



1997

Notes: Sheets v. Brethren Mutual: Maryland's High Court Misconstrues CGL to Cover Excluded Economic Loss Caused by Negligent Misrepresentation

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Recommended Citation

Lawrence, Gregory T. (1997) "Notes: Sheets v. Brethren Mutual: Maryland's High Court Misconstrues CGL to Cover Excluded Economic Loss Caused by Negligent Misrepresentation," *University of Baltimore Law Review*: Vol. 27: Iss. 1, Article 7.
Available at: <http://scholarworks.law.ubalt.edu/ublr/vol27/iss1/7>

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SHEETS v. BRETHERN MUTUAL: MARYLAND'S HIGH COURT MISCONSTRUES CGL TO COVER EXCLUDED ECONOMIC LOSS CAUSED BY NEGLIGENT MISREPRESENTATION

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I. INTRODUCTION

Liability insurance plays an essential role in modern society.¹ By pooling risk,² insurers enable businesses to use funds that would otherwise be retained to self-insure against potential liability.³ Society in general benefits from liability insurance in at least two re-

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1. One commentator opined that liability insurance is the lifeblood of capitalism: "Cease [the] institution [of liability insurance] and every industrial wheel, from the watchmaker's tiny mainspring to the turbines of the power plant, will cease its revolutions. No manufacturer, railroader, fabricator, druggist or industrialist will continue to risk his fortune." Melvin M. Belli, *The Social Value of Liability Insurance*, 13 HASTINGS L.J. 169, 172 (1961); accord Peter J. Neeson & Phillip J. Meyer, *The Comprehensive General Liability Policy and Its Business Risk Exclusions: An Overview*, in REFERENCE HANDBOOK ON THE COMPREHENSIVE GENERAL LIABILITY POLICY: COVERAGE PROVISIONS, EXCLUSIONS, AND OTHER LITIGATION ISSUES 75, 83 (Peter J. Neeson ed., 1995) ("[I]nsurance is an economic necessity without which industry could not function.").
 2. For a summation of risk pooling techniques and pitfalls, see George Priest, *The Current Insurance Crisis and Modern Tort Law*, 96 YALE L.J. 1521, 1539-50 (1987).
 3. See *id.* at 1539 ("Insurance provides a method for [insureds] to equalize the amount of money available to them over diverse states of the world—states in which losses occur and those in which there are no losses."); Laurie Vasichek, Note, *Liability Coverage for "Damages Because of Property Damage" Under the Comprehensive General Liability Policy*, 68 MINN. L. REV. 795, 795 (1984); see also Terri D. Keville, Note, *Advertising Injury Coverage: An Overview*, 65 S. CAL. L. REV. 919, 921 (1992) ("Insurers are excellent loss spreaders because they are able to pool risk."); Priest, *supra* note 2, at 1542 ("[A]n insurer is an agent for the diversification of risk.").

spects.⁴ First, an increase in the flow of money creates a more active economy.⁵ Second, insurers provide funds necessary to satisfy judgments.⁶ However, the relationships between insurers, insureds, and society do not exist in a vacuum. Poorly drafted policies⁷ and misguided judicial opinions⁸ undermine the arrangements, resulting in negative economic consequences such as steep premiums and coverage curtailment.⁹ Thus, it is essential that insurers, insureds, practitioners, and judges all fully appreciate the scope and limitations of liability policies.¹⁰

The primary vehicle of business liability insurance is the Comprehensive/Commercial General Liability Insurance¹¹ Policy

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4. Commentators have noted various additional ways society benefits from liability insurance. See, e.g., Priest, *supra* note 2, at 1540 n.101 (noting that insurers may persuade insureds to decrease risk); Keville, *supra* note 3, at 920 (noting insurance system's impact on the reduction of accidents by means of deterrence).
 5. See Vasichek, *supra* note 3, at 795 (“[C]ommodity prices decrease in proportion to the lower cost of protection, and psychological inhibition to expansion and innovation caused by gambling on the chance of liability are reduced.”).
 6. See *id.* at 795-96 (“[T]he public . . . also is assured the continued protection of products liability law made viable by the availability of funds to pay judgments.”).
 7. See *id.* at 796 (“The efficacy of liability insurance is purely illusory . . . when policies do not adequately delineate the liability risks transferred.”).
 8. See Keville, *supra* note 3, at 922 (“When courts find coverage where none was mutually intended, they further undermine the ability of insurers to predict future losses. This situation in turn makes it extremely difficult for insurers to price insurance accurately and fairly.”).
 9. Reduction in the availability of liability insurance may affect consumers, especially those with low incomes. See Priest, *supra* note 2, at 1585-87.
 10. If liability insurance is not conveyed clearly and interpreted correctly, it merely replaces the gamble of potential liability with the gamble of coverage. See Vasichek, *supra* note 3, at 796.
 11. The Comprehensive General Liability Policy was renamed the “Commercial General Liability Policy” in 1986. See Keville, *supra* note 3, at 919 n.1, quoted in *Bailer v. Erie Ins. Exch.*, 344 Md. 515, 533 n.5, 687 A.2d 1375, 1384 n.5 (1997). The name was changed because insurers believed the term “comprehensive” might invite courts to expand coverage beyond the parties’ intentions. See *id.*, cited in *Bailer*, 344 Md. 515, 533 n.5, 687 A.2d at 1384 n.5; cf. George H. Tinker, *Comprehensive General Liability Insurance—Perspective and Overview*, 25 FED’N INS. COUNS. Q. 217, 220 (1975). Prior to the renaming of the CGL, one commentator noted that the CGL “is ‘comprehensive’ only in the sense that it combines certain historic forms of coverage into an integrated whole [It] is not, and was never conceived to be, an ‘all-risk’ liability policy.” Tinker, *supra*, at 220.

(CGL).¹² The CGL is a standardized form policy that provides both liability and litigation protection for the insured.¹³ The litigation protection, known as the "duty to defend," is important for two reasons. First, because litigation costs can be staggering, the duty to defend provides a substantial economic benefit to the insured.¹⁴ Second, because there is no duty to defend unless a claim is potentially covered under the policy, duty to defend precedent serves as a bellwether to the scope of coverage afforded by policies.¹⁵

This Note examines the Maryland Court of Appeals's decision in *Sheets v. Brethren Mutual Insurance Co.*,¹⁶ a case which the United States Supreme Court found enlarged the scope of coverage afforded by CGLs under Maryland law.¹⁷ In *Sheets*, the court of appeals addressed whether a CGL¹⁸ provides coverage for damages

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12. See, e.g., Robert M. Tyler, Jr. & Todd J. Wilcox, *Pollution Exclusion Clauses: Problems in Interpretation and Application Under the Comprehensive General Liability Policy*, 17 IDAHO L. REV. 497, 498 (1981) (noting that all types of business ventures use CGLs for liability protection); see also Steven E. Leder, *Commercial General Liability*, in SECOND ANNUAL INSURANCE LAW INSTITUTE C-1, C-1 (Maryland Institute for Continuing Professional Education of Lawyers, Inc. ed. 1997) ("The 'Commercial General Liability Policy' . . . forms the backbone of liability protection for business owners.").
 13. See Leder, *supra* note 12, at C-1.
 14. One commentator opined that the duty to defend is one of the most important benefits the insured receives in a standard liability policy. See Andrew Janquitto, *Insurer's Duty to Defend in Maryland*, 18 U. BALT. L. REV. 1, 53 (1988). The duty to defend is important to insurers because it enables them to gain control over the litigation and settlement process. See *id.* at 3.
 15. See generally, e.g., *Gov't Employees Ins. Co. v. Ropka*, 74 Md. App. 249, 257, 536 A.2d 1214, 1218 (1988) ("It is generally true that an insurer has no duty to defend a cause of action against an insured if that cause of action asserts liability on the part of the insured that comes within an exclusion in the insurance policy.").
 16. 342 Md. 634, 679 A.2d 540 (1996).
 17. See *Lords Landing Village Condominium Council of Unit Owners v. Continental Ins. Co.*, 117 S. Ct. 1731, 1733 (1997) (per curiam) (remanding insurance coverage case back to the United States Court of Appeals for the Fourth Circuit in light of *Sheets*).
 18. The policy at issue in *Sheets* was a farm owner's general liability policy. See *Sheets*, 342 Md. at 638, 679 A.2d at 541-42. Farm owner's liability insurance is merely a slightly modified CGL. See generally 7A JOHN ALAN APPLEMAN, *INSURANCE LAW AND PRACTICE* § 4501.17, at 292 (Walter F. Berdal ed. 1979) (noting that farm owner's policies should be construed substantially the same as other liability policies and calling this type of policy a "comprehensive farm liability policy"); 1 ROWLAND H. LONG, *THE LAW OF LIABILITY INSURANCE* § 3.07[10] (1992) (noting that the distinction between a standard CGL and a farm owner's policy is the definition of the term "insured").

arising from negligent misrepresentations.¹⁹ In deciding this issue, the court made the following conclusions of Maryland insurance law: (1) ordinary negligence constitutes an “accident” if the insured neither expected nor intended the resulting damage;²⁰ (2) negligent misrepresentation constitutes an “accident” if the insured neither foresaw nor expected the resulting damage;²¹ and (3) loss of use of a defective septic system constituted property damage under the so called “loss of use” prong.²²

Part II of this Note examines the underpinnings of the *Sheets* opinion: the rules governing construction of insurance contracts, the duty to defend, the judicial gloss placed on selected terms in the CGL (“occurrence” and “property damage”), the tort of negligent misrepresentation, and a survey of jurisdictions that already have addressed whether CGLs cover damages caused by negligent misrepresentations. Part III of this Note provides a detailed account of the facts, holding, rationale, and dissent in *Sheets*. In Part IV, this Note contends that *Sheets* was wrongly decided because the court of appeals misconstrued the loss of use prong to provide coverage for economic loss of the sort not covered under CGLs. This Note further contends that two policy exclusions, which were neither raised by the insurer nor considered by the *Sheets* court, precluded coverage for the underlying claim: the “loss of use” and “premises alienated” exclusions.²³ Conversely, this Note concludes that the *Sheets* majority clarified the murky distinctions regarding the term “accident,” correctly concluding that ordinary negligence and negligent misrepresentations could constitute an accident, provided that the insured did not subjectively intend or expect the resulting damage.

II. BACKGROUND

A. *The Three Tiers of Policy Construction Under Maryland Law*

Unlike some jurisdictions, Maryland courts purport not to con-

19. See *Sheets*, 342 Md. at 636-37, 679 A.2d at 541. The underlying suit settled before the case reached the Court of Appeals of Maryland. See *id.* at 638, 679 A.2d at 542. Because the terms of settlement were not available, the court of appeals only addressed the duty to defend, not the duty to indemnify. See *id.*

20. See *id.* at 652, 679 A.2d at 548.

21. See *id.* at 657, 679 A.2d at 551 (quoting *Harleysville Mut. Cas. Co. v. Harris & Brooks, Inc.*, 248 Md. 148, 154, 235 A.2d 556, 559 (1967)).

22. See *id.* at 645, 679 A.2d at 545.

23. This Note also raises the issue of whether a third exclusion, the “owned property” exclusion, also precluded coverage.

strue insurance policies most strongly against the insurer.²⁴ Rather,

24. See, e.g., *Cheney v. Bell Nat'l Life Ins. Co.*, 315 Md. 761, 766, 556 A.2d 1135, 1138 (1989). The *Cheney* court declared, "Maryland does not follow the rule, adopted in many jurisdictions, that an insurance policy is to be construed most strongly against the insurer." *Id.* However, it is unclear which rule of construction adopted in other jurisdictions the court of appeals was referring to when it distinguished Maryland law from other jurisdictions.

There are two primary doctrines of insurance law construction that courts generally use to construe policies against insurers: the doctrine of *contra proferentum* and the doctrine of reasonable expectations. With certain qualifications, the doctrine of *contra proferentum* directs that courts construe ambiguous policy terms against the insurer as drafter of the policy. See, e.g., *Bailer v. Erie Ins. Exch.*, 344 Md. 515, 522, 687 A.2d 1375, 1378 (1997) (construing ambiguous terms against an insurer only if ambiguity remains after considering extrinsic evidence). See generally, 2 LEE R. RUSS, COUCH ON INSURANCE § 22:18 (3d ed. Supp. 1996) ("[T]he doctrine of *contra proferentum* . . . construes the policy against [the] insurance company . . ."). In some form, the doctrine of *contra proferentum* is the law in every state and the District of Columbia. See *Kunin v. Benefit Trust Life Ins. Co.*, 910 F.2d 534, 538-39 (9th Cir. 1990); see also 13 JOHN ALAN APPLEMAN & JEAN APPLEMAN, INSURANCE LAW AND PRACTICE § 7401, at 197 n.1 (1975) (noting near unanimity of courts applying the doctrine of *contra proferentum*). See generally Michael B. Rappaport, *The Ambiguity Rule and Insurance Law: Why Insurance Contracts Should Not Be Construed Against the Drafter*, 30 GA. L. REV. 171, 173 n.2 (1995) (noting that the doctrine of *contra proferentum* is also known as the "ambiguity rule"). One factor that distinguishes whether a jurisdiction is more or less favorable to insurers is how aggressively courts in that jurisdiction invoke the doctrine of *contra proferentum*. See JEFFREY W. STEMPER, INTERPRETATION OF INSURANCE CONTRACTS § 5.8, at 196-97 (1994) (separating jurisdictions into three categories: "strong," "moderate," and "weak").

The second doctrine of construction, the doctrine of reasonable expectations, directs that "objectively reasonable expectations of [insureds] regarding terms of insurance contracts will be honored even though [a] painstaking study of the policy provisions might have negated those expectations." Robert E. Keeton, *Insurance Law Rights at Variance with Policy Provisions*, 83 HARV. L. REV. 961, 967 (1970). The doctrine of reasonable expectations is the law in approximately half of the states; Maryland courts do not apply this doctrine. See STEMPER, *supra*, § 11.1, at 312 & n.8.

In a dispute over a manuscript policy, Maryland law is arguably more favorable to the insured than jurisdictions that more readily construe policies against the insurer. See generally 2 RUSS, *supra*, § 22:18. A manuscript policy contains provisions that are specifically negotiated between the insurer and the insured, *i.e.*, the policy is not a standard form policy. See *Maryland Cas. Co. v. Armco, Inc.*, 822 F.2d 1348, 1350 (4th Cir. 1987) (noting that the policy at issue was " 'manuscript' in several instances: that is, some provisions are negotiated and specifically written for this insured"), *cited with disapproval in Bausch & Lomb, Inc. v. Utica Mut. Ins. Co.*, 330 Md. 758, 781, 625 A.2d 1021, 1032 (1993) (disagreeing with the *Armco* court's construction of the term

courts construe insurance policies, like other contracts, as a whole to effectuate the intentions of the parties.²⁵

There are roughly three tiers of analysis for construing insurance policies under Maryland law: (1) determining whether terms are ambiguous and construing unambiguous terms without reference to extrinsic evidence; (2) construing ambiguous terms by considering extrinsic evidence, looking first to persuasive authority from other jurisdictions that have already construed the term; and (3) construing terms that remain ambiguous against the insurer as drafter of the document.

In the first tier of analysis, Maryland courts attempt to confine their inquiry to the language in the policy.²⁶ Unless expressly defined in the policy, words are given their customary meaning, measured by the reasonable expectations of the prudent layperson.²⁷

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- "damages"). In at least one jurisdiction that readily construes policies against the insurer, courts do not construe the manuscript policies against the insurer even if the terms are ambiguous. *See Koch Eng'g Co. v. Gibraltar Cas. Co.*, 878 F. Supp. 1286, 1288 (E.D. Mo. 1995) (applying Missouri law; reasoning that manuscript policies should not be construed against insurers because they are negotiated between two equal parties on a level playing field). Conversely, Maryland law makes no such distinction. If ambiguity remains after considering extrinsic evidence, Maryland courts construe the policy against the insurer as drafter of the document regardless of whether the policy is a manuscript policy or a standard form policy. *See Cheney*, 315 Md. at 766-67, 556 A.2d at 1138; *see also, e.g., Armco*, 822 F.2d at 1350-53 (construing manuscript policy by applying Maryland law without special rules of construction).
25. *See Pacific Indem. Co. v. Interstate Fire & Cas. Co.*, 302 Md. 383, 388, 488 A.2d 486, 488 (1985); *Bond v. Pennsylvania Nat'l Mut. Cas. Ins. Co.*, 289 Md. 379, 384, 424 A.2d 765, 768 (1981); *see also Sullins v. Allstate Ins. Co.*, 340 Md. 503, 508, 667 A.2d 617, 619 (1995); *Aragona v. St. Paul Fire & Marine Ins. Co.*, 281 Md. 371, 375, 378 A.2d 1346, 1348 (1977). *But cf. George K. Hartwick, How to Read a Liability Insurance Policy*, 13 HASTINGS L.J. 175, 175 (1961) ("An insurance policy is of course a contract; but it is no longer possible to approach an insurance problem simply by resorting to the law of contracts. A substantial body of law has developed which is particularly applicable to contracts of insurance, and different from that applicable to contracts generally.").
 26. *See Pacific Indem. Co.*, 302 Md. at 389, 488 A.2d at 489; *see also Board of Trustees of State Colleges v. Sherman*, 280 Md. 373, 380, 373 A.2d 626, 629 (1977) ("[W]here a contract is plain and unambiguous, there is no room for construction, and it must be presumed that the parties meant what they expressed . . .").
 27. *See Bausch & Lomb*, 330 Md. at 779, 625 A.2d at 1031; *Cheney*, 315 Md. at 766, 556 A.2d at 1138; *see also Simkins Indus., Inc. v. Lexington Ins. Co.*, 42 Md. App. 396, 405, 401 A.2d 181, 186 (1979) (stating that courts should view terms from the perspective of a "reasonably prudent person applying for insurance, rather than from view of lawyer"); *cf. Catalina Enters., Inc. Pension Trust v.*

However, if evidence shows that the parties intended to employ a term in a specialized or technical sense, the court should proceed to the second tier of analysis.²⁸

In determining reasonable expectations, one factor courts consider is the purpose of the contract.²⁹ Courts also examine the policy's character, as well as the facts and circumstances at the time of execution.³⁰ Terms in insurance policies must be read in the context of the entire document, not according to any single clause, phrase, or section.³¹ The terms control unless they violate a statute, regulation, or public policy.³² Absent controlling authority, Maryland courts faced with construing a new term or provision must inquire: "What is the customary and normal meaning of [the term] in the context of [the type of policy being construed]?"³³

The Court of Appeals of Maryland has used three sources to ascertain the customary and normal meaning of policy terms: "*Webster's Dictionary*, *Random House Dictionary*, [and], less often, *Black's*

Hartford Fire Ins. Co., 67 F.3d 63, 66 (4th Cir. 1995) ("It is axiomatic under Maryland law that a court should avoid reading [an insurance] contract in a way that produces an absurd result, especially when a reasonable interpretation is available.").

28. See *Sullins*, 340 Md. at 508, 667 A.2d at 619 (stating that words are given their ordinary meaning "unless there is an indication that the parties intended to use the words in a technical sense").
29. See *Collier v. MD-Individual Practice Ass'n*, 327 Md. 1, 6, 607 A.2d 537, 539 (1992) ("One factor in determining the ordinary and accepted meaning of a contract term is the purpose of the contract.").
30. See *Pacific Indem. Co.*, 302 Md. at 388, 488 A.2d at 488.
31. See *Teamsters Local 639-Employers Health Trust v. Reliable Delivery Serv., Inc.*, 42 Md. App. 485, 488-89, 401 A.2d 191, 194 (1979), cited in *Catalina*, 67 F.3d at 66.
32. See, e.g., *Mutual Fire, Marine & Inland Ins. Co. v. Vollmer*, 306 Md. 243, 250, 508 A.2d 130, 133 (1986). The court of appeals has been reluctant to void coverage on the grounds that it is against public policy. See generally, e.g., *Bailer v. Erie Ins. Exch.*, 344 Md. 515, 535, 687 A.2d 1375, 1385 (1997) (holding that insuring against intentional invasion of privacy is not against public policy); *First Nat'l Bank of St. Mary's v. Fidelity & Deposit Co.*, 283 Md. 228, 241-43, 389 A.2d 359, 366-67 (1978) (holding that insuring against punitive damages is not against public policy).
33. *Collier*, 327 Md. at 6, 607 A.2d at 539. In *Collier*, the court of appeals stated, "In the absence of a controlling legal definition . . . the question becomes, 'What is the customary and normal meaning of "full-time student" in the context of a group health insurance policy?' " *Id.*; cf. *Bausch & Lomb*, 330 Md. at 779, 625 A.2d at 1031 ("A word's ordinary signification is tested by what meaning a reasonably prudent layperson would attach to the term.").

