. Frank Casserino Constr., Inc.*, 721 F.Supp.2d 1209 (M.D. Fla. 2010).

In *Casserino*, it was undisputed that water damage at a building constructed by Casserino was not discovered by the building owner until several years after MCC's policy period expired. *See id.,* at 1211-12. MCC brought a declaratory action asking the court to declare that no property damage had manifested in MCC's policy period because it was not discovered during the policy period. The building owner's expert opined that the damage from water intrusion would have been visible "upon a prudent engineering inspection" at the time of the first measurable rains after the completion of construction, which would have been the MCC policy period. *See id.,* at 1216.

The court agreed with MCC that Florida follows the manifestation trigger, but it stated that "manifestation" is distinguishable from "discovery." *Id.,* at 1216-17. The *Casserino* court found that property damage manifests when it *could have*

been discovered upon a prudent engineering investigation, not when it was actually discovered. The court stated:

> That no one saw or "discovered" damage caused by water intrusion during the policy period is of no moment. Under Florida's applicable "trigger" theory and the unambiguous language of the CGL policies..., the only relevant question is whether physical injury to the buildings manifested itself during the period of coverage.

Id., at 1217.

The *Casserino* decision has been followed in two other Florida federal cases. *See United Nat'l Ins. Co. v. Best Truss Co.*, 2010 WL 5014012 (S.D. Fla. 2010); *Mid-Continent Cas. Co. v. Siena Home Corp.*, 2011 WL 2784200 (M.D. Fla. 2011). In the *Best Truss* case, the U.S. Southern District held that proof of discovery of the damage is not required to trigger coverage if the damage was visible and capable of being discovered. *Best Truss*, 2010 WL 5014012 at *4. In *Siena Home*, this Court held adopted *Casserino* and further elaborated on the meaning of "manifestation". This Court stated:

> The "manifestation" or "occurrence" of property damage, for purposes of determining coverage... is the time that such damage was discernable and reasonably discoverable either because it was open and obvious or upon a prudent engineering investigation, and not the time of actual discovery where the two circumstances come about in sequence at different times.

Siena Home, 2011 WL 2784200, at *3.

MCC disagrees with the meaning of the term "manifestation" accorded to it in *Casserino*, *Best Truss* and *Siena Home*. Such an interpretation lacks any clarity.

Who is to say when property damage was "discoverable," or when an engineering inspection would have been "prudent?" How does such a standard help an insurer determine whether or not it has a duty to defend or indemnify? The only interpretation that provides any certainty is that property damage "manifests" when it is discovered. The *Casserino/Best Truss/Siena Home* interpretation is also contrary to any reasonable interpretation of the term "manifest." For example, according to Black's Law Dictionary, "manifest" means:

> Evident to the senses, especially to the sight, obvious to the understanding, evident to the mind, not obscure or hidden, and is synonymous with open, clear, visible, unmistakable, indubitable, indisputable, evident, and self-evident. …

Black's Law Dictionary (6th ed. 1990).

Under the *Casserino/Best Truss/Siena Home* interpretation, property damage is "manifest" not when it is discovered but rather when it is "discoverable," even if completely "hidden from view," if a "prudent" engineering inspection might have led to its discovery. Among other things, such an interpretation creates a question of fact in every case as to when such an inspection would have been "prudent." That interpretation flies in the face of the dictionary definition, which requires that the property damage be "evident … especially to the sight … not obscure or hidden … open, clear, visible, unmistakable, indubitable, indisputable, evident, and self-evident." Therefore, MCC maintains that the *Casserino/Best Truss/Siena Home* interpretation is wrong, and MCC asks this Court to give the term

"manifest" its logical and proper meaning, i.e., when the property damage is actually discovered, or at a minimum when it is so open and obvious that it should have been seen.

That said, whether this Court applies the *Casserino/Best Truss/Siena Home* interpretation or MCC's interpretation, MCC was entitled to summary judgment in any event. That is because as stated above, MCC's duty to defend is determined solely by the allegations in the underlying action, and in this case Carithers specifically alleged in the Third Amended Complaint that the construction defects at issue **were not discovered until 2010** and **could not have been discovered by a reasonable inspection before 2010**. [D.E.69-1 at ¶ 10] (emphasis added). Thus, under either interpretation of the term "manifest," Carithers pleaded the underlying action out of coverage. Based on the underlying allegations, this Court must find that MCC had no duty to defend, and therefore no duty to indemnify Cronk Duch in the underlying action, and that MCC was entitled to summary judgment as a matter of law.

