IN THE SUPREME COURT OF THE STATE OF OREGON

FOUNTAINCOURT HOMEOWNERS' ASSOCIATION and
FOUNTAINCOURT CONDOMINIUM OWNERS' ASSOCIATION,
Plaintiffs,

v.

FOUNTAINCOURT DEVELOPMENT, LLC; et. al.,
Defendants.

FOUNTAINCOURT DEVELOPMENT, LLC; et. al.,
Third-Party Plaintiffs,

v.

ADVANCED SURFACE INNOVATIONS, INC.,
an Oregon corporation; et. al.,
Third-Party Defendants.

VOSS FRAMING, INC., assignee for FountainCourt Homeowners' Association, assignee for FountainCourt Condominium Owners' Association, on behalf of FountainCourt Development, LLC, on behalf of Matrix Development Corporation,
and on behalf of Legend Homes Corporation,
Fourth-Party Plaintiff,

v.

DANA CHRISTOPHER; and RED HILLS CONSTRUCTION, INC.,
Fourth-Party Defendants.

June 2015

FOUNTAINCOURT HOMEOWNERS' ASSOCIATION and
FOUNTAINCOURT CONDOMINIUM OWNERS' ASSOCIATION,
Garnishors-Respondents,
Respondents on Review,

v.

AMERICAN FAMILY MUTUAL INSURANCE COMPANY,
Garnishee-Appellant,
Petitioner on Review.

Washington County Circuit Court No. C075333CV

CA No. A147420

SC No. S062691

CORRECTED BRIEF - *AMICI CURIAE* ASSOCIATED GENERAL CONTRACTORS OF AMERICA, OREGON-COLUMBIA CHAPTER; PACIFIC NORTHWEST CHAPTER OF THE ASSOCIATED BUILDERS AND CONTRACTORS INC.; HOME BUILDERS ASSOCIATION OF METROPOLITAN PORTLAND; PROFESSIONAL REMODELERS ORGANIZATION OF THE HBA OF METRO PORTLAND; INDEPENDENT ELECTRICAL CONTRACTORS OF OREGON, INC.; CENTRAL OREGON BUILDERS ASSOCIATION; HOME BUILDING ASSOCIATION OF MARION AND POLK COUNTIES; NORTHWEST UTILITY CONTRACTORS ASSOCIATION; OREGON HOME BUILDERS ASSOCIATION; AND NATIONAL ASSOCIATION OF HOME BUILDERS

Petition for Review of the Decision of the Court of Appeals from a Judgment of the Circuit Court of Washington County, Honorable Judge Marco A. Hernandez
Decision Filed: August 6, 2014
Judges: Armstrong, Presiding; and Duncan, J.; Brewer, J., pro tempore,
Affirmed with Opinion

Attorneys for *Amici Curiae* Associated General Contractors of America, Oregon-Columbia Chapter; Pacific Northwest Chapter of the Associated Builders and Contractors Inc.; Home Builders Association of Metropolitan Portland; Professional Remodelers Organization of the HBA of Metro Portland; Independent Electrical Contractors of Oregon, Inc.; Central Oregon Builders Association; Home Building Association of Marion and Polk Counties; Northwest Utility Contractors Association; Oregon Home Builders Association; and National Association of Home Builders

Michael E. Farnell, OSB No. 922996
Steven R. Powers, OSB No. 013825
Parsons Farnell & Grein, LLP
1030 SW Morrison St.
Portland, OR 97205
Phone: (503) 222-1812
Email: mfarnell@pfglaw.com
spowers@pfglaw.com

Attorneys for Plaintiffs/Garnishors-Respondents on Review FountainCourt Homeowners' Association and FountainCourt Condominium Owners' Association:
Anthony L. Rafel
Rafel Law Group PLLC
1100 SW 6th Ave., Suite 1600
Portland, OR 97204
Phone: (503) 808-9960
Email:arafel@rafellawgroup.com

Robert L. O'Halloran
4170 NE Alameda
Portland, OR 97212
Phone: (503) 249-3766
Email:bohalloran2001@yahoo.com

Attorneys for Garnishee-Petitioner on Review American Family Mutual Insurance Company:
John R. Barhoum
Chock Barhoum LLP
121 SW Morrison St., Suite 415
Portland, OR 97204
Phone: (503) 477-4061
Email:john.barhoum@chockbarhoum.com

James E. Oliver, Jr.
Jim Oliver Law
P.O. Box 13225
Portland, OR 97213
Phone: (503) 481-9993
Email: jimoliverlaw@gmail.com

L. Kathleen Chaney
4949 S. Syracuse St., Suite 600
Denver, CO 80237
Phone: (303) 799-8889
Email: kchaney@lclaw.net

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I. Statement of Amici Curiae

When any of us buys a general liability insurance policy, we pay for two fundamental benefits: (1) a paid-for defense lawyer if we get sued (*i.e. the duty to defend, inclusive of the duty to settle*), and (2) protection against liability imposed (*i.e. the duty to indemnify*). Insurers aggressively market these benefits and they receive handsome premiums in exchange for providmg them. The insured is *not* paid to protect the insurer. This baseline dynamic can sometimes get lost in the minutiae of insurance coverage litigation. It shouldn't. "It must not be forgotten that the purpose of insurance is to insure, and that eonstruetion should be taken which will render the contract operative, rather than inoperative." *Phil Schroeder, Inc. v. Royal Globe Ins. Co.*, 659 P2d 509, 511 (Wash 1983), *adh'd to as modified on recons*, 683 P2d 186 (Wash 1984); *see also W. Cas. & Sur. Grp. v. Coloma Twp.*, 364 NW2d 367, 370 (Mich App 1985) ("Since the purpose of insurance is to insure, the courts should not construe a policy to defeat coverage unless the language requires it."); *Gentry v. Yorkshire Ins. Co., Ltd., of York, England*, 5 SE2d 565, 568 (SC 1939) ("We have said, and here say again, that the purpose of insurance is to protect the insured, the person who takes it out and pays for it.").

This court recognized the same animating principle long ago when it wrote that an insurance policy should be given "a liberal construction as favorable to the insured as in good conscience will be permitted, and every reasonable intendment will be allowed in support of a view that will protect the insured and defeat a forfeiture." *Land v. West Coast Life Ins. Co.*, 201 Or 397, 401, 270 P2d 154 (1954). Insurers are professional litigants; insureds are not. Insurers have unlimited resources; insureds do not. This enduring imbalance, the adhesive nature of the insurance bargain, and the fundamental protective purpose of the product marketed and sold explain the rules that govern disputes between insurers and their insureds. It is not a level playing field, and it is not supposed to be.