Law Dictionary.”³⁴ Correspondingly, ambiguities arise if a reasonably prudent layperson would conclude that the language is susceptible to more than one meaning.³⁵ Conflicting judicial interpretations in other jurisdictions are evidence of ambiguity.³⁶ However, terms in an insurance policy may be ambiguous in one context and not in another.³⁷

In the second tier of analysis, Maryland courts construe ambiguous terms by considering extrinsic evidence.³⁸ Judicial construction of the term in other jurisdictions is the first level of extrinsic evidence a court consults when faced with an ambiguity.³⁹ Precedents from other jurisdictions provide guidance for construing ambiguous terms because, like states that adopt uniform statutes, parties adopting an insurance policy that has been construed across the nation adopt the policy with the construction it has received in other states.⁴⁰ Indeed, while a court may find a term ambiguous on its

34. *Pacific Indem. Co.*, 302 Md. at 388, 488 A.2d at 488.

35. *See, e.g.*, *Truck Ins. Exch. v. Marks Rentals, Inc.*, 288 Md. 428, 433, 418 A.2d 1187, 1190 (1980); *Pacific Indem. Co.*, 302 Md. at 338, 488 A.2d at 489 (“The language used may be ambiguous if it is ‘general’ and may suggest two meanings to a reasonably prudent layperson.”). For an in-depth discussion of ambiguity, see Rappaport, *supra* note 24, at 178-87.

36. *See Sullins v. Allstate Ins. Co.*, 340 Md. 503, 518, 667 A.2d 617, 624 (1995) (“[I]f other judges [from other jurisdictions] have held alternative interpretations of the same language to be reasonable, that certainly lends some credence to the proposition that the language is ambiguous and must be resolved against the drafter.”). Nevertheless, Maryland courts must still undertake an independent inquiry to determine whether a term is ambiguous. *See id.* at 517-18, 667 A.2d at 624 (noting that a court would be abdicating its judicial role if it did not engage in an independent inquiry despite authority from other jurisdictions).

37. *See, e.g., Sullins*, 340 Md. at 508, 667 A.2d at 619. In *Sullins*, for example, the court of appeals held that a “pollution exclusion” clause was ambiguous as applied to lead paint, *see id.* at 516, 667 A.2d at 623, thereby implying that the clause unambiguously excluded coverage for chemical spills. *See id.* at 516 n.2, 667 A.2d at 622 n.2 (noting that most cases upholding application of the pollution exclusion involved “environmental exposure”).

Regarding exclusions, the Court of Appeals of Maryland declared, “If the exclusion totally swallows the insuring provision, the provisions are completely contradictory. That is the grossest form of ambiguity . . . [and the insurer] would be obligated to defend and indemnify.” *Bailer*, 344 Md. at 525, 687 A.2d at 1380.

38. *See, e.g., id.* at 508, 667 A.2d at 619.

39. *See Pacific Indem. Co.*, 302 Md. at 401, 488 A.2d at 495.

40. *See id.* This rule was adopted by the court of appeals in *Stanely v. American Motorists Insurance Co.*, 195 Md. 180, 188, 73 A.2d 1, 4 (1950). The *Stanely* court

face, the court may nonetheless treat the term as unambiguous and adopt the construction placed on it by courts in other states.⁴¹

If no court has construed the term in a similar situation, or if there are conflicting constructions from other jurisdictions, the court then considers extrinsic evidence offered by the parties.⁴² In reality, however, useful extrinsic evidence is often unavailable.⁴³ A court construes the policy as a matter of law if there is no dispute of fact regarding the extrinsic evidence.⁴⁴ However, if there is a material dispute of fact pertaining to construction of the policy, it must be resolved at trial.⁴⁵

If no extrinsic evidence is offered that clarifies the ambiguity, courts proceed to the third tier.⁴⁶ In the third tier, courts construe the policy against the insurer as drafter of the document.⁴⁷ Again, either of two contingencies must have occurred to arrive at this tier: (1) the term was ambiguous and the parties did not offer extrinsic evidence to clarify the ambiguity; or (2) the term was ambiguous and resort to extrinsic evidence failed to clarify the ambiguity.

B. The Duty to Defend Under Maryland Law

Under CGLs, the insurer is obligated to provide both litigation and liability protection to the insured.⁴⁸ The protection afforded by

reasoned that this rule is a useful one, and, with respect to the insurer, it may be regarded as fact. *See id.* at 189, 73 A.2d at 4. Presumably, the *Stanely* court recognized that insurers, mostly multi-state businesses, would be privy to interpretations by courts in other states.

41. *See Fisher v. Tyler*, 284 Md. 100, 106-07, 394 A.2d 1199, 1203 (1978) (“[W]hile the contract term on its face may be ambiguous, which under other circumstances would ordinarily generate a jury question, the court in this situation may treat the term as unambiguous and, absent any factual dispute, adopt, as a matter of law, that construction placed on the language by the courts of other states.”).
42. *See Pacific Indem. Co.*, 302 Md. at 389, 488 A.2d at 489. For example, the construction placed on the policy by both parties before the dispute arose serves as an important aid to courts construing policies. *See, e.g., Hurt v. Pennsylvania Threshermen & Farmers’ Mut. Cas. Ins. Co.*, 175 Md. 403, 407, 2 A.2d 402, 404 (1938).
43. *See* STEMPER, *supra* note 24, § 5.2, at 182.
44. *See Pacific Indem. Co.*, 302 Md. at 389, 488 A.2d at 489.
45. *See id.*
46. *See id.* at 405, 488 A.2d at 497.
47. *See id.* This doctrine of construction is known as the doctrine of *contra proferentum*. *See supra* note 24.
48. *See, e.g., Brohawn v. Transamerica Ins. Co.*, 276 Md. 396, 409-10, 347 A.2d 842, 851 (1975); Janquitto, *supra* note 14, at 1-2.

the insurer's duty to defend is sometimes referred to as "litigation insurance."⁴⁹ Notably, the duty to defend is not a product of common law.⁵⁰ Rather, it is a contractual obligation, presumably bargained for between the parties.⁵¹

1. The Potentiality Rule

The CGL duty to defend clause provides as follows: "[T]he company shall have the right and duty to defend any suit against the insured seeking damages on account of such bodily injury or property damage, even if any of the allegations of the suit are groundless, false, or fraudulent"⁵² Under Maryland law, this clause has been interpreted as imposing a duty to provide a legal defense if there is a potentiality that the policy may cover a claim asserted against the insured.⁵³ If both claims covered under the policy and claims outside the policy are asserted against the insured, the insurer is usually obligated to provide a defense for all of the claims.⁵⁴

49. See *Brohawn*, 276 Md. at 410, 347 A.2d at 851 (referring to *International Paper Co. v. Continental Cas. Co.*, 320 N.E.2d 619, 621 (N.Y. 1974)); Janquitto, *supra* note 14, at 4 ("[L]iability insurance . . . is in reality litigation insurance as well.").

50. See *Riviera Beach Volunteer Fire Co. v. Fidelity & Cas. Co.*, 388 F. Supp. 1114, 1120 (D. Md. 1975); Janquitto, *supra* note 14, at 3 (citing, *e.g.*, *Steyer v. Westvaco Corp.*, 450 F. Supp. 384, 389 (D. Md. 1978)).

51. See *Brohawn*, 276 Md. at 409-10, 347 A.2d at 851; see also *All-Star Ins. Corp. v. Steel Bar, Inc.*, 324 F. Supp. 160, 163 (N.D. Ind. 1971); Janquitto, *supra* note 14, at 3; *cf. Steyer*, 450 F. Supp. at 394 (refusing to find a duty to defend where the policy explicitly disclaimed such duty). In *Brohawn*, the court of appeals noted that both the insurer and the insured have a vested interest in securing the duty to defend. See *Brohawn*, 276 Md. at 409-10, 347 A.2d at 851. The insured's interest is obvious—it protects the insured from the burden of paying for a legal defense. See *id.* at 409, 347 A.2d at 851. The insurer's interest is in controlling litigation that could result in its duty to indemnify. See *id.* at 410, 347 A.2d at 851.

52. 7C APPLEMAN, *SUPRA* note 18, § 4682, at 22 n.9 (1978 CGL); Leder, *supra* note 12, at C-87 (1973 CGL).

53. See *Sullins v. Allstate Ins. Co.*, 340 Md. 503, 509, 667 A.2d 617, 619-20 (1995); *Aetna Cas. & Sur. Co. v. Cochran*, 337 Md. 98, 102, 651 A.2d 859, 861 (1995); *Brohawn*, 276 Md. at 408, 347 A.2d at 850.

54. See, *e.g.*, *Southern Md. Ass'n v. Bituminous Cas. Corp.*, 539 F. Supp. 1295, 1299 (D. Md. 1982) (applying Maryland law; discussing *Steyer*, 450 F. Supp. at 389); see also Janquitto, *supra* note 14, at 39-40 (noting that the insurer can provide a partial defense if legal costs can readily be apportioned between covered and noncovered claims); *cf.*, *e.g.*, *Aetna Cas. & Sur. Co. v. Spancrete of Ill.*,

The court of appeals fully articulated the "potentiality rule" in *Brohawn v. Transamerica Insurance Co.*⁵⁵ The *Brohawn* court stated that under a standard duty to defend provision, an insurer is obligated to defend "if there is a *potentiality* that the claim could be covered by the policy."⁵⁶ Accordingly, the *Brohawn* court held that despite the insured's guilty plea to criminal assault, the insurer was obligated to defend against a negligence claim arising from the same occurrence, notwithstanding a clause in the policy excluding coverage for intentional acts.⁵⁷ The court reasoned that this was logical because the guilty plea was not binding on the jury in the civil suit.⁵⁸ Thus, the jury could have found that the insured's actions were negligent, as opposed to intentional, and, therefore, covered under the policy.⁵⁹ As the results in *Brohawn* and its progeny make clear, the duty to defend under the potentiality rule is a low thresh-

Inc., 726 F. Supp. 204, 207 (N.D. Ill. 1989) (stating that under Illinois law, so long as one of the grounds for recovery is potentially covered, an insurer must provide the defense against the entire complaint even if one of the theories of recovery is explicitly excluded).

55. 276 Md. 396, 347 A.2d 842 (1975). In Maryland, the potentiality rule was first announced in *United States Fidelity & Guaranty Co. v. National Paving & Contracting Co.*, 228 Md. 40, 54, 178 A.2d 872, 879 (1962). See also Janquitto, *supra* note 14, at 11 n.53.
56. *Brohawn*, 276 Md. at 408, 347 A.2d at 850 (citing *National Paving & Contracting Co.*, 228 Md. at 54, 178 A.2d at 872).
57. The policy excluded, however, "any act committed by . . . the Insured with intent to cause injury or damage to person or property." *Id.*
58. See *id.* at 403-04, 347 A.2d at 848 (noting that the insured would have an opportunity to explain a guilty plea to the jury in a civil suit).
59. See *id.* The *Brohawn* court also considered whether it was appropriate for a court to fully adjudicate the insurer's obligations under the policy in relation to the pending, underlying tort action. See *id.* at 404-07, 347 A.2d at 848-50. The court held that if the issues presented in a declaratory judgment action are independent and separable from those in the underlying tort suit, the trial court may exercise its discretion in entertaining a suit to determine policy coverage. See *id.* at 405, 347 A.2d at 848-49 (noting, *e.g.*, the issue of whether insured paid policy premiums would generally be appropriate for determination in a declaratory judgment action). Conversely, if the issues raised in a declaratory judgment action to determine the extent of coverage would require addressing ultimate issues of fact which are also at issue in the pending, underlying suit by a third party, a declaratory judgment action would be inappropriate. See *id.* at 406-07, 347 A.2d at 848-49 (noting that the effect would be to force the insured to defend "against the vast resources and expertise of her insurer who would be trying to prove that which was its contractual duty to disprove").

old to satisfy.⁶⁰

2. The Exclusive Pleading Rule

The potentiality rule is closely tied to the "exclusive pleading rule." The exclusive pleading rule directs that courts look only to the plaintiff's complaint in the underlying suit to determine the insurer's duty to defend.⁶¹ Under Maryland law, however, the exclusive pleading rule is a one-way street.⁶² In *Aetna Casualty & Surety Co. v. Cochran*,⁶³ the court of appeals limited the application of the exclusive pleading rule to insurers only by extending the potentiality rule to encompass affirmative defenses made by the insured.⁶⁴

The *Cochran* court addressed whether an insured's affirmative defense of self-defense potentially placed the underlying claims for assault, battery, and loss of consortium within the policy coverage.⁶⁵ The policy excluded claims for injury or damage "expected or intended from the standpoint of the 'insured,'" but included claims for harm "resulting from the use of reasonable force to protect persons or property."⁶⁶ Thus, the court held that the insurer was obligated to provide a defense because the insured's answer to the complaint potentially brought the claim within the insurer's duty to

60. See generally, e.g., *Sullins v. Allstate Ins. Co.*, 340 Md. 503, 518, 667 A.2d 617, 624 (1995) (holding that a lead paint claim was not encompassed within the pollution exclusion clause); *Janquitto*, *supra* note 14, at 16 ("[T]he duty to defend exists unless it can be conclusively shown as a matter of law that there is no possible factual or legal basis on which the insurer may eventually be found liable under its duty to indemnify.").

61. See, e.g., *Brohawn*, 276 Md. at 408, 347 A.2d at 850 (quoting *Lee v. Aetna Cas. & Sur. Co.*, 178 F.2d 750, 751-52 (2d Cir. 1949) (Learned Hand, C.J.)). *Lee* is noted as being the most cited case for the exclusive pleading rule. See *Janquitto*, *supra* note 14, at 7. In *Lee*, the court declined to relieve an insurer from its duty to defend, notwithstanding that the insurer had information outside of the complaint conclusively establishing that the underlying claim fell within a policy exclusion. See *Lee*, 178 F.2d at 752-53. Notably, the *Lee* court sustained the denial of the insurer's duty to indemnify the insured using the extrinsic evidence; in other words, coverage was excluded but the insurer nevertheless had a duty to defend. See *id.*; see also *Janquitto*, *supra* note 14, at 8 n.38.

62. See *Aetna Cas. & Sur. Co. v. Cochran*, 337 Md. 98, 112, 651 A.2d 859, 866 (1995).

63. 337 Md. 98, 651 A.2d 859 (1995).

64. See *id.* at 111-12, 651 A.2d at 866.

65. See *id.* at 100, 651 A.2d at 860.

66. *Id.* at 101, 651 A.2d at 861.

indemnify.⁶⁷ The court added that extrinsic evidence proffered by the insured will trigger coverage under the potentiality rule only if the insured can demonstrate that "there is a reasonable potential that the issue triggering coverage will be generated at trial"⁶⁸

3. The Comparison Test

When applying the potentiality and exclusive pleading rules, Maryland courts engage in a two-step inquiry⁶⁹ known as the "comparison test."⁷⁰ This analytical framework was first prescribed in *St. Paul Fire & Marine Insurance Co. v. Pryseski*.⁷¹ First, the court ascertains "what is the coverage and what are the defenses under the terms and requirements of the insurance policy."⁷² The court then determines if "the allegations in the [underlying] tort action potentially bring the tort claim within the policy's coverage."⁷³ In dicta, the *Pryseski* court noted that the potentiality rule usually becomes relevant only in the second step of the comparison test.⁷⁴

The *Pryseski* court's indication that the potentiality rule might become relevant in the first step of the comparison test created confusion within the Maryland legal community.⁷⁵ In *Northern Assurance Co. of America v. EDP Floors, Inc.*,⁷⁶ the court of appeals responded to this confusion by disavowing its dicta in *Pryseski*.⁷⁷ The *Northern Assurance* court declared that applying the potentiality rule in the first step, whereby the court determines the scope of the insurer's duty to indemnify, "would in effect create a canon of insur-

67. See *id.* at 112, 651 A.2d at 866. The court's holding, though premised on the insured's affirmative defense, is more accurately based on the sufficiency of the insured's representations to the insurer that the underlying actions were in self-defense. See *id.* at 101 n.2, 651 A.2d at 861 n.2 (noting that the record before the court of appeals did not contain the insured's answer in the underlying suit).

68. *Id.* at 112, 651 A.2d at 866 (noting that the insured cannot simply assert frivolous defenses to trigger the duty to defend).

69. See *Cochran*, 337 Md. at 103-04, 651 A.2d at 862; *St. Paul Fire & Marine Ins. Co. v. Pryseski*, 292 Md. 187, 193, 438 A.2d 282, 285 (1981).

70. See, e.g., *Janquitto*, *supra* note 14, at 17.

71. See *Pryseski*, 292 Md. at 193-94, 438 A.2d at 285.

72. *Id.* at 193, 438 A.2d at 285.

73. *Id.*

74. See *id.* at 193-94, 438 A.2d at 285.

75. See *Janquitto*, *supra* note 14, at 20 (noting that *Pryseski* court's qualification that the potentiality test may become relevant in the first step "has created abundant confusion").

76. 311 Md. 217, 533 A.2d 682 (1987).

77. See *id.* at 226, 533 A.2d at 686.

ance contract interpretation that gives every benefit of doubt to the insured, in contravention of our many holdings that the unambiguous language in an insurance contract is to be afforded its ordinary and accepted meaning.”⁷⁸ Hence, the comparison test now simply stands as an analytical framework rather than a rule of insurance policy construction. The first step involves application of the rules of construction in determining the scope of coverage—not whether a court can construe the policy so as to raise a potentiality of coverage.⁷⁹ The second step involves whether, given the construction produced in the first step, there is a potentiality that the insurer will be required to indemnify the insured.⁸⁰

C. Construction of Selected Terms in Liability Policies: “Occurrence” & “Property Damage”

Under the second step of the comparison test, a court determines whether the allegations in the underlying tort suit potentially fall within the scope of the insurer’s duty to indemnify.⁸¹ The liberal pleading practice in Maryland and most jurisdictions complicates this inquiry because plaintiffs need not plead their cause of action with specificity.⁸² Therefore, the second step in the comparison test often requires examining the elements of the cause of action alleged in the plaintiff’s complaint and determining whether the allegations allege liability potentially covered under the policy.

Any meaningful analysis of the second step of the comparison test must account for the scope of coverage adduced in the first step.⁸³ Thus, for analysis purposes, this Note centers its inquiry on

78. *Id.*

79. See Janquitto, *supra* note 14, at 22.

80. See *id.*

81. See *St. Paul Fire & Marine Ins. Co. v. Prysieski*, 292 Md. 187, 393-94, 438 A.2d 283, 285 (1981).

82. See 7C APPLEMAN, *supra* note 18, § 4683, at 55 (stating that federal pleadings may not provide enough information to make an informed judgment concerning the duty to defend). One commentator noted that despite different standards between the federal and Maryland pleading rules, Maryland’s pleading practice also causes difficulty because it permits parties to plead in the alternative. See Janquitto, *supra* note 14, at 38 (comparing FED. R. CIV. P. 8 (notice pleading) with MD. RULE 2-303 (modified notice pleading)). The same commentator also suggested that an insurer faced with ambiguous pleadings should consider assuming the defense under a reservation of rights and make a motion for a more definite statement to properly assess the underlying facts. See *id.* at 39.

83. See *supra* notes 69-80 and accompanying text for a discussion of the compari-

the coverage agreement in the CGL.⁸⁴

With minor changes depending on the version, the CGL coverage agreement provides:

The company will pay on behalf of the insured all sums which the insured shall become legally obligated to pay as damage because of

A. bodily injury or

B. property damage

to which this insurance applies, caused by an occurrence

. . . .⁸⁵

Under the first step of the comparison test, a court construing this provision would determine that the insurer has an obligation to indemnify the insured if the following two conditions exist: (1) bodily injury or property damage, (2) caused by an occurrence.⁸⁶

1. "Property Damage"

Judicial construction of the term "property damage" has been somewhat unpredictable.⁸⁷ Prior to 1966, the CGL provided that property damage was "injury to or destruction of property."⁸⁸ Courts construed this to encompass liability for intangible rights and obligations⁸⁹ such as economic losses.⁹⁰ In an effort to hedge this unin-

son test.