Carithers has implicitly acknowledged that MCC had no duty to defend the underlying action. Carithers did so by amending their complaint in this declaratory action. Curiously, Carithers contended in the amended complaint that MCC should have recognized that the allegations of when property damage was "discovered" and/or "discoverable" were merely intended to surmount statute of limitations

issues. [D. E. 17, ¶ 17]. That novel and self-serving contention should have been rejected by the district court and must be rejected now by this Court as being, among other things, completely irrelevant. Pursuant to the case law cited herein, an insurer's duty to defend is determined solely by the underlying allegations. An insurer is not required to ignore allegations, as Carithers suggested in his response to MCC's Motion for Summary Judgment, nor is there any Florida case that would support such a contention.

In summary, the district court erred as a matter of law in denying MCC's motion and granting Carithers' motion. This Court should reverse with directions to enter judgment in favor of MCC.

B. THE DISTRICT COURT ERRED AS A MATTER OF LAW IN RULING THAT ALL CLAIMED DAMAGES CONSTITUTED "PROPERTY DAMAGE" UNDER FLORIDA LAW.

There are several cases in Florida state and federal court jurisprudence discussing what coverage is available to a general contractor in the context of a construction defect action under a standard Insurance Services Office, Inc. ("ISO") CGL coverage form such as that used by MCC. Prior to the Supreme Court of Florida's decision in *United States Fire Ins. Co. v. J.S.U.B., Inc.*, 979 So. 2d 871 (Fla. 2007) ("*J.S.U.B.*"), the law in Florida was that there was no coverage under a general contractor's CGL policy for property damage to any part of the work, whether or not some or all of the work had been performed by subcontractors. *See*

Lassiter Constr. Co. v. American States Ins. Co., 699 So. 2d 768 (Fla. 4th DCA 1997). However, *Lassiter* was disapproved by *J.S.U.B.*

Accordingly, *J.S.U.B.* is now recognized as the seminal case and the foundation for all subsequent decisions applicable to the question of what coverage is available to a general contractor under its CGL policy for construction defects. Another highly significant and relevant case, *Auto-Owners Ins. Co. v. Pozzi Window Co.*, 984 So. 2d 1241 (Fla. 2008), started in a federal forum but was ultimately decided by the Supreme Court of Florida when the Eleventh Circuit certified a question to the Supreme Court of Florida.

Under the law of *J.S.U.B.* and *Pozzi Windows,* as well as the other cases discussed below that followed those two decisions, the first question in this case is, what constitutes "property damage" as that term has been interpreted in the context of a general contractor's CGL policy where, as here, the work was performed by subcontractors? As discussed below, the courts make significant distinctions between (1) defective work that is not physically damaged, (2) defective work that only damages itself but not another component of the work, and (3) defective work that damages another component of the work. Only the latter category, i.e., physical damage caused by one subcontractor's work to the work of a different subcontractor, i.e., a different component of the general contractor's work, constitutes "property damage" under *J.S.U.B.*, *Pozzi Windows* and their progeny.

The first two categories, however, do not constitute "property damage" under the case law. For those categories of damages, one need not even consider exclusions because the policy's insuring agreement, i.e., the grant of coverage requiring "property damage," has not been met.

