COURT OF APPEALS
DECISION
DATED AND FILED

March 31, 2011

A. John Voelker
Acting Clerk of Court of Appeals

Appeal No. 2010AP347 **Cir. Ct. No. 2009CV2007**

STATE OF WISCONSIN **IN COURT OF APPEALS**
DISTRICT IV

GENERAL CASUALTY COMPANY OF WISCONSIN,

PLAINTIFF,

V.

RAINBOW INSULATORS, INC.,

DEFENDANT,

KBS CONSTRUCTION, INC.,

DEFENDANT-THIRD-PARTY PLAINTIFF-APPELLANT,

V.

E&A ENTERPRISES, INC.,

THIRD-PARTY DEFENDANT-CO-APPELLANT,

ACUITY, A MUTUAL INSURANCE COMPANY,

THIRD-PARTY DEFENDANT-RESPONDENT.

APPEAL from an order of the circuit court for Dane County: DANIEL R. MOESER, Judge. *Affirmed*.

Before Vergeront, P.J., Lundsten and Blanchard, JJ.

¶1 BLANCHARD, J. This is a duty-to-defend insurance case in the construction context, involving defects in the construction of a condominium building that caused acoustical problems for residents. KBS was the general contractor for the project and hired subcontractors that included E&A Enterprises, Inc. KBS filed a third-party complaint[1] against E&A and its insurer, Acuity, alleging that E&A breached its contract with KBS through faulty installation of metal resilient channels that act as sound absorbers, and by refusing to correct the faulty installation. KBS claims that these errors resulted in two categories of damage: the loss of use and enjoyment of the condominium units by residents, and the physical destruction of ceilings required to fix the noise problem. Acuity moved for summary judgment, asserting that its policies do not cover KBS's allegations against E&A. The circuit court granted summary judgment to Acuity, and E&A appeals the court's order.

¶2 The issue presented is whether KBS's complaint alleges facts that, if proven, would result in coverage for E&A under Acuity's insurance policy, thus triggering Acuity's duty to defend E&A. We conclude that although both of the

[1] General Casualty, as the insurer of another subcontractor on the project, Rainbow Insulators, Inc., filed the original lawsuit against KBS and Rainbow, seeking a declaratory judgment that Rainbow's insurance policies did not cover KBS's insurance dispute with Rainbow and for reimbursement of defense costs. In response, KBS filed a counterclaim against General Casualty and Rainbow for Rainbow's alleged defective work and a third-party complaint against E&A and its insurer Acuity, which is at issue here. The claims of General Casualty and Rainbow are not at issue in this appeal.

policies at issue provide initial coverage, the "your work" exclusion in one form and the "contract" exclusion in the other preclude coverage. We therefore conclude that Acuity has no duty to defend E&A and affirm.

BACKGROUND

¶3 The allegations in KBS's complaint for breach of contract against E&A include the following. Under the KBS-E&A contract, E&A agreed to handle metal stud framing and drywall for the project. After construction was completed in 2006, residents experienced noise problems. An inspector hired by the condominium owner determined that mistakes by E&A created the noise problems, including using screws that were too long in attaching resilient channels to drywall, thus causing the screws to contact wood trusses, and incorrectly orienting the resilient channels, installing them in the wrong direction. KBS alleged that this was faulty workmanship that directly caused the acoustical problems.

¶4 The complaint further alleges that the noise problems required immediate corrective measures by KBS to permit residents to enjoy the use of their units. E&A fixed its mistakes in one unit. However, E&A refused to assume the costs of correcting its mistakes on that unit, or to fix the errors throughout the rest of the building without additional payment. Because there was no reasonable alternative to fixing the problems, KBS was obligated to take on the expensive project of demolishing all of the ceilings, save one, in order to remove and reinstall the resilient channels in the correct orientation, using appropriate screws. KBS alleges as damages: (1) "the loss of use and enjoyment of the condominium units," and (2) "the physical destruction of ceilings directly necessitated by E&A's acts or omissions."