84. See 7C APPLEMAN, *supra* note 18, § 4682, at 22 n.9 (1978 CGL); see also David S. Garbett, Comment, *The Duty to Defend Clause in a Liability Insurance Policy: Should the Exclusive Pleading Test be Replaced?*, 36 U. MIAMI L. REV. 235, 236 n.2 (1982) (noting that all liability policies contain substantially the same indemnity and duty to defend clauses).
85. 7C APPLEMAN, *supra* note 18, § 4682, at 22 n.9 (1978 CGL); Tinker, *supra* note 11, at 238 (1973 CGL); Leder, *supra* note 12, at C-87 (1973 CGL). See Tinker, *supra* note 11, at 220-21, for a brief discussion of the history and origin of the CGL. For an outline of the various provisions in a CGL, including judicial construction of the terms by Maryland courts, see Leder, *supra* note 12, at C-1 to C-72. See also Phillips L. Goldsborough & Jon H. Grube, *The Comprehensive General Liability Policy & Related Coverages*, in SELECTED PROBLEMS IN INSURANCE LAW 1, 11-37 (Maryland Institute for Continuing Professional Education of Lawyers, Inc. ed., 1983).
86. *Cf., e.g.*, *Sheets v. Brethren Mutual Ins. Co.*, 342 Md. 634, 641-43, 679 A.2d 540, 543-44 (1996) (applying the first step of the comparison test to identical policy terms and producing the same scope of an insurer's duty to indemnify).
87. See Leder, *supra* note 12, at C-8 (explaining the history of redrafting the CGL in response to judicial misconstruction of the term "property damage").
88. *Id.*
89. See *id.*; *Hauenstein v. Saint Paul-Mercury Indem. Co.*, 65 N.W.2d 122, 125

tended construction, drafters added the word “tangible” to the definition of “property damage.”⁹¹ Nevertheless, courts continued to hold that CGLs covered economic losses.⁹² Finally, in 1973 the drafters amended the definition to require “*physical* injury to or destruction of tangible property.”⁹³ This change was fairly effective in excluding coverage for economic loss.⁹⁴

Since 1973, the CGL has also defined “property damage” to include the “loss of the use of tangible property that is not physically injured.”⁹⁵ Commentators have noted that this “loss of use” prong provides a narrow scope of coverage.⁹⁶ Indeed, this prong provides a narrow window of coverage for economic loss.⁹⁷ The classic example

(Minn. 1954) (holding that diminution in value is covered property damage under CGL).

90. See Leder, *supra* note 12, at C-8 (“[P]urely economic loss was not intended to be covered by [CGL] underwriters.”). “[E]conomic loss is loss of an expectancy interest created by contract” Michael R. McCann, Note, *Atlantis Revisited: Recovery Under Maryland Law for Purely Economic Loss Against Negligent Builders and Manufacturers*, 23 U. BALT. L. REV. 521, 522 (1994). “Economic loss includes such things as the loss of value or the use of the product itself, the cost to repair or replace the product, or the lost profits resulting from the loss of use of the product.” A.J. Decoster Co. v. Westinghouse Elec. Corp., 333 Md. 245, 250, 634 A.2d 1330, 1332 (1994); see also McCann, *supra*, at 522.
91. See Leder, *supra* note 12, at C-8.
92. See *id.* (citing United States Fidelity & Guar. v. Nevada Cement Co., 561 P.2d 1335 (Nev. 1977)).
93. See *id.*
94. See, e.g., Sting Sec., Inc. v. First Mercury Syndicate, Inc., 791 F. Supp. 555, 562 (D. Md. 1992) (applying Virginia law); Kartridg Pak Co. v. Travelers Indem. Co., 425 N.W.2d 687, 689 (Iowa Ct. App. 1988) (recognizing that 1973 revision of CGL, inserting the term “physical injury” into the definition of “property damage,” restricted coverage for intangible losses); see also John P. Arness & Randall D. Eliason, *Insurance Coverage for “Property Damage” in Asbestos and Other Toxic Tort Cases*, 72 VA. L. REV. 943, 963 (1986) (“Courts have interpreted the [1973 CGL] requirement of physical injury rather strictly.”); Herbert J. Bauman, *Broad Form Property Liability Coverage: An Overview*, in REFERENCE HANDBOOK ON THE COMPREHENSIVE GENERAL LIABILITY POLICY: COVERAGE PROVISIONS, EXCLUSIONS, AND OTHER LITIGATION ISSUES 117, 125-26 (Peter J. Neeson ed. 1995).
95. E.g., Arness & Eliason, *supra* note 94, at 962-63 (quoting 1973 CGL); Bauman, *supra* note 94, at 125 (same); accord *Sheets v. Brethren Mut. Ins. Co.*, 342 Md. 634, 641, 679 A.2d 540, 543 (1996).
96. See, e.g., Arness & Eliason, *supra* note 94, at 967-68; Goldsborough & Grube, *supra* note 85, at 17-18.
97. Cf. Arness & Eliason, *supra* note 94, at 960 (“[T]he claim for loss of use is one for loss of intangible property—profits.”). See generally A.J. Decoster Co. v. Westinghouse Elec. Corp., 333 Md. 245, 250, 634 A.2d 1330, 1332 (1994) (“Ec-

provides: "[I]f a crane buckles and blocks the entrance to a building resulting in its loss of use, the loss of use would be covered even though the building was not physically injured."⁹⁸

Commentators have also noted that the limited coverage provided by the loss of use prong is circumscribed by the "loss of use" exclusion,⁹⁹ one of four "business risk" exclusions.¹⁰⁰ The loss of use exclusion provides that coverage does not apply to loss of use resulting from the failure of the insured's product or work "to meet the level of performance, quality, fitness or durability warranted or represented by the insured."¹⁰¹ However, this exclusion does not preclude coverage for "loss of use of *other* tangible property resulting from the sudden and accidental physical injury to or destruction of the . . . insured's products or work."¹⁰² For example, the loss of use of an adjacent landowner's property that is not physically damaged

onomic loss includes . . . lost profits resulting from the loss of use of the product."). *But cf.* Bauman, *supra* note 94, at 129 ("The loss of use must be attributable to an interference with the use of tangible property and not merely an economic loss caused by the insured's negligence.").

98. Tinker, *supra* note 11, at 232 (noting that this was the example given by the drafters of the 1966 CGL); *accord* Arness & Eliason, *supra* note 94, at 968; Goldsborough & Grube, *supra* note 85, at 17-18. Another way loss of use occurs is by the incorporation of the insured's defective product into a larger product. *See* Vasichcek, *supra* note 3, at 804. For example, the failure of an alternator sold by an insured and incorporated into an engine might not cause physical injury to the engine, but rather loss of use. *See id.* Note, however, that CGLs contain coverage exclusions for damage to the alternator itself. *See id.* at 804 n.7 (quoting exclusions "(l)" and "(m)" in the 1966 CGL and exclusions "(n)" and "(o)" in the 1973 CGL).
99. *See* Arness & Eliason, *supra* note 94, at 968 n.88.
100. *See* Woodfin Equities Corp. v. Harford Mut. Ins. Co., 110 Md. App. 616, 641, 678 A.2d 116, 128 (1996), *rev'd on other grounds*, 344 Md. 399, 687 A.2d 652 (1997). For an overview of all business risk exclusions, see Neeson & Meyer, *supra* note 1, at 75-115. *See also* Century I Joint Venture v. United States Fidelity & Guar. Co., 63 Md. App. 545, 553-57, 493 A.2d 370, 374-77 (1985) (providing an excellent discussion and analysis of business risk exclusions; holding that condominiums constituted "products" sold by the insured); 2 ALLAN D. WINDT, INSURANCE CLAIMS & DISPUTES § 11.10, at 243-57 (3d ed. 1995 & Supp. 1997) (examining business risk exclusions under the heading "Insured's Work/Product Exclusion"); Leder, *supra* note 12, at C-57 to C-60 (providing Maryland law overview).
101. Tinker, *supra* note 11, at 278 (quoting 1973 CGL exclusion (m)), *quoted in* Arness & Eliason, *supra* note 94, 968 at n.88; *accord* Goldsborough & Grube, *supra* note 85, at 43; Neeson & Meyer, *supra* note 1, at 78-79.
102. Tinker, *supra* note 11, at 278 (emphasis added) (quoting 1973 CGL exclusion (m)); *accord* Neeson & Meyer, *supra* note 1, at 79; *see also* Vasichcek, *supra* note 3, at 804 n.47.

may be covered even if the loss of use was caused by property damage to the insured's building, an excluded loss.¹⁰³

In *Pyles v. Pennsylvania Manufacturers' Ass'n Insurance Co.*,¹⁰⁴ the Court of Special Appeals of Maryland addressed whether an underlying complaint alleged property damage covered under a CGL.¹⁰⁵ The insured in *Pyles*, a home builder, orally contracted with a purchaser to maintain \$750,000 worth of builder's risk insurance on a home under construction.¹⁰⁶ The builder only purchased \$250,000 of risk insurance, and a fire ensued that destroyed the home.¹⁰⁷ Because the damage exceeded the amount of builder's risk insurance actually obtained, the homeowner brought suit against the builder, alleging negligence and breach of contract based on the builder's failure to obtain the agreed upon amount of risk insurance.¹⁰⁸

The builder contacted his CGL insurer and requested that it defend him in the underlying suit.¹⁰⁹ The insurer refused, and the builder lost the underlying suit.¹¹⁰ The builder then brought a de-

103. See Tinker, *supra* note 11, at 234 (construing 1973 CGL provisions); see also *United Capitol Ins. Co. v. Special Trucks, Inc.*, 918 F. Supp. 1250, 1260-61 (N.D. Ind. 1996) (citing cases that hold that loss of use and consequential damages—that are not part of the repair program—caused by the damage to the insured's work or product are covered); cf. *Weedo v. Stone-E-Brick, Inc.*, 405 A.2d 788, 791-92 (N.J. 1979) (“[P]oorly-performed work will . . . have to be replaced or repaired by the tradesman or a surety. On the other hand, should [the tradesman's product] fall from the wall, and thereby cause injury to the homeowner or his neighbor standing below or to a passing automobile, an occurrence of harm arises which is the proper subject of risk-sharing as provided in [the CGL].”); *Reliance Ins. Co. v. Povia-Ballantine Corp.*, 738 F. Supp. 523, 526 (S.D. Ga. 1990) (providing an example of the distinction between injury to the insured's product and liability to a third person: stucco falling from a wall and striking someone is covered, but replacing the stucco is not).

104. 90 Md. App. 320, 600 A.2d 1174 (1992).

105. The policy stated, “ ‘Property damage’ means . . . physical injury to or destruction of tangible property which occurs during the policy period, including the loss of use thereof at any time resulting therefrom” *Id.* at 323, 600 A.2d at 1176.

106. See *id.* at 321, 600 A.2d at 1175.

107. See *id.* at 322, 600 A.2d at 1175.

108. See *id.*

109. See *id.* The *Pyles* court did not state whether the CGL insurer and the builder's risk insurer were the same entity. Nonetheless, the policies are distinct—a builder's risk insurance policy provides coverage for a broader range of contingencies relating solely to a specific project. See 7A APPLEMAN, *supra* note 18, § 4492.03, at 44.

110. See *Pyles*, 90 Md. App. at 322, 600 A.2d at 1175.

claratory judgment action against his CGL insurer, requesting that it be required to indemnify him for the costs incurred from both the judgment and defending the suit.¹¹¹ Ruling in favor of the insurer, the circuit court held that the underlying claim lacked a sufficient nexus to property damage in order to establish a potentiality that the insurer would have a duty to indemnify.¹¹²

On appeal, the court of special appeals began its analysis of the insurer's duty to defend by construing the phrase "because of property damage."¹¹³ The intermediate appellate court interpreted this phrase as requiring "a direct causal link or nexus between an insured's liability and property damage."¹¹⁴ However, in the underlying suit the court found the basis of the claim was breach of contract and negligence, not property damage.¹¹⁵ Hence, the court ruled that the insurer had neither the duty to defend under the potentiality rule nor the duty to indemnify the insured for the judgment.¹¹⁶

In *Woodfin Equities Corp. v. Harford Mutual Insurance Co.*,¹¹⁷ the Court of Special Appeals of Maryland addressed the loss of use prong of the definition of "property damage" in an appeal from a declaratory judgment action coverage dispute.¹¹⁸ In the underlying

111. *See id.* at 323, 600 A.2d at 1176. Pursuant to a settlement agreement, the builder assigned his rights under the CGL to the homeowner. *See id.* at 322, 600 A.2d at 1175. Thus, the plaintiff in the declaratory judgment action against the insurer was also the plaintiff in the underlying suit. *See id.* at 322-23, 600 A.2d at 1175-76.

112. *See id.* at 323-24, 600 A.2d at 1176.

113. *Id.* at 325, 600 A.2d at 1177.

114. *Id.*

115. The court noted that property damage was a factual predicate to the builder's liability in the underlying suit. *See id.* The *Pyles* court concluded, however, that this factual predicate status did not make the potential liability "on account of property damage." *Id.*

116. *See id.* at 325-26, 600 A.2d at 1177. The court of special appeals cited other jurisdictions in accordance with the rule it adopted, noting that Maryland law did not resolve the issue. *See id.* at 325, 600 A.2d at 1177 (citing, *e.g.*, *Reliance Ins. Co. v. Gary C. Wyatt, Inc.*, 540 So. 2d 688 (Ala. 1988)).

117. 110 Md. App. 616, 678 A.2d 116 (1996) (Wilner, C.J., joining majority opinion), *rev'd in part on other grounds*, 344 Md. 399, 415, 687 A.2d 652, 659 (1997) (declining to address merits because the trial court did not issue a written declaratory judgment). The court of special appeals decided *Woodfin* after *Sheets*, the subject case of this Note.

118. The policy language at issue came from the 1973 CGL. *Compare Woodfin*, 110 Md. App. at 639-40, 678 A.2d at 127 (quoting coverage provisions at issue), *with Leder*, *supra* note 12, at C-87 to C-88 (1973 CGL).

suit, developers and general contractors of a hotel obtained a default judgment against an insured subcontractor that installed the hotel's heating, ventilation, and air conditioning (HVAC) system.¹¹⁹ The underlying complaint, alleging negligence, breach of contract, and breach of warranty, sought damages caused by the failure of a large number of the HVAC units.¹²⁰ These damages included loss of the use of guest suites, cost of repairs and replacements, and management time expended addressing the HVAC system failure.¹²¹

In the declaratory judgment action, the insurer asserted that the underlying claims did not involve property damage arising out of an occurrence, and, even if so, the business risk exclusions precluded finding coverage.¹²² After hearing testimony, the trial court held in favor of the insurer without specifying which contention asserted by the insurer was dispositive.¹²³

The Court of Special Appeals of Maryland reversed in part and affirmed in part the trial court's ruling regarding coverage. The court held that the CGL did not cover the owner's expenses relating to the removal, repair, or replacement of the faulty HVAC units.¹²⁴ The court found that because defective workmanship is not an occurrence, the policy did not cover damage to the HVAC units.¹²⁵ Alternatively, the court held that even if an occurrence caused the damage, a business risk exclusion¹²⁶ precluded coverage.¹²⁷ The exclusion provided that the CGL does not cover "property damage to the named insured's products arising out of such

119. See *Woodfin*, 110 Md. App. at 622, 678 A.2d at 118-19.

120. See *id.* at 623, 678 A.2d at 119.

121. See *id.* at 623-24, 678 A.2d at 119.

122. See *id.* at 628, 640-42, 678 A.2d at 121, 127-28. See generally *supra* note 100 and accompanying text (discussing business risk exclusions).

123. See *Woodfin*, 110 Md. App. at 629, 678 A.2d at 122 (noting only that the trial court held in favor of the insurer). Notably, the Court of Appeals of Maryland reversed the court of special appeals solely because the court of special appeals reached the merits of the case without the benefit of a written declaration from the circuit court. See *Harford Mut. Ins. Co. v. Woodfin Equities Corp.*, 344 Md. 399, 415, 687 A.2d 652, 659 (1997).

124. See *Woodfin*, 110 Md. App. at 651, 678 A.2d at 133.

125. See *id.* at 648, 678 A.2d at 131 ("Courts uniformly hold that when property damage arising out of the insured's defective workmanship is confined to the insured's own work product, the damage is not caused by an 'occurrence' within the meaning of the CGL policy." (citing, e.g., *Reliance Ins. Co. v. Mogavero*, 640 F. Supp. 84 (D. Md. 1986))).

126. See generally *supra* note 100 and accompanying text (discussing business risk exclusions).

127. See *Woodfin*, 110 Md. App. at 649-50, 678 A.2d at 132.

products or any part of such products."¹²⁸

Conversely, regarding loss of use of the guest suites, the court of special appeals held that the policy covered such damage because the breaking down of the HVAC units, though property damage excluded under the policy, constituted an occurrence.¹²⁹ Thus, the loss of use of the guest suites constituted property damage caused by an occurrence under the CGL.¹³⁰ The court noted that the loss of use exclusion¹³¹ explicitly did not apply to the loss of use of property caused by the failure of the insured's property or work.¹³²

2. "Occurrence"

Since 1966, CGLs have defined "occurrence" as an "accident."¹³³ CGLs also provide that damages are not covered if they are either expected or intended from the standpoint of the insured.¹³⁴

128. *Id.* at 650, 678 A.2d at 132. Because the definition of "insured's product" included property sold by the insured, the court rejected the insurer's argument that the CGL excluded damage to the HVAC units because ownership was transferred. *See id.* at 650-51, 678 A.2d at 132. In any event, the court added, the result would be the same because of the "completed operations hazard" exclusion. *See id.* at 651 n.9, 678 A.2d at 133 n.9.

129. *See id.* at 652, 678 A.2d at 133 ("To the extent that the insured's defective workmanship causes damage to [property other than the product or completed work of the insured], courts uniformly hold that such damage is caused by an 'occurrence,' and is, therefore, compensable under the CGL policy.").

130. *See id.* at 652, 678 A.2d at 133.

131. *See supra* notes 99-103 and accompanying text for a discussion of the loss of use exclusion.

132. *See Woodfin*, 110 Md. App. at 653, 678 A.2d at 133-34. Likewise, the court noted that the other business risk exclusions—the insured's property and completed operations hazard exclusions—were inapplicable. *See id.* at 653, 678 A.2d at 134. *See generally supra* note 100 and accompanying text (discussing business risk exclusions).

133. *See Tinker*, *supra* note 11, at 256, *see also Leder*, *supra* note 12, at C-93 (1973 CGL); *id.* at C-104 (1985 CGL); *id.* at C-116 (1996 CGL). The 1973 CGL provides: " 'Occurrence' means an accident, including continuous or repeated exposure to conditions, which results in bodily injury or property damage neither expected or intended from the standpoint of the insured." *Leder*, *supra* note 12, at C-93. The 1985 and 1996 CGLs both provide: " 'Occurrence' means an accident, including continuous or repeated exposure to substantially the same general harmful conditions." *Id.* at C-104 (1985 CGL); *id.* at C-116 (1996 CGL).

134. The 1973 CGL accomplished this by adding this provision into the definition of "occurrence." *See supra* note 133. The 1985 and 1996 CGLs accomplish this through an exclusion that provides that the policy does not cover " 'property damage' expected or intended from the standpoint of the insured." *Leder*,

Moreover, insurers sometimes modify CGLs to provide for a more explicit definition of "occurrence."¹³⁵

In *Haynes v. American Casualty Co.*,¹³⁶ the Court of Appeals of Maryland addressed the definition of "accident." In *Haynes*, an insured contractor instructed his employee to excavate land up to an adjacent landowner's property.¹³⁷ The employee excavated beyond the property line, and the adjacent landowner sued.¹³⁸ The contractor's insurer began to provide a defense, but during the course of the litigation the insurer denied liability under the policy and refused to pay for the ensuing legal bills and judgment.¹³⁹ Thereafter, the contractor filed suit against the insurer.¹⁴⁰ In the circuit court, the insurer asserted that the damage to the adjoining landowner was not an accident because the employee clearly intended to excavate the adjoining land and the policy language did not include mistakes.¹⁴¹ The trial judge found in favor of the insurer, and the insured appealed to the court of appeals.¹⁴²

On appeal, the court of appeals addressed the distinction between "accidental means" and "accidental result."¹⁴³ The court reiterated Justice Cardozo's warning that adopting such a distinction would "plunge this branch of the law into a Serbonian Bog."¹⁴⁴ The

supra note 12, at C-96 (1985 CGL (exclusion "a.")); *id.* at C-106 (1996 CGL (exclusion "a.")). *See generally* Government Employees Ins. Co. v. Ropka, 74 Md. App. 249, 257, 536 A.2d 1214, 1218 (1988) ("It is generally true that an insurer has no duty to defend a cause of action against an insured if that cause of action asserts liability on the part of the insured that comes within an exclusion in the insurance policy.").