American Family Mutual Insurance Company (American Family) has lost its way in this appellate proceeding. It swung for the fences in the Court of Appeals, adopting a purposeful strategy of abandoning its purported policy exclusions, on which it has the burden of proof, and advocating instead for a rule that would center the dispute on—and only on— the policy's initial insuring agreement, on which the insured has the burden of proof. American Family then specially fashioned the burden so that it could never be satisfied. Not surprisingly, the Court of Appeals rejected that

approach. *FountainCourt Homeowners v. FountainCourt Develop.*, 264 Or App 468, 334 P3d 973, *rev allowed*, 357 Or 111 (2014).

In this court, American Family reintroduces its policy exclusions, issues wholly unpreserved, and argues that although its insured is bound by the underlying liability judgment, American Family is not. According to American Family, it is free instead to relitigate the underlying liability for purposes of the insurance coverage dispute and to make for a new and different liability, but this time liability of a kind not covered. In effect, American Family purports to create an alternative reality in which its duty to indemnify is divorced from the very thing against which it promised to indemnify. A contract of indemnity does not work that way. And insurers paid to protect their insureds do not handle claims this way.

On behalf of Oregon contractors, therefore, *amici curiae* seek to hold insurers to their end of the bargain and respectfully urge this court to reaffirm its longstanding principles governing the interpretation of insurance contracts, principles that soundly reject American Family's attempt to rewrite its policy as a means to effectively foreclose insurance coverage for liability because of accidentally caused continuous and progressive property damage.

II. Summary of Argument

American Family made a tactical decision in the Court of Appeals to forgo argument on its policy exclusions, opting instead to seek a rule that would make it impossible for insureds to carry American Family's version of their burden of proof on the insuring agreement in continuous and progressive property damage cases. That tactical decision did not pan out, and American Family does not like the rule it ended up with following the decision by the Court of Appeals. This court should affirm the decision of the Court of Appeals because American Family is obligated to "pay those sums that [Sideco, Inc. (Sideco)] becomes legally obligated to pay as damages because of * * * 'property damage'" caused by an occurrence, provided some property damage occurs during American Family's policy period. The verdict rendered against Sideco was for negligence resulting in property damage. And American Family has conceded that property damage occurred during its policy periods. These things satisfy the insuring agreement and there is nothing further to determine.

Amici also ask this court to reject American Family's contention that insureds in continuous and progressive property damage cases cannot access their bargained-for insurance coverage unless they can prove exactly how much of the continuous and progressive damage occurred in a given policy

period. To put this misguided contention to rest once and for all, *amici* ask this court to state once again that the timing provision in American Family's insuring agreement (property damage occurring during the policy period) is not a limitation on coverage but rather a trigger of coverage, and to expressly adopt the "all sums" rule under which any triggered policy must, absent some other basis for withholding coverage, protect the insured up to the limits of the triggered policy.

Last, *amici* ask this court to adopt the analysis by the Court of Appeals addressing the relationship between the adjudicated liability of the insured and the insurance policy issued to the insured. The Court of Appeals properly interpreted and applied American Family's policies as the contracts of indemnity they are. A contract of indemnity cannot logically be divorced from the underlying liability to which it relates. A final, non-appealable judgment against the insured is an unchangeable thing the insured is legally obligated to pay. American Family suggests that any time it defends an insured pursuant to a reservation of rights any judgment against the insured that may result binds the insured but not American Family, which is free to relitigate the underlying case in the hopes that a second try will yield a fictional liability that is not covered. A contract of indemnity cannot by

litigated in a parallel universe or according to an alternative reality. The only relevant liability is the one actually imposed on the insured.

III. Argument

A. Longstanding interpretive principles and the terms and conditions of American Family's policies demonstrate that FountainCourt carried its burden to prove that the underlying verdict came within the insuring agreement.

The overwhelming majority of cases settle. This is true as well for cases in which the defense is controlled by an insurance company. Every once in a while, however, an insurer elects to gamble on a trial of the claims against its insured. When that insurer defends under reservation of rights, it gambles with the insured's money. The general question presented here is what happens next when the insurer gambles and loses. The specific question presented here is the treatment of an underlying jury verdict awarding damages for negligently caused property damage under an insurance policy providing indemnity against liability because of accidentally caused property damage. If it sounds like the stated coverage perfectly tracks the adjudicated liability, that is because it does.

American Family issued two commercial general liability (CGL) policies to Sideco for sequential policy periods spanning from May 2, 2004,

to May 1, 2006.[1] American Family makes passing reference to this court's long-settled analytical construct for interpreting and applying policy language but never returns to it, spending its pages instead on a creative survey of case law. *See Interstate Fire & Cas. Co. v. Archdiocese of Portland in Oregon*, 318 Or 110, 117, 864 P2d 346 (1993) (policy interpretation does not begin with case law; "[r]ather, it begins with an examination of the words of the applicable provisions in the insurance policy").

Policy language is construed from the perspective of the "ordinary purchaser of insurance." *Totten v. New York Life Ins. Co.*, 298 Or 765, 771, 696 P2d 1082 (1985); *North Pacific Ins. v. American Mfrs. Mutual Ins.*, 200 Or App 473, 478, 115 P3d 970 (2005). Where policy terms are unambiguous, they are enforced as written. *Groshong v. Mut. of Enumclaw Ins. Co.*, 329 Or 303, 308, 985 P2d 1284 (1999). However, where policy terms are susceptible to more than one interpretation, Oregon courts undertake a sequence of analytical steps to determine the meaning of the language. *Hoffman Construction Co. v. Fred S. James & Co.*, 313 Or 464, 469-71, 836 P2d 703 (1992). Courts first determine whether the competing

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[1] Although immaterial to the issues before this court, it is worth noting that the first policy incepted on May 2, 2004, not May 1. *See* SER 20.

interpretations are plausible when viewed in light of the immediate context of the policy language and in the broad context of the policy as a whole. *Id.* If only one interpretation continues to be reasonable after contextual review, that interpretation controls. *Id.* If, however, both interpretations continue to be reasonable, the policy language is deemed ambiguous and will be construed in favor of coverage for the insured. *Id.* Finally, because insurers have unfettered power to draft policy language as they see fit, courts burden them with the consequences of poor drafting. *See Northern Pacific Ins. Co. v. Hamilton*, 332 Or 20, 29, 22 P3d 739 (2001) ("It is the insurers' burden to draft exclusions and limitations that are clear" and "the court does not permit the party who drafted the term or phrase to benefit from the obscurity").