¶5 Acuity moved for declaratory judgment and summary judgment on its cross-claim against E&A, asking the court to find that Acuity has no duty to defend or indemnify E&A, because Acuity's insurance policies do not provide coverage for KBS's allegations. The circuit court granted summary judgment in favor of Acuity, finding that E&A's policies do not cover KBS's allegations. E&A appeals, contending that both policies provide it with insurance coverage.

DISCUSSION

I. Standard of Review

¶6 We review a grant of summary judgment de novo, employing the same methodology as the circuit court, and benefiting from the court's analysis. *See* ***Green Spring Farms v. Kersten***, 136 Wis. 2d 304, 314-16, 401 N.W.2d 816 (1987). A party is entitled to summary judgment when no genuine issues of material fact are in dispute and the party is entitled to judgment as a matter of law. ***Id.***; WIS. STAT. § 802.08(2) (2009-10).[2]

¶7 Turning to the specific context of duty-to-defend cases, we determine whether an insurer has a duty to defend an insured party in an action by comparing the factual allegations of the complaint to the terms of the policy. ***Estate of Sustache v. American Family Mut. Ins. Co.***, 2008 WI 87, ¶20, 311 Wis. 2d 548, 751 N.W.2d 845. The insurer's duty "is triggered by the allegations contained within the four corners of the complaint." ***Id.*** We liberally construe those allegations and assume all reasonable inferences in favor of a duty to defend.

[2] All references to the Wisconsin Statutes are to the 2009-10 version unless otherwise noted.

Id., ¶21. The insurer has a duty to defend if "the complaint" alleges facts which, if proven, would give rise to liability covered under the terms and conditions of the policy." ***Sola Basic Ind., Inc. v. U.S. Fidelity & Guar. Co.***, 90 Wis. 2d 641, 646, 280 N.W.2d 211 (1979). When we construe the terms of an insurance policy, our interpretation is a legal inquiry that we conduct independently of the circuit court, while benefiting from its analysis. *See* ***Estate of Sustache***, 311 Wis. 2d 548, ¶18.

¶8 The goal of that inquiry "is to determine and give effect to" the intentions of the parties. ***Wisconsin Label Corp. v. Northbrook Prop. & Cas. Ins. Co.***, 2000 WI 26, ¶23, 233 Wis. 2d 314, 607 N.W.2d 276. We interpret insurance polices as they would be understood by a reasonable person in the insured's position. ***Id.***, ¶25. Ambiguity in coverage terms are construed against the insurer. ***Estate of Sustache***, 311 Wis. 2d 548, ¶21.

¶9 The general approach, which we follow below, is to first consider whether an insurance policy makes an initial grant of coverage for the allegations. ***Id.***, ¶22. If not, the analysis concludes with the determination that there is no coverage. ***Id.*** If there is an initial grant of coverage, we examine whether any exclusion precludes coverage. ***Id.***, ¶23. There is no duty to defend "unless coverage survives application of the policy exclusions." ***State Farm Fire & Cas. Co. v. Acuity***, 2005 WI App 77, ¶9, 280 Wis. 2d 624, 695 N.W.2d 883.

¶10 Under these standards, we examine whether initial coverage is available to E&A under either of the two Acuity forms, and if so, whether any exclusions apply to preclude coverage under that policy. We discuss each form in turn, although as will be seen there is some overlap in the analysis because the policies share some terminology that is used with the same apparent intent.

II. Bis-Pak Business Liability and Medical Expenses Coverage Form

A. Initial Grant of Coverage

¶11 Taking first the commercial general liability policy called the Bis-Pak Liability and Medical Expenses Coverage Form, this policy provides initial coverage for "those sums that the insured becomes legally obligated to pay as damages because of … property damage" caused by an "occurrence." "Property damage" is defined as (1) "Physical injury to tangible property, including all resulting loss of use of that property" or (2) "Loss of use of tangible property that is not physically injured."