135. *See, e.g.*, John Hancock Mut. Life Ins. Co. v. Plummer, 181 Md. 140, 142, 28 A.2d 856, 857 (1942) (construing a policy providing coverage for bodily injury "caused solely by external, violent and accidental means").

136. 228 Md. 394, 179 A.2d 900 (1962).

137. *See id.* at 395, 179 A.2d at 901.

138. *See id.*

139. *See id.* at 395-96, 179 A.2d at 901.

140. *See id.* at 396, 179 A.2d at 901-02.

141. *See id.* at 396, 179 A.2d at 902.

142. *See id.*

143. The court of appeals stated that it did not intend to make a universal ruling as to whether or not a distinction between accidental means and results should be made. *See id.* at 399-400, 179 A.2d at 904.

144. *Id.* at 399 n.1, 179 A.2d at 904 n.1 (quoting *Landress v. Phoenix Mut. Life Ins. Co.*, 291 U.S. 491, 499 (1934) (Cardozo, J., dissenting)). The Serbonian Bog reference comes from JOHN MILTON, *PARADISE LOST*, bk. 2, l. 592 (1667): "A gulf profound as the Serbonian Bog Betwixt Damiat and mount Casius old, where Armies whole have sunk" *Id.*, quoted in *Haynes*, 228 Md. at 399 n.1,

court avoided this distinction, holding that unless the policy expressly requires either an accidental means or result, courts should interpret the term "accident" as encompassing either accidental means or results.¹⁴⁵ To hold otherwise, the court reasoned, would put too narrow an interpretation on the contract and limit recovery to those situations where both the result and the means were accidental.¹⁴⁶ Moreover, in addressing the insurer's contention that the policy did not include coverage for intentional acts, the court clarified that an accident may result from an intentional act if something unusual, unexpected, and unforeseen occurs.¹⁴⁷ Thus, "an act attributable solely to negligence may be an accident."¹⁴⁸ Applied to the facts in *Haynes*, the court found that even though the employee intentionally excavated the land, the policy afforded coverage because the result was accidental—the employee did not intentionally excavate the wrong land.¹⁴⁹

In *Harleysville Mutual Casualty Co. v. Harris & Brooks, Inc.*,¹⁵⁰ the Court of Appeals of Maryland again addressed the scope of the term "accident." In the underlying suit, adjacent homeowners brought an action to recover for smoke damage to their homes

179 A.2d at 904 n.1.

In his dissent in *Landress*, Justice Cardozo posited that, in the strictest sense, there is no such thing as an accident. *See Landress*, 291 U.S. at 499 (Cardozo, J., dissenting). He opined that the distinction between accidental means and result would not survive the application of the principle that ambiguities in insurance contracts are construed against the insurance company as drafter of the document. *See id.* Hence, he concluded, because the average person believes that there is such a thing as an accident, the distinction between result and means is untenable. *See id.*

145. *See Haynes*, 228 Md. at 400-01, 179 A.2d at 904. The court of appeals noted that it previously addressed this distinction twice before when it construed policies that covered "bodily injury 'caused solely by external, violent and accidental means.'" *Id.* at 400, 179 A.2d at 904 (citing *John Hancock Mut. Life Ins. Co. v. Plummer*, 181 Md. 140, 28 A.2d 856 (1942), and *Home Beneficial Life Ins. Co. v. Partain*, 205 Md. 60, 106 A.2d 79 (1954)). The court noted that those policies expressly required the court to limit coverage to accidental means. *See Haynes*, 228 Md. at 400, 179 A.2d at 904.

146. *See Haynes*, 228 Md. at 400, 179 A.2d at 904.

147. *See id.* at 397, 179 A.2d at 902 (discussing Justice Rive's "well reasoned dissent" in *M.R. Thomason, United States Fidelity & Guar. Co. v. United States*, 248 F.2d 417, 420-21 (5th Cir. 1957) (Rives, J., dissenting)).

148. *Haynes*, 228 Md. at 398, 179 A.2d at 903 (quoting *Minkov v. Reliance Ins. Co. of Philadelphia*, 149 A.2d 260, 263 (N.J. Super. Ct. App. Div. 1959)).

149. *See id.* at 399, 179 A.2d at 903.

150. 248 Md. 148, 235 A.2d 556 (1967).

caused from the insured contractor burning piles of trees for thirty-six hours.¹⁵¹ The contractor's insurer appealed a declaratory judgment in favor of the insured, and the court of appeals considered whether damage to the adjacent homes was caused by an accident.¹⁵²

In addressing the scope of the policy's phrase "caused by an accident," the court of appeals sought to attribute to the term "accident" its customary and ordinary meaning.¹⁵³ The court referred to two dictionaries and determined that an accident is an event that takes place without one's foresight or expectation.¹⁵⁴ The court reaffirmed its previous definition in *Haynes*, that an accident can include an intentional act if the result is something unforeseen, unusual, and unexpected.¹⁵⁵ The court added, however, that an accident must take place "without one's foresight or expectation."¹⁵⁶ Because the contractor had not taken precautionary measures when burning the trees, the court found the resulting damage should have been expected because it could not have been caused without the contractor's foresight or expectation.¹⁵⁷

In *State Farm Mutual Auto Insurance Co. v. Treas*,¹⁵⁸ the court of appeals addressed whether an insurer had a duty to indemnify its insured for a judgment based on striking a pedestrian with a car.¹⁵⁹ The insured had already pleaded guilty to common law manslaughter and had received a six-year prison sentence.¹⁶⁰ The court reaffirmed that an intentional act may be considered an accident "if in that act, something unforeseen, unusual and unexpected occurs

151. *See id.* at 150, 235 A.2d at 557.

152. *See id.* at 151, 235 A.2d at 557. The insured subcontractor received judgment in his favor in the circuit court. *See id.*

153. *See id.*

154. *See id.* The court quoted the SHORTER OXFORD ENGLISH DICTIONARY (2d ed. 1939), which defined "accident" as "anything that happens; an event; especially an unforeseen contingency," and WEBSTER'S TWENTIETH CENTURY DICTIONARY (1950), which defined "accident" as "a happening; an event that takes place without one's foresight or expectation; an event that proceeds from an unknown cause, or is an unusual effect of a known cause, and therefore not expected." *Harleysville*, 248 Md. at 151, 235 A.2d at 557.

155. *See Harleysville*, 248 Md. at 151-52, 235 A.2d at 558.

156. *Id.* at 154, 235 A.2d at 559.

157. *See id.*

158. 254 Md. 615, 255 A.2d 296 (1969).

159. In the declaratory judgment act against the insurer, the circuit court judge found that the death of the victim was caused by an accident. *See id.* at 617, 255 A.2d at 297.

160. *See id.* at 618, 255 A.2d at 298.

which produces the result.”¹⁶¹ Comparing the facts with those in *Harleysville*, the court reasoned that if the failure to take precautions to prevent property damage was not an accident, the court “cannot say that . . . accelerating and braking to induce [the victim] to move [from in front of the car], and finally striking her when she refused to do so,” is an accident.¹⁶²

In *Ed. Winkler & Son, Inc. v. Ohio Casualty Insurance Co.*,¹⁶³ the Court of Special Appeals of Maryland addressed whether an insurer had an obligation to defend its insured, a jewelry store owner, in a suit for false arrest, slander, and malicious prosecution arising from false accusations of shoplifting.¹⁶⁴ Construing the term “accident,” the court looked first to the dictionary to determine the word’s customary and ordinary meaning.¹⁶⁵ The court of special appeals recited the definition adopted in *Harleysville*, adding that the key consideration is the “unexpected nature of the event or its aftermath.”¹⁶⁶ Applying this formulation, the court concluded that the insured’s actions were deliberate and that the effect was well within the insured’s foresight and expectation.¹⁶⁷ Hence, the court held the insurer had no duty to defend.¹⁶⁸

In *IA Construction Corp. v. T & T Surveying, Inc.*,¹⁶⁹ the United States District Court for the District of Maryland addressed whether an insured subcontractor’s surveying error was an accident covered

161. *Id.* at 619, 255 A.2d at 298 (quoting *Harleysville*, 248 Md. at 151-52, 235 A.2d at 558).

162. *Id.* at 620, 255 A.2d at 299.

163. 51 Md. App. 190, 441 A.2d 1129 (1982), *overruled by* *Sheets v. Brethren Mut. Ins. Co.*, 342 Md. 634, 654, 679 A.2d 540, 550 (1996).

164. *See Ed. Winkler*, 57 Md. App. at 191, 441 A.2d at 1130.

165. *See id.* at 194, 441 A.2d at 1132 (discussing *Harleysville*, 248 Md. at 151, 235 A.2d at 558, regarding the proposition that courts should look to a dictionary as a starting point for determining customary and normal meaning).

166. *Id.* at 194, 441 A.2d at 1132. The court quoted 7A APPLEMAN, *supra* note 18, § 4492, at 17: “‘As used in insurance policies[,], “accident”] is simply an undesigned, sudden, and unexpected event, usually of an afflictive or unfortunate character, and often accompanied by a manifestation of force, but it does not mean the natural and ordinary consequences of a negligent act.’” *Ed. Winkler*, 51 Md. App. at 195, 441 A.2d at 1132.

167. *See Ed. Winkler*, 51 Md. App. at 195, 441 A.2d at 1132.

168. The court held that because it was “clear” that the actions taken by the insured were not an accident, there was no potentiality that the claim was covered under the policy; therefore, the insurer had no duty to defend. *See id.* at 196, 441 A.2d at 1133.

169. 822 F. Supp. 1213 (D. Md. 1993) (mem.), *cited with disapproval in* *Sheets v. Brethren Mutual Ins. Co.*, 342 Md. 634, 654 n.4, 679 A.2d 540, 550 n.4 (1996).

under its CGL.¹⁷⁰ In the underlying suit, a general contractor had been commissioned to build a passenger train platform at Camden Yards Station in Baltimore.¹⁷¹ The general contractor sued the insured subcontractor, asserting claims of negligence, professional malpractice, and breach of contract based on the subcontractor's alleged use of erroneous data in laying the platform's foundation.¹⁷² In a declaratory judgment action to determine coverage under the subcontractor's CGL, the district court held that the subcontractor's insurer was not obligated to indemnify.¹⁷³ The district court explicitly followed the definition in *Ed. Winkler*, that an " 'accident' means an 'undesigned, sudden and unexpected event, usually of an afflictive or unfortunate character, and often accompanied by a manifestation of force, but it does not mean the natural and ordinary consequences of a negligent act.' "¹⁷⁴ In denying the insurer's obligation to indemnify, the judge opined: "[T]his is the stuff of the construction trade (and of professional malpractice insurance), not a risk protected against by a general liability policy."¹⁷⁵

D. *The Tort of Negligent Misrepresentation Under Maryland Law*

The tort of negligent misrepresentation was not recognized at early common law.¹⁷⁶ A plaintiff injured by false representations could bring an action only for fraud.¹⁷⁷ This limitation caused many hardships because an action for fraud requires a plaintiff to prove that the defendant made a false statement with *scienter*, an intent to defraud.¹⁷⁸ An honest belief, no matter how unreasonable, does not

170. See *IA Constr. Corp.*, 822 F. Supp. at 1214.

171. See *id.*

172. See *id.* The general contractor had to demolish portions of its completed work because the platform was at the wrong level. See *id.* Because the court found no accident, it never reached the issue of whether the damages prayed for constituted property damage within the terms of the policy. See *id.* at 1215 n.2. But see Leder, *supra* note 12, at C-9 (stating that the court in *IA Constr. Corp.* did find property damage).

173. See *IA Constr. Corp.*, 822 F. Supp. at 1215.

174. *Id.* (quoting *Ed. Winkler*, 51 Md. App. at 195, 441 A.2d at 1132).

175. *Id.* at 1215.

176. See *Martens Chevrolet, Inc. v. Seney*, 292 Md. 328, 333, 439 A.2d 534, 537 (1982); see also RICHARD J. GILBERT & PAUL T. GILBERT, *MARYLAND TORT LAW HANDBOOK* § 17.4, at 197 (2d ed. 1992).

177. See *Martens Chevrolet*, 292 Md. at 333, 439 A.2d at 537.

178. See, e.g., *Suburban Properties Management, Inc. v. Johnson*, 236 Md. 455, 460, 204 A.2d 326, 329 (1964); see also *Martens Chevrolet*, 292 Md. at 334, 439 A.2d at 537-38 (recognizing that the tort of negligent misrepresentation stemmed from the recognition of the hardships resulting from the strictures of an ac-

satisfy the requirement of *scienter* if the speaker has information to justify it.¹⁷⁹

In *Virginia Dare Stores v. Schuman*,¹⁸⁰ the court of appeals first recognized the tort of negligent misrepresentation in Maryland.¹⁸¹ The plaintiff, a cleaning laborer, and the defendant, a store owner, stood as employer-employee at the time of the misrepresentation.¹⁸² An agent of the store owner told the laborer that a dress display case was sturdy enough to stand on while cleaning out-of-reach portions of the shop.¹⁸³ Relying on the agent's statement, the laborer stepped onto the case and it collapsed, injuring the laborer.¹⁸⁴ Recognizing recovery for negligent statements, the court outlined the elements of negligent representation:

[Negligent misrepresentation] is not necessarily confined to injuries arising from contractual relations; that the action lies for negligent words, recovery being permitted where one relies on the statements of another, negligently volunteering an erroneous opinion, intending that it be acted upon, and knowing that loss or injury are likely to follow if it is acted upon.¹⁸⁵

Since *Virginia Dare Stores*, the elements for misrepresentation have remained constant.¹⁸⁶ To state a cause of action for negligent

tion for deceit); GILBERT & GILBERT, *supra* note 176, § 17.1.4, at 193; W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 107, at 741 (5th ed. 1984).

179. See *Donnelly v. Baltimore Trust & Guar. Co.*, 102 Md. 1, 30, 61 A. 301, 312-13 (1905) (quoting *Derry v. Peek*, 14 App. Cas. 337 (H.L. 1889)).

180. 175 Md. 287, 1 A.2d 897 (1938).

181. See *id.* at 291-92, 1 A.2d at 899.

182. See *id.* at 287, 1 A.2d at 898-99. The plaintiff was actually employed by a company contracting with the defendant store owner. Nonetheless, the court concluded that the defendant owed some duty, either as an employee of the store's contractor or as an individual doing work both on the defendant's premises and under the defendant's direction. See *id.* at 291, 1 A.2d at 898-99 (by implication).

183. See *id.* at 290, 1 A.2d at 900.

184. See *id.*

185. *Id.* at 291-92, 1 A.2d at 899. The *Virginia Dares Stores* court primarily relied on two cases from other jurisdictions. See *id.* (citing *International Prod. Co. v. Erie R.R. Co.*, 155 N.E. 662 (N.Y. 1927), and *Cunningham v. C.R. Pease House Furnishing Co.*, 69 A. 120 (N.H. 1908)).

186. See, e.g., *Gross v. Sussex, Inc.*, 332 Md. 247, 259, 630 A.2d 1156, 1162 (1993); *Weisman v. Connors*, 312 Md. 428, 444, 540 A.2d 783, 791 (1988); *Holt v. Kolker*, 189 Md. 636, 639, 57 A.2d 287, 288 (1948); *Virginia Dare Stores*, 175 Md.

misrepresentation under Maryland law, a plaintiff must establish the following five elements: (1) the defendant owes a duty of care to the plaintiff; (2) the defendant negligently asserts a false statement of material fact; (3) the defendant intends that the statement be relied upon by the plaintiff; (4) the defendant knows that the plaintiff intends to rely upon the statement; and (5) the plaintiff relies upon the statement, sustaining damage as a direct result of the misstatement.¹⁸⁷

1. Arm's Length Transactions

After some confusion as to the viability of the tort of negligent misrepresentation,¹⁸⁸ the court of appeals extended the tort to arm's length transactions in *Martens Chevrolet, Inc. v. Seney*.¹⁸⁹ The plaintiff, a purchaser of an automobile dealership, brought suit against the seller for, *inter alia*, alleged negligent misrepresentations concerning the financial conditions of the company.¹⁹⁰ The issues before the court were whether the tort of negligent misrepresentation was still viable and, if so, whether arm's length transactions qualified as proper subjects of the tort.¹⁹¹ The court held affirmatively on both issues.¹⁹² Additionally, the court held that an integration clause in a

at 291-92, 1 A.2d at 899.

187. See, e.g., *Weisman*, 312 Md. at 444, 540 A.2d at 791.

188. After *Virginia Dare Stores*, the court of appeals limited the tort of negligent misrepresentation to personal injuries. See *Holt*, 189 Md. at 639, 57 A.2d at 288. In *Holt*, a plumber told the plaintiff that a porch was safe to walk on. Relying on the plumber's statement, the plaintiff stepped on the porch and fell through. See *id.* at 638-39, 57 A.2d at 288. The court held that there was no liability because the plumber owed no duty to make accurate representations. See *id.* In dicta, the court of appeals limited the tort to personal injuries only. See *id.* at 639, 57 A.2d at 288.

In *Brack v. Evans*, 230 Md. 548, 187 A.2d 880 (1963), the court of appeals addressed whether economic losses could be recovered in an action for negligent misrepresentation. In *Brack*, the plaintiff sought damages for negligent misrepresentations by a stockbroker. See *id.* at 552-53, 187 A.2d at 882. The court held that economic losses could be recovered for negligent misrepresentation. See *id.* at 554, 187 A.2d at 883 (implied holding).

In a later case, the court implied that the tort was no longer viable. See *Delmarva Drilling Co. v. Tuckahoe Shopping Ctr., Inc.*, 268 Md. 417, 427, 302 A.2d 37, 41-42 (1973).

189. 292 Md. 328, 338 n.7, 439 A.2d 534, 539-40 n.7 (1982).

190. See *id.* at 330, 439 A.2d at 536. For an in-depth discussion of *Martens Chevrolet*, see Susan F. Martielli, Note, *Martens Chevrolet v. Seney—Extending the Tort of Negligent Misrepresentation*, 42 MD. L. REV. 596 (1983).

191. See *Martens Chevrolet*, 292 Md. at 338 n.7, 439 A.2d at 539-40 n.7.

192. See *id.*

contract does not shield parties from tort liability for misrepresentations.¹⁹³ If the rule were otherwise, the court reasoned, the effect would be to permit parties to circumvent the implied covenant of good faith in every contract.¹⁹⁴

2. Limited to Statements of Fact³

In *Weisman v. Connors*,¹⁹⁵ the court of appeals addressed whether an employee could maintain a cause of action against his employer for negligent misrepresentation of future intentions and current facts at the time of entering into an employment contract.¹⁹⁶ The plaintiff succeeded at trial in obtaining a jury verdict in excess of two million dollars based on evidence that his employer lied at the time of contracting.¹⁹⁷ In reviewing the record, the court of appeals found no evidence that the employer negligently misrepresented his intentions and that the evidence established that the employer was merely clarifying the actual duties entailed in this newly created position.¹⁹⁸ However, the court reasoned that the verdict might have rested solely on negligent misrepresentations concerning the current state of affairs at the place of employment, a proper basis for liability because the statements did not involve the employer's intentions or expectations.¹⁹⁹ Moreover, the court stated that in "making representations, 'the negligence may occur in either obtaining or in communicating the information'" relating to past or present facts.²⁰⁰ Thus, because the jury's verdict regarding negligent representation could have been based on either state-

193. *See id.* The integration clause in *Martens Chevrolet* provided: "[This contract] supersedes all prior and contemporaneous agreements and understandings, inducements or conditions, expressed or implied, oral or written . . ." *Id.*

194. *See id.*

195. 312 Md. 428, 540 A.2d 783 (1988).

196. *See id.* at 441, 540 A.2d at 789. The *Weisman* opinion contains an in-depth discussion of the historical development of the tort of negligent misrepresentation in Maryland. *See id.* at 443-48, 540 A.2d at 790-93.

197. The court of special appeals affirmed. *See Weisman v. Connors*, 69 Md. App. 732, 736-37, 519 A.2d 795, 797 (1987).

198. *See Weisman*, 312 Md. at 454, 540 A.2d at 796.

199. *See id.* at 457-58, 540 A.2d at 797-98.