In *J.S.U.B.*, the court concluded that "defective work performed by a subcontractor that causes damage to the contractor's completed project ... can constitute 'property damage' caused by an 'occurrence' as those terms are defined in a standard form commercial general liability policy." The policy in *J.S.U.B.* contained a "subcontractor exception" to the "damage to your work" exclusion. But as stated by the *J.S.U.B.* court, "[o]f course, the subcontractor's exception to the general exclusion for a contractor's defective work becomes important only if there is coverage under the initial insuring provision." *Id.* at 880. The court further stated: "[F]aulty workmanship or defective work that has damaged the otherwise nondefective completed project has caused 'physical injury to tangible property' within the plain meaning of the definition of the policy. If there is no damage beyond the faulty workmanship or defective work, then there may be no resulting 'property damage.'" *Id.* at 889. *See also Amerisure Mut. Ins. Co. v. Auchter Co.*, 673 F.3d 1294 (11th Cir. 2012)(applying *J.S.U.B* and *Pozzi Windows* and stating that under Florida law a general contractor's CGL policy did not provide coverage for the removal of a defective roof installed by the roofing subcontractor that did

not damage any other subcontractor's work because the removal and replacement of the roof did not constitute "property damage").

The *J.S.U.B.* decision also stands for another proposition relevant to this case. The court cited with approval a prior decision by the Third District Court of Appeal, *Auto Owners Ins. Co. v. Tripp Constr., Inc.,* 737 So. 2d 600 (Fla. 3d DCA 1999), for recognizing the distinction between the cost of repairing and replacing the actual defects in the construction, which is not covered, and the cost of repairing the damage caused by defective components to other elements of the subject homes, which is covered. *J.S.U.B.,* 979 So. 2d at 889 (citing *Tripp,* 737 So. 2d at 601-602).

The Supreme Court of Florida restated the rule in *Auto Owners Ins. Co. v. Pozzi Window Co.,* 984 So. 2d 1241, 1248 (Fla. 2008), stating: "There is a difference between a claim for the costs of repairing or removing defective work, which is not a claim for 'property damage,' and a claim for the costs of repairing damage caused by the defective work, which is a claim for 'property damage.'"). Thus, if there is no damage beyond the faulty workmanship or defective work, then there is no resulting "property damage." *Id.* See also 9A *Russ and Segala Couch on Ins.,* §129:6 (3rd Ed.) ("The costs incurred to repair a defective product or defective work do not constitute property damage under a commercial general liability policy."); *Assurance Co. of America v. Lucas Waterproofing Co.,* 581

Supp. 2d 1201, 1209 (S.D. Fla. 2008)(applying *JSUB* and *Pozzi Windows* and finding that although the cost of repairing other components of the work damaged because of defective waterproofing was "property damage," the cost of removing and replacing the defective waterproofing itself was not "property damage"); *Arnett v. Mid-Continent Cas. Co.,* 2010WL2821981 (S.D. Fla. 2010)(applying *JSUB* and *Pozzi Windows* to a general contractor's policy and stating that under Florida law, "[c]overage therefore extends to costs to repair damages caused by construction defects, but not to repair or replace the defective work itself").

The opinion of the Southern District of Florida in *Assurance Company of America v. Lucas Waterproofing Co. Inc.,* 581 F.Supp.2d 1201 (S.D. Fla.2008) is also relevant. That case involved an insurance coverage dispute arising out of construction defects in work performed on condominium complexes in Vero Beach, Florida. There, it was claimed that membrane waterproofing under cast stone pavers on the porches of the condominiums had been defectively installed. The work was completed on July 25, 1999, and shortly thereafter the buildings were exposed to wind and rain from Hurricanes Floyd and Irene. The owner brought suit against the contractor alleging construction design defects in the buildings, "including property damage caused by water inside the decorative soffit beams under the balconies, resulting in peeling and bubbling paint and mildew

growth, as well as stucco discoloration or efflorescence." *Lucas Waterproofing,* 581 F.Supp.2d at 1204.

In considering the coverage issues raised by that case, the court reviewed the insurance policy's provisions regarding "property damage" caused by an "occurrence." *Id.* at 1209. There, the pertinent policies defined "property damage" as "physical injury to tangible property, including all resulting loss of use of that property." *Id.* That is, of course, the same definition as in the policies in the present case. The court stated the following regarding what was and was not "property damage":

> A claim for the cost of removing or repairing defective work does not constitute a claim for "property damage." A claim for the cost of repairing damage of other elements of the subject property that was caused by the defective work is a claim for "property damage" under a CGL policy.
>
> Thus, any claim for costs incurred by repairing the defective waterproofing is not covered by the TransContinental policies. However, costs incurred by repairing damages to other parts of the buildings that were damaged as a result of the defective waterproofing constitutes "property damage" and may be covered by the TransContinental policies.