¶12 Acuity challenges the circuit court's conclusion that KBS's complaint alleges damages caused by both types of tangible property damage, "physical injury" and "loss of use," which, if proven, would provide initial coverage under the Bis-Pak form. We discuss the arguments related to each type of property damage in turn.

1. Bis-Pak Initial Coverage: Physical Injury to Tangible Property

¶13 We begin by considering whether KBS's allegations, if proven, would create liability for E&A to pay damages because of "[p]hysical injury to tangible property, including all resulting loss of use of that property." Acuity argues that KBS does not allege "physical injury" sufficient to provide initial coverage, because KBS does not allege injury to the property beyond that injury directly resulting from KBS's *own repair efforts* in tearing out and replacing the defectively installed construction elements, and that KBS's repair efforts do not count as physical injury to property. We conclude that Acuity's argument is not relevant to the question of whether KBS alleged "physical injury to tangible

property" because it does not matter what caused the property damage under the policy language at issue.

¶14 The phrase "physical injury to tangible property" in an insurance policy is clear in its meaning and not ambiguous. ***Wisconsin Label Corp.***, 233 Wis. 2d 314, ¶31. When "injury" "is qualified by the word 'physical,' its meaning is limited to physical damage." ***Id.*** Accordingly, "the phrase 'physical injury' ordinarily refers to some sort of physical damage" to property, ***id.***, such as "an alteration in appearance, shape, color, or in other material dimension." *See*, *e.g.*, ***Travelers Ins. Co. v. Eljer Mfg., Inc.***, 757 N.E.2d 481, 502 (Ill. 2001).

¶15 KBS's complaint alleges that E&A's conduct directly resulted in damages caused by "the physical destruction of ceilings," namely the demolition of all but one of the ceilings of the building. These are allegations of physical injury (physical destruction) to tangible property (ceilings). Accordingly, these allegations, if proven, would constitute "property damage" under the Bis-Pak form under the plain language of the policy.

¶16 In the face of this plain language creating initial coverage, Acuity's only contrary contention is to assert that the circumstances that gave rise to the physical damage, namely the repair efforts, do not constitute "physical injury to tangible property." However, it does not matter what gave rise to the physical damage for purposes of determining whether the destruction of the ceilings constitute property damage. The scope of coverage for alleged "property damage" depends solely on the policy language. *See* ***American Family Mut. Ins. Co. v. American Girl, Inc.***, 2004 WI 2, ¶¶33, 35, 268 Wis. 2d 16, 673 N.W.2d 65 (the sinking, buckling, and cracking of a warehouse qualified as "property damage," defined in the policy as "physical injury to tangible property"). Acuity's argument

is based on allegations not relevant to the language of the property damage definition. The definition does not contain language that limits coverage based on what caused the physical injury; it requires only "physical injury to tangible property." Therefore, whether the property damage was caused by repair efforts is not relevant to the narrow issue raised here, namely whether KBS alleges "physical injury to tangible property."

¶17 In sum, we conclude based on the unambiguous policy language that the policy provides an initial grant of coverage because KBS alleges "physical injury to tangible property."

2. Bis-Pak Initial Coverage: Loss of Use of Tangible Property Not Physically Injured

¶18 Next we address whether KBS has alleged damages under the second part of the "property damage" definition, "[l]oss of use of tangible property that is not physically injured." Acuity argues that KBS has failed to allege a claim for "loss of use," because KBS's "loss of use" claim is made on behalf of third parties not joined in the suit, namely residents of the condominium, and therefore is not a claim for its own "loss of use." In purported support for this argument, Acuity cites ***Wausau Tile, Inc. v. County Concrete Corp.***, 226 Wis. 2d 235, 593 N.W.2d 445 (1999). We conclude that coverage exists under the plain language of the policy, and Acuity fails to present a developed argument to the contrary based on ***Wausau Tile***, or otherwise.