200. *Id.* at 456, 540 A.2d at 796 (citation omitted). The court also highlighted that four of the representations were in a written contract, raising the issue of whether statements in a contract can serve as a basis for a negligent misrepresentation claim. *See id.* at 456 n.4, 540 A.2d at 797 n.4. Reserving judgment, the court noted "that the availability of both tort and contract actions for the same kind of harm has engendered considerable confusion and complexity." *Id.* (citing *KEETON ET AL.*, *supra* note 178, § 92, at 655).

ments concerning facts or intentions, the court remanded for consideration of only the factual representations.²⁰¹

3. Measure of Damages

In an extensive footnote, the *Weisman* court noted that damages in negligent misrepresentation claims should be measured under the flexibility rule set forth in *Hinkle v. Rockville Motor Co.*²⁰² In *Hinkle*, the Court of Appeals of Maryland addressed the proper method for calculation of damages in suits alleging fraud.²⁰³ The *Hinkle* court noted that it previously accepted both the “benefit-of-the-bargain” and “out-of-pocket” calculations, never adopting either approach to the exclusion of the other.²⁰⁴ Because fraud is founded on a breach of contract, the *Hinkle* court reasoned, either approach is appropriate.²⁰⁵ Hence, the court adopted four guidelines comprising the flexibility rule in measuring damages for fraud:

- “(1) If the defrauded party is content with the recovery of only the amount he actually lost, his damages will be measured under that rule;
- (2) if the fraudulent representation also amounted to a warranty, recovery may be had for loss of the bargain because a fraud accompanied by a broken promise should cost the wrongdoer as much as the latter alone;
- (3) where the circumstances disclosed by the proof are so vague as to cast virtually no light upon the value of the property had it conformed to the representations, the court will award damages equal only to the loss sustained; and
- (4) where . . . the damages under the benefit of the bargain rule are proved with sufficient certainty, that rule will be employed.”²⁰⁶

201. *See id.* at 460, 540 A.2d at 799.

202. 262 Md. 502, 278 A.2d 42 (1971), *cited in Weisman*, 312 Md. at 459-60 n.6, 540 A.2d at 798 n.6.

203. *See Hinkle*, 262 Md. at 504, 278 A.2d at 43.

204. *See id.* at 510, 278 A.2d at 46-47.

205. *See id.* at 510, 278 A.2d at 47 (quoting *Webster v. Woolford*, 81 Md. 329, 330, 32 A. 319, 320 (1895) (“The action, it is true, is in the nature of an action for tort (deceit), but it is a tort founded on a breach of contract (in regard to the sale of property), and, there being no question as to exemplary damages, the rule as to the measure of damages is the same as in case for breach of contract in regard to the sale of property.”)).

4. Reasonableness of Reliance

In *Village of Cross Keys, Inc. v. United States Gypsum Co.*,²⁰⁷ the court of appeals addressed the requisite reasonableness of a plaintiff's reliance in a negligent misrepresentation claim.²⁰⁸ The plaintiffs, an architect and a developer, sued United States Gypsum, Inc. for, *inter alia*, negligent misrepresentation based on allegedly defective specifications contained in a brochure promoting the defendant's brick veneer.²⁰⁹ The court held that the plaintiffs' reliance on the plans in the brochure was not reasonable because the plaintiffs did not even use the defendant's products as specified in the brochure.²¹⁰ The court noted that the tort of negligent misrepresentation is more restrictive than fraud; moreover, the court concluded that liability for negligent misrepresentation is more narrow when complaining of only pecuniary loss.²¹¹

E. *The Duty to Defend Negligent Misrepresentation Claims*

Whether CGL insurers have a duty to defend against negligent misrepresentation claims raises three issues. First, does a negligent misrepresentation constitute an occurrence?²¹² Second, does a negligent misrepresentation result in property damage?²¹³ Third, notwithstanding the first two issues, does any exclusion preclude coverage?²¹⁴

Only a relatively small number of jurisdictions have directly confronted these issues. For ease in organization, this Note divides those jurisdictions into two categories: (1) jurisdictions that hold CGLs do not cover liability for negligent misrepresentations (major-

206. *Id.* at 511-12, 278 A.2d at 47 (alteration in original) (quoting *Selman v. Shirley*, 85 P.2d 384, 394 (Or. 1938)).

207. 315 Md. 741, 556 A.2d 1126 (1989).

208. *See id.* at 759-60, 556 A.2d at 1134-35.

209. *See id.* at 744, 556 A.2d at 1127.

210. *See id.* at 760, 556 A.2d at 1135.

211. *See id.* at 756-57, 556 A.2d at 1133 (citing RESTATEMENT (SECOND) OF TORTS §§ 311, 552 (1965)).

212. For an in-depth discussion of judicial construction of the term "occurrence," see *supra* notes 133-75 and accompanying text.

213. For an in-depth discussion of judicial construction of the term "property damage," see *supra* notes 87-132 and accompanying text.

214. *See generally* *Gov't Employees Ins. Co. v. Ropka*, 74 Md. App. 249, 257, 536 A.2d 1214, 1218 (1988) (noting that an insurer has no duty to defend if liability comes within an exclusion in the policy).

ity); and (2) those that hold CGLs do cover liability for negligent misrepresentations (minority).

1. Majority Rule: Liability for Negligent Misrepresentations is not Covered Under CGLs

In *Safeco Insurance Co. of America v. Andrews*,²¹⁵ the United States Court of Appeals for the Ninth Circuit decided the seminal case regarding CGL²¹⁶ insurers' duty to defend against negligent misrepresentation claims. In *Safeco*, an insured seller of a home brought an action against its insurer seeking a declaration that the insurer had a duty to defend in an underlying suit.²¹⁷ In the underlying suit, the purchaser of the home sued the insured seller for, *inter alia*, negligent misrepresentation based on the seller's failure to inspect the home and inform the purchaser of material facts affecting its value, including defective drainage from the main sewer line.²¹⁸ Thus, the *Safeco* court addressed whether negligent misrepresentation may constitute an accident and, if so, whether the damages sought were property damage.²¹⁹

The *Safeco* court held that the relief sought did not constitute property damage.²²⁰ The court reasoned that the purchaser was seeking damages for economic loss—the difference between the actual value of the property and its value as represented—not damage to tangible property.²²¹ Moreover, the court reasoned, even if the relief sought was property damage under the policy, the alleged misrepresentations were not “an ‘occurrence’ or a ‘peril insured against’ under the terms of the policy.”²²² Therefore, there being no

215. 915 F.2d 500 (9th Cir. 1990) (applying California law).

216. The policy at issue in *Safeco* was a homeowner's policy. *See id.* at 501. Nevertheless, the language at issue was substantially the same as in the CGLs. *See generally* Tinker, *supra* note 11, at 218 (noting that because CGL language is found in other liability forms, principles and precedents overlap between CGLs and other forms of liability policies).

217. *See Safeco*, 915 F.2d at 501.

218. *See id.* The purchaser claimed that the seller failed to disclose that the land was susceptible to landslides, the electrical wiring and plumbing was defective, and the basement leaked. *See id.*

219. *See id.* at 501-02.

220. *See id.* at 502.

221. *See id.* (“[The] claims do not expose [the insured] to liability for any damage to tangible property, but rather for economic loss resulting from [the insured's] alleged failure to discover and disclose facts relevant to the property's value and desirability.”).

222. *Id.*

potentiality that the insurer would be liable for a judgment against the insured, the court held that the insurer had no duty to defend.²²³

The majority of jurisdictions that have addressed the issue have followed the *Safeco* decision.²²⁴ To date, jurisdictions holding CGLs

223. *See id.*

224. *See* State Farm Fire & Cas. Co. v. Brewer, 914 F. Supp. 140, 142-43 (S.D. Miss. 1996) (applying Mississippi law; finding negligent misrepresentation did not result in property damage); Safeco Ins. Co. of Am. v. Tozier, No. CIV.A.93-2453-GTV, 1994 WL 476304, at *3 (D. Kan. Aug. 16, 1994) (applying Kansas law; finding negligent misrepresentation did not result in property damage); M.L. Foss, Inc. v. Liberty Mut. Ins. Co., 885 P.2d 284, 285-86 (Col. Ct. App. 1994) (maintaining that negligent misrepresentation is not an occurrence and, nevertheless, did not result in property damage); SCA Disposal Services of New England, Inc. v. Central Nat'l Ins. Co. of Omaha, No. 900393, 1994 WL 879689, at *4 (Mass. Super. Apr. 12, 1994) (finding losses caused by negligent misrepresentation were not property damage); Martin v. State Farm Fire & Cas. Co., 932 P.2d 1207, 1213 (Or. Ct. App. 1997) (“[The misrepresentation] claim is not based on physical damage to the property but on the liability that the plaintiffs incurred when they purchased it.”); State Farm Lloyds v. Kessler, 932 S.W.2d 732, 738-39 (Tex. Ct. App. 1996) (finding negligent misrepresentation is not an occurrence and damage therefrom is economic loss, not property damage); Qualman v. Bruckmoser, 471 N.W.2d 282, 285 (Wis. Ct. App. 1991) (finding negligent misrepresentation did not result in property damage, including loss of use); *see also* United States Fidelity & Guar. Co. v. Warwick Dev. Co., 446 So. 2d 1021, 1023 (Ala. 1984) (holding misrepresentations are not an occurrence and do not result in property damage), *quoted in* State Farm Fire & Cas. Co. v. Gwin, 658 So. 2d 426, 428 (Ala. 1995); Aetna Cas. & Sur. Co. v. Cotter, 522 N.E.2d 1013, 1015 (Mass. Ct. App. 1988) (finding misrepresentation did not produce bodily injury or property damage); Tschimperle v. Aetna Cas. & Sur. Co., 529 N.W.2d 421, 424-25 (Minn. Ct. App. 1995) (holding negligent misrepresentation cannot be an accident and resulting loss of investment does not constitute property damage); Fisher v. Fitchburg Mut. Ins. Co., 560 A.2d 630, 632-33 (N.H. 1989) (finding negligent misrepresentation not an occurrence and resulting loss did not constitute property damage); First Wyo. Bank, N.A., Jackson Hole v. Continental Ins. Co., 860 P.2d 1094, 1101 (Wyo. 1993) (finding negligent misrepresentation not an occurrence and declining to address “property damage” issue). *But see* First Newton Nat'l Bank v. General Cas. Co. of Wis., 426 N.W.2d 618, 624-26 (Iowa 1988) (finding negligent misrepresentation constitutes an occurrence); Colomb v. United States Fidelity & Guar. Co., 539 So. 2d 940, 942 (La. Ct. App. 1989) (implied holding) (distinguishing between breach of contract and negligent misrepresentation, and implying the latter constitutes an occurrence); Sheets v. Brethren Mut. Ins. Co., 342 Md. 634, 645, 657, 679 A.2d 540, 545, 551 (1996) (holding negligent misrepresentation constitutes an occurrence if resulting damage is neither expected nor foreseen and, under the facts, damage was property damage in the form of loss of use); Commercial

do not cover liability from negligent misrepresentations, either because of lack of an occurrence or property damage, include Alabama, California, Colorado, Massachusetts, Minnesota, New Hampshire, Oregon, Texas, Wisconsin, and Wyoming.²²⁵

Courts in the majority have offered further clarification and rationale for the *Safeco* holdings. Regarding the "property damage" holding, some courts explained the lack of property damage from misrepresentations in terms of a lack of a causal nexus.²²⁶ For exam-

Union Ins. Co. v. Royal Ins. Co., 658 A.2d 1081, 1082-83 (Me. 1995) (implied holding) (assuming that negligent misrepresentation claim would be potentially covered if it happened when policy was active, thereby implying negligent misrepresentation constitutes an occurrence); Aetna Cas. & Sur. Co. v. Metropolitan Baptist Church, 967 F. Supp. 217, 223 (S.D. Tex. 1996) (applying Texas law; holding negligent misrepresentation constitutes an accident); State Farm Fire & Cas. Co. v. Helminiak, 659 N.E.2d 385, 389 (Ohio Ct. C.P. 1995) (holding negligent misrepresentation constitutes an accident); see also *SL Indus., Inc. v. American Motorists Ins. Co.*, 607 A.2d 1266, 1276-77 (N.J. 1992) (holding common law fraud may constitute an occurrence so long as the insured did not subjectively intend to inflict the harm alleged).

Note that the federal district court in *Metropolitan Baptist Church* and the Court of Appeals of Texas are in direct conflict over the status of Texas law on this issue. Compare *Metropolitan Baptist Church*, 967 F. Supp. at 223-24 (noting on December 16, 1996 that the issue has not been addressed by the Texas courts, and holding negligent misrepresentation constitutes an occurrence), with *Kessler*, 932 S.W.2d at 738-39 (holding on October 31, 1996 that negligent misrepresentation is not an occurrence and that damage therefrom is economic loss, not property damage).

225. See cases cited *supra* note 224 (providing precedent from Alabama, Colorado, Kansas (federal district court opinion), Massachusetts, Minnesota, Mississippi (federal district court opinion), New Hampshire, Oregon, Texas, Wisconsin, and Wyoming); *Safeco*, 915 F.2d at 502 (California).
226. See, e.g., *Martin*, 932 P.2d at 1213 ("There is thus no causal connection between the misrepresentations and the physical damage; the only causal connection is with damage to the plaintiffs' economic interests, which the policies do not cover."); *SCA Disposal Services*, 1994 WL 879689, at *4 ("[T]here is no causal connection between [the insured's] alleged misrepresentations . . . and the property damage at the site."); *Kessler*, 932 S.W.2d at 737 ("The [insureds'] alleged misrepresentations did not cause the drainage and foundation problems; those problems existed before negotiations began."); see also *Brewer*, 914 F. Supp. at 142-43 ("The alleged misrepresentation of Defendants did not cause property damage. The termites caused the property damage."); *Gwin*, 658 So. 2d at 428 ("[W]e must conclude that any alleged misrepresentations . . . did not cause the [termite damage] . . ."); *Qualman*, 471 N.W.2d at 285 ("There is no question that the defective condition of the house is an element in the [plaintiffs'] complaint. Nevertheless, those defects cannot be considered the cause of the [plaintiffs'] damages . . .").

ple, in *Martin v. State Farm Fire & Casualty Co.*,²²⁷ the Court of Appeals of Oregon noted that the underlying misrepresentation claim was predicated on property damage in the form of contamination.²²⁸ However, the court found that the complaint did not allege that the misrepresentation caused the damage; rather, the complaint alleged that the misrepresentation caused the plaintiffs to buy property that was already damaged.²²⁹ Thus, the court found that there was no causal connection between the damage and the misrepresentation.²³⁰

Regarding the *Safeco* "occurrence" holding, many courts following *Safeco* have focused on the relationship between negligent misrepresentation and fraud. For example, in *Chatton v. National Union Fire Insurance Co. of Pittsburgh*,²³¹ the California Court of Appeals, adhering to the rule adopted in *Safeco*, stated that the rationale for not treating negligent misrepresentation as an accident is that the claim requires an element of intentional action—intent to induce reliance.²³² Thus, the tort is a subspecies of fraud.²³³

As with the opinion in *Chatton*, most courts following *Safeco* have held, at least alternatively, that negligent misrepresentation does not constitute an accident and that the damages sought in a negligent misrepresentation action do not constitute property damage.²³⁴

In *First Wyoming Bank, N.A., Jackson Hole v. Continental Ins. Co.*,²³⁵ the Supreme Court of Wyoming decided whether, under a CGL, an insurer of a bank had a duty to defend against a claim of negligent

227. 932 P.2d 1207 (Or. Ct. App. 1996).

228. *See id.* at 1213.

229. *See id.*

230. *See id.*

231. 10 Cal. App. 4th 846 (Cal. Ct. App. 1992).

232. *See id.* at 861.

233. *See id.* at 861-62 (citing, *e.g.*, *Gagne v. Bertran*, 275 P.2d 15 (Cal. 1954)).

234. *See, e.g.*, *Tschimperle v. Aetna Cas. & Sur. Co.*, 529 N.W.2d 421, 424-25 (Minn. Ct. App. 1995) (deciding whether investment company's misrepresentations to investors were accidents and whether loss of investment was property damage under CGL, and holding both negligent misrepresentation and damages therefrom do not constitute accident and property damage, respectively). *But cf.* *Western Cas. & Sur. Co. v. Hays*, 781 P.2d 38, 41 (Ariz. Ct. App. 1989) (following majority rule that negligent misrepresentation does not constitute an accident, yet declining to consider the alternative holding that losses were not property damage covered under the policy).

235. 860 P.2d 1094 (Wyo. 1993).

misrepresentation involving loans.²³⁶ The court added a new perspective to the *Safeco* rationale. The court reiterated that the intentional element of the claim, inducing reliance, precluded the claim from being an accident.²³⁷ The court added, moreover, that the claim asserted against the bank was essentially a breach of contract claim.²³⁸ Noting that it had previously construed the term "accident" as not encompassing coverage for breach of contract,²³⁹ the court reasoned that the insured bank's attempt to make a distinction between a careful breach, which would not be an accident, and a negligent breach, which would be an accident, was a "unique, creative idea" that finds no support in case law.²⁴⁰

a. *Effect of "Premises Alienated" Exclusion*

Every CGL since 1943 has contained a "premises alienated" exclusion.²⁴¹ This exclusion provides that the policy does not cover "property damage to premises alienated by the named insured arising out of such premises or any part thereof . . ." ²⁴² This exclusion is intended to preclude coverage where the insured fails to disclose the existence of a defect or to repair property prior to its sale.²⁴³

In *Stull v. American States Insurance Co.*,²⁴⁴ the United States District Court for the District of Maryland addressed whether, under

236. *See id.* at 1099.

237. *See id.* at 1100 (citing *Dykstra v. Foremost Ins. Co.*, 17 Cal. Rptr. 2d 543 (Cal. Ct. App. 1993)).

238. *See id.* at 1099.

239. *See id.* (quoting *Action Ads, Inc. v. Great Am. Ins. Co.*, 685 P.2d 42, 45 (Wyo. 1984) ("We conclude that the coverage clause . . . encompasses liability which the law imposes on all insureds for their tortious conduct and not on the liability which a particular insured may choose to assume pursuant to contract.")).

240. *Id.* at 1100 ("The [b]ank's position seems to be that a careful breach of contract is an action only in contract but a negligent breach sounds in both contract and tort. We find no law to support this unique, creative idea.").

241. *See Tinker, supra* note 11, at 278.

242. *Tinker, supra* note 11, at 278 (1973 CGL); *accord Leder, supra* note 12, at C-55 (1986 CGL) (precluding coverage for " 'Property damage' to: . . . (2) Premises you sell, give away or abandon, if the 'property damage' arises out of any part of those premises"); *Leder, supra* note 12, at C-108 (1996 CGL) (same). Since 1986, the premises alienated, owned property, and care, custody, and control exclusions have been merged into one exclusion. *See Leder, supra* note 12, at C-55. For a discussion of the premises alienated exclusion, see 2 WINDT, *supra* note 100, § 11.17, at 291.

243. *See Leder, supra* note 12, at C-57.

244. 963 F. Supp. 492 (D. Md. 1997) (applying Maryland law).

Maryland law, a CGL insurer had a duty to defend its insured, a gasoline station owner, against a negligent misrepresentation claim.²⁴⁵ The underlying claim was based on representations made to the purchaser of the station regarding the quality of the groundwater.²⁴⁶ In the declaratory judgment action, the insurer asserted three defenses, including that the premises alienated exclusion precluded coverage.²⁴⁷

The district court held in favor of the insurer, finding that the premises alienated exclusion precluded coverage.²⁴⁸ The court noted that no Maryland court had ever construed the premises alienated clause.²⁴⁹ Relying on *Reliance Insurance Co. v. Povia-Ballatine*,²⁵⁰ the court found that the exclusion operated to exclude claims based on the sale of the insured's real property regardless of when the alleged wrongful act occurred.²⁵¹

b. Effect of "Owned Property" Exclusion

CGLs are only designed to cover liability to third persons.²⁵² Thus, CGLs contain provisions that specifically exclude coverage for loss sustained by the insured. One such provision is the "owned property" exclusion.²⁵³ With slight modification depending on the version of CGL, this provision excludes coverage for "property damage to . . . property owned or occupied by or rented to the insured."²⁵⁴

245. *See id.* at 493.

246. *See id.*

247. *See id.* The insurer also asserted that damages were not caused by an occurrence, and, even if they were, the pollution exclusion clause precluded coverage. *See id.*

248. *See id.* at 494.

249. *See id.*

250. 738 F. Supp. 523 (S.D. Ga. 1990).

251. *See Stull*, 963 F. Supp. at 494.

252. *See, e.g., Leder, supra* note 12, at C-56 (citing *Bausch & Lomb v. Utica Mut. Ins. Co.*, 330 Md. 758, 625 A.2d 1021 (1993)).