Section I 1. of American Family's policies, titled "Insuring Agreement," provides, in part:

> a. [American Family] will pay those sums that the insured becomes legally obligated to pay as damages because of "bodily injury" or "property damage" to which this insurance applies.
>
> * * * * *
>
> b. This insurance applies to "bodily injury" and "property damage" only if:
>
> (1) The "bodily injury" or "property damage" is caused by an "occurrence" that takes place in the "coverage territory";

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

(SER 9). The policy further defines the terms "property damage" and "occurrence" as follows:

> 13. "Occurrence" means an accident, including continuous or repeated exposure to substantiality the same general harmful conditions.
>
> * * * * *
>
> 17. "Property damage" means:
>
> a. Physical injury to tangible property, including all resulting loss of use of that property. All such loss of use shall be deemed to occur at the time of the physical injury that caused it; or
>
> b. Loss of use of tangible property that is not physically injured. All such loss of use shall be deemed to occur at the time of the "occurrence" that caused it.
>
> * * * * *

(SER 12).

Thus, by its terms, American Family's policies promise payment of "[1] those sums that [Sideco] becomes legally obligated to pay [2] as damages [3] because of * * * 'property damage,'" provided that [4] the property damage is accidentally caused and [5] property damage occurs during the policy period.

1. Those sums that [Sideco] becomes legally obligated to pay

A jury rendered a verdict against Sideco in the amount of $485,877.84. Sideco is legally obligated to pay it and American Family does not contend otherwise.

2. As damages

The cost of repairing property belonging to the members of FountainCourt Homeowners' Association and FountainCourt Condominium Owners' Association (collectively, FountainCourt) was reduced to a money award. American Family does not contend otherwise.

3. Because of Property Damage

Insurers commonly misstate this element of the insuring agreement. American Family claims that FountainCourt must prove "what portion of the damages assessed against Sideco is *for* 'property damage.'" BOM 20 (emphasis supplied). That is not what the text of the insuring agreement states. American Family's policy form does not use the word "for"; it uses the words "because of." The insuring agreement extends coverage to liability *because of* property damage. American Family's argument that the Court of Appeals and the trial court were wrong because the jury, according to American Family, could have awarded damages *for* the repair of water-

damaged building components and *for* the defective condition causing that damage is misguided for several reasons.

First, as has been briefed at length and as recognized by the Court of Appeals, the case against Sideco was tried on the sole theory of negligence, an element of which is proof of property damage. Because Sideco's liability could not exist but for a factual finding of property damage, Sideco's liability is, by definition, "because of" property damage. American Family has no textual answer to this legal imperative.

Second, "'because of' can, and should, be read to mean: as a consequence of, on account of, or arising from." Turner, Insurance Coverage of Construction Disputes § 6:22 (2d ed); *see also Federated Mut. Ins. Co. v. Concrete Units, Inc.*, 363 NW2d 751, 757 (Minn. 1985) ("the most sensible reading of the * * * phrase 'damages because of * * * property damage,' requires the insurer to pay all damages which are causally related to an item of 'property damage' which satisfies either of the policy's definitions") (second ellipsis in original; emphasis omitted); *American Home Assur. Co. v. Libbey-Owens-Ford Co.*, 786 F2d 22 (1st Cir 1986) ("consequential damages suffered as a result of physical injury to any product * * * would be covered"). Again, this reading is grounded in the

policy's text, it is reasonable, and it is therefore mandated by the principles of *Hoffman Construction.*

When an expert in underlying construction defect litigation identifies building components damaged by water intrusion, that expert naturally develops a scope of repair that addresses not only the damaged wood but also the hole allowing the water to get in. Any suggestion that the cost of closing the hole causing property damage is not a cost "because of" property damage is, respectfully, unreasonable.

Third, American Family assumes that construction defects and "property damage" are always mutually exclusive, but American Family cites no policy language or case for that proposition. "[T]he harmful presence of work, product, or other material that must be removed should be sufficient in itself to qualify as a physical injury to the property on which it is found." Turner, Insurance Coverage of Construction Disputes § 6:29 (2d ed). If Sideco unintentionally but nonetheless improperly affixed siding to the FountainCourt buildings, why haven't those buildings suffered a physical injury? The ordinary insured could certainly conclude they had, and that fact drives the interpretive inquiry under *Hoffman Construction.*

An example illustrates the point. Assume that the framing work in an apartment building is so defectively performed that the building is

structurally unsound and at risk of imminent collapse when fully occupied overnight. Reasonable minds would readily agree that the building is damaged before it falls to the ground. American Family's blanket assertion that construction defects are never "property damage" is unsupportable.

Fourth, costs to mitigate further property damage are costs "because of" property damage. *See, e.g., Globe Indem. Co. v. State of California*, 43 Cal App 3d 745, 751, 118 Cal Rptr 278 (5th Dist 1974) ("[S]ince all of the fire suppression costs in question were extended to prevent further damage to tangible property, it can be said that the insured became legally obligated to pay these fire suppression costs *because of damage* to tangible property.") (emphasis in original). Once it is established that property damage has occurred, the policy covers the cost to mitigate ongoing injury. Any other result would have insurers paying far more to resolve serially filed lawsuits after every Oregon winter. That is not a reasonable result and a fair reading of American Family's policy language pursuant to *Hoffman Construction* does not require it.

And fifth, American Family reprises its argument that "property damage" within the meaning of the insuring agreement means damage to property other than the insured's work. BOM 22-26. There is absolutely no textual support for that interpretation. The policies define "property

damage" to mean "[p]hysical injury to tangible property, including all resulting loss of use of that property." SER 12. Nowhere does this definition speak to particular property. The Court of Appeals made quick work of this argument: "we reject the idea that the 'your work' distinction is, as American Family urges, one inherent in the definition of 'property damage,' rather than an exclusion under the policy." *FountainCourt*, 264 Or App at 483-84 (footnote omitted).

When it seeks to support the argument with reference to the "your work" exclusion, moreover, American Family turns the rules of policy interpretation upside down. *See* BOM 25. Policy language must be interpreted in a way that gives effect to all provisions and that renders no term or condition superfluous. *Hoffman Construction*, 313 Or at 472 ("We assume that parties to an insurance contract do not create meaningless provisions"); *New Zealand Ins. v. Griffith Rubber*, 270 Or 71, 75, 526 P2d 567 (1974) (an insurance policy is to be reasonably interpreted "so that no part of it is ignored and effect can be given to every word and phrase"). If damage to the insured's completed work is not "property damage" within the meaning of the insuring agreement, there is no need for an exclusion withdrawing coverage for the same thing. If in cases involving damage to the insured's work the insured cannot get past the insuring agreement, the

exclusion is wholly superfluous. Contrary to American Family's argument, it is the "your work" exclusion that proves the insurer's contractual intent in the insuring agreement. This is a matter of plain language and clear context under *Hoffman Construction.*

American Family relies for its argument on this court's decision in *Oak Crest Constr. Co. v. Austin Mut. Ins. Co.*, 329 Or 620, 998 P2d 1254 (2000). BOM 22. *Oak Crest* is by far the most mis-cited case in construction defect coverage disputes in this state. Nowhere in its *Oak Crest* opinion did this court write that the policy term "property damage" means only damage to property other than the insured's work. *Oak Crest* is instead a case about the term "accident."

