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Supplying Wrong Construction Materials Resulting in Rip-and-Tear Damage Not an "Occurrence," 7th Circuit Holds

Insurance Coverage and Bad Faith Alert **| February 28, 2020**
By: Anthony L. Miscioscia and Timothy A. Carroll

The construction contract calls for International Building Code-compliant lumber. The insured doesn't supply that. What the insured does supply gets installed but then ripped out and replaced, causing damage to the surrounding property into which the lumber was integrated. Such circumstances — not uncommon in the construction industry — do not constitute an "occurrence" under Illinois law, according to the U.S. Court of Appeals for the Seventh Circuit in an opinion published yesterday. *Lexington Insurance Company v. Chicago Flameproof & Wood Specialties Corporation*, No. 19-1062, 2020 U.S. App. LEXIS 6006 (7th Cir. Feb. 27, 2020).

The insured in *Chicago Flameproof* was an Illinois-based "distributor of commercial building materials, including fire retardant and treated lumber ('FRT lumber')." A residential and commercial contractor contracted with the insured for "a particular brand of FRT lumber, D-Blaze lumber, for use in the four projects." Despite the insured's alleged knowledge that the lumber was being purchased to comply with International Building Code (IBC) standards adopted in Minnesota, the site of the construction projects, the insured allegedly "made a 'unilateral decision' to instead deliver its in-house FlameTech brand lumber, which purportedly was not IBC-compliant FRT lumber, and "thereby 'did not meet the IBC definition of FRT lumber' and therefore 'was not actually FRT lumber.'" Not aware of using the wrong lumber, the contractor installed it but, after later discovering it, was instructed to remove it and replace it with IBC-certified FRT lumber. Doing so resulted in damage to the "surrounding materials into which the lumber had been integrated." The insured was sued for breach of contract, breach of warranties, negligent misrepresentation, and on other related causes of action.

The insurer in *Chicago Flameproof* filed suit, seeking a declaration that it did not owe a duty to defend the insured in the underlying suit. Entering judgment for the insurer, the Illinois federal district court held that if, as alleged, the insured "knowingly supplied non-IBC-compliant lumber and concealed that it did so, . . . then the property damage that allegedly resulted from tearing out that non-compliant lumber cannot be said to have been caused by an accident." On appeal, the Seventh Circuit Court of Appeals affirmed that holding, concluding the underlying suit did not allege an "occurrence," defined in the policy as "an accident."

Under Illinois law, the Court observed, an accident is "an unforeseen occurrence, usually of an untoward or disastrous character or an undesigned sudden or unexpected event of an inflictive or unfortunate character," and that if damage " 'is the rational and probable consequence of the act or, stated differently, the natural and ordinary consequence of the act,' then the act 'is not an accident.' " The Court of Appeals also observed that "[f]aulty workmanship may constitute an occurrence if it results in damages that exceed the scope of the insured's work product," or "where the insured 'was unaware of the defective nature' of its component until after it was incorporated into a finished product."

Concluding that the underlying suit did not allege an "occurrence," as so defined, the Court reasoned that "[t]here was nothing regarding the natural and ordinary consequences of supplying uncertified lumber for projects that require certified lumber that was unknown or hidden to [the insured] at the time it shipped the uncertified lumber." The rip-and-tear damage alleged, therefore, "was the natural and ordinary result of [the insured's] deliberate decision to supply, and conceal that it had supplied, uncertified lumber," and thus not an "occurrence."

If you have any questions or need more information, contact Anthony L. Miscioscia (miscioscia@whiteandwilliams.com; 215.864.6356) or Timothy A. Carroll (carrollt@whiteandwilliams.com; 215.864.6218).