Id.

The court's ultimate ruling in that case was that the insurance policy did not provide liability insurance coverage for the owner's claim for repairs of the defective work, but that the insurance policy would provide coverage only to the

extent that the defective work damaged other portions of the buildings including the soffit beams, stucco, and peeling and bubbling paint. *Id.*

Applying the above cases to the facts of this case, it is clear that the district court erred as a matter of law in finding that all of Carithers' damages were for "property damage." Specifically, the court erred in finding that damages associated with outdoor tiles ($7,500), brick coating ($9,425), and a defective balcony ($3,325) were for "property damage." [D.E. 126].

The first item of damage listed on the Judgment is replacement of the mud base under Carithers' outdoor patio stone tiles. [D.E. 71-3]. There was nothing wrong with the mud base itself, it was allegedly just the wrong mud base for that specific function, which caused some tiles to crack. [Tr. at pg. 84, lines 10-14]. The testimony was undisputed that the installation of the mud base and the tiles was performed by a single subcontractor, thus they constituted a single component of the work. [Tr. at pg 66, lines 20-25]. It was also undisputed that the mud base and tiles did not cause any physical damage to any other component of the work. Therefore, under *J.S.U.B.* and the other cases cited above, including this Court's decision in *Amerisure Mut. Ins. Co. v. Auchter Co.,* 673 F.3d 1294 (11th Cir. 2012), the damages awarded for mud base and tile replacement were not for "property damage." Just as in *Auchter Co.,* where this Court stated that under Florida law a general contractor's CGL policy did not provide coverage for the

removal of a defective roof installed by the roofing subcontractor that did not damage any other subcontractor's work because the removal and replacement of the roof did not constitute "property damage," the removal/repair/replacement of mud base and tile in this case cannot constitute "property damage."

Carithers' counsel argued below that the stone tiles had actually been purchased by Carithers. But that does not take the tiles outside the definition of "your work," which is:

> **22.** "Your work":
>
> **a.** Means:
>
> **(1)** Work or operations performed by you or on your behalf; and
>
> **(2)** **Materials, parts or equipment furnished in connection with such work or operations.**

[D.E 69-4, 5, 6, 7 at V (22)](Emphasis added).

Therefore, the removal and/or replacement of the mud base and the tiles does not constitute damages because of "property damage," because no matter who purchased the tiles it was all the insured's defective work, which did not cause damage to any other component of the work.

Carithers was also awarded $9,425.00 in damages for installation of protective coating on exterior porous brick where the original Boral coating on that brick failed. [D.E 71-3]. It was undisputed that a single masonry subcontractor installed the brick and the Boral coating, and the testimony was also undisputed

that the masonry subcontractor's work did not damage any other component of the work, only his own work. [Tr. at pg. 97, lines 3-9]. Therefore, as with the mud base and tiles, the damages awarded in connection with the brick work were not for "property damage" under MCC's CGL policy pursuant to *J.S.U.B.*, *Pozzi Windows, Auchter* and the other cases cited above.

Third, Carithers was awarded $3,325 for the replacement of a defective balcony. [D.E. 71-3] The testimony was undisputed that the defective balcony installation caused damage to itself. [Tr. at pg. 98, lines 18-21]. Thus, like the mud base/tiles and the brick/coating damages, the damages awarded in connection with the replacement of the balcony were not because of "property damage" under an MCC policy.

In summary, the court erred as a matter of law in awarding damages in connection with the mud base and tiles, the brick and coating, and the balcony, because none of those damages were for "property damage" under Florida law as that term has been interpreted by this Court and Florida's state and federal courts.

C. THE DISTRICT COURT ERRED AS A MATTER OF LAW IN RELYING ON AN INAPPLICABLE STATUTE TO DENY MCC'S MOTION FOR LEAVE TO AMEND ITS PLEADINGS TO CONFORM TO THE EVIDENCE.