American Family also cites the unpublished decision in *MW Builders, Inc. v. Safeco Ins. Co. of Am.*, 267 Fed Appx 552 (9th Cir 2008). With all due respect to the Ninth Circuit, though the result may have been right in *MW Builders*, the court's reasoning was not. As noted above, the principles of *Hoffman Construction* preclude a finding that the words "physical injury to tangible property" mean "physical injury to tangible property unless that tangible property is your work." But when it comes to the interplay between the insuring agreement and the "your work" exclusion, what may be a "no

harm, no foul" mistake as to an insured subcontractor is a very different thing as to an insured general contractor.

The "your work" exclusion, which is included in Section I 2. of the policy, titled "Exclusions," provides, in part:

> This insurance does not apply to:
>
> * * * * *
>
> l. Damage to Your Work
>
> "Property damage" to "your work" arising out of it or any part of it and included in the "products-completed operations hazard[.]"
>
> This exclusion does not apply if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor.

SER 9-10. Where the subject property damage is limited to a subcontractor's work, the result may well be the same whether analyzed as a matter of the insuring agreement, as the Ninth Circuit did in *MW Builders*, or as a matter of the "your work" exclusion, as required by *Hoffman Construction*. Costs simply and only to repair the subcontractor's own defective work are uncovered either way.

But a general contractor's "work" is the entire building or project. For these kinds of insureds, the difference is everything. If damage to a general contractor's work is not "property damage," contrary to the term's

plain language definition, the general contractor is completely uninsured for its only business activity—this despite a clear exception to the "your work" exclusion that restores coverage for damage to or arising out of the work of the insured's subcontractors. Again, American Family's argument deprives this absolutely essential "give back" of any and all effect. When American Family asks this court to adopt the Ninth Circuit's reasoning in *MW Builders*, it is asking this court to render illusory all liability insurance sold to general contractors in Oregon.[2] Courts will not sanction consideration given for a mere illusion of coverage. *See, e.g., Bailer v. Erie Ins. Exch.*, 687 A2d 1375, 1380 (1997) ("If the exclusion totally swallows the insuring provision, the provisions are completely contradictory."); *Purrelli v. State Farm Fire & Cas. Co.*, 698 So2d 618, 620 (Fla App 1997) (applying the doctrine to find coverage); *Martinez v. Idaho Counties Reciprocal Mgmt. Program*, 999 P2d 902, 907 (2000) (same); *see also Schray v. Fireman's Fund Ins. Co.*, 402 F Supp 2d 1212, 1218 (D Or 2005) (implying that the Oregon Supreme Court would not sanction illusory coverage).

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[2] It bears reminding that this is, of course, the very insurance general contractors are required to purchase. *See* ORS 701.073 ("A contractor who possesses a license as required under this chapter shall have in effect public liability, personal injury and property damage insurance covering the work of the contractor.").

4. Property damage accidently caused

The term "occurrence" "means an accident, including continuous or repeated exposure to substantially the same general harmful conditions." SER 12. American Family does not suggest, and the record is utterly devoid of support for the proposition, that Sideco intended to cause the property damage suffered by FountainCourt's members. Indeed, the underlying jury finding of negligence would seem to put the matter to rest. American Family nonetheless persists, arguing that "Oregon law is clear that costs incurred to replace Sideco's defective work are neither an 'occurrence" nor 'property damage' under the American Family policy." BOM 21. Once again, no text-based support is provided for this reading of the policy; American Family simply relies on the same cases briefed to, and dismissed by, the Court of Appeals.

Amici wish to comment, however, on American Family's citation to *Oak Crest* as support for its claim that damages awarded in negligence are not covered "when the damages awarded clearly are contractual in nature." BOM 23. This passing reference cannot go unanswered for two reasons. First, American Family does not get to refashion the judgment against Sideco. *Amici* discuss this important point more thoroughly below. Second, the premise underlying that statement is wrong in ways that matter critically

to construction contractors. The statement assumes that damages for breach of contract are never covered, an assumption that finds no support in any term or provision in American Family's policies. *Amici* agree with American Family when it says the label on the underlying cause of action against the insured does not govern the coverage question. *See id.* Nowhere in the insuring agreement do the words "tort" or "contract" appear. Coverage exists for those sums the insured becomes legally obligated to pay as damages because of property damage. American Family already knows this because it unsuccessfully ventured the same argument in the Wisconsin Supreme Court in *American Family Mut. Ins. Co. v. American Girl, Inc.*, 673 NW2d 65 (Wisc 2004):

> [T]here is nothing in the basic coverage language of the current CGL policy to support any definitive tort/contract line of demarcation for purposes of determining whether a loss is covered by the CGL's initial grant of coverage. "Occurrence" is not defined by reference to the legal category of the claim. The term "tort" does not appear in the CGL policy.

Id. at 77. The terms and conditions of the policy control, and covered liability can just as easily be imposed in contract as it can in tort.

This matters greatly because construction defect plaintiffs routinely allege companion causes of action in negligence and contract, in which the very same facts are alleged to support both claims. More often than not, the factual allegations supporting one of these claims are simply incorporated by

reference into the other claim. What principled basis could there be, based on the language of the insuring agreement, to distinguish contract from tort liability based on identical facts? If a contractor unintentionally makes mistakes in its performance of the work, which mistakes result in property damage, that contractor will be sued in contract and negligence. And if that contractor is found liable because of accidentally caused property damage, the liability is covered, whether liability is imposed on one or both causes of action. *Hoffman Construction* permits no other result.

Unfortunately, none of this stops insurers from doing mischief with *Oak Crest.* They say *Oak Crest* stands for the proposition that breach of contract is never covered. This court did not say that.

> We recognize, as we did in *Kisle* [*v. St. Paul Fire & Marine Ins.*, 262 Or 1, 6, 495 P2d 1198 (1972)], that the same conduct might be actionable under both tort and contract theories. However, applying the foregoing principle to the facts in the summary judgment record in the present case, we conclude that, as alleged, plaintiff's claim arose solely from a breach of contract, and therefore, is not covered by the policy. Although the record establishes that plaintiff spent approximately $10,000 for the repair of a subcontractor's "deficient" painting work, it cannot support a conclusion that the problem with the cabinetry and woodwork painting results from the subcontractor's breach of a duty to act with due care. Had the facts demonstrated that the claimed problem with the cabinets and woodwork was the result of that kind of breach, or that plaintiff might be liable to the owners in tort for other damage, that might have qualified as an "accident" within the meaning of the commercial general liability policy. But plaintiff here failed to establish that a question of fact existed in that regard,

> as plaintiff was required to do to show that there had been a covered event under the policy.

