STATE OF MICHIGAN

IN THE CIRCUIT COURT FOR THE COUNTY OF LEELANAU

FARM BUREAU MUTUAL INSURANCE COMPANY OF MICHIGAN,

Plaintiff,

v

File No. 03-6248-CK
HON. PHILIP E. RODGERS, JR.

MARSHALL SCOTT MIKULA, JENNIFER MIKULA, SCOTT KISSAU, LORI KISSAU, VIRGINIA CULLEN and LIBERTY MUTUAL GROUP,

Defendants.
_____/

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Attorney for Defendants Mikula

Blake K. Ringsmuth (P44013)
Attorney for Defendants Kissau and Cullen

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DECISION AND ORDER REGARDING
CROSS-MOTIONS FOR SUMMARY DISPOSITION

Defendant Scott Mikula is a residential builder. Defendant Jennifer Mikula is his wife. They will be referred to collectively as "Mikula." In October of 1998 and March of 1999, Mikula purchased two adjoining lots in the Pine Woods development for the purpose of constructing "spec" homes. Both homes were constructed and sold, the first to Defendant

Virginia Cullen ("Cullen") in March 2000 and the second to Defendants Scott and Lori Kissau (collectively "Kissau") in September 2000.

In April of 2001, both homes experienced a sudden influx of water into the basements. Mikula made several attempts to rectify the problem in 2002, but was unsuccessful. In October of 2002, Kissau moved and, by February of 2003, Cullen moved.

Kissau and Cullen each filed a lawsuit against Mikula to recover their damages. Those lawsuits have now been consolidated. The claims and damages asserted are essentially the same, i.e., breach of contract, breach of warranty, negligent construction, negligence and violations of the Consumer Protection Act. The basis of all these claims is that the homes were built too close to the water table. When the water table rose, it resulted in the basements filling up with water, damaging personal property and improvements and requiring Kissau and Cullen to incur clean up expenses, additional electric utility charges, loss of use of the homes and loss of the value of the homes.

Mikula claims that the cause of the abrupt rise in the water table that led to the flooding was unauthorized work in a wetland by two landowners who own property to the north of the Kissau and Cullen homes that resulted in backup of water draining through a natural gully. Since the problem was corrected in May of 2003, the water has ceased to come into the basements of the Kissau and Cullen homes.

At all times pertinent hereto, Mikula was insured under a Farm Bureau Insurance Company Contractors Comprehensive General Liability Policy. This declaratory action was initiated by Farm Bureau Insurance Company ("Farm Bureau") seeking a ruling that the policy provides no coverage for any of the claims made by Cullen and Kissau and that Farm Bureau has no duty to defend Mikula in the related actions.

In response to the Court's Civil Scheduling Conference Order, Farm Bureau and Mikula filed cross-motions for summary disposition, pursuant to MCR 2.116(C)(10), each claiming that there is no genuine issue of material fact and that they are entitled to judgment as a matter of law. Although Farm Bureau's original position was that there is no applicable insurance coverage at all, Farm Bureau now concedes that it has a duty to defend Mikula because of the allegations of damage to personal property. Therefore, Farm Bureau asks the Court to rule only that there is no coverage for the damage to the homes themselves.

Mikula, as well as Cullen and Kissau, rely upon *Fresard v Michigan Millers Mutual Ins Co*, 97 Mich App 584; 296 NW2d 112 (1980), aff'd by an equally divided Court 414 Mich 686; 327 NW2d 286 (1982), reh den 417 Mich 1103 (1983) and argue that none of the exclusions defeat coverage.

On Monday, January 5, 2004, the Court heard the oral arguments of counsel and took the matter under advisement. The Court now issues this written decision and order and, for the reasons stated herein, grants Farm Bureau's Motion for Summary Disposition and denies Mikula's Motion for Summary Disposition.

Applicable Law

The construction of an insurance contract with clear language is a question of law. *G & A, Inc v Nahra*, 204 Mich App 329, 330; 514 NW2d 255 (1994). An insurance policy must be enforced in accordance with its terms. *Upjohn Co v New Hampshire Ins Co*, 438 Mich 197, 207; 476 NW2d 392 (1991). An insurance company is not liable for a risk it did not assume. *Auto-Owners Ins Co v Churchman*, 440 Mich 560, 567; 489 NW2d 431 (1991); *Kaczmarck v La Perriere*, 337 Mich 500, 60 NW2d 327 (1953).