¶19 Under the plain language of the Bis-Pak policy, there is initial coverage for KBS's allegations. The policy defines "property damage" in its second definition as "[l]oss of use of tangible property that is not physically injured," but does not define who must suffer the "loss of use." KBS alleges that

E&A's work resulted in excessive noise and acoustical problems, which in turn caused KBS significant damages due to "the loss of use and enjoyment of the condominium units." We conclude that the allegations in the complaint satisfy the requirements for a "loss of use" claim.

¶20 In a brief assertion, Acuity contends that ***Wausau Tile*** precludes KBS's loss of use claim. ***Wausau Tile*** is inapplicable because it decided whether an insurance policy provided coverage for economic loss. ***Id.*** at 245. The ***Wausau Tile*** court held that the economic loss alleged in that case was not "property damage" within the meaning of that policy's "property damage" definition containing the same language at issue here. ***Id.*** at 267-68. Acuity does not provide a developed argument explaining why this ruling is relevant here. We therefore decline to address this undeveloped argument. *See* ***State v. Pettit***, 171 Wis. 2d 627, 646-47, 492 N.W.2d 633 (Ct. App. 1992).

¶21 In sum, we conclude that KBS alleged damages caused by both types of "property damage" to create initial coverage under the Bis-Pak policy. We therefore move on to determine whether any exclusion of the Bis-Pak policy precludes coverage under both types of tangible property damage for which there is an initial grant of coverage.

B. Bis-Pak Exclusions

¶22 Acuity argues that either the "impaired property" or "Damage to Your Work" exclusion ("your work" exclusion) in the Bis-Pak policy precludes coverage for KBS's allegations of both types of property damage. We agree that the "your work" exclusion precludes coverage, because E&A's allegedly negligent installation of the resilient channels caused property damage that did not occur on E&A's property, and E&A's work was completed at the time the damages arose.

Accordingly, we do not address the parties' arguments regarding the allegedly independent grounds for exclusion under the "impaired property" exclusion.

¶23 The "your work" exclusion precludes coverage for: "*Property damage* to *your work* arising out of it or any part of it and included in the *products-completed operations hazard*."[3] It does not apply "if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor." The definition of "products-completed operations hazard" states in relevant part:

> *"Products-completed operations hazard"*:
>
> a. Includes 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.

¶24 The policy defines "[y]our work" as "[w]ork or operations performed by you or on your behalf" and "[m]aterials, parts or equipment furnished in connection with such work or operations." It is undisputed that the resilient channels, including the too-long screws, are "your work." The channels

[3] The "your work" exclusion appears to be missing the word "or" in the following text: "Property damage to *your work* [or] arising out of it." In addressing the same wording in the same policy provision, which was also missing the "or," our supreme court concluded that this language is not ambiguous and interpreted it as if it included the "or." ***Stuart v. Weisflog's Showroom Gallery, Inc.***, 2008 WI 86, ¶63, 311 Wis. 2d 492, 753 N.W.2d 448. In addition, the exception to the "your work" exclusion makes clear that the exclusion should be interpreted as if it included the "or." The exception to the exclusion states, "[t]his exclusion does not apply if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor." Therefore, we treat the missing "or" as a scrivener's error of no significance, as our supreme court has at least impliedly also done.

and screws are E&A's own work, because they are materials or parts furnished in connection with work performed by E&A, specifically the installation of the materials.

¶25 The language of the "your work" exclusion is not ambiguous. ***Stuart v. Weisflog's Showroom Gallery, Inc.***, 2008 WI 86, ¶63, 311 Wis. 2d 492, 753 N.W.2d 448. The exclusion "applies to property damage arising out of 'your work,' where that work occurs away from the premises owned or rented by the person doing the work and where the work was completed at the time of the damage." ***Id.***

¶26 Applying this language, we conclude that the "your work" exclusion is clearly applicable to E&A's allegedly negligent installation of the resilient channels, because the property damage: (1) arose out of E&A's work; (2) did not occur on E&A's premises, and; (3) occurred after E&A's work was completed.

