

LEGAL ALERT

March 2005

INSURANCE COVERAGE FOR DEFECTIVE CONSTRUCTION AFCON INC. v ELLIS-DON MICHIGAN, INC.

By Matthew L. Meyer, Attorney

The Michigan Court of Appeals recently addressed and reconfirmed the prevailing rule in Michigan which states that defects in one's own work are not covered under a typical commercial general liability ("CGL") policy, but damage to the property of another party is typically covered. The case of AFCON, Inc v Ellis – Don Michigan, Inc., et al, Docket No. 250100, February 22, 2005, involved the construction of a sewer treatment facility that was to be built on the banks of the Rouge River. Ellis-Don Michigan, Inc. (Ellis-Don), the general contractor, hired AFCON, Inc. (AFCON) to build retaining walls during excavation. One of the retaining walls moved and caused a deep two hundred foot long crack in the soil held back by the wall. Ellis-Don incurred over \$175,000 in extra charges arising from the shifting retaining wall.

Ellis-Don pursued a claim against AFCON's insurer for the costs stemming from the wall movement. The insurer rejected the claim and cited the "Business Risk" exclusions in the policy which excluded coverage for the following type of damage:

k. Damage to Your Product

"Property damage" to "your work" arising out of it or any part of it.

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."

The main issue in the case was whether Ellis-Don's damages could be defined as "property damage," or whether its damages "were merely additional costs expended to remedy the defective wall." The court held that Ellis-Don's damages were not "property damage" and denied coverage.

Ellis-Don argued that the deep crack in the soil constituted "property damage." The court rejected that argument and reasoned that "the crack was merely a natural occurrence that happened as a result of the wall movement." The court focused on the line of Michigan cases that only found coverage where there was actual physical injury to the tangible property of others.

Coverage Found

In Calvert v Herbert Roofing 807 F. Supp 435 (ED Mich 1992), the court found coverage when there was damage to the interior of a building from a leaky roof. Similarly, the court found coverage for fire damage to a tunnel under construction and construction equipment in Dimambro-Northend Assoc v United Constr. Inc., 154 Mich App 306 (1986). Also, in the case of Bundy Tubing v Royal Indem, 298 F2d 151 (6th Cir 1962), the court found coverage existed where defective tubing used for radiant heating leaked and evidently damaged buildings and their contents. Also, in Radenbaugh v Farm Bureau, 240 Mich App 134 (2000), the court found coverage where the insured provided faculty schematics to contractors who constructed a homeowner's foundation which resulted in damage to the foundation and to the home itself.

No Coverage

The foregoing cases are contrasted with the line of Michigan cases which found no coverage for faulty workmanship absent some sort of damage to the property of others. For example, in Z&R Electric v Cincinnati Ins. Co, Docket No. 226605 June 5, 2001, the court found no coverage when a large motor failed on several occasions and needed expensive repairs. The court in Z&R stated that "unlike the damage to other individuals' property at issue in Bundy, Calvert and Radenbaugh, the record here does not include evidence that the motor's failure damaged any other part or aspect of the facility. The malfunction merely made the system

inoperative in the same way that the defective concrete made the water treatment plant in Vector unusable, with the defects in both cases requiring massive repair and replacement efforts.”

The case of Hawkeye v Vector, 185 Mich App 369 (1990) involved a concrete subcontractor who sought coverage for the removal of 13,000 cubic yards of concrete that did not meet project specifications. The court denied coverage and ruled that the installation of defective concrete merely constituted faulty workmanship.

The Bottom Line

Michigan courts continue to focus on whether the insured’s faulty work product damaged the property of others when determining if there is insurance coverage for defective construction. If there is no damage to the property of others, then typically there is no coverage under a CGL.

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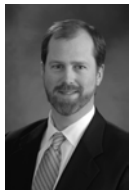
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