An insurance policy must be read as a whole to determine if it is ambiguous. Where there is no ambiguity, the court will enforce the terms of the contract as written. *Stine v Continental Casualty Co*, 419 Mich 89, 114; 349 NW2d 127 (1984); *Murphy v Seed-Roberts Agency, Inc*, 79 Mich App 1, 7-9; 261 NW2d 198 (1977). The court must interpret the terms of the contract in accordance with their "commonly used meaning," *Group Ins Co of Michigan v Czopek*, 440 Mich 590, 596; 489 NW2d 444 (1992); *Fireman's Fund Ins Co v Ex-Cell-O Corp*, 702 F Supp 1317, 1323, n 7 (ED Mich 1988), and must take into account the reasonable expectations of the parties. *Vanguard Ins Co v Clarke*, 438 Mich 463, 472; 475 NW2d 48 (1991).

The court cannot create ambiguity where the terms of the contract are clear. *Churchman, supra* at 567; 489 NW2d 431; *Metropolitan Property & Liability Ins Co v DiCicco*, 432 Mich 656, 666; 443 NW2d 734 (1989), reh den with addenda to opinion 433 Mich 1202; 446 NW2d 291 (1989), citing *Edgar's Warehouse, Inc v United States Fidelity & Guaranty Co*, 375 Mich 598; 134 NW2d 746 (1965); *Patek v Aetna Life Ins Co*, 362 Mich 292; 106 N2d 828 (1961); *Dimambro-Northend Associates v United Construction, Inc*, 154 Mich App 306, 313; 397 NW2d

547 (1986); *Farm Bureau Mutual Ins Co v Hoag*, 136 Mich App 326, 332; 356 NW2d 630 (1984). However, where an ambiguity exists, the court will construe the policy in favor of the insured. *Auto Club Ins Ass'n* v *DeLaGarza*, 433 Mich 208, 214; 444 NW2d 803 (1989); *Powers v DAIIE*, 427

Mich 602, 624; 398 NW2d 411 (1986). Any ambiguities will be liberally construed in favor of the insured party. *Calhoun v Auto Club Ins Assoc*, 177 Mich App 85; 441 NW2d 54 (1989).

An insurer that intends to exclude coverage under certain circumstances should clearly state those circumstances in the section of its policy entitled "exclusions." *Transamerica Ins Corp of America v Buckley*, 169 Mich App 540; 426 NW2d 696 (1988). Each exclusion is meant to be read with the insuring agreement, independently of every other exclusion. The exclusions should be read seriatim, not cumulatively. There is no instance in which an exclusion can properly be regarded as inconsistent with another exclusion, since they bear no relationship with one another. *Fresard v Michigan Millers Mut Ins Co*, 414 Mich 686; 327 NW2d 286 (1982).

As our Supreme Court said in *Auto-Owners Ins Co v Churchman*, 440 Mich 560, 566-567; 489 NW2d 431 (1992):

> An insurance policy is much the same as any other contract. It is an agreement between the parties in which a court will determine what the agreement was and effectuate the intent of the parties. Accordingly, the court must look at the contract as a whole and give meaning to all terms. Further, '[a]ny clause in an insurance policy is valid as long as it is clear, unambiguous and not in contravention of public policy.' This Court cannot create ambiguity where none exists.
>
> Exclusionary clauses in insurance policies are strictly construed in favor of the insured. However, coverage under a policy is lost if any exclusion within the policy applies to an insured's particular claims. Clear and specific exclusions must be given effect. It is impossible to hold an insurance company liable for a risk it did not assume. [Citations omitted.]
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> The inquiry does not necessarily end, however, with the rules of construction. A court may also consider the reasonable expectations of the insured. *Vanguard Ins Co v Clarke*, 438 Mich 463, 472; 475 NW2d 48 (1991). A court must look at the policy language from an objective standpoint and determine whether an insured could have reasonably expected coverage.

Applicable Policy Provisions

Under the opening statements in the Business Liability Section of the subject policy, Farm Bureau agreed as follows:

> We [Farm Bureau] will pay, on behalf of the Insured, all sums which the Insured becomes legally obligated to pay as damages because of bodily injury or property damage caused by an occurrence to which this insurance applies.