¶27 The alleged property damage arose of out E&A's work. "As used in a liability insurance policy, the words 'arising out of' are very broad, general and comprehensive. They are commonly understood to mean originating from, growing out of, or flowing from, and require only that there be some causal relationship between the injury and the risk ...." ***Holsum Foods Div. of Harvest States Cooperatives v. Home Ins. Co.***, 162 Wis. 2d 563, 572, 469 N.W.2d 918, (Ct. App. 1991) (citation omitted). KBS alleges that E&A's faulty installation of the resilient channels "were a direct … cause" of both types of damage included in the definition of "property damage": (1) physical injury to the ceilings, because they had to be torn out; and (2) loss of use of the condominium units.

¶28 E&A's allegedly negligent installation did not occur on E&A's property. The work occurred at Monroe Commons and the owner of the property is Monroe Neighbors.

¶29 Finally, E&A's work was completed before the damages occurred. The complaint specifically alleges that after the completion of the construction project in 2006 (the E&A work), the Monroe Commons' residents began experiencing the noise problems (the loss of use) that led to the need to make the repairs (physical injury to tangible property).

¶30 E&A fails in its reply brief to counter Acuity's contention that the "Damage to Your Work" exclusion bars coverage for "[p]roperty damage to your work arising out of it or any part of it."

¶31 We conclude that the allegations fit within the "your work" exclusion in the Bis-Pak policy, because KBS alleges that E&A's work caused "property damage," did not occur on E&A's property, and was completed at the time the damages arose.

III. Contractors' Errors and Omissions Coverage Form

¶32 The second policy at issue is a professional liability policy called the Contractors' Errors and Omissions Coverage (E&O) Form. The parties dispute whether the E&O form provides initial coverage, and if so, whether the "contract" exclusion applies. We first discuss whether KBS's allegations fit under the policy's initial grant of coverage, which we conclude is a question easily resolved based on application of the same terminology used in the Bis-Pak policy as is discussed above. We then turn to the "contract" exclusion in the E&O policy.

¶33 Acuity argues that the E&O policy does not provide initial coverage because KBS has failed to allege damages due to "property damage." We disagree, because we conclude that KBS has alleged "property damage" to "your work" based on the plain language of the policy.

¶34 The E&O policy provides coverage for "damages because of *property damage* to *your product*, *property damage* to *your work*, *property damage* to *impaired property* or *recall expense* that arises out of *your product*, *your work*, or any part thereof." The E&O policy uses the same definition as the Bis-Pak policy for "property damage" and "your work." As discussed above, KBS has alleged "property damage" that fits within the "your work" exclusion. We therefore conclude that the E&O policy provides initial coverage.

¶35 Because KBS's allegations fit under the initial coverage, we next determine whether such coverage is precluded under the "contract" exclusion.

¶36 The "contract" exclusion in the E&O form excludes coverage for "damages arising out of any … [d]elay or failure by you or anyone acting on your behalf to perform a contract or agreement in accordance with its terms." By its terms, the exclusion applies because KBS's allegations are based on E&A's failure to perform according to the terms of the construction contract between KBS and E&A.

¶37 E&A argues that the E&O form provides coverage for KBS's allegations, despite the "contract" exclusion, because the alleged property damage arose out of E&A's negligent acts, errors, or omissions. In other words, E&A asserts that, because KBS alleged that negligent conduct caused E&A to breach the contract, the policy provided coverage.

¶38 In support of this argument, E&A cites ***1325 North Van Buren, LLC v. T-3 Group, Ltd.***, 2006 WI 94, ¶57, 293 Wis. 2d 410, 716 N.W.2d 822, in which our supreme court found initial coverage for allegations against the insured that "sound[ed]" in negligence, but which arose in the context of a contract between the insured and a developer. However, ***1325 North Van Buren*** does not support E&A's argument because it (1) addressed whether *initial coverage* for the developer's breach of contract claim existed under a professional liability policy that did not have a "contract" exclusion, and (2) recognized that a professional liability policy *could* contain a valid "contract" exclusion precluding coverage for alleged facts arising out of a breach of contract, if that was the intent of the parties.