Oak Crest, 329 Or at 628-29. This court struck a clear distinction between breaches based on a failure of timely performance and breaches based on a failure of workmanlike performance. *Id.* at 627 ("'We find [that] there is a significant distinction between negligent performance of a contract and a complete failure of timely performance.'") (*quoting Kisle*, 262 Or at 6); *see also* Appleman, 8 Insurance Laws and Practices § 4851 at 56 (same).

And to the extent that the *Oak Crest* opinion can be said to couch coverage in terms of tortious conduct, such references are typically a vestige of policy forms no longer in use. *See* Turner, Insurance Coverage of Construction Disputes § 6:8 ("Unfortunately, the foregoing turn of events was overlooked by some post-1966 courts who mechanically clung to the old rule which emanated out of the then-obsolete policy language.") The author continues:

> In fact, it was actually the intention of the insurers in changing to the new language in 1966 to cover damages for breach of contract. An associate general counsel of a major liability insurer, writing in a periodical for insurance counsel in 1975, unflinchingly stated, "That portion of the coverage grant is intentionally broad enough to include the insurer's obligation to pay damages for breach of contract as well as tort, within limitations imposed by other terms of the coverage agreement (*e.g.*, bodily injury and property damage as defined, caused by an occurrence) * * *."

Id. (*quoting* Tinker, Comprehensive General Liability Insurance—Perspective and Overview, 25 Fed'n Ins Couns Q 217, 265 (1975)).

5. Property damage during the policy period

American Family argues that FountainCourt cannot prevail because it cannot apportion the adjudicated liability between property damage that occurred within American Family's policy periods and property damage that occurred outside those policy periods. That is incorrect for at least three reasons.

a) The "All Sums" Rule

Oregon is functionally an "all sums" state and it has been for some time. *Amici* respectfully ask this court to dispose of American Family's implied allocation argument by expressly adopting the "all sums" rule and joining its sister court in Washington State.

American Family's argument ignores its own policy language and the fundamental distinction between the trigger of coverage and the scope of coverage. The distinction was made clear in *St. Paul Fire v. McCormick & Baxter Creosoting*, 126 Or App 689, 870 P2d 260, *modified on recons*, 128 Or App 234, 875 P2d 537 (1994), *aff'd in part, rev'd in part*, 324 Or 184, 923 P2d 1200 (1996), a continuous and progressive environmental damage

case in which insurers advanced an argument very similar to American Family's here:

> Our analysis of the trigger of coverage issue does not require going beyond the plain meaning of the policies, which provide for damages for injury or destruction of property *during* the policy period. * * *
>
> * * * * *
>
> Insurers argue that, nonetheless, M&B will not be able to prove that it sustained a loss by reason of damage to property during each of the policy periods. The trial court agreed with insurers that M&B would not be able to apportion damage and that that basis required adopting the manifest trigger theory. * * * **The apportionment of liability is a separate issue from the trigger of coverage issue** and, on this record, cannot be resolved on summary judgment. * * *
>
> Under the plain language, all that is required to trigger coverage is damage to property *during* the policy period.

126 Or App at 698-700 (italics in original; citations and footnote omitted; bold and underlined emphasis supplied).

On review, this court affirmed the ruling by the Court of Appeals on this issue and explained, in a portion of its own opinion entitled "Trigger of Coverage" that:

> [t]he operative phrase in the trigger clauses contained in the caused-by-accident policies is "during the policy period." * * * The trigger clause states that, if an insurable event—*i.e.*, an accident—happens at some point in the course of the policy period, **then that event is covered**. * * *
>
> * * * * * *

> * * * If *property* is injured during the policy period, there has been an "occurrence," and coverage under the policy is triggered.

St. Paul Fire v. McCormick & Baxter Creosoting, 324 Or 184, 201, 923 P2d 1200 (1996) (italics in original; bold and underline emphasis supplied).

McCormick & Baxter makes unequivocal the distinction between the trigger of coverage and apportionment of coverage among policy periods. The trigger provision does not speak to apportionment; if an event triggers coverage, "then the event is covered." *Id.* An argument like the one American Family makes here—that an apportionment rule should be read into its trigger provision—has been soundly rejected by this court. Properly interpreted, a policy is triggered when there is evidence of physical injury to property during the policy period.

Although this court has not formally announced an "all sums" rule, it adopted the rule's underlying principles in *Lamb-Weston v. Oregon Auto Ins. Co.*, 219 Or 110, 341 P2d 110 (1959), which the Court of Appeals later discussed in detail in *Cascade Corp. v. American Home Assurance Co.*, 206 Or App 1, 135 P3d 450 (2006), *rev dismissed*, 342 Or 645 (2007). In *Cascade Corp.*, the Court of Appeals explained that the principle underlying this court's decision in *Lamb-Weston* was that "each insurer is fully liable to the insured." *Cascade Corp.*, 206 Or App at 9. In that case, the insured

sought coverage for property damage resulting from continuous and progressive environmental contamination occurring over a number of years. The iusured settled with all but one of its insurers providing coverage during the period of time in question. The evidence demonstrated continuing damage between 1961 and 1970, that the damage was unexpected, and that it oecurred during each of the insurer's policy periods. When entering judgment for the insured, however, the trial court limited the lone remaining insurer's coverage responsibility to an allocable share of the insured's unsatisfied liability based on its understanding of the principles announced in *Lamb-Weston*. *Cascade Corp.*, 206 Or App at 6-7. The Court of Appeals concluded that the trial court erred in not requiring the insurer to pay the insured loss up to its policy limits. *Id.* at 9.

Importantly, the Court of Appeals explained: "The purpose of the *Lamb-Weston* analysis is to allocate responsibility among those insurers whose policies are available to pay the claim; it does not permit an insurer to pay less than the limits of the applicable policy, leaving the insured with a loss for which there is no coverage." *Cascade Corp.*, 206 Or App at 9. In so concluding, the court emphasized that each insurer had an obligation to make the insured whole to the extent of its policy limits. "In all circumstances, an insurer must pay up to the limits of its policy." *Id.* at 12.

Nowhere in that analogous continuous and progressive property damage context did the court mention apportionment or allocation, let alone require the insured to prove liability based upon some discrete measure of property damage occurring in any particular policy period. Nor did the court require the insured to prove that the past and future environmental response costs were allocable to the lone remaining insurer's policy period.