Rule 15(b) permits pleadings to be amended "to cause them to conform to the evidence and to raise...issues [not raised by the pleadings]" and codifies the rule of conforming the allegations to the evidence. Rule 15(b) is "intended to

promote the objective of deciding cases on their merits rather than in terms of the relative pleading skills of counsel or on the basis of a statement of the claim or defense that was made at a preliminary point in the action and later proves to be erroneous." 6A *Wright & Miller* § 1491 at 5-6. Indeed, the law favors amendments to pleadings, especially after discovery has closed. "Amendments to conform to the evidence *are desirable* because they bring the pleadings in line with the issues that actually were developed at trial; this is permitted even though material inserted by amendment was not presented by the pleadings as originally drawn." 6A *Wright & Miller* § 1493 at 15 (emphasis added).

The Eleventh Circuit particularly favors motions to amend under Rule 15(b). In *Menendez v. Perishable Distributors, Inc.*, 763 F.2d 1364, 1379 (11th Cir. 1985), the Court of Appeals stressed that "Rule 15(b) authorizes the district court to permit belated amendments and directs the court to 'do so freely when the presentation of the merits of the action will be subserved thereby'." (citing Fed. R. Civ. P. 15(b)).

Rule 15(b) specifically states that a motion for amendment of the pleadings to cause them to conform with the evidence may be made by "any party at any time; even after judgment." "Rule 15(b) permits the motion [to conform the pleadings to the evidence] to be made throughout the entire period during which the action is in the district court ...." 6A *Wright & Miller* § 1494 at 51. Thus, in

American Eagle Credit Corp. v. Select Holdings, Inc., 865 F. Supp. 800 (S.D. Fla. 1994) (Moore, J.), a fraud case, the district court applied Rule 15(b) to amend the Complaint after the conclusion of a bench trial to conform the Complaint to the evidence presented at trial. Rejecting defendant's protest that the amendment came too late, the court drew the distinction between an amendment that would set forth a new claim, and one that would only state an additional theory of liability. The court stated that the amendment did not "seek to assert an entirely new cause of action," but only "a new theory of liability. The underlying claim for fraud...remains constant." 865 F. Supp. at 809-10. The court emphasized that application of Rule 15(b) was required to avoid "[l]ocking parties into the strict language of their pleadings," thereby creating "a 'tyranny of formalism' inhibiting courts from adjudicating cases on their merits." 865 F. Supp. at 809, quoting *In re Santa Fe Downs, Inc.,* 611 F.2d 815, 817 (10th Cir. 1980).

In this action, on the first day of trial Carithers expert witness Brett Newkirk testified for the first time that wood rot cannot exist but for the presence of fungus. Carithers had not pleaded damage as a result of fungus. [Tr. at 113, lines 2-25 – 114, lines 1-4]. MCC therefore moved to conform its pleadings to the evidence that wood rot is not caused solely by water, that fungus must also be present in addition to water. [Tr. at 141]. Counsel for MCC argued as follows:

> MR. CATIZONE: Before we rest, Your Honor, we want to file an ore tenus motion to amend the pleadings to conform to the evidence and

> as -- specifically with respect to Mr. Newkirk's testimony. Mr. Newkirk, in his affidavit, talked about water damage, and there was nothing in his expert testimony about mold or fungi. There was only testimony --
>
> THE COURT: Well, that's right, yeah.
>
> MR. CATIZONE: -- in his affidavit. But in his testimony, he testified that water doesn't cause wood rot; fungus causes wood rot. That was Mr. Newkirk's testimony here at trial. Okay. Now, the only reason -- I want to ask the pleadings to be conformed to the evidence is because this is the first time anybody in this case has asserted that the wood rot was caused by fungus. We need to amend our answer to conform to the evidence. All four of our policies include a mold, fungi, mildew exclusion, which we never raised in our answer because they never alleged mold originally; they never alleged fungi. There was no testimony about fungi until Mr. Newkirk made that definitive statement, water doesn't cause wood rot; fungus causes wood rot. So based on that testimony, which we ask that we be allowed to amend our answer to include our fungus exclusion, because it was never an issue until today.

The district court found after argument on the issue that:

> Now as to whether we - - first of all, I specifically exclude anything with respect to the subject of mold because it was declined all the way through. But I think the thing this case involves is the subject of wood rot. Specifically, how wood rot comes into play is not, frankly a concern in this case. The concern is that there was wood rot and there was wood rot because of defective construction, and that's what's the issue facing this Court. And I don't think we need to concern ourselves anymore with this. [Tr. at 143-44].

