

Leaky Plumbing in Condominium Constituted Common Element, Requiring Coverage to Condominium Owner as Additional Insured Under Condominium Association Liability Policy

In *Fireman's Fund Ins. Co. v. Pierre – Louis*, 2006 WL 2796381 (Ill.App. 1st Dist. September 29, 2006), an Illinois appellate court considered whether a condominium owner was an additional insured under a condominium association's general liability policy. The plaintiff Fireman's Fund issued a general liability policy to 155 North Harbor Drive Condominium Association. Section II of the policy defined an insured to include "each other unit owner of the described condominium, but only with respect to liability arising out of ownership, maintenance or repair of that portion of the premises which is not owned solely by the unit owner." *Pierre-Louis*, 2006 WL 2796381 at *1.

The defendant Pierre-Louis owned a condominium at 155 North Harbor Drive in Chicago. In July 2003, members of the condominium association maintenance staff responded to a report of a leak in his unit. Their investigation revealed the kitchen faucet supply line was causing a leak. Water was also discovered under the kitchen sink, on the kitchen and hardwood floors in the dining room, and the living room, bedroom and closet carpets. In response, the condominium association sent a letter to the defendant advising him of the condition, and that 22 other condominium owners in the building of reported water damage as a result of the leak in his unit. The condo association thus demanded he rectify the situation.

In October 2003, Suburban Bank and Trust, the titleholder of one of the damaged units adjacent to the defendant, filed a complaint in the Circuit Court of Cook County sounding in negligence and gross negligence (hereinafter referred to as "the Suburban lawsuit"). The defendant tendered his defense of the Suburban lawsuit to the plaintiff Fireman's Fund. Fireman's declined to defend the underlying lawsuit

on the grounds that the defendant's alleged liability arose out of that portion of the premises which was owned, occupied and used solely and used exclusively by him, that is, the kitchen water supply line. Fireman's thus filed a complaint for declaratory judgment seeking a finding the defendant was not entitled to coverage.

Cook County Circuit Court Judge Daniel R. Donnersberger disagreed, granting a cross-motion for summary judgment filed by the defendant insured. The trial court found Fireman's had a duty to defend the defendant in the Suburban lawsuit, and awarded \$25,000.00 in attorney's fees to the defendant for the fees and costs incurred and defending the lawsuit. However, for reasons not explained in the opinion, the defendant's request for reimbursement of the settlement amount paid to settle the Suburban lawsuit was denied. (The defendant did not file a cross appeal, and thus the appellate court never considered whether there was a duty to indemnify under the policy.)

The issue on appeal was thus whether the lawsuit alleged damages that arose out of the defendant's ownership, maintenance or repair of a portion of the condominium unit not owned solely by him and not reserved for his exclusive use or occupancy. Fireman's argued that because the underlying complaint alleged the defendant was the "title holder of record of Unit 3110 Harbor Drive" and maintained "his premises in a careless and negligent fashion," this language indicated Suburban was suing the defendant solely because he was the individual owner of the unit, thereby disqualifying him as an additional insured under the policy. The appellate court rejected this reasoning. The court noted that at the time of the loss, the declarations of condominium ownership and of easements, restrictions, covenants and bylaws for the 155 Harbor Drive Condominium Association stated all pipes in the building were common elements. As the insurance policy covered all of the unit owners with respect to those portions of the premises that were not reserved for exclusive use, the court found

that the water pipes were part of the common elements. The court reasoned that water pipes supply the entire building with water, and cannot be considered to be used exclusively by any one unit, even when those water pipes reach into the unit. As a result, the court affirmed and found there was a duty to defend the underlying action.

No Coverage Afforded Where Insured's Insurance Agent Failed to Procure Owner's Automobile Insurance Policy

In *Founders Insurance Company v. White*, 2006 WL 2715267 (Ill.App. 1st Dist. September 22, 2006), an Illinois appellate court was faced with the issue of whether Great Northern Insurance Agency was the agent of the plaintiff, Founders Insurance Company. The defendant Tamietha White was the driver in a car vs. pedestrian accident. In December 2002, White was driving her car when she struck a pedestrian, minor Christina Williams. Via her guardian and next friend, Williams sued White for personal injuries. Founders denied coverage to White, on the basis that at the time of the accident, White was operating a vehicle that she owned, which was outside the coverage of her non-owner's insurance policy. The summary judgment papers showed that in September of 2002, White, with the assistance of Great Northern, obtained non-owner's vehicle insurance policy issued by Founders. The terms of the policy unequivocally provided coverage to White only when she was operating a vehicle that she did not own.