Like Washington, Oregon should make explicit the "all sums" approach. In *American National Fire Ins. Co. v. B.L. Trucking*, 951 P2d 250 (Wash 1998), the Washington Supreme Court addressed the issue of cost allocation between insurer and insured where the insured was covered for only a portion of the time of continuous and progressive pollution damage. *Id.* at 251. Just like American Family does in this case, the insurer, Maryland/Northern Insurance Company of New York (Northern), argued that it was responsible "only for property damage occurring *during the policy period*, its liability ends when the triggered policy period ends." *Id.* at 253 (emphasis in original). Northern argued that it agreed in its policy only:

> to pay on behalf of the insured all sums which the insured shall become legally obligated to pay as damages because of physical injury to or destruction of tangible property *which occurs during the policy period to which this insurance applies* and is caused by an occurrence.

Id. (citation omitted, emphasis in original). The Washington Supreme Court disagreed.

After reviewing earlier cases, the court concluded that "all insurers on the risk during the time of ongoing damage have a joint and several obligation to provide full coverage for all damages. * * * In other words, when damage occurs during a policy period, that policy is triggered." *Id.* at 254. In noting that this is the majority rule, the court explained:

> We hold that once a policy is triggered, the policy language requires insurer to pay all sums for which the insured becomes legally obligated, up to the policy limits. Once coverage is triggered in one or more policy periods, those policies provide full coverage for all continuing damage, without any allocation between insurer and insured.

B.L. Trucking, 951 P2d at 256-57 (footnote omitted). Notably, an insurer is free to draft clear and unambiguous language into its policy requiring a "pro rata/time on the risk" rather than an "all sums" approach, though mere deviations in standard insurance language are deemed insufficient. *See, e.g.*, *Mut. of Enumclaw Ins. Co. v. Onebeacon Ins. Co.*, 158 Wash App 1006 (2010) (holding that "[o]nce a policy is triggered, allocability is appropriate only if a rational allocation scheme can be devised by the court or the policy explicitly provides for pro rata allocation."); *Fluke Corp. v. Hartford Acc. & Indem. Co.*, 7 P3d 825, 828 n 1 (2000), *as modified* (Oct. 23, 2000), *aff'd*, 145 Wash 2d 137, 34 P3d 809 (2001) (holding, in its determination of the

scope of coverage provided by a policy's insuring agreement, that the policy "uses the words 'those sums' instead of 'all sums,' an insignificant distinction in this context."). However, an insurer that chooses not to include in its policy such limiting language in a clear and unambiguous manner may not be heard to complain after an otherwise covered loss has occurred.

In sum, this court should formally adopt the "all sums" approach because it is consistent with the policy language at issue in this case and consistent with the principles announced by this court in *Lamb-Weston*.

b) By Its Terms, American Family's Policies Cover Liability Because of Property Damage Occurring Outside the Policy Period.

Once again, the premise underlying American Family's argument is not consistent with the terms of its policies. That is, language elsewhere in the insuring agreement speaks directly to coverage for property damage occurring outside the policy period. Section I 1.c. of the insuring agreement provides, in part:

> c. "Bodily injury" or "property damage" which occurs during the policy period and was not, prior to the policy period, known to have occurred by any insured listed under Paragraph 1. of Section II -- Who Is an Insured or any "employee" authorized by you to give or receive notice of an "occurrence" or claim, *includes any continuation, change or resumption of that "bodily injury" or "property damage" after the end of the policy period.*

(SER 9; emphasis added). Thus, the very policy form American Family asks this court to review includes language that contradicts its proposed rule of law, *i.e.*, that insureds must prove damages because of property damage happening *solely* within the policy period.

c) The Liability Because of Continuous and Progressive Property Damage Does Not Change From One Policy Period to the Next.

It is simply incorrect to assume, as American Family does, that liability resulting from continuous and progressive property damage changes from one year to the next. Expert scopes of repair, the principal drivers of liability, are not developed that way. Assume a general contractor is insured by Company #1 for two years and Company #2 for one year. After the policies expire the insured is sued by the building owner for water intrusion causing dry rot to structural members of the building. The evidence indicates dry rot during each relevant policy period, and the trier of fact determines that the only way to meaningfully repair the building is to replace the damaged structural members and eliminate the water intrusion with new siding, awarding the owner damages sufficient to accomplish these ends. A damages award like this is not tied to discrete units of property damage along a time continuum; the liability because of property damage is instead the same in every triggered policy period. Put another way, the

underlying expert's prescribed scope of repair does not change depending on the year in which the damage occurred, even if just a single year is implicated.

Even under American Family's view of the trigger provision, isolating property damage within a particular policy period matters only if doing so operates to segment the insured's liability. As the example illustrates, however, an insured's liability for continuous and progressive damage is indivisible and cannot be compartmentalized into discrete policy periods. If the underlying expert prescribes new siding because of continuing damage caused by water intrusion, the liability attributable specifically to the property damage in each policy period is the same cost for the same siding. The Court of Appeals recognized this as well:

> [G]iven the progressive and continuing nature of the harm alleged by FountainCourt and found by the jury—water intrusion causing property damage—the award of damages reflected in the judgment against Sideco could represent an award of damage for property damage—that is, "[p]hysical injury to tangible property"—that occurred *entirely* during the American Family policy period.

FountainCourt, 264 Or App at 487 (second bracketed text and emphasis in original).

Ultimately, then, FountainCourt did not have to guess at anything in order to satisfy its burden under the insuring agreement. American Family

conceded that property damage occurred during its policy periods. Its policies were therefore triggered up to their respective limits. And a jury verdict in negligence fixes as an unchangeable fact Sideco's liability because of accidentally caused property damage. It is for this reason that American Family asks this court for a rule allowing American Family to relitigate Sideco's liability to FountainCourt so that American Family can come up with an underlying liability more to its liking. This court should decline the invitation.

B. American Family Cannot Create a Parallel Universe in Which Sideco's Liability to FountainCourt is Transformed into Something Different and Thereafter Evaluated for Coverage

Before turning to the subject of issue preclusion, *amici* pause to clear out some underbrush. Contrary to another of American Family's flawed premises, the verdict against Sideco is not "mixed" or "unallocated." *See* BOM 1, 18-20. That is, there is no uncovered claim in this case; rather, as the Court of Appeals explained, "FountainCourt's claim against Sideco proceeded to a jury trial on a single theory: negligence causing physical property damage." *FountainCourt*, 264 Or App at 474. And even if this were a mixed claim case, American Family does not explain why that fact should inure to the detriment of the insured. *See, e.g., Magnum Foods, Inc. v. Continental Cas. Co.*, 36 F3d 1491, 1499 (10th Cir 1994) ("If it were

impossible to determine on what basis the jury made its award, the damages would be presumed to be covered.") (citation omitted).