> Our total liability for all damages, including completed operations hazard, products hazard, and damages for care and loss of services, as a result of any one occurrence will not exceed the limit of liability stated in the Declarations as applicable to each occurrence.
>
> As stated in the Declarations, however, the General Aggregate Limit shown under Business Liability is the most we will pay for all occurrences during the policy period, except for damages as a result of the completed operations hazard and products hazard.
>
> The Products-Completed Operations Aggregate Limit is the most we will pay for all occurrences during the policy period with respect to the completed operations hazard and products hazard.

Exclusions contained in the original form insurance contract include, in pertinent part, that the insurance does not apply:

> 1. to liability assumed by the Insured under any contract or agreement, except an incidental contract;[1] but *this exclusion does not apply to a warranty of fitness or quality of your products or a warranty that work performed by or on behalf of you will be done in a workmanlike manner*;[2] [Emphasis added.]

Other exclusions as amended by the Contractor's Amendatory Endorsement include, in pertinent part, that the insurance does not apply:

> 14. to property damage to your product arising out of it or any part of it;

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[1] The definition of incidental contract was extended by the Contractor's Amendatory Endorsement to include "any contract or agreement relating to the conduct of your business."

[2] This exclusion appears in the original policy. The other applicable exclusions were rewritten in the Contractor's Amendatory Endorsement.

15. to property damage to your work arising out of it or any part of it and included in the completed operations hazard and products hazard.[3]

"Completed operations hazard and products hazard" are defined in the Contractor's Amendatory Endorsement to include "all bodily injury and property damage occurring away from premises you own or rent and arising out of your product or your work, except:

(1) products that are still in your physical possession; or
(2) work that has not yet been completed or abandoned."

It is apparent from reading the policy that not only are there exclusions to the broad general liability coverage, but there are exceptions to the exclusions. Exclusion 1 excludes liability assumed by the Insured under any contract or agreement, **except** an incidental contract ("any contract or agreement relating to the conduct of your business.") Exclusion 1 also contains an exception to the exclusion for "a warranty of fitness or quality of products or a warranty that work performed by or on behalf of the Insured will be done in a workmanlike manner."

Exclusion 14 excludes from coverage "property damage to the Insured's work and work product arising out of it or any part of it." Exclusion 15 excludes property damage to the Insured's work that is included in the completed operations hazard and products hazard which include "all bodily injury and property damage occurring away from premises you own or rent and arising out of your product or your work." The only difference between Exclusion 14 and Exclusion 15 is that Exclusion 14 applies to the home during construction whereas Exclusion 15 applies to the home after the

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[3] Exclusion 15 originally read: "to property damage to work performed by you or on your behalf arising out of the work, or any portion of the work, or out of materials, parts, or equipment furnished in connection with the work." This original wording was deleted and replaced by this new wording in the Contractor's Amendatory Endorsement which also redefined "completed operations hazard and products hazard" to include "all bodily injury and property damage occurring away from premises you own or rent and arising out of your product or your work, except:

(1) products that are still in your physical possession; or

construction has been completed and the home sold. Exclusion 15 applies here because the subject homes were completed and sold. Some of the case law discussed herein deals with exclusions similar to Exclusions 1 and 14 and the interplay between them which is arguably the same as the interplay between Exclusion 1 and Exclusion 15 which applies after the construction has been completed.

Discussion

Mikula, Cullen and Kissau rely upon *Fresard* in which contradictory exclusions similar to Exclusions 1 and 14 in this case were determined to be ambiguous by the Court of Appeals and interpreted in favor of the insured to exclude coverage for negligent construction, but grant coverage for claims based on breach of warranty. *Id* at 589-590.

Farm Bureau, on the other hand, relies upon cases such as *Jones v Philip Atkins Const Co*, 143 Mich App 150; 371 NW2d 508 (1985) and *Tiano v Aetna Casualty & Surety Co*, 102 Mich App 117; 301 NW2d 476 (1980) which it claims overrule *Fresard.*

In *Fresard*, the plaintiffs constructed a house. Water accumulated in the basement after the foundation was laid, but before the structure was finished. The house was nonetheless completed and sold to the Hardings. The Hardings sued the plaintiffs, who were insured under a comprehensive general liability policy issued by the defendant. The plaintiffs' comprehensive general liability policy did not include products liability and completed operations coverage. The defendant undertook the defense of the Hardings under a reservation of rights agreement. The plaintiffs brought a declaratory judgment action seeking a ruling that the defendant was obligated under the policy to defend the suit and pay any judgment rendered against them.