Accordingly, MCC's motion to conform the pleadings to the evidence was denied after argument on the issue. Thereafter, the district court found in its Order on Indemnity [D.E. 126 at fn 2]:

> One of Plaintiffs' witnesses, Brett Douglas, testified that the wood rot in Plaintiffs'garage developed because the water incursion allowed microscopic "critters" such as fungi to grow in the wood. (Tr. at 113.) Mid-Continent then argued that the Policy would exclude coverage for damage to the garage because the Policy contains a "Fungus, Mildew and Mold Exclusion." (Policy at ML 12 17 (04 01).) But Mid-Continent has been aware since the inception of this matter that the damage to the garage was caused by wood rot, which is by definition "decomposition from the action of bacteria or fungi." Definition of verb "rot,"www.merriam-webster.com/dictionary/rot (last visited March 3, 2014). Mid-Continent cannot now rely on an exclusion that it has never before mentioned in this litigation.

The district court's order misses the point entirely. MCC was not arguing that it did not know about wood rot or fungus. MCC was arguing that its pleadings should be conformed to the evidence that wood rot is not only caused by "repeated wettings" as previously disclosed, but that there must exist fungus *combined with* water in order for wood rot to occur. It was not pleaded by Carithers, and this testimony was not disclosed before trial, as Mr. Newkirk did not disclose an opinion that wood rot cannot exist but for the presence of fungi. Thus, MCC's motion should have been granted, and the district court erred as a matter of law in denying said motion. It seemed, at least when argued at trial, that the district court had concluded that if property damage was caused by construction defects the exclusion had no application. The decision to write the exclusion out of the policy and/or the conclusion that the exclusion would not apply constitute legal error.

The district court also improperly relied on Section 627.426(2) in its Order [D.E. 126 at fn 2] in ruling that MCC could not amend its pleadings to rely on the

"Fungus, Mildew and Mold Exclusion." By its express terms, Section 627.426(2) can create an estoppel where an insurer fails to properly reserve rights with respect to a "particular coverage defense." In interpreting that statute, the Supreme Court of Florida has stated that the statute only applies to coverage defenses based on conditions such as late notice, and not to exclusions. *AIU Ins. Co. v. Block Marina Investment, Inc.,* 544 So. 2d 998 (Fla. 1989).The court stated:

> We do not construe the term to include a disclaimer of liability based on a complete lack of coverage for the loss sustained. Under this construction, for example, if the insurer fails to comply with the requirements of the statute, it may not declare a forfeiture of coverage which otherwise exists based on a breach of a condition of the policy. However, its failure to comply with the requirements of the statute will not bar an insurer from disclaiming liability where a policy or endorsement has expired or where the coverage sought is expressly excluded or otherwise unavailable under the policy or under existing law.

AIU, 544 So. 2d at 999.

Because §627.426 does not apply to exclusions, the district court erred as a matter of law in relying on that section in denying MCC's motion for leave to amend the pleadings. Based on the expert's trial testimony that wood rot cannot exist in the absence of fungus, and the liberal rule regarding amendment of pleadings to conform to the evidence, the court should have allowed the amendment. The court's misinterpretation of §627.426 constitutes legal error and must be corrected by this Court.

It is undisputed that with the exception of damaged appliances, virtually all damages other than those discussed above in connection with the tiles, brick and balcony were because of "property damage" caused by wood rot, i.e., by fungus. Therefore, this Court should find that MCC's motion for leave should have been granted and that its "fungus, mildew and mold" exclusion bars coverage for all damages associated with wood rot.

CONCLUSION

For the reasons stated herein, this Court should reverse the judgment of the district court and remand for judgment to be entered in favor of MCC.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I HEREBY CERTIFY that this brief complies with the type-volume limitation set forth in Federal Rules of Appellate Procedure 32(a)(7)(B). This brief contains 8,977 words.

/s/ John R. Catizone
JOHN R. CATIZONE

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of *Brief of Appellant* was furnished by U.S. Mail on this 22nd day of July, 2014, to the following:

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