253. *See generally Leder, supra* note 12, at C-55 (explaining premises alienated, owned property, and care, custody, and control exclusions have been merged into one exclusion).

254. *Tinker, supra* note 11, at 275 (1973 CGL); *accord Leder, supra* note 12, at C-55 (1986 CGL). *See generally* *Goldsborough & Grube, supra* note 85, at 37-41 (explaining the owned property exclusion); *Tinker, supra* note 11, at 275-76 (same). Notably, the CGL construed in *Sheets* contained the owned property exclusion. *See* Joint Record Extract at 91, *Sheets v. Brethren Mut. Ins. Co.*, 342 Md. 634, 679 A.2d 540 (1996) (No. 95-47, Sept. Term, 1995) (exclusion "q.").

In *Allstate Insurance Co. v. Chaney*,²⁵⁵ the United States District Court for the Northern District of California held that even if negligent misrepresentation in the sale of a home amounts to property damage, as opposed to economic loss, such damages are excluded under the owned property exclusion.²⁵⁶ Noting that the insured sellers owned the property at the time of the misrepresentation, the *Chaney* court found no potentiality of coverage for the negligent misrepresentation claim.²⁵⁷

2. Minority Position: Liability for Negligent Misrepresentations is Covered Under CGLs

A minority of jurisdictions that have addressed the issue hold that CGLs cover liability for negligent misrepresentations.²⁵⁸ To date, these jurisdictions include Iowa, Louisiana, Maryland, Maine, New

255. 804 F. Supp. 1219 (N.D. Cal. 1992) (Armstrong, J.). Note that the two cases providing contrasting constructions of the CGL are from the same federal district. See *infra* note 274 and accompanying text.

256. See *Chaney*, 804 F. Supp. at 1223.

257. See *id.* Along the same line of reasoning, a Massachusetts court held that personal injuries inflicted on a purchaser of a home were not covered under the seller's homeowner policy because the injuries manifested after termination of the policy. See *Frohberg v. Merrimack Mut. Fire Ins. Co.*, 612 N.E.2d 273, 275 (Mass. App. Ct. 1993). The *Frohberg* court addressed a misrepresentation claim in which the plaintiff sought damages for respiratory injury caused by inhaling formaldehyde foam insulation, which the insured seller represented was not present in the home. See *id.* at 274 & n.1.

258. See *First Newton Nat'l Bank v. General Cas. Co.*, 426 N.W.2d 618, 624-26 (Iowa 1988) (finding negligent misrepresentation constitutes an occurrence); *Colomb v. United States Fidelity & Guar. Co.*, 539 So. 2d 940, 942 (La. Ct. App. 1989) (implied holding) (distinguishing between breach of contract and negligent misrepresentation, thereby implying that the latter constitutes an occurrence); *Sheets*, 342 Md. at 645, 657, 679 A.2d at 545, 551 (holding negligent misrepresentation constitutes an occurrence if the resulting damage is neither expected nor foreseen, and, under facts, damage was covered by the loss of use prong); *Commercial Union Ins. Co. v. Royal Ins. Co.*, 658 A.2d 1081, 1083 (Me. 1995) (implied holding) (assuming that a policy, if active, would potentially cover a negligent misrepresentation claim, thereby implying negligent misrepresentation constitutes an occurrence); *SL Indus., Inc. v. American Motorists Ins. Co.*, 607 A.2d 1266, 1276-77 (N.J. 1992) (holding common law fraud may constitute an occurrence so long as the insured did not subjectively intend to inflict the harm alleged, thereby implying that negligent misrepresentation constitutes an occurrence); *State Farm Fire & Cas. Co. v. Helminiak*, 659 N.E.2d 385, 389 (Ohio Ct. C.P. 1995) (holding that negligent misrepresentation constitutes an accident).

Jersey, and Ohio.²⁵⁹

In *First Newton National Bank v. General Casualty Co. of Wisconsin*,²⁶⁰ the Supreme Court of Iowa addressed whether, under two separate commercial liability policies,²⁶¹ an insurer had a duty to defend its insured bank against a negligent misrepresentation claim arising from the foreclosures on farm property.²⁶² In the underlying suit, two farm owners brought, *inter alia*, fraud and negligent misrepresentation claims against the bank based on a bank officer's advice to deal with a local investor.²⁶³ The farm owners asserted their claims as counterclaims when the bank attempted to foreclose on the farms after the investor failed to pay the mortgages that were in his name.²⁶⁴ *See id.* at 620-21.

The policies at issue defined "occurrence" as an accident, neither expected nor intended by the insured.²⁶⁵ The court noted that it previously held that a "happening" was neither expected nor intended so long as the insured did not intend or expect both the event and the resulting injury.²⁶⁶ In holding that negligent misrepresentation potentially falls within this definition, the court distinguished between negligent and fraudulent misrepresentation.²⁶⁷ The

259. *See supra* note 258 (providing precedent).

260. 426 N.W.2d 618 (Iowa 1988).

261. One policy was a multi-peril policy, and the other policy was a commercial umbrella policy. The multi-peril policy covered property damage, defined to include "loss of the use of tangible property which has not been physically injured or destroyed," caused by an occurrence, defined as "an accident . . . neither expected nor intended from the standpoint of the insured." *Id.* at 622. The multi-peril policy also contained a supplemental liability portion that extended coverage to personal injury "to which this insurance applies . . . arising out of the conduct of the named insured's business." *Id.* The umbrella policy covered property damage, defined essentially the same as in the multi-peril policy. *See id.*

262. *See id.* at 619-20.

263. *See id.* at 620-21. The other claims were constructive fraud and violation of the Iowa Uniform Securities Act. *See id.* at 621.

265. *See id.* at 624-25. Each policy phrased the definitions differently, but the court found the two sufficiently similar to analyze them under the same framework. *See id.* at 625.

266. *See id.* at 625 (citing *Altena v. United Fire & Cas. Co.*, 422 N.W.2d 485 (Iowa 1988)).

267. *See id.* (quoting *Gordon-Gallup Realtors, Inc. v. Cincinnati Ins. Co.*, 265 S.E.2d 38, 40 (S.C. 1980) (holding that because the policy expressly covers negligence, the insurer had a duty to defend against a negligent misrepresentation claim)). Notably, the insurance policies construed by the *First Newton* court did not expressly provide coverage for negligence. In fact, the commercial umbrella policy specifically excluded coverage for "claims arising out of error

court reasoned that the former connotes negligent rather than intentional conduct, and hence is encompassed under the term "accident."²⁶⁸ The court then addressed the insurer's assertion that the damages sought in the underlying claim did not allege property damage because there was no physical damage to the property.²⁶⁹ Pointing to the alternative definitions within both policies, which defined property damage to include loss of the use of property which is not physically injured, the court held that the plaintiffs alleged such loss by asserting that they will lose their homes, thus the loss of use.²⁷⁰

a. *Coverage Under BFE Advertising Injury Endorsement*

Between 1973 and 1985, the Broad Form Comprehensive General Liability Endorsement (BFE) provided optional endorsements that could be added to the CGL at additional cost.²⁷¹ Since 1986, these additional endorsements have been modified and incorporated into the CGL, thereby increasing the scope of coverage.²⁷² One of these additional endorsements, the "advertising injury" endorsement, provides coverage for advertising injury.²⁷³

In *American States Insurance Co. v. Canyon Creek*,²⁷⁴ the United States District Court for the Northern District of California held

or omission or a mistake." *Id.* at 622.

268. *See id.* at 625. The court also noted that negligent misrepresentation claims arise in the course of transactions in which the defendant has a pecuniary interest. *See id.* (quoting RESTATEMENT (SECOND) OF TORTS § 552 (1977)).

269. *See id.* at 626.

270. *See id.* The court stated that its holding was in step with the majority of courts which have addressed the property damage issue. *See id.* Notably, however, the opinions cited by the court primarily dealt with another issue: pecuniary loss as a loss of use. *See, e.g.,* Continental Cas. Co. v. Gilbane Bldg. Co., 461 N.E.2d 209, 212-13 (Mass. 1984), *cited in* First Newton Nat'l Bank, 426 N.W.2d at 626.

271. *See* Keville, *supra* note 3, at 926; Leder, *supra* note 12, at C-2.

272. *See* Keville, *supra* note 3, at 926; Leder, *supra* note 12, at C-2.

273. *See* Keville, *supra* note 3, at 926. The BFE did not contain the advertising injury endorsement until 1981. *See id.* The advertising injury endorsement provides coverage for, *inter alia*, "injury aris[ing] out of libel, slander, defamation, violation of right of privacy, piracy, unfair competition, or infringement of copyright, title or slogan." *See* Keville, *supra* note 3, at 926 (quoting 1981 BFE advertising injury endorsement). The 1986 CGL incorporates a modified version of the BFE, but it does not include coverage for defamation, piracy, and unfair competition. *See* Keville, *supra* note 3, at 927.

274. 786 F. Supp. 821 (N.D. Cal. 1991) (Orrick, J.). Note that the two cases providing contrasting constructions of the CGL are from the same federal district. *See supra* note 255 and accompanying text.

that the BFE advertising injury endorsement covered negligent misrepresentation claims.²⁷⁵ The court noted that although negligent misrepresentation does not constitute an occurrence,²⁷⁶ and damages sought were excluded economic losses,²⁷⁷ the claims were covered under the advertising injury endorsement—which included the term “unfair competition.”²⁷⁸

b. Coverage Under Commercial Umbrella Policy

In *Universal Underwriters Insurance Co. v. Youngblood*,²⁷⁹ the Supreme Court of Alabama addressed whether, under a commercial umbrella policy²⁸⁰ explicitly providing that the term “occurrence” includes negligence, an insurer had a duty to defend its insured, a car dealership.²⁸¹ In the underlying suit, employees of the insured alleged breach of employment contract, negligent hiring, and negligent misrepresentation, all of which arose from miscalculation of sales commissions and failure to pay insurance premiums as obligated.²⁸² The *Youngblood* court held that because the term “accident” does not exclude negligent actions, the insurer had a duty to defend its insured.²⁸³ Notably, however, the policy in question explicitly included coverage for negligent administration of the sort alleged in the underlying suit.²⁸⁴

275. See *Canyon Creek*, 786 F. Supp. at 827. The language was from the 1981 BFE. See *supra* note 273 (quoting 1981 BFE advertising injury endorsement). See Keville, *supra* note 3, for an in-depth discussion of all advertising injury provisions.

276. See *Canyon Creek*, 786 F. Supp. at 825.

277. See *id.*

278. See *id.* at 827. Note that the 1986 CGL, which incorporates much of the BFE, does not include coverage for unfair competition. See *supra* note 273.

279. 549 So. 2d 76 (Ala. 1989).

280. Commercial umbrella policies are relatively inexpensive policies designed to protect against rare catastrophic loss in the form of excess judgments. See Lisa K. Gregory, Annotation, “Excess” or “Umbrella” Insurance Policy as Providing Coverage for Accidents with Uninsured or Underinsured Motorists, 2 A.L.R.5th 922 (1992).

281. See *Youngblood*, 549 So. 2d at 77-78.

282. See *id.* at 77.

283. See *id.* at 78-79.

284. See *id.* The policy included coverage for negligent administration of the insured employer’s profit sharing, medical, hospitalization, and life insurance benefits programs. See *id.*

c. Coverage for Common Law Fraud Under CGL

In *SL Industries, Inc. v. American Motorists Insurance Co.*,²⁸⁵ the Supreme Court of New Jersey analyzed a CGL to determine whether an insurer had a duty to defend its insured against a claim for statutory age discrimination and common law fraud.²⁸⁶ An employee alleged that the CEO of the insured corporation induced the employee's early retirement by fraudulently misrepresenting the elimination of his position.²⁸⁷ After settling the claim, the insured corporation brought a declaratory judgment action against its insurer seeking a declaration that both the CGL and Comprehensive Catastrophe Liability Policy covered the claims, thereby requiring the insurer to indemnify it for the cost of litigation and settlement.²⁸⁸

The Supreme Court of New Jersey first disposed of the statutory age discrimination claim, holding that because the statute denied compensatory damages for emotional injuries caused by age discrimination, neither policy would cover this type of claim.²⁸⁹ The court then addressed whether the policies' provisions providing coverage for an occurrence could encompass the common law fraud claim. Both policies defined "occurrence" as "an accident . . . neither expected nor intended from the standpoint of the insured."²⁹⁰ The court noted that fraud has an intentional aspect, the intent to induce reliance on the false representation, which constitutes a subjective intent to injure.²⁹¹ Nonetheless, the court reasoned that in the context of insurance law, the intent to injure would not necessarily preclude the act from being deemed an accident.²⁹²

285. 607 A.2d 1266 (N.J. 1992).

286. *See id.* at 1269.

287. *See id.* The employee, an executive who agreed to retire on his 62nd birthday, alleged that the company hired a younger replacement several months before his departure. *See id.*

288. *See id.* at 1270. The corporation settled the claim for \$430,000 and spent approximately \$100,000 defending the suit. *See id.*

289. *See id.* at 1271.

290. *Id.* at 1269-70. The difference between the two policies was that the CGL provided coverage for bodily injury, defined as "injury, sickness or disease," while the Comprehensive Catastrophe Liability Policy provided coverage for personal injury, defined to include "humiliation." *Id.* at 1269-70.

291. *See id.* at 1277.

292. *See id.* (suggesting that there may be a middle ground between the two extremes, *i.e.*, between purely subjective and objective tests).

The court recited three possible interpretations of the definition of "accident" previously espoused by New Jersey courts: (1) that the subjective intent to injure precludes coverage because the act is not accidental, even if the injury inflicted differed from that intended;²⁹³ (2) that if the intentional act had the inherent probability of inflicting the degree of harm actually incurred, coverage would be denied—if it did not, the court would ascertain whether the actor intended the harm;²⁹⁴ and (3) that an accident will be found unless the actual harm inflicted conforms precisely with what the actor was substantially certain would result.²⁹⁵ In determining which approach to adopt, the court attempted to satisfy the two competing aims of New Jersey insurance law: compensating victims and deterring intentional wrongdoing.²⁹⁶

The court adopted the second approach, which inquires into the subjective intent of the actor when the harm sustained is not an inherent probability of the action, and precludes coverage when the harm is a probable outcome of the action.²⁹⁷ Applying this approach to the fraud claim in the underlying suit, the court noted that in a wrongful discharge context, courts are reluctant to impute an intent to cause bodily harm.²⁹⁸ Thus, the court remanded the case back to the trial court to determine if the officer who had made the fraudulent representation had subjectively intended to cause the employee's emotional distress.²⁹⁹

III. *SHEETS v. BRETHERN MUTUAL*

In *Sheets v. Brethren Mutual Insurance Co.*,³⁰⁰ the Court of Appeals of Maryland addressed an issue of first impression under Maryland

293. *See id.* This view is referred to as the "Lyons" test, named after the opinion in which it was espoused. *See generally* Lyons v. Hartford Ins. Group, 310 A.2d 485, 488-89 (N.J. Super. Ct. App. Div. 1973).

294. *See SL Indus.*, 607 A.2d at 1277-78 (citing Prudential Property & Cas. Ins. Co. v. Karlinski, 598 A.2d 918 (N.J. Super. App. Div. 1991)). The *SL Industries* court stated, "[W]hen the result of an action conforms to that which one would predict," no further inquiry is needed; the act is not encompassed under the rubric of "accident." *Id.* at 1278.

295. *See id.* at 1278 (citing Hanover Ins. Group v. Cameron, 298 A.2d 715 (N.J. Super. Ct. Ch. Div. 1973)).

296. *See id.*

297. *See id.*

298. *See id.* at 1278-79. Presumably, this reluctance promotes the public policy of ensuring satisfaction of judgments in favor of victims. *See generally id.*

299. *See id.* at 1279.

300. 342 Md. 634, 679 A.2d 540 (1996).

law: whether a CGL³⁰¹ insurer has a duty to defend against a claim of negligent misrepresentation.³⁰²

In the underlying suit, the plaintiffs, purchasers of a farm, alleged intentional and negligent misrepresentation claims against the insured sellers, the Sheetses.³⁰³ The Sheetses represented that the farm house septic system was in working condition, when in fact it was inadequate.³⁰⁴ Three weeks after the purchasers moved into the farm house, the septic system failed.³⁰⁵ When the purchasers brought suit, the Sheetses contacted their CGL³⁰⁶ insurer, Brethren Mutual Insurance Company, and requested that it fund the defense against the negligent misrepresentation claim.³⁰⁷ Brethren denied the request, contending the policy did not cover misrepresentation torts.³⁰⁸ Thereafter, the Sheetses brought a declaratory judgment action against Brethren, requesting the court to declare that Brethren must reimburse the Sheetses for the cost of defending the suit.³⁰⁹

At trial, the circuit court granted summary judgment in favor of Brethren.³¹⁰ The court found that there was a lack of a causal nexus between the negligent misrepresentation and the damage to the septic system.³¹¹ Alternatively, the court held that the damages alleged in the underlying suit were economic losses excluded under

301. The policy at issue in *Sheets* was a farm owner's general liability policy. *See id.* at 640, 679 A.2d at 541-42. *See generally supra* note 18 (noting that a farm owner's liability policy is merely a slightly modified CGL).

302. *See id.* at 637, 645, 679 A.2d at 541, 545.

303. *See id.* at 637, 679 A.2d at 541.

304. *See id.*

305. *See id.*

306. The policy was a farm owner's liability policy. *See generally supra* note 18 (noting that a farm owner's liability policy is merely a slightly modified CGL).

307. *See Sheets*, 342 Md. at 637-38, 679 A.2d at 541-42. The Sheetses conceded that a clause in the policy excluding coverage for intentional acts precluded coverage for the intentional misrepresentation claim. *See id.* at 637 n.1, 679 A.2d at 541 n.1. *See generally supra* note 54 and accompanying text (noting that if the complaint alleges one claim that is covered under the policy, the insurer must usually provide a defense against all claims, including those not covered).

308. *See Sheets*, 342 Md. at 638, 679 A.2d at 542.

309. *See id.* Originally, the Sheetses sought a declaration that Brethren was required to defend and indemnify the Sheetses if a judgment was entered against them in the underlying suit. *See id.* However, the Sheetses settled the underlying suit before the case reached the court of appeals. *See id.* Because the record did not include the details of the settlement, the court of appeals limited its decision to Brethren's duty to defend. *See id.*

310. *See id.*

311. *See id.* at 643, 679 A.2d at 544.

the policy.³¹² During a pending appeal, the court of appeals granted certiorari on its own motion.³¹³

In considering the scope of Brethren's duty to defend, the court of appeals began by applying the comparison test.³¹⁴ First, the court noted that the CGL³¹⁵ provided coverage for property damage caused by an occurrence.³¹⁶ The CGL defined "occurrence" as an accident; it defined "property damage" as either "[p]hysical injury to tangible property, including all resulting loss of use of that property," or "[l]oss of the use of tangible property that is not physically injured."³¹⁷ The policy also contained a standard duty to defend clause which provided that Brethren had the right and duty to defend any suit seeking damages covered under the policy.³¹⁸

Proceeding to the second step of the comparison test, the court addressed the circuit court's causation analysis.³¹⁹ The court of appeals reiterated its precedent addressing causation and the duty to defend.³²⁰ As long as a plaintiff's complaint alleges liability that is potentially covered by the policy, the court reiterated, an insurer has an obligation to defend its insured, no matter how illogical or attenuated the claim.³²¹ Hence, the court found that any defense of causation should be asserted against the plaintiffs in the underlying suit, not by the insurer against its insured in an attempt to escape its duty to defend.³²²

Continuing with the second step, the court examined whether a negligent misrepresentation could constitute an accident.³²³ The court first addressed Brethren's contention that the loss incurred by

312. See Joint Record Extract at 33, *Sheets* (No. 95-47).

313. See *Sheets*, 342 Md. at 638, 679 A.2d at 542. See generally MD. RULE 8-304(a) (granting the court of appeals authority to grant certiorari on its own motion while cases are pending before the court of special appeals).

314. See *Sheets*, 342 Md. at 640, 679 A.2d at 542-43. For an in-depth discussion of the comparison test, see *supra* notes 69-80 and accompanying text.

315. The policy was a farm owner liability policy. See generally *supra* note 18 (noting that a farm owner's liability policy is merely a slightly modified CGL).

316. See *Sheets*, 342 Md. at 640, 679 A.2d at 543.

317. *Id.* at 641, 679 A.2d at 543.

318. See *id.* at 640, 679 A.2d at 543. See generally *supra* text accompanying note 85 (quoting CGL duty to defend clause).