The argument American Family really makes is that any time an insurer provides a defense under a reservation of rights, the post-judgment coverage dispute should go like this: If the adjudicated liability is not covered, the insured is bound by it, but if the adjudicated liability is covered, the insurer is not bound by it and can relitigate the case in the hopes that a second try will achieve an uncovered result. *See* BOM 15. That position has no basis in Oregon law and it is patently unfair.

For starters, the current state of Oregon law makes every insured defense subject to a reservation of rights. Regrettably, Oregon has yet to adopt the doctrine of coverage by estoppel. *See ABCD...Vision v. Fireman's Fund Ins. Companies*, 304 Or 301, 306, 744 P2d 998 (1987) ("[e]stoppel cannot be invoked to expand insurance coverage or the scope of an insurance contract"). This unfortunately means that, in Oregon, no amount of insurer bad faith can affect an insurer's right to assert policy defenses. It also means an insurer never has to issue a reservation of rights letter in Oregon; the insurer can lie in the weeds and assert any defense it elects to assert at any time, expressly reserved or not. Given this, the rule sought by American Family would reward every insurer with a free look at the

judgment against the insured and, if favorable to the insurer, to accept it, or, if unfavorable to the insurer, to reject it and relitigate the liability case against the insured in subsequent coverage litigation. That is not the sort of protection Oregon insureds believe they are buying.

The Court of Appeals seems to have recognized the fundamental unfairness of such a rule. And in responding to it the Court of Appeals illuminates an important issue that does not appear to have been treated previously by an Oregon appellate court. The Court of Appeals correctly noted that an insurance policy is a contract of indemnity. As such, it cannot be divorced from the judgment to which its indemnity obligation relates. In other words, the judgment against Sideco is what it is, and it cannot be changed without defeating the essential purpose and function of a contract of indemnity. Sideco will always be liable to FountainCourt based upon a jury verdict in negligence. American Family cannot seek to fashion some kind of parallel universe or alternative reality that fictionalizes a different basis for Sideco's liability, and then deny coverage for that one.

This is why the Court of Appeals did not view the binding nature of the underlying judgment through the lens of issue preclusion. It is not a question of which *facts* bind American Family in the coverage dispute; rather, it is a question of whether an adjudicated liability, fixed and

immutable, is or is not subject to American Family's contract of insurance. If the coverage issue relates to the conduct of the insured giving rise to his liability, the coverage dispute should be, as the Court of Appeals concluded, a question of law for the court, based on a review of the underlying verdict and judgment or, if those documents do not answer the question, then based on a review of the larger underlying record, including the pleadings, evidence submitted to the trier of fact, and the jury instructions. In no event can the insurer purport to relitigate, for purposes of the coverage dispute, the basis for the insured's liability to the underlying plaintiff.

Only where there is a coverage dispute genuinely extraneous to the underlying liability is it appropriate to find new facts in the coverage dispute. For example, is the subject car a covered auto under the policy? Is the judgment debtor a covered insured? Have the policy limits been exhausted by other claims? Was the insurer prejudiced by late notice? Absent special circumstances, coverage issues like these do not implicate the basis for the underlying liability and therefore do not risk decoupling the contract of indemnity from the actual liability to which it relates.

All of that said, and while respectfully urging this court to adopt the reasoning of the Court of Appeals, *amici* acknowledge that this court's jurisprudence has historically invoked in this context the principles of issue

preclusion. If this court is inclined to adhere to that approach, American Family fares no better.

This court's decision in *Jarvis et ux v. Indemnity Ins. Co.*, 227 Or 508, 363 P2d 740 (1961), directly addresses the import of an underlying jury verdict in a subsequent coverage action. In *Jarvis*, the plaintiffs prevailed against the insured in underlying litigation involving damage to plaintiffs' house trailer while it was being moved from Winchester Bay to Madras. *Id.* at 510. The plaintiffs alleged that the transportation was hired for valuable consideration whereas the insured alleged that it was a part of a joint enterprise. In the subsequent coverage action, the issue was whether the plaintiffs' judgment was rendered upon facts which were within the terms and conditions of the insured's policy. *Id.* at 510-11.

Ultimately, this court held that collateral estoppel applied and that the uncontradicted evidence submitted in the coverage action, in the form of the underlying pleadings, proved that the judgment was founded upon a factual situation that was outside the scope of coverage. *Id.* at 517-18. In so concluding, however, this court began by observing that the general rule is that an underlying judgment is conclusive in a subsequent coverage action "if the issue decided in the prior action was material to the judgment and is identical with the issue claimed in the later action to be *res judicata*, even

though the insurer was not a party to the first action." *Id.* at 511-12. In reaching its conclusion, the court examined the pleadings in the underlying case and even observed that a transcript of the trial would have provided extrinsic evidence to prove what is or is not *res judicata*. *Id.* at 513-14. "The proof in the [underlying liability trial] *must be presumed*, in the absence of evidence to the contrary, *to have conformed to the pleadings*. The pleadings clearly took the case out of the coverage of the defendant's insurance policy." *Id.* at 517 (emphasis added) .

Importantly, there is nothing in *Jarvis* that supports American Family's contention that a court in a subsequent coverage action cannot view evidence such as the pleadings, trial transcript, and the underlying jury's verdict to determine, as a matter of law, whether the claim falls within the terms and conditions of the insurance policy. In fact, *Jarvis* stands for precisely the opposite conclusion; that is, that the pleadings, trial transcript, and the underlying jury's verdict are the types of evidence by which a subsequent coverage claim is litigated. Moreover, *Jarvis* makes clear that when a court is faced with a coverage question it may use evidence from the underlying liability proceeding to make a presumption, absent compelling evidence to the contrary, about the meaning of that evidence as it relates to the coverage issue. *See id.* at 517.

If issue preclusion is to be the governing standard, therefore, there can be no principled distinction between the preclusive effect of liability based on hired transportation in *Jarvis* and the preclusive effect here of liability based on negligently caused property damage. Accordingly, this court should conclude that FountainCourt properly satisfied its burden when it demonstrated that the harm alleged—that is, ongoing and progressive property damage caused by water intrusion resulting from Sideco's negligence—was within the insuring agreement of American Family's policies.

Further, there is nothing in *Ferguson v. Birmingham Fire Ins. Co.*, 254 Or 496, 460 P2d 342 (1969), which was decided eight years after *Jarvis*, that disturbs the *Jarvis* framework. In *Ferguson*, this court held that an insurer had a duty to defend even where only one allegation is covered by the policy and others may fall outside of the policy. "[I]f a complaint contains two counts, one based upon willful conduct and one based upon negligent conduct, the insurer would have a duty to defend because of the allegation falling within policy coverage. * * * If the complaint, without amendment, may impose liability for conduct covered by the policy, the insurer is put on notice of the possibility of liability and it has a duty to defend." *Ferguson*, 254 Or at 506-07.