After discovery concluded, Founders filed a motion for summary judgment. In the motion, Founders argued Great Northern was not its agent; thus, if White had a dispute regarding the type of insurance coverage for which she had applied, White should have sued Great Northern. Founders further asserted that under the clear and unambiguous language of the policy, coverage was only afforded where White incurred liability due to driving a vehicle that she did not own. Because there was no material issue of fact White

owned the vehicle involved in the accident, there was no coverage for the loss.

On appeal, White admitted the non-owners insurance policy she purchased from Founders did not afford coverage for the car accident. To circumvent this undisputed fact, White alleged she meant to purchase or should have purchased an owner's policy, and therefore, Great Northern procured the wrong policy. In turn, it was argued that Great Northern's alleged mistake should be imputed to Founders, based on White's assertion that Great Northern was Founders agent.

In considering this issue, the appellate court noted that an insurance broker owes a duty to the insured, while the insurance agent owes a duty to the insurer. *Young v. Allstate Insurance Company*, 351 Ill. App. 3d 151, 162, 812 N.E. 2d 741 (2004). Further, citing *Young*, the court noted that "to determine whether a certain individual acted as a broker or an agent, we must analyze the following four factors: (1) who first set that individual in motion; (2) who controlled that individual's action; (3) who paid that individual; and (4) whose interests that individual was protecting." *Young*, 351 Ill. App. 3d at 162-63.

Based on Young's four-factor test, the appellate court concluded Great Northern did not act as Founders' agent, but instead served as White's agent. Most notable was the fact that White indisputably set Great Northern in motion when she sought Great Northern's assistance in procuring automobile insurance. Further, Great Northern worked with 15 to 20 insurance companies, and White obtained her policy from Founders because Founders offered the most competitive rates for a non-owners policy for someone in White's position. Moreover, Great Northern financed a portion of the premium owed by White to the plaintiff, to the benefit of White. Finally, Founders' senior claims/coverage analyst and vice president of underwriting confirmed that Great Northern was not Founders' agent and Great Northern was an independent insurance broker. The appellate court thus concluded that the circuit was correct in granting summary judgment, and affirmed.

Significantly, the appellate court noted that Great Northern had collected a premium from White on behalf of Founders, and under some limited circumstances, had the authority to bind insurance coverage for White. The court found, however, that these facts were insufficient to generate a material issue of fact that Great Northern was Founders agent.

All Primary Insurance Policies Must Be Exhausted Before Excess Policy May Be Selected by Insured for Indemnification

Kajima Construction Services, Inc. v. St. Paul Fire and Marine Insurance, 2006 WL 2662703 (Ill.App. 1st Dist. September 15, 2006), considered for the first time in Illinois whether the selective tender rule supercedes well-settled principles of Illinois law regarding horizontal exhaustion. General contractor Kajima Construction Services and its insurer Tokio Marine and Fire Insurance brought a declaratory judgment action against subcontractor Midwestern Steel Fabricators, Inc.'s insurer St. Paul Fire and Marine Insurance Company. The declaratory judgment action sought the reimbursement of a \$1,000,000 contribution by Tokio to indemnify Kajima in an underlying personal injury lawsuit. Upon the parties' cross motions for summary judgment, the trial court granted summary judgment in favor of the defendant St. Paul. The appellate court affirmed.

In December 1997, Kajima entered into a construction contract with Midwestern. Under the contract, Midwestern was to obtain and maintain commercial general liability insurance with \$1,000,000 of primary coverage and \$5,000,000 of umbrella coverage. Kajima was named as an additional insured on Midwestern's policy pursuant to the agreement. Midwestern subsequently provided Kajima with a certificate of insurance reflecting primary coverage limits of \$2,000,000 and \$5,000,000 in excess coverage issued by St. Paul, naming Kajima as an additional insured.

During the construction project, Thomas Jones, an employee of Midwestern's subcontractor, was seriously injured. Jones filed a personal injury suit against Kajima and Midwestern sounding in negligence. In response, Kajima made a "targeted tender" to Midwestern and St. Paul requesting to be defended and indemnified. St. Paul agreed to defend Kajima under reservation of rights.

The Jones case settled during trial for \$3,000,000. St. Paul paid its primary limits of \$2,000,000, and Tokio contributed its primary limits of \$1,000,000 to satisfy the settlement. Tokio and Kajima filed a declaratory judgment against St. Paul, seeking reimbursement of Tokio's contribution to the settlement. They argued that Tokio was not responsible for defending or indemnifying Kajima because Kajima made a targeted tender to St. Paul for defense and indemnification. St. Paul argued that Illinois law required that all primary policies be exhausted prior to reaching a true excess policy. The circuit

court agreed, and entered summary judgment in favor of St. Paul.