The policy contained an exclusion identical to Exclusion 1 in the present case, and several other exclusions, one of which stated that the insurance did not apply "to property damage to work performed by or on behalf of the named insured arising out of the work or any portion thereof, or out of materials, parts or equipment furnished in connection therewith." This exclusion is essentially the same as Exclusion 14 (and Exclusion 15 regarding completed operations hazard and products hazard) in the present policy.

The Supreme Court was equally divided. In an opinion by Justice Kavanagh, the Court affirmed the Court of Appeals, holding that the insurance contract was ambiguous because there

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(2) work that has not yet been completed or abandoned."

was more than one reasonable interpretation of the policy language and, therefore, the policy should be construed against the insurer and in favor of coverage.

The Michigan Supreme Court has not overruled *Fresard*. Other courts have, however, questioned, distinguished or declined to follow *Fresard*. For example, *Fresard* was criticized in *Hawkeye-Security Ins Co v Vector Const Co*, 185 Mich App 369, 385; 460 NW2d 329 (1990) for adopting the "minority view," citing *St Paul Surplus Lines Ins Co v Diversified Athletic Services*, 707 F Supp 1506 (ND Ill 1989). In *St Paul Surplus*, the insurer brought an action for a declaratory judgment that it had neither a duty to defend nor to indemnify its insured in connection with a claim involving a defective skating rink. The United State District Court for the Northern District of Illinois declined to adopt a magistrate's report and recommendation because it followed the minority view as represented by the Supreme Court of Maine in *Baybutt Constr Corp v Commercial Union Ins Co*, 455 A2d 914 (Me 1983). In *Baybutt*, the court noted that exclusions like Exclusion 14 in the present case, when standing alone, are unambiguous and exclude coverage to an insured for a breach of contract or warranty based on faulty workmanship or materials, but when such an exclusion is considered with the exception to an exclusion like Exclusion 1, the correlative effect is a clouding of meaning and an internal inconsistency. Consequently, the court in *St Paul Surplus* adopted the majority view that the exception to an exclusion like Exclusion 1 could not grant coverage for warranty claims and is subject to all other exclusions.

The Court of Appeals panel in *Hawkeye-Security* opted not to follow *Fresard.* Instead the panel followed *Stillwater Condo Ass'n v American Home Assurance Co*, 508 F Supp 1075 (D Mont 1981), aff'd 688 F2d 848 (CA 9, 1982) and adopted the "majority view" that:

> . . .exclusionary clauses limit the scope of coverage provided under the insurance contract; they do not grant coverage. Moreover, . . . each individual exclusion refers, not to the other exclusions, but to the hazards insured against *by the insurance contract.* Accordingly, "exclusions are to be read 'with the insuring agreement, independently of every other exclusion.'" [Citations omitted.]

In *Jones v Philip Atkins Constr Co*, 143 Mich App 150; 371 NW2d 508 (1985), the Court of Appeals distinguished *Fresard* because *Fresard* involved an ambiguity created by an apparent conflict between two exclusions found in the same section of the policy whereas, in *Jones*, a completed operations exclusion contained in an endorsement attached to the comprehensive general liability policy was found to be unambiguous and held to prevail over general provisions

of the policy to exclude coverage for injuries sustained by a person who received an electrical shock while repairing an air conditioner in a building which the general contractor had completed four years earlier. The *Jones* court found the case of *Tiano v Aetna Casualty & Surety Co*, 102 Mich App 177; 301 NW2d 476 (1980) to be more on point because the insured did not purchase completed operations coverage and there was a completed operations exclusion in a separate endorsement attached to the policy. The Court held that endorsements or riders prevail over form provisions of a contract and the policy remains in effect as altered by the endorsements.[4]

Like the *Jones* and the *Tiano* cases, the present case involves a conflict between exclusions found in different sections of the policy. Exclusion 1 is found in Section II - Business Liability and Exclusions 14 and 15, as amended, are found in the Contractors Amendatory Endorsement.

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[4] See also, *Reliance Nat'l Ins Co v Harfield*, 228 F3d 909 (8th Cir 2000) where the court declined to follow *Fesard*; *O'Shaughnessy v Smuckler Corp*, 543 NW2d 99 (Minn App, 1996) where the court recognized an abrogation; and *Upjohn Co v Aetna Casualty & Surety Co*, 850 F Supp 1342 (WD MI 1993) where the court questioned *Fresard.*

However, unlike the builders in the *Jones* and the *Tiano* cases, Mikula did purchase completed operations hazard and products hazard coverage.[5]

Conclusion

After a thorough review of the subject policy, including the exclusions, exceptions to the exclusions and exceptions to the exceptions, and the caselaw, as well as listening to the arguments of counsel, the Court finds that the subject insurance policy is not ambiguous.