319. See *Sheets*, 342 Md. at 643, 679 A.2d at 544.

320. See *id.* at 643-45, 679 A.2d at 544-45.

321. See *id.* at 643, 679 A.2d at 544 (citing 7C APPLEMAN, *supra* note 18, § 4686, at 172 (noting that an insurer is not generally permitted to contradict matters alleged in the underlying suit to defeat its duty to defend)).

322. See *id.* at 644, 679 A.2d at 545.

323. See *id.* at 654, 679 A.2d at 550.

the purchasers was economic loss and not encompassed under the rubric of "property damage."³²⁴ The court accepted, as the Sheetses conceded in the circuit court, that the money spent by the purchasers to repair the septic system constituted excluded economic loss.³²⁵ Conversely, the court noted that the policy also defined "property damage" as the "'[l]oss of use of tangible property which is not physically injured.'"³²⁶ Because the essence of the purchasers' claim rested on the inability to use the septic system, the court concluded, the claim asserted a loss of use covered under the policy.³²⁷

Next, the court analyzed whether the term "accident" encompassed negligent misrepresentations. Because negligent misrepresentations are a form of negligence, the court reasoned that it had to first determine whether negligence, as a category of events, could constitute an accident.³²⁸ The court noted that it had previously addressed whether a negligent act constituted an accident under other policies.³²⁹ Upon close examination of its *Harleysville*³³⁰ opinion, however, the court found support for two distinct definitions of the

324. *See id.* at 645-46, 679 A.2d at 545.

325. *See id.* *See generally supra* note 89 (defining "economic loss").

326. *Sheets*, 342 Md. at 645-46, 679 A.2d at 545.

327. *See id.* The court's analysis of the property damage issue totals two paragraphs and contains no citations to authority:

Next, we must determine whether the trial judge was legally correct in holding that the damages to the septic system were not covered as "property damage" under the policy. The Sheetses concede that the money spent to fix the system was economic loss and thus not covered under the policy as property damage.

Also included within the policy's definition of property damage, however, is "[l]oss of use of tangible property that is not physically injured." The Sheetses argue that the trial judge failed to look beyond the allegation of economic loss to see that the complaint alleged property damage in terms of a loss of use of the septic system to the [purchasers]. We agree. The [purchasers] claim they were deprived of the use of their septic system. This alleged "loss of use" was property damage as defined in and covered by the Brethren policy. The trial court therefore erred as a matter of law on this issue.

Id.

328. *See id.* at 646, 679 A.2d at 546.

329. *See id.* at 650-51, 679 A.2d at 547-48 (citing *State Farm Mut. Auto Ins. Co. v. Treas*, 254 Md. 615, 255 A.2d 296 (1969), *Harleysville Mut. Ins. Co. v. Harris & Brooks, Inc.*, 248 Md. 148, 235 A.2d 556 (1967), and *Haynes v. American Cas. Co.*, 228 Md. 394, 179 A.2d 900 (1962)). *See supra* notes 133-75 and accompanying text for an in-depth discussion of Maryland precedent addressing the term "occurrence."

330. 248 Md. 148, 235 A.2d 556 (1967).

term "accident," only one of which could ever encompass a negligent act.³³¹ The court restated the two definitions: (1) an accident is an event that takes place without one actually foreseeing or expecting the result; and (2) an accident is an event that takes place which one should not have expected or foreseen.³³² The first definition focuses on the subjective foresight of the insured.³³³ The second definition requires an objective analysis, thereby essentially eliminating the potentiality that the policy covers a negligence claim.³³⁴ In selecting which definition to adhere to, the court attempted to determine which definition a reasonably prudent layperson would attach to the term "accident."³³⁵ The court found that the subjective standard was more in accord with such expectations, and hence held that an accident was "an event that takes place without the insured's foresight or expectation."³³⁶ The court added that if it adopted the objective standard, then insurance policies employing the term "accident" would be rendered meaningless.³³⁷

The court of appeals next addressed whether, given that negligence could constitute an accident, a negligent misrepresentation could constitute an accident.³³⁸ The court noted the split among other jurisdictions which have faced this issue.³³⁹ The court of appeals explained that in jurisdictions that have precluded coverage, courts have generally held that because the cause of action for negligent misrepresentation requires an intentional element, inducing

331. See *Sheets*, 342 Md. at 651-52, 679 A.2d at 548.

332. See *id.* at 651, 679 A.2d at 548.

333. See *id.*

334. See *id.* Because negligence is measured by an objective standard, if the term "accident" is also measured by such a standard, then, *a fortiori*, an accident could never be a negligent act. See generally *id.* But see 7A APPLEMAN, *supra* note 18, § 4492.03, at 38 (noting the rebuttable presumption under tort law, that persons intend ordinary consequences of their acts, does not apply in insurance coverage disputes).

335. See *Sheets*, 342 Md. at 652, 679 A.2d at 549 (citing *Sullins v. Allstate Ins. Co.*, 340 Md. 503, 508, 667 A.2d 617, 619 (1995)).

336. *Id.* at 652, 679 A.2d at 548 (quotations omitted) (emphasis added). The court noted its disagreement with two courts that adopted the objective standard. See *id.* at 654 n.4, 679 A.2d at 550 n.4 (overruling *Ed. Winkler & Son, Inc. v. Ohio Cas. Ins. Co.*, 51 Md. App. 190, 441 A.2d 1129 (1982), and noting disapproval of *IA Constr. Corp. v. T & T Surveying, Inc.*, 822 F. Supp. 1213 (D. Md. 1993)).

337. See *id.* at 653, 679 A.2d at 549.

338. See *id.* at 654, 679 A.2d at 550.

339. See *id.* at 655, 679 A.2d at 550.

reliance, it cannot constitute an accident.³⁴⁰ Moreover, the court noted, the California cases holding the term “accident” does not encompass negligent misrepresentations rely on California’s recognition of negligent misrepresentation as a subspecies of fraud.³⁴¹ Under Maryland law, however, the court of appeals pointed out that it has repeatedly refused to extend fraud to encompass liability for negligence.³⁴² In accordance with its reaffirmation that negligence may constitute an accident, the court held that a negligent misrepresentation may also be an accident if the resulting injury or damage is an event that takes place without the insured’s foresight or expectation.³⁴³ The court reasoned that the intentional aspect of the tort—inducing reliance—was not dispositive because both the falsity of the statement and the resulting damage may be accidental.³⁴⁴ Because the court held that negligent misrepresentation could constitute an accident, and because the court found the underlying claim alleged property damage under the loss of use prong, the court ordered Brethren to reimburse the Sheetses for the costs incurred defending the underlying suit.³⁴⁵

In a dissenting opinion, Chief Judge Murphy and Judge Karwacki noted their disagreement with the majority’s holding that negligent misrepresentation may constitute an accident on two grounds.³⁴⁶ First, they reasoned that negligent misrepresentation has two intentional aspects—assertion and inducing reliance—either of which preclude encompassing the tort under the rubric of “accident” in insurance policies.³⁴⁷ To assert, the dissenters reasoned, is not to accidentally blurt; it is “[t]o state as true[,] declare[,] or] maintain.”³⁴⁸ The dissenters contended that their position is consistent with the common understanding that voluntary verbal statements cannot be considered accidents as the term is used in insurance policies.³⁴⁹ Similarly, Chief Judge Murphy and Judge Karwacki

340. *See id.* at 656, 679 A.2d at 550-51.

341. *See id.* at 656, 679 A.2d at 550 (citing, *e.g.*, *Chatton v. National Union Fire Ins. Co.*, 13 Cal. Rptr. 2d 318, 328 (Ct. App. 1992)).

342. *See id.* at 656, 679 A.2d at 550-51 (citing *Ellerin v. Fairfax Sav.*, 337 Md. 216, 238-39, 652 A.2d 1117, 1128 (1995)).

343. *See id.* at 657, 679 A.2d at 551.

344. *See id.*

345. *See id.* at 658, 679 A.2d at 551.

346. *See id.* at 658-59, 679 A.2d at 552 (Murphy, C.J., & Karwacki, J., dissenting).

347. *See id.* at 661, 679 A.2d at 552-53 (Murphy, C.J., & Karwacki, J., dissenting).

348. *Id.* at 660, 679 A.2d at 552 (Murphy, C.J., & Karwacki, J., dissenting) (quoting BLACK’S LAW DICTIONARY 116 (6th ed. 1990)).

349. *See id.* at 660, 679 A.2d at 553 (Murphy, C.J., & Karwacki, J., dissenting).

continued, intent to induce reliance cannot be considered accidental.³⁵⁰ Though some negligent actions involve volitional aspects,³⁵¹ they noted that the "inducing reliance" element of negligent misrepresentation entails a designed and intended outcome, hence inconsistent with the concept of an accident.³⁵²

Chief Judge Murphy and Judge Karwacki's second basis for dissenting focused on basic principles of construction.³⁵³ They reiterated that words are to be given the meaning that a reasonably prudent layperson would attach to them.³⁵⁴ They criticized the majority for engaging in tortured legal construction and stated firmly that negligent misrepresentation is clearly not an accident.³⁵⁵

IV. ANALYSIS

A. *The Sheets Court Misconstrued the "Loss of Use" Prong to Cover Excluded Economic Loss*

The Court of Appeals of Maryland wrongly decided *Sheets* because it failed to recognize that the underlying negligent misrepresentation claim, like most negligent misrepresentation claims, alleged liability for economic loss of the sort not covered under CGLs.³⁵⁶ This misconception of the policy, specifically the "loss of

350. *See id.* at 660-61, 679 A.2d at 553 (Murphy, C.J., & Karwacki, J., dissenting).

351. *See id.* at 661 n.1, 679 A.2d at 553 n.1 (Murphy, C.J., & Karwacki, J., dissenting) (noting, *e.g.*, a simple negligence claim may arise from negligently hitting someone with a rock—the throwing is intentional but the resulting injury is not).

352. *See id.* at 661, 679 A.2d at 553 (Murphy, C.J., & Karwacki, J., dissenting).

353. *See id.* at 662, 679 A.2d at 553 (Murphy, C.J., & Karwacki, J., dissenting).

354. *See id.* (Murphy, C.J., & Karwacki, J., dissenting) (quoting *Sullins v. Allstate Ins. Co.*, 340 Md. 503, 508, 667 A.2d 617, 619 (1995)).

355. *See id.* at 662, 679 A.2d at 553 (Murphy, C.J., & Karwacki, J., dissenting).

356. *Cf., e.g., Aetna Cas. & Sur. Co. v. Cotter*, 522 N.E.2d 1013, 1014 (Mass. Ct. App. 1988) ("Although one might imagine a misrepresentation, for example concerning the wholesomeness of food or strength of a tree limb, which would cause bodily injury, generally a misrepresentation is an incorporeal tort, like defamation, which does not cause bodily injury or property damage independent of conditions or acts which themselves are the consequences of negligence.").

Indeed, in light of the Court of Appeals of Maryland's declaration in *Weisman v. Connors*, 312 Md. 428, 540 A.2d 783 (1988), the plaintiff in a negligent misrepresentation claim always seeks redress for economic loss. *See supra* notes 195-202 and accompanying text (discussing *Weisman*).

The *Sheets* court correctly noted that liability policies generally do not provide coverage for economic loss. *See id.* at 654, 679 A.2d at 545 (implied hold-

use” prong, resulted from two errors by the *Sheets* court: (1) the court failed to methodically apply its rules of construction to the loss of use prong; and (2) the court construed the loss of use prong in isolation, thereby overlooking the substantial limiting effect of the “loss of use” exclusion.

ing) (“The *Sheets* court concedes that the money spent to fix the system was economic loss and thus not covered under the policy as property damage.”). Economic loss is the loss of an expectancy interest created by contract. *See supra* note 89 (defining the term “economic loss”). A plaintiff asserting a cause of action for negligent misrepresentation, unlike an ordinary negligence claim, seeks either benefit-of-the-bargain or out-of-pocket damages, both contractually-based remedies. *See supra* notes 202-06 and accompanying text (outlining damages calculation in negligent misrepresentation claims under Maryland law); DAN B. DOBBS, *THE LAW OF REMEDIES*, § 9.2(1), at 695 (2d ed. 1993) (noting that benefit-of-the-bargain damages in misrepresentation claims are exactly like expectancy damages in contracts claims); *id.* § 9.2(2), at 697-98 (noting that out-of-pocket damages have practical effect of rescission for mistake, a contract remedy). Notably, neither form of relief seems appropriate for a suit in which the plaintiff and defendant are not in privity of contract or when relief is sought for bodily injury. However, the court in *Hinkle v. Rockville Motor Co.*, 262 Md. 502, 278 A.2d 42 (1971), stated, “[T]he action is one of tort rather than contract and . . . it has always been recognized that tort remedies are designed to compensate for actual harm suffered.” *Id.* at 505, 278 A.2d at 44. Where appropriate, therefore, that passage supports calculation of damages by traditional tort measures. *See id.*; *see also* *Village of Cross Keys, Inc. v. United States Gypsum Co.*, 315 Md. 741, 756, 556 A.2d 1126, 1133 (1989) (“[T]he tort [of negligent misrepresentation] will lie for the recovery of pecuniary losses, as well for physical harm.”).

Contractually-based remedies are awarded in negligent misrepresentation suits because the duty to speak with reasonable care most commonly arises between parties in privity of contract. *See KEETON ET AL.*, *supra* note 178, § 107, at 105 (Supp. 1988) (“The most common example of the duty to speak with reasonable care will undoubtedly be grounded in a business or professional relationship or one in which there is a pecuniary interest.”). *Compare* *Weisman v. Connors*, 312 Md. 428, 540 A.2d 783 (1988) (addressing negligent misrepresentation claim based on employment contract), *with* *Virginia Dare Stores v. Schuman*, 175 Md. 287, 1 A.2d 897 (1938) (addressing negligent misrepresentation claim based on duty owed to business invitee). *See generally* *First Wyo. Bank v. Continental Ins. Co.*, 860 P.2d 1094, 1099 (Wyo. 1993) (noting that liability insurance under Wyoming law does not encompass coverage for contractual obligations). Undoubtedly, the availability of both contract and tort remedies for the same harm complicates a court’s inquiry into the scope of an insurer’s duty to defend and, ultimately, to indemnify. *Cf. KEETON ET AL.*, *supra* note 178, § 92, at 655 (“The availability of both [tort and contract] liability for precisely the same kind of harm has brought about confusion and unnecessary complexity.”), *cited in* *Weisman*, 312 Md. at 456 n.4, 540 A.2d at 797 n.4.

First, the court's reliance on the fact that the purchasers in the underlying suit alleged a loss of use was completely unsupported by reference to precedent.³⁵⁷ Thus, the court violated an important rule of construction. Because no controlling authority had construed the loss of use prong, the court of appeals should have inquired: "What is the customary and normal meaning of ["loss of use"] in the context of the [CGL]?"³⁵⁸ The *Sheets* court did not inquire into the customary and ordinary use of the term "loss of

357. See *supra* note 327 (quoting court's entire analysis).

358. *Collier v. MD-Individual Practice Ass'n*, 327 Md. 1, 6, 607 A.2d 537, 539 (1992). For an in-depth analysis of the rules regarding construction of terms in insurance policies, see *supra* notes 24-47 and accompanying text.

The *Sheets* court failed to address the court of special appeals's decision in *Pyles v. Pennsylvania Manufacturers' Ass'n Ins. Co.*, 90 Md. App. 320, 600 A.2d 1174 (1992), the only Maryland precedent that has addressed the term "property damage." Indeed, the circuit court judge relied on *Pyles* in holding that the underlying claim was not covered because of a lack of causal nexus. See Joint Record Extract at 32, *Sheets* (No. 95-47) ("I am persuaded by the authority that has been cited in the *Pyles* case and the *Safeco* case. There appears to be no causal nexus."). The *Sheets* court rejected the "lack of causal nexus" holding because it found such reasoning violated the potentiality rule. See generally *Brohawn v. Transamerica Ins. Co.*, 276 Md. 396, 408, 347 A.2d 842, 850 (1975) (construing duty to defend clause to obligate insurer to defend if there is a potentiality that the policy may cover a claim).

In *Pyles*, the court of special appeals held that property damage to a home that was razed by fire was not covered under a builder's CGL because the basis of the claim was not that the builder caused the fire; the basis was breach of contract: the builder failed to perform its contractual obligation to get the agreed amount of insurance. See *Pyles*, 90 Md. App. at 325, 600 A.2d at 1177. See generally *supra* notes 104-16 and accompanying text (providing full discussion of *Pyles*). Thus, although there was property damage—the burned building—there was no allegation of a causal nexus between the damage and any action by the insured. See *Pyles*, 90 Md. App. at 325, 600 A.2d at 1177; cf. *State Farm Fire & Cas. Co. v. Brewer*, 914 F. Supp. 140, 142-43 (S.D. Miss. 1996) ("The alleged misrepresentation of Defendants did not cause property damage. The termites caused the property damage."). See generally *supra* notes 226-30 and accompanying text (discussing courts which have found the lack of a causal nexus to property damage precludes coverage for negligent misrepresentation claims).

The *Sheets* court apparently avoided the impact of *Pyles* by pointing out that the underlying plaintiffs claimed that the *Sheets* court caused them to purchase an inadequate septic system, as opposed to an already damaged system, which was subsequently damaged because of overuse. See *Sheets*, 342 Md. 643, 679 A.2d at 544. Therefore, because the use of the septic system was alleged to have been in reliance of the misrepresentation, hence caused by it, the *Sheets* court found the claim alleged a causal nexus. See *id.* at 645, 679 A.2d at 545.

use.”³⁵⁹ As further developed below, the implicit definition adopted by the court, that a loss of use occurs whenever the plaintiff can point to tangible property that he has been deprived of because of economic loss,³⁶⁰ is too encompassing and illogical. In short, the court negated a basic limitation in the policy—that economic loss is generally excluded.³⁶¹

As the opinions cited elsewhere in *Sheets* demonstrate, the loss of use prong has been interpreted in two divergent manners.³⁶² The majority of jurisdictions that have addressed this issue have concluded that the loss of use prong does not encompass the loss of property due to negligent misrepresentations.³⁶³ Otherwise, the majority of courts have reasoned, the economic loss limitation would be meaningless.³⁶⁴ The minority position was espoused in *First Newton National Bank*.³⁶⁵ The *First Newton* court found that the plaintiffs’ loss of the use of their farm homes because of foreclosure con-

359. See generally *Bausch & Lomb, Inc. v. Utica Mut. Ins. Co.*, 330 Md. 758, 779, 625 A.2d 1021, 1031 (1993) (noting terms are given ordinary, customary meaning).

360. See generally, e.g., *First Newton Nat’l Bank v. General Cas. Co.*, 426 N.W.2d 618, 626 (1988) (finding that because farm owners alleged they were in danger of losing their homes, they alleged property damage in the form of loss of use).

361. Cf. *Bailer v. Erie Ins. Co.*, 344 Md. 515, 536, 687 A.2d 1375, 1385 (1997) (Chasanow, J., dissenting) (“In straining to provide insurance coverage for a ‘peeping Tom’ with a video camera, this [c]ourt nullifies a specific limitation of coverage in an insurance policy.”).

362. Compare *First Newton Nat’l Bank*, 426 N.W.2d at 626 (holding that although the claim sought economic loss, the loss of use provision encompassed the claim because farm owners contended they will be ejected from their homes), with *Safeco Ins. Co. v. Tozier*, No. CIV.A.93-2453-CTV, 1994 WL 476304 (D.Kan. Aug. 16, 1994) (reasoning that the claim did not arise from property damage, it arose from already defective conditions, hence relief sought was merely economic loss).

363. Compare *General Ins. Co. v. Western Am. Dev. Co.*, 603 P.2d 1245, 1247 (Or. Ct. App. 1979) (holding a loss of use was not alleged despite insured seller’s misrepresentation concerning extent of easement) (majority position), with *First Newton Nat’l Bank*, 426 N.W.2d at 626 (holding loss of use alleged by farm owners because they contended that they will be ejected from their homes) (minority position).