On appeal, the court considered the rationales underlying the selective tender and horizontal exhaustion doctrines. The court recognized that the selective tender doctrine requires that an insured covered by multiple concurrent policies has the right to choose which insurer will defend and indemnify it with respect to a specific claim. The court noted the Illinois Supreme Court clearly established an insured's right to select exclusive coverage among concurrent primary insurance policies, citing *John Burns Const. Co. v. Indiana Ins. Co.*, 189 Ill.2d 570, 574, 727 N.E.2d 211 (2000). The rationale underlying this rule is that the insured may choose to forego an insurer's assistance for various reasons, including the insured's fear that premiums would increase or that the policy would be cancelled in the future.

Horizontal exhaustion, on the other hand, applies to an insured who has multiple primary and excess policies covering a common risk. "If a covered claim occurs, the theory of horizontal exhaustion requires the insured to exhaust all primary policy limits before invoking excess coverage." *Kajima Construction*, 2006 WL 2662703 at *3. This rule is based on the rationale that to permit an insured to pursue coverage from certain excess insurers to the exclusion of others would "blur the distinction between primary and excess insurance [citations] and it would allow certain primary insurers to escape unscathed when they would otherwise bear the initial burden of providing indemnification." *Id.*, citing *U.S. Gypsum*, 268 Ill.App. 3d at 654.

The court noted that in the instant case it was undisputed Kajima had \$3,000,000 in primary general liability coverage available to it: the Tokio policy provided \$1,000,000 in primary coverage, and the St. Paul coverage provided \$2,000,000 in primary coverage to Midwestern, naming Kajima as an additional insured. It was also undisputed the umbrella policy issued by St. Paul to Midwestern was a true excess policy.

The court found *Illinois Emcasco Insurance Co. v. Continental Casualty Co.*, 139 Ill.App.3d 130, 134, 487 N.E.2d 110 (1st Dist. 1985), particularly instructive. In that case the Appellate Court for the First District recognized the general differences between primary coverage and umbrella policies. In *Illinois Emcasco*, the court concluded that an umbrella policy is unique, that it is always excess over and above other contracts with few exceptions, and thus cannot be activated until all primary

coverage is exhausted. Based on this and other prior authority, the *Kajima* court held it could not accept the plaintiff's invitation to apply the vertical exhaustion rule. The court thus held the selective tender rule should be applied to circumstances where concurrent primary coverage exists for additional insureds. Thus, to the extent defense and indemnity costs exceed primary limits, the deselected insurer or insurers' primary policies would have to answer for the loss prior to invoking coverage under an excess policy. The court therefore held the circuit court properly denied the plaintiff's motion for summary judgment.

Insured's Mistaken Cutting of Trees on Wrong Lots Constituted Covered "Occurrence" Under Commercial General Liability Policy

In *Pekin Insurance Company v. Miller*, 2006 WL 20065606 (Ill.App. 1st Dist. August 8, 2006), an Illinois appellate court discussed whether a tree cutter's commercial general liability policy afforded a defense for the insured's mistake in cutting trees on the wrong lot. The trial court found the insurer had a duty to defend. The appellate court affirmed.

The insured, Ken Miller, operated a tree cutting service and was hired to clear trees off certain lots. Certain property owners filed suit for trespass and violations of the Wrongful Tree Cutting Act, as well as additional counts of negligent trespass. They alleged Sarang Corporation hired Miller to remove trees from lots 13, 14 and 15 of a subdivision and instead, Miller cleared trees from lots 10, 11 and 12, which were owned by the plaintiffs. Miller tendered his defense to his insurer, Pekin Insurance Company. Pekin filed a declaratory judgment action, asserting coverage was excluded. Specifically, Pekin first contended its CGL policy did not cover the property damage because Miller's actions do not constitute an "occurrence" under the policy. Under the policy, property damage was covered only if the damage was caused by an "occurrence." An "occurrence" is defined as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." *Miller*, 2006 WL 20065606 at *2. Pekin argued Miller's actions were intentional, not accidental. Illinois courts have defined an accident under CGL policies as "an unforeseen occurrence, usually of a disastrous character or an undersigned sudden or unexpected event of an inflictive or unfortunate character." *Id.*

The court rejected the contention that Miller's removal of trees on the underlying

plaintiffs' property was intentional and thus not an "occurrence" under the policy. There was no evidence Miller intended the harmful result, that is, the clearing of the trees on the wrong property. The court therefore concluded it was irrelevant that the underlying complaint alleged the insured actions were intentional; it was the resulting "property damage" that would have to be expected and intended in order for coverage to be forfeited. The court thus concluded the allegations of the underlying complaint constituted an "occurrence" within coverage of the policy, creating a duty to defend.