The policy affords coverage for bodily injury or property damage caused by an occurrence to which the insurance applies. Exclusion 1 excludes from coverage any liability assumed by Mikula under any contract for service. But, Exclusion 1 does not apply to a warranty of fitness or quality or a warranty that the work will be done in a workmanlike manner.

Exclusions 14 and 15 as amended by the Contractor's Amendatory Endorsement. They exclude from coverage "property damage to your product arising out of it or any part of it" and "property damage to your work arising out of it or any part of it and included in the completed operations hazard and products hazard," respectively. The definitions of "completed operations hazard" and "products hazard" were also deleted and replaced by the Endorsement to read: "'completed operations hazard and products hazard' includes all bodily injury and property damage occurring away from premises you own or rent and arising out of your product or your work."

The damage at issue here is property damage to the homes themselves allegedly arising out of Mikula's improper siting of or excavating for the homes.[6] The exception to Exclusion 1

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[5] In the Guardian Policy Declarations for both policy period June 21, 1999 to June 21, 2000 and policy period June 21, 2000 to June 21, 2001 a Products-Completed Operations Aggregate limit of $1,000,000 is shown. Presumably the premium Mikula paid was determined based on such coverage being included. As noted above, Section II Business Liability starts with a declaration that Farm Bureau will pay, among other things, "for all occurrences during the policy period with respect to the completed operations hazard and products hazard" which again is defined to include "all bodily injury and property damage occurring away from premises owned by the Insured and arising out of the Insured's product or work, when the work has been completed."

makes such damage covered only if it occurs as a result of a breach of warranty. Exclusion 15 excludes such damage from coverage if it arises out of Mikula's work and occurs after construction has been completed and the premises sold.

Coverage under the insurance policy is lost because Exclusion 15 applies to the facts presented in this case. Exclusion 15 relieves Farm Bureau of liability with regard to the costs of repairing or replacing the homes assuming Mikula's performance was faulty.[7] It does not, however, relieve Farm Bureau of liability for damage to property other than to the structures themselves or for loss of use of those structures. See, *Radenbaugh v Farm Bureau General Ins Co of Michigan*, 240 Mich App 134, 150; 610 NW2d 272 (2000).[8]

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[6] Counsel for Mikula, Cullen and Kissau argued that improper siting of the home or failing to properly excavate was not a part of the "work" because such things are not a part of the tangible end product. In *Radenbaugh, supra*, however, giving defective instructions to a basement contractor regarding construction of a mobile home basement and the erection of the mobile home on the basement was considered part of the "work."

[7] Of course, if Mikula was not negligent in siting and excavating the homes, i.e., if fault lies in the negligence of those who engaged in unauthorized disruption of the neighboring wetlands, then there is no basis for coverage.

[8] In *Radenbaugh*, the insured sold a mobile home and, in conjunction with the sale, provided erroneous schematics and instructions to the contractors hired to construct the basement foundation and erect the home on the basement. That conduct caused damage to the home and its basement. Farm Bureau refused to defend or indemnify under a commercial general liability policy. The insurance company asserted, among other things, that there was no duty to defend or indemnify by operation of the business risk exclusion (identical to Exclusion 14 and Exclusion 15 with respect to completed operations). The Court rejected this argument because the second amended complaint did not pertain solely to damages to the product of the insured (the mobile home) but also to property damages to the basement and other consequential damages. The Court relied upon *Underwriters at Interest v SCI Steelcon*, 905 F Supp 441 (WD Mich 1995) and held that such an exclusion relieves the insurer of liability with regard to the costs of repairing the structure where the contractor's performance is faulty, but it does not relieve them of liability for property damage to property other than the structure itself or loss of use of the structure. *Id* at 150.

The Plaintiff Farm Bureau's motion for summary disposition is granted. The Defendant Mikula's motion for summary disposition on this issue is denied.

IT IS SO ORDERED.

This decision and order resolves the last pending claim and closes the case.

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HONORABLE PHILIP E. RODGERS, JR.
Circuit Court Judge

Dated: _____