In *dicta*, this court commented on the limits of estoppel by judgment, commentary that American Family seizes upon:

> The judgment should operate as an estoppel only where the interests of the insurer and insured in defending the original action are identical—not where there is a conflict of interest. If the judgment in the original action is not binding upon the insurer or insured in a subsequent action on the issue of coverage, there would be no conflict of interests between the insurer and the insured in the sense that the insurer could gain any advantage in the original action which would accrue to it in a subsequent action in which coverage is in issue.

Id. at 510-11 (footnotes omitted). As an initial matter, *dicta* has no precedential effect. *Halperin v. Pitts*, 352 Or 482, 493-94, 287 P3d 1069 (2012). Respectfully, moreover, this *dicta* is problematic for at least two reasons. First, it appears to sanction the alternative reality paradigm. The *dicta* considers a scenario in which the insured might actually be liable to the plaintiff for an unintentional trespass, but the insurer, for purposes of a post-judgment coverage dispute, would be free to relitigate the liability and attempt to transform it into an intentional trespass so that the insurer could then escape its indemnity obligation. This idea runs headlong into the issue identified by the Court of Appeals—contracts of indemnity do not work like that.

Second, if conflicts of interest are relevant, they must be conflicts that genuinely prejudice the insurer in a way that can fairly matter. In this

connection, it cannot be said that the insurer in *Ferguson* is genuinely prejudiced because the party suing its insured tried to, but did not succeed in, proving an intentional trespass. Insurers paid to protect the insured are not supposed to root for the underlying plaintiff, nor are they supposed to give the plaintiff's uncovered claim another run to see if they can succeed where the plaintiff did not. Any claim of a conflict of interest predicated on the insurer's unity of interest with the underlying plaintiff should be rejected out of hand. If the underlying plaintiff puts on evidence of a covered liability, and if the trier of fact is persuaded by that evidence and renders a verdict accordingly, how can the insurer claim to be prejudiced? It might wish the plaintiff had proved a different case, or that the jury had been persuaded by other evidence, but how can that wish relieve the insurer from the judgment that the plaintiff actually obtained and that the insured is legally obligated to pay?

Finally, if conflicts can matter, this court should hold that American Family must, before it can be relieved of the preclusive effect of the prior proceeding, establish that an alternative theory outside of the insurance agreement was actually tried and submitted to the jury. *See Public Service Co. of Colorado v. Osmose Wood Preserving, Inc.*, 813 P2d 785, 789 (Colo

Ct App 1991) (so holding by interpreting Restatement (Second) of Judgments § 57(3) (1982)). That, of course, did not happen in this case.

In the end, there is nothing in this record to suggest that Sideco and American Family's interests diverged in the underlying liability proceeding; indeed, both were interested in a finding of zero liability, a proposition with which the jury did not agree.

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IV. Conclusion

Accordingly, this court should reject American Family's attempt to constrict the terms of its insurance policy because it would adversely impact contractors and others similarly situated that face potential liability associated with continuous and progressive injury or damage, and saddle contractors with an unfair burden that is not grounded in the terms of the policy.

Respectfully submitted,

s/Michael E. Farnell
Michael E. Farnell, OSB No. 922996
Steven R. Powers, OSB No. 013825
Parsons Farnell & Grein, LLP
Attorneys for *Amici Curiae*
Associated General Contractors of America, Oregon-Columbia Chapter; Pacific Northwest Chapter of the Associated Builders and Contractors Inc.; Home Builders Association of Metropolitan Portland; Professional Remodelers Organization of the HBA of Metro Portland; and Independent Electrical Contractors of Oregon, Inc.; Central Oregon Builders Association; Home Building Association of Marion and Polk Counties; Northwest Utility Contractors Association; Oregon Home Builders Association; and National Association of Home Builders

Date: June 19, 2015

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Brief Length

I certify that (1) this brief complies with the word-count limitation in ORAP 5.05(2)(b) and (2) the word-count of this brief (as described in ORAP 5.05(2)(a) is 9,058 words.

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I certify that the size of the type in this brief is not smaller than 14 point for both the text of the brief and footnotes as required by ORAP 5.05(4)(g).

s/Michael E. Farnell
Michael E. Farnell

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I hereby certify that on June 19, 2015, I filed the original **CORRECTED BRIEF - AMICI CURIAE ASSOCIATED GENERAL CONTRACTORS OF AMERICA, OREGON-COLUMBIA CHAPTER; PACIFIC NORTHWEST CHAPTER OF THE ASSOCIATED BUILDERS AND CONTRACTORS INC.; HOME BUILDERS ASSOCIATION OF METROPOLITAN PORTLAND; PROFESSIONAL REMODELERS ORGANIZATION OF THE HBA OF METRO PORTLAND; and INDEPENDENT ELECTRICAL CONTRACTORS OF OREGON, INC.; CENTRAL OREGON BUILDERS ASSOCIATION; HOME BUILDING ASSOCIATION OF MARION AND POLK COUNTIES; NORTHWEST UTILITY CONTRACTORS ASSOCIATION; OREGON HOME BUILDERS ASSOCIATION; AND NATIONAL ASSOCIATION OF HOME BUILDERS** with the Appellate Court Administrator at the following address:

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Attorneys for Plaintiffs/Garnishors-Respondents on Review FountainCourt Homeowners' Association and FountainCourt Condominium Owners' Association:

Anthony L. Rafel
Rafel Law Group PLLC
1100 SW 6th Ave., Suite 1600
Portland, OR 97204
Phone: (503) 808-9960
Email: arafel@rafellawgroup.com
(served electronically)

Robert L. O'Halloran
4170 NE Alameda
Portland, OR 97212
Phone: (503) 249-3766
Email: bohalloran2001@yahoo.com
(served electronically)

Attorneys for Garnishee-Petitioner on Review American Family Mutual Insurance Company:

John R. Barhoum
Chock Barhoum LLP
121 SW Morrison St., Suite 415
Portland, OR 97204
Phone: (503) 477-4061
Email:john.barhoum@chockbarhoum.com
(served electronically)

James E. Oliver, Jr.
Jim Oliver Law
P.O. Box 13225
Portland, OR 97213
Phone: (503) 481-9993
Email: jimoliverlaw@gmail.com
(served conventionally)

L. Kathleen Chaney
Lambdin & Chaney, LLP
4949 S. Syracuse St., Suite 600
Denver, CO 80237
Phone: (303) 799-8889
Email: kchaney@lclaw.net
(served conventionally)

s/Michael E. Farnell
Michael E. Farnell