Pekin next argued that two exclusions of the CGL policy precluded coverage, exclusions j(5) and j(6). Exclusion j(5) of the policy excluded coverage for property damage to "that particular part of real property on which you or any contractors or subcontractors working directly or indirectly on your behalf while performing operations, if the 'property damage' arises out of those operations." Section j(6) excluded coverage for property damage to: "[t]hat particular part of any property that must be restored, repaired or replaced because 'your work' was incorrectly performed on it." Such exclusions, noted the court, are typical in CGL insurance policies, because CGL policies are "intended to protect the insured from liability for injury or damage to the persons or property of others; they are not intended to pay the costs associated with repairing and replacing the insured's defective work and products, which are purely economic losses." *Id.* at *3, quoting *Eljer Manufacturing*, 197 Ill. 2d at 314.

Though the court could not locate an Illinois state court decision squarely confronting the precise fact pattern presented by the case, it did find a Minnesota Supreme Court decision with similar facts, *Thommes v. Milwaukee Insurance Company*, 641 N.W. 2d, 877 (Minn. 2002). In that case, the insured also entered into a contract to clear land for commercial development, but cleared one-half acre of land owned by a different owner who never consented to the work. Milwaukee Insurance Company declined to defend or indemnify based on exclusions j(5) and j(6). That court distinguished between two types of risks undertaken by an insured contractor: those of business risk, for which the insured may be liable as a matter of contract law, which are not covered, and the risk that a contractor's work or product will cause bodily injury or property damage to others' property, which is covered. The Minnesota court went on to hold exclusion j(5) was ambiguous because the policy did not define the phrase "that particular part of

real property" or the word "operations." Moreover, the exclusion did not expressly apply to operations performed on the property of third parties. The court also held the exclusion in section j(6) was ambiguous because it was subject to two separate interpretations: either the work was "incorrectly performed" and performed on the wrong property, or the work was "incorrectly performed" because the manner in which the work was performed was faulty or defective. The court thus construed both exclusions narrowly against the insurer, and concluded the exclusion applied only to work performed in a faulty or defective manner, and thus did not bar coverage.

The *Pekin Insurance* court adopted the *Thommes* holding and thus found both exclusions were ambiguous in this context. As a result, the court affirmed the circuit court's decision and held Pekin was obligated to defend Miller in the underlying lawsuit.

U.S. District Court Holds Insured's Negligent Manufacture of Product Constituted "Occurrence" Requiring Indemnification for \$70 Million Judgment

In *Wausau Underwriters Insurance Company v. United Plastics Group, Inc., et al.*, 2006 WL 2633248 (N.D.Ill. September 11, 2006), U.S. District Judge Darrah confronted whether Ohio Casualty Insurance Company had a duty to indemnify United Plastics Group (UPG) for a \$70 million judgment. The facts of the underlying case were as follows: Microtherm manufactures and sells electronically controlled tankless water heaters under the name "Seisco." UPG was one of the companies that manufactured molded plastic chambers for use in the Seisco water heaters. The evidence at trial showed UPG was aware of problems and concerns Microtherm had had with the previous manufacturer, including that the previous manufacturer had used too low a melt temperature in manufacturing the plastic chambers. Knowing full well that the chambers were supposed to be molded at a temperature of 540 to 580 degrees Fahrenheit, UPG manufactured the plastic chambers at a melt temperature 70 to 100 degrees lower than the recommended melt temperature.

In February 2002, Seisco realized UPG was using these low temperatures and became concerned. Around that time, the water chambers began failing, causing the water heaters to malfunction. Microtherm filed suit alleging breach of contract, breach of the duty of good faith, fraud and misrepresentation, breach of express and implied warranties, negli-

gence, and deceptive trade practices. The lawsuit alleged UPG's conduct resulted in damage and injury to Microtherm's products, work or services, the water heaters, and customers' property. After a six-week jury trial, a verdict was returned in favor of Microtherm and against UPG. In summary, the jury found UPG failed to comply with the warranty by furnishing or selecting goods that were not suitable for a particular purpose, failing to perform services in a good and workmanlike manner. The jury also found UPG made a negligent misrepresentation concerning the quality of the goods, but awarded no damages on that count.

