

## Insurance & Reinsurance - Canada

### Every Bulldog has its day: appeal court rules on insurance for unusable products

Contributed by **McMillan LLP**

August 16 2011

**Facts**  
**Decisions**  
**Comment**

Insurers offering commercial general liability policies have a new cautionary tale after the British Columbia Court of Appeal ruled that insurers may be required to compensate their insureds for unusable products.

#### Facts

The dispute involved a plastic bag manufacturer, Bulldog Bag Ltd, which provided more than 1 million printed plastic bags to SureGro, a customer that used Bulldog's bags for its soil and manure business. SureGro noticed that after some of the bags were filled with SureGro products, the print faded and ran off, making the labelling on the bags illegible. As a result, the bags were deemed unfit for use. Bulldog provided SureGro with replacements and credited it for the unused defective bags. SureGro proceeded to transfer the contents of the defective bags to the new bags, which cost it over C\$780,000. SureGro was able to claim this amount from Bulldog; however, Bulldog was denied insurance coverage for its claim from AXA, its insurer. Bulldog claimed only for the content transfer costs plus the value of soil and manure contained in the defective bags that were lost or destroyed in the process. Bulldog did not claim for the cost of replacing the defective bags.

Bulldog's commercial general liability policy outlined coverage for property damage due to an "accident" or "occurrence". The policy defined 'property damage' as "physical injury to or physical destruction of tangible property, including loss of use thereof, or loss of use of tangible property that has not been physically injured or destroyed". AXA argued that the only physical injury or damage to tangible property was to the bags themselves, which were Bulldog's own property and work product. Accordingly, the other costs incurred were attributable to pure economic loss, which AXA did not cover.

#### Decisions

At trial level, the court ruled that Bulldog's policy covered only the value of the lost or destroyed soil and manure contained in the defective bags. This amounted to approximately C\$12,000 and left Bulldog responsible for a loss of over C\$770,000.

Between the time of Bulldog's trial and the court of appeal's decision, the Supreme Court of Canada decided *Progressive Homes Ltd v Lombard General Insurance Co*. In that case the insured, a general contractor, built a housing development that was later found to contain defects that allowed rainwater to enter and damage parts of the building. Progressive was denied indemnification under the commercial general liability policy that it held with its insurer.

The lower courts in *Progressive* determined that Progressive's commercial general liability policy covered "property damage" caused by an "occurrence", but was restricted to claims for damage to property outside of the insured's work product.

The Supreme Court of Canada ruled that Progressive's claim for physical damage for the construction defects to its housing developments was covered by its commercial general liability policy. The Supreme Court determined that the terms 'property damage' and 'occurrence' in the policy did not exclude property that the insured contracted and supplied. Accordingly, the Supreme Court found that Progressive's insurers had a duty to defend it.

After the Supreme Court decision in *Progressive*, the issue in the appeal of *Bulldog* shifted from an interpretation of the commercial general liability policy's insuring provision to the question of whether any of the exclusions in the commercial general

Author

Hartley Lefton



liability policy applied.

AXA conceded that Bulldog's defective bags were an 'occurrence' resulting in 'property damage', but argued that the policy's work product exclusion negated coverage for the cost of the contents transfer from the defective bags to new ones. AXA attempted to argue that the costs relating to the contents transfer of the bags were related to the loss of use of the bags, which involved repairing and replacing Bulldog's defective work product. Consequently, AXA reasoned that there was no claim for damage.

The court of appeal disagreed and held that the work product exclusion did not apply. The court distinguished between a claim for loss of use and a loss flowing from a loss of use (eg, the transfer and recovery costs of the manure and soil resulting from the loss of use of the bags). Because the claim was not for "loss of use" of Bulldog's bags, but rather for the cost of salvaging and transferring the manure and soil, those costs were determined not to be excluded from coverage under the policy. As the work product exclusion did not specify that coverage would be excluded for "claims that flow from" the defective product, the work product exclusion was found not to apply.

## Comment

Insurers and insureds can take a number of lessons from this case. Specifically, insurers, insureds and their brokers are advised to:

- assess whether work product exclusions should include losses incurred as a result of defects in the insured's own work, goods or products, and set premiums accordingly;
- review the business practices of the insured to verify the coverages and exclusions that they intend to apply;
- discuss mitigation techniques in the cases of an occurrence under the policy to ensure that post-occurrence acts by the insured do not invalidate coverage; and
- meet with counsel if in doubt about their rights or obligations.

For further information on this topic please contact [Hartley Lefton](#) at *McMillan LLP* by telephone (+1 416 865 7000), fax (+1 416 865 7048) or email ([hartley.lefton@mcmillan.ca](mailto:hartley.lefton@mcmillan.ca)).

The materials contained on this website are for general information purposes only and are subject to the [disclaimer](#).

ILO is a premium online legal update service for major companies and law firms worldwide. In-house corporate counsel and other users of legal services, as well as law firm partners, qualify for a free subscription. Register at [www.iloinfo.com](http://www.iloinfo.com).

---

## Online Media Partners