364. See, e.g., *Sting Sec., Inc. v. First Mercury Syndicate, Inc.*, 791 F. Supp. 555, 562 (D. Md. 1992) (Motz, J.) (applying Virginia law). In *Sting*, Judge Motz opined that the plaintiff might argue that a loss of use was alleged because the economic loss hampered the ability to efficiently use other products. See *id.* Nonetheless, he concluded that “[s]uch an argument would be extremely weak.” *Id.*

365. 426 N.W.2d 618 (1988). To date, no other jurisdiction has followed the minority position.

stituted property damage covered under the policy.³⁶⁶ This conclusion, however, judicially expands the scope of coverage beyond the perimeters of the policy.³⁶⁷ Likely, it will either lead to anomalous, untenable results or will be abandoned or modified by the court of appeals in the future.³⁶⁸

The drafters of the CGL intended for the loss of use prong to cover a narrow risk. The classic example provides that if the insured's negligence causes a store's entrance to be blocked, the liability for the loss of use of the store would be covered property damage under the loss of use prong.³⁶⁹ Nonetheless, this narrow coverage was not intended to transform CGLs into performance bonds.³⁷⁰ Specifically, the loss of use occasioned by the failure of property to perform as warranted was not intended to be covered under the loss of use prong.³⁷¹

Secondly, the *Sheets* court construed the loss of use prong in isolation, ignoring the loss of use exclusion.³⁷² The loss of use exclusion limits the coverage afforded by the loss of use prong to the "loss of use of *other* tangible property resulting from sudden or accidental injury to or destruction of the . . . insured's product or

366. *See id.* at 626.

367. *Cf.* *First Wyo. Bank v. Continental Ins.*, 860 P.2d 1094, 1100 (Wyo. 1993) (finding the distinction between a negligent and a careful breach of contract a "unique, creative idea" without support in case law); *Sting*, 791 F. Supp. at 562 (finding this line of reasoning "extremely weak").

368. *Cf. supra* notes 87-93 and accompanying text (chronicling the history of re-drafting the CGL to thwart judicial construction encompassing coverage for economic loss). *See infra* notes 410-11 and accompanying text for a proposal to adopt the more reasoned construction of the loss of use prong and related exclusions in *Woodfin Equities Corp. v. Harford Mutual Insurance Co.*, 110 Md. App. 616, 678 A.2d 116 (1996) (Wilner, C.J., joining majority opinion), *rev'd in part on other grounds*, 344 Md. 399, 415, 687 A.2d 652, 659 (1997). *See generally supra* notes 117-32 (providing in-depth discussion of *Woodfin*).

369. *See supra* note 98 and accompanying text.

370. *Cf.* *IA Constr. Corp. v. T & T Surveying, Inc.*, 822 F. Supp. 1213, 1215 (D. Md. 1993) ("This is the stuff of the construction trade (and of professional malpractice insurance), not a risk protected against by a general liability policy."); Vasich, *supra* note 3, at 804 n.47 ("[L]iability insurance policies are not meant to be performance bonds."). *See supra* notes 169-75 for discussion of *IA Construction Corp.*

371. *See, e.g., Sting Sec., Inc. v. First Mercury Syndicate, Inc.*, 791 F. Supp. 555, 562 (D. Md. 1992) (Motz, J.) (applying Virginia law). *See generally supra* note 364 (discussing *Sting*).

372. For a discussion of the loss of use exclusion, *see supra* notes 99-103 and accompanying text.

work.³⁷³ The loss of use found by the *Sheets* court was not of other tangible property. It was the insured's product—the septic system.³⁷⁴

B. The Sheets Court Correctly Concluded CGLs Generally Provide Coverage for Ordinary Negligence

In their dissent, Chief Judge Murphy and Judge Karwacki observed that the majority unnecessarily addressed whether the term "accident" encompassed negligence.³⁷⁵ The majority's dicta, however, clarified the viability of CGL coverage for negligent acts.³⁷⁶ The new rule, that negligent acts constitute an accident so long as the resulting damage is neither expected nor intended from the standpoint of the insured, effectuates the reasonable expectations of the prudent layperson.³⁷⁷ The dissenters' admonishment that this rule plunges a court's inquiry into the dreaded Serbonian Bog,³⁷⁸ moreover, cannot be avoided. Negligent acts, as opposed to negligent omissions, necessarily require a court to separate the means from the end because acting itself is intrinsically intentional.³⁷⁹ In a negligence context, moreover, this dichotomy is natural and in step with reasonable expectations of the reasonably prudent layperson.³⁸⁰

373. *E.g.*, Neeson & Meyer, *supra* note 1, at 79; *see also* Tinker, *supra* note 11, at 233-34; Vasichcek, *supra* note 3, at 804 n.47.

374. *Cf.* Century I Joint Venture v. United States Fidelity & Guar. Co., 63 Md. App. 545, 553-57, 493 A.2d 370, 374-77 (1985) (holding that condominiums constituted "products" sold by insured).

375. *See* *Sheets v. Brethren Mut. Ins. Co.*, 342 Md. 634, 661, 679 A.2d 540, 553 (1996) (Murphy, C.J., & Karwacki, J., dissenting).

376. *See, e.g.*, Harleysville Mut. Ins. Co. v. Harris & Brooks, Inc., 248 Md. 148, 235 A.2d 556 (1967) (supporting both subjective and objective approaches), *cited in* *Sheets*, 342 Md. at 651, 679 A.2d at 548.

377. *See* *Sheets*, 342 Md. at 652, 679 A.2d at 548.

378. *See id.* at 661-62, 679 A.2d at 553 (Murphy, C.J., & Karwacki, J., dissenting) (citing *Landress v. Phoenix Mut. Life Ins. Co.*, 291 U.S. 491, 499 (Cardozo, J., dissenting)); *supra* note 144 (explaining the Serbonian Bog reference).

379. For a comprehensive discussion regarding CGL coverage for negligence, *see* 7A APPLEMAN, *supra* note 18, § 4492.03, at 38-46.

380. The contrary view, that a negligent act cannot be an accident, is nonsense. *See id.* at 39 n.8. One commentator lucidly stated:

The average insured is an average man, possessing frailties and prone to carelessness either by act or omission. . . . [H]e recognizes his imperfections when he insures, and pays for protection from the consequences of careless, as distinguished from immoral, acts. The insurer knows this when it accepts his premiums. He is, accordingly, entitled to that protection—and the minority rule would deprive him of it.

C. *The Sheets Court Correctly Concluded Negligent Misrepresentations Constitute Accidents*

Maryland's alignment with the minority regarding whether negligent misrepresentation constitutes an accident is another step in the court of appeals's continuing trend towards construing policies in favor of the insured.³⁸¹ However, the *Sheets* court did not rely on this rule of construction.³⁸² Instead, the court painstakingly reviewed its precedent and concluded that a negligent misrepresentation, like ordinary negligence, constitutes an accident if the resulting harm was neither expected nor intended from the standpoint of the insured.³⁸³ Viewed in isolation, this conclusion is in step with the reasonable expectations of the prudent layperson.³⁸⁴

Jurisdictions in the majority should re-examine their position regarding whether negligent misrepresentations constitute accidents. What happens, for example, if a guest injures himself by diving into a pool in reliance on the owner's negligent misrepresentation that the pool is twenty feet deep, when in fact it is five?³⁸⁵ The intentional aspect of the negligent misrepresentation—intending to induce reliance—would not transform the act into an intentional act meant to be excluded under CGLs. As the *Sheets* court correctly noted, so long as the speaker neither expected nor intended the resulting harm, a negligent misrepresentation constitutes an accident.³⁸⁶

D. *CGL Provisions That Could Enable Practitioners to Circumvent or Reinforce Sheets*

Prudent practitioners will note that the *Sheets* court did not address certain provisions contained in CGLs, including the CGL con-

Id.

381. See, e.g., *Sullins v. Allstate Ins. Co.*, 340 Md. 503, 667 A.2d 617 (1995) (construing a pollution exclusion clause to not preclude coverage for lead-based paint claims).

382. See generally *Sheets*, 342 Md. at 654-58, 679 A.2d at 550-51.

383. See *id.*

384. See generally, *Bausch & Lomb Inc. v. Utica Mut. Ins. Co.*, 330 Md. 758, 779, 625 A.2d 1021, 1031 (1993) (noting that policy terms should be read to effectuate expectations of reasonably prudent layperson).

385. Cf., e.g., *Virginia Dare Stores, Inc. v. Schuman*, 175 Md. 287, 294, 1 A.2d 897, 900 (1938) (addressing a case where person injured himself because he relied on the misrepresentation that a display case was sturdy enough to support his weight).

386. See *Sheets*, 342 Md. at 657, 679 A.2d at 551.

strued in *Sheets*,³⁸⁷ that could enable insurers or insureds to either circumvent or reinforce the *Sheets* holdings. Two standard provisions can be successfully invoked to circumvent the *Sheets* court's "loss of use" holding. First, as noted above, the *Sheets* court never considered the loss of use exclusion, which greatly circumscribes the loss of use prong.³⁸⁸ Second, the *Sheets* court did not address the "premises alienated" exclusion.³⁸⁹ In *Stull v. American States Insurance Co.*,³⁹⁰ the United States District Court for the District of Maryland, applying Maryland law, held that the premises alienated exclusion, which every CGL since 1943 contains,³⁹¹ operates to exclude negligent misrepresentation claims based on the sale of the insured's real property.³⁹²

Furthermore, the *Sheets* court did not address a third exclusion, the "owned property" exclusion, that may also be invoked to circumvent the *Sheets* "loss of use" holding.³⁹³ In *Allstate Insurance Co. v. Chaney*,³⁹⁴ the United States District Court for the Northern District of California held that even if negligent misrepresentation in the sale of the home amounted to property damage, the owned property exclusion precluded recovery because the representation occurred while the insured seller still owned the property.³⁹⁵

Conversely, the *Sheets* court did not address a provision that may provide an alternative ground to reach the result of the *Sheets* court's holding that negligent misrepresentations can constitute an accident. In *American States Insurance Co. v. Canyon Creek*,³⁹⁶ the United States District Court for the Northern District of California

387. See Joint Record Extract at 88-93, *Sheets v. Brethren Mut. Ins. Co.*, 342 Md. 634, 679 A.2d 540 (1996) (No. 95-47) (providing selected excerpts of the CGL at issue).

388. See *supra* notes 372-74 and accompanying text.

389. See *supra* notes 241-51 and accompanying text for a discussion of the "premises alienated" exclusion.

390. 963 F. Supp. 492 (D. Md. 1997) (applying Maryland law). For a discussion of *Stull*, see *supra* notes 244-51 and accompanying text.

391. See *Tinker*, *supra* note 11, at 278.

392. See *Stull*, 963 F. Supp. at 494 (adopting the reasoning in *Reliance Ins. Co. v. Povia-Ballantine Corp.*, 738 F. Supp. 523 (S.D. Ga. 1990)).

393. See *supra* notes 252-57 and accompanying text for a discussion of the owned property exclusion.

394. 804 F. Supp. 1219 (N.D. Cal. 1992) (Armstrong, J.). For a discussion of *Chaney*, see *supra* notes 255-57.

395. See *Chaney*, 804 F. Supp. at 1223.

396. 786 F. Supp. 821 (N.D. Cal. 1991) (Orrick, J.). For a discussion of *Canyon Creek*, see *supra* notes 274-78 and accompanying text.

held that despite its conclusion that negligent misrepresentation does not constitute an accident, negligent misrepresentations are covered under the CGL via the BFE advertising injury endorsement, which includes "unfair competition."³⁹⁷ Notably, however, the CGL has incorporated the BFE advertising injury endorsement as part of the CGL proper since 1986, conspicuously omitting the term "unfair competition."³⁹⁸

That the insurer in *Sheets* failed to raise applicable exclusions—and that the court did invoke them as part of construing the policy as a whole—demonstrates the reality that few people read the entire CGL. Because public policy goals woven into specialized rules of construction engulf insurance law, coverage disputes often center on fact-specific, complex case law that lawyers and judges must methodically analyze.³⁹⁹ Too much emphasis on precedent, however, can result in overlooking provisions that moot case law. Thus, because contract law governs insurance law, the first place to start is the language of the policy.

E. *Impact of Sheets*

As the United States Supreme Court recognized, the *Sheets* decision appreciably enlarged the scope of coverage afforded under CGLs in Maryland.⁴⁰⁰ Most significantly, the *Sheets* court's dicta providing that negligent acts can constitute an accident clarifies a murky area of Maryland insurance law.⁴⁰¹ In this respect, insured defendants will enjoy the scope of coverage both parties intended.⁴⁰² Likewise, the *Sheets* holding that negligent misrepresentations can constitute an accident logically flows from the same reasoning that ordinary negli-

397. *See id.* at 827.

398. *See supra* notes 271-73 (explaining the history of the advertising injury endorsement).

399. *See generally* Hartwick, *supra* note 25, at 175 ("An insurance policy is, of course, a contract; but it is no longer possible to approach an insurance problem simply by resorting to the law of contracts. A substantial body of law has developed which is particularly applicable to contracts of insurance, and different from that applicable to contracts generally.").

400. *See* *Lords Landing Village Condominium Council of Unit Owners v. Continental Ins. Co.*, 117 S. Ct. 1731, 1733 (1997) (per curiam) (remanding an insurance coverage dispute case back to the United States Court of Appeals for the Fourth Circuit in light of *Sheets*).

401. *See supra* notes 133-75 and accompanying text for a discussion of the court of appeal's treatment of the term "accident."

402. *See supra* notes 24-47 and accompanying text (discussing policy construction).

gence can constitute an accident. The fact that negligence takes the form of speech is completely irrelevant.

Conversely, the court's isolated and piecemeal approach to analyzing the loss of use prong erroneously enlarged the scope of the duty to defend.⁴⁰³ Indeed, the CGL in *Sheets* explicitly excluded the property damage alleged in the underlying complaint via two exclusions: the loss of use and premises alienated exclusions.⁴⁰⁴ By engaging in isolated construction of policy terms, the *Sheets* court expanded the potentiality rule to trigger the duty to defend in suits that do not seek damages covered under the policy.⁴⁰⁵

Likewise, the *Sheets* court ignored the obvious conflict between finding that the policy did not cover economic loss, which the plaintiffs in the underlying suit sought, and still finding coverage.⁴⁰⁶ The court's construction of the term "loss of use" essentially swallowed the general limitation against covering economic loss.⁴⁰⁷ The ramification of this construction could prove unfairly costly for insurance coffers.⁴⁰⁸ If the *Sheets* reasoning is taken to its logical conclusion, the progeny of *Sheets* might again construe liability policies as generally providing coverage for economic loss. Economic loss is the stuff of professional malpractice insurance, not a risk protected against under a CGL.⁴⁰⁹

403. *But see generally* Pacific Indem. Co. v. Interstate Fire & Cas. Co., 302 Md. 383, 388, 488 A.2d 486, 488 (1985) (noting that insurance contracts are to be construed as a whole).

404. A third exclusion, the owned property exclusion, may have also precluded coverage. *See supra* note 395 and accompanying text.

405. *But see supra* notes 52-60 (discussing the potentiality rule).

406. *Cf. Bailer v. Erie Ins. Co.*, 344 Md. 515, 536, 687 A.2d 1375, 1385 (1997) (Chasanow, J., dissenting) (stating the *Bailer* majority ignored a specific policy limitation). In *Bailer*, the majority held that an insurer was obligated to defend and indemnify its insured for invasion of privacy under a policy that covered invasion of privacy as "personal injury," despite that the policy excluded "personal injury . . . expected or intended" by the insured." *Id.* at 517, 687 A.2d at 1376. The *Bailer* court reasoned: "If the exclusion totally swallows the insuring provision, the provisions are completely contradictory." *Id.* at 525, 687 A.2d at 1380.

407. *Cf. id.* at 525, 687 A.2d at 1380.

408. *Cf. Keville, supra* note 3, at 922 (noting judicial misconstruction of policies has unilaterally expanded insurers' risk, causing some companies to fail).

409. *See Allstate Ins. Co. v. Morgan*, 806 F. Supp. 1460, 1464 (N.D. Cal. 1992) ("In general, the claims alleged in the [underlying] complaint are simply not the type of claims that the homeowner's policy was designed to cover."); *cf. IA Constr. Corp. v. T & T Surveying, Inc.*, 822 F. Supp. 1213, 1215 (D. Md. 1993) ("This is the stuff of the construction trade (and of professional malpractice

Since the *Sheets* opinion, the Court of Special Appeals of Maryland decided *Woodfin Equities Corp. v. Harford Mutual Insurance Co.*⁴¹⁰ The *Woodfin* decision, which was reversed on technical grounds, contains a lucid discussion, analysis, and application of the loss of use prong. The *Woodfin* court precisely delineated between property damage covered by the loss of use prong and property damage excluded under the various policy exclusions. When faced with construing the loss of use prong again, the court of appeals should consider adopting the court of special appeals's reasoning in *Woodfin*.⁴¹¹

V. CONCLUSION

The *Sheets* decision marks a departure from the rules of construction governing insurance contracts under Maryland law.⁴¹² Moreover, the court's conclusion regarding whether the claim against the Sheetses alleged property damage covered under the CGL lacks sound support.⁴¹³ The court did not make the prescribed inquiry when it construed the term "loss of use," a term that has not been addressed by controlling authority.⁴¹⁴ Instead, the court undertook an isolated, piecemeal approach to analyzing the term, thereby overlooking two exclusions—the loss of use and premises alienated exclusions—that precluded coverage.⁴¹⁵ By contravening

insurance), not a risk protected against by a general liability policy."). See *supra* notes 169-75 for discussion of *IA Construction Corp.*

410. 110 Md. App. 616, 678 A.2d 116 (1996) (Wilner, C.J., joining majority opinion), *rev'd in part on other grounds*, 344 Md. 399, 415, 687 A.2d 652, 659 (1997) (reversing the portion of the court of special appeals's opinion addressing merits; declining to address merits itself because the trial court did not issue a written declaratory judgment). For an in-depth discussion of *Woodfin*, see *supra* notes 117-32.
411. Judge Wilner, who was Chief Judge of the Court of Special Appeals of Maryland when *Woodfin* was decided, joined the court of special appeals's majority opinion in *Woodfin*. See *id.* (Wilner, C.J., joining majority opinion). In 1997, Judge Wilner was appointed to the Court of Appeals of Maryland.
412. See *supra* notes 24-47 and accompanying text for discussion of rules governing construction of insurance policies. See *supra* notes 48-80 and accompanying text for discussion of the rules for determining an insurer's duty to defend.
413. See *supra* notes 95-98 and accompanying text (noting the majority of courts and commentators find the loss of use prong has an extremely narrow application).
414. See *supra* note 33 and accompanying text (quoting test applied to new policy terms under Maryland law).
415. See generally *Teamsters Local 639-Employers Health Trust v. Reliable Delivery Serv., Inc.*, 42 Md. App. 485, 488-89, 401 A.2d 191, 194 (1979) (noting that policies should be construed as a whole). A third exclusion, the owned property

firmly rooted rules of construction, the Court of Appeals of Maryland has placed a judicial gloss on the definition of the term "loss of use" which plunges this area of law into the reincarnated, dreaded Serbonian Bog,⁴¹⁶ throwing CGL insurers back into the business of insuring against excluded economic loss.⁴¹⁷

Conversely, the *Sheets* court made a needed clarification in the area of ordinary negligence.⁴¹⁸ The court's dicta, that negligent acts can constitute an accident if the resulting harm is neither expected nor intended by the insured,⁴¹⁹ effectuates the reasonable expectations of the reasonably prudent layperson.⁴²⁰ The court's conclusion that negligent misrepresentations are also accidents if the resulting harm is neither expected nor intended by the insured is, likewise, in accord with reasonable expectations.⁴²¹

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exclusion, may also have been overlooked. *See supra* note 395 and accompanying text.

416. *See supra* note 144 (explaining the Serbonian Bog reference). This would not be the first time the Serbonian Bog was reincarnated. *See generally* John D. Frederick, *Remarks Delivered on the Occasion of the Presentation of the Fordham-Stein Award to the Honorable William Hughes Mulligan*, 59 *FORDHAM L. REV.* 479, 483 (1991) (quoting Judge Mulligan's reply to questions regarding his use of the obscure Serbonian Bog reference in opinions ("[Nobody knows] what it means, but they know it isn't good . . .")).

417. *See supra* note 87-93 and accompanying text (chronicling history of redrafting CGL to thwart judicial construction encompassing coverage for economic loss).

418. *See supra* note 331 and accompanying text (noting two contradictory definitions of "accident" in pre-*Sheets* precedent).

419. *See* *Sheets v. Brethren Mut. Ins. Co.*, 342 Md. 634, 652, 679 A.2d 545, 548 (1996).

420. *See generally, e.g.,* *Bausch & Lomb, Inc. v. Utica Mut. Ins. Co.*, 330 Md. 758, 799, 625 A.2d 1021, 1031 (1993) (noting that under Maryland law, terms should be construed to effect reasonable expectations of prudent layperson).

421. *See generally id.*