After the verdict, Wausau Underwriters Insurance Company filed a declaratory judgment action against UPG regarding a separate insurance coverage issue arising from the jury verdict. Ohio Casualty was granted leave to intervene, and likewise sought a declaration that it owed no coverage to UPG. Microtherm, as a judgment creditor, and assignee of the rights to indemnity was also granted leave to intervene. Ohio Casualty's declaratory judgment action went to a bench trial, resulting in a court find Ohio Casualty had a duty to indemnify UPG.

Before trial, Ohio Casualty filed a motion in limine seeking to exclude all evidence except for the jury's findings from the underlying action, which were incorporated into the final judgment. Microtherm and UPG argued they were not attempting to avoid the Microtherm jury findings or to collaterally attack it. They instead sought to offer evidence that there was "property damage" as defined in the insurance policies, an issue that was never tried by or submitted to the Texas jury in the underlying case. Citing *Pekin Insurance Company v. Pulte Home Corp.*, 344 Ill.App. 3d 64, 71, 800 N.E. 2d 466 (2003), the court noted that issues germane only to coverage, and not liability, may be present that would not have been litigated in the underlying case, requiring additional testimony. Because the issue was whether "property damage" as defined by the policy was suffered, the court determined evidence on this issue was admissible, and thus, denied Ohio Casualty's motion *in limine*. The court also rejected Ohio Casualty's argument that Microtherm was collaterally estopped from relitigating the Microtherm lawsuit. The court reasoned that the issues pertaining to coverage, specifically whether there was property damage as defined in the Ohio Casualty policy, were quite different from the issues litigated in the Texas lawsuit. The court thus rejected the collateral estoppel argument as well.

At the bench trial before the district court, it was established that UPG molded the plastic chambers that were placed in the units between November and December 2001, and over 600 of the chambers failed. The UPG chambers' failure caused a short in the circuit board of the water heater due to water leaking, rendering the heaters useless. The chamber leaks also caused damage to customers' homes, causing distributors to lose confidence in Microtherm, in turn causing a precipitous drop in sales resulting in lost profits and loss of value to Microtherm.

The court first considered whether "property damage" occurred as defined by the policy. The court dispatched with this issue in a one sentence ruling, finding Microtherm had clearly demonstrated there was physical injury to tangible property and the loss of use of tangible property: the Seisco units and damage to third parties homes and business premises and personal property within the buildings. The court devoted more discussion to the issue of whether there was an "occurrence" as defined by the policy. The Ohio Casualty CGL policy defined "occurrence" as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." The court noted Illinois law defined "an accident" as "an unforeseen occurrence, usually of an untoward or disastrous character, or an undesigned sudden or unexpected event of an inflictive or unfortunate character." However, the natural and ordinary consequences of an act do not constitute an accident. Thus, even if property damage is not intended, it can be expected and be excluded from coverage. Such property damage is expected if it should have been "reasonably anticipated by the insured." *Wausau*, 2006 WL 2633248 at *8.

Based on this authority, Ohio Casualty argued that because UPG knowingly manufactured the plastic chamber that was unsuitable for holding water, UPG should have expected the water would leak from the chamber. The court rejected this argument, holding that "it is not the leaking of water that must be expected or foreseen; it is the resulting property damage that must be expected or foreseen." The court concluded that Microtherm and UPG proved the defects in UPG's product caused damage to another's property and that the resulting damage was not intended, expected or foreseen. The court thus held the resulting property damage was "an occurrence" under the Ohio Casualty policy.

The court also briefly considered Ohio Casualty's argument that various policy

exclusions excluded coverage. The court disagreed that any such exclusions applied. First, the court considered exclusion A of the Ohio Casualty Insurance policy, which excluded coverage for property damage that is expected by the insured. The court determined this exclusion did not apply based on its analysis that UPG had not expected the resulting property damage. Next, the court considered exclusion E, which excluded coverage for "impaired property," or "property that has not been physically injured." The court held Ohio Casualty failed to demonstrate the water heaters were impaired property because they could not demonstrate the property could be restored by the "repair, replacement, adjustment or removal of UPG's water chamber or through UPG's failing the terms of this contract or agreement." The court next considered whether exclusions F and G applied, which exclude coverage to "property damage to your product arising out of its, or any part of it" and "property damage to your work arising out of it or any part of it and included in the products completed operations hazard." The court rejected these exclusions applied, as UPG did not seek coverage based on damage to its product. Finally, the court rejected the argument that exclusion H applied, as that section excludes coverage for the cost of calling or replacing faulty chambers. Because neither such event occurred, exclusion H was found not to apply.

For these reasons, the court concluded UPG was entitled to indemnification under the policy, and entered final judgment in favor of Microtherm and UPG and against Ohio Casualty.

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