¶39 In ***1325 North Van Buren***, the insurer argued that no initial coverage existed for a developer under a professional liability insurance policy, which contained similar initial coverage language to the E&O form in this case, because the developer was suing a contractor for breach of contract. ***Id.***, ¶¶51, 53-54. Our supreme court rejected this argument, concluding that there was initial coverage for allegations associated with the breach of contract claim because the allegations were based on a "'negligent act, error, or omission'" of the insured's "failure to adhere to professional standards, sounding in negligence, but arising in the context of a contract between" the insured and the developer. ***Id.***, ¶57; *see* ***id.***, ¶62 ("It is entirely possible that one could do a negligent act, which would form the basis for a breach of contract claim."). In reaching this result, the court recognized that, even though the particular policy at issue did not contain a "contract" exclusion, "[i]t would be an easy matter to have the insurance policy state that it does not cover facts that arise out of what is a breach of contract, if that was indeed [the] intention." ***Id.*** Therefore, ***1325 North Van Buren*** *does not* support E&A's argument that the "contract" exclusion does not apply. KBS's

allegations give rise to *initial coverage* under the E&O form because, similar to the developer's claim in ***1325 North Van Buren***, E&A's allegedly negligent actions, namely using too-long screws and installing resilient channels in the wrong direction, formed the basis for KBS's breach of contract claim. However, unlike in ***1325 North Van Buren,*** the E&O form here specifically excludes coverage, under the "contract" exclusion, for damages arising out of an insured's failure to perform a contract. KBS expressly alleges that pursuant to the terms of the contract between KBS and E&A, E&A agreed to perform certain requirements for the project including "the metal stud and drywall requirements," and that E&A's failure to perform these requirements breached the contract terms. Because KBS alleges a failure of E&A to perform its contract in accordance with its terms, the allegations fall squarely within the "contract" exclusion.

¶40 In a related argument, E&A asserts that in addressing the "contract" exclusion, the circuit court erroneously treated as determinative the fact that KBS pled a breach of contract cause of action, and that the duty-to-defend analysis should instead turn solely on the factual allegations contained in the complaint, which E&A asserts sound in negligence. *See* ***id.***, ¶58 (insurance coverage is not dependent on the theory of liability pled). We disagree that the court made this error. The court properly compared the factual allegations in the complaint to the relevant terms of the policies, in this instance determining that the conduct alleged in the complaint, if proven, would constitute failure to perform a contract, regardless of the cause of action selected by E&A.

¶41 Separately, E&A argues that this interpretation of the exclusion is absurd, because it would render the E&O policy meaningless, in that every time an insured enters into a contract, it would lose coverage for any negligent acts, errors or omissions in work performed under the contract. We disagree that our

interpretation of this exclusion cannot be correct because it would render the policy useless. Although KBS's specific allegations in this case fit the contract exclusion, this does not defeat coverage in all other scenarios. The exclusion applies only if the insured, or anyone acting on behalf of the insured, "[d]elay[s] or fail[s] … to perform the contract in accordance with its terms," and damages arise out of that delay or failure. It does not exclude all claims of any sort that might arise during the course of work performed under a contract, as E&A suggests. As one example, because contractors owe common law duties of care to those with whom they contract, as to all other persons, the "contract" exclusion would not operate to preclude E&O policy coverage arising from a tort claim that involves conduct that is not a delay or failure to perform under a contract term. *See* ***Alvarado v. Sersch***, 2003 WI 55, ¶16, 262 Wis. 2d 74, 662 N.W.2d 350 ("'[i]n Wisconsin, one always owes a duty of care to the world at large'") (citation omitted)).

CONCLUSION

¶42 We conclude that the complaint does not allege facts that, if proven, would result in coverage under either of the two insurance policies. Although both forms provide initial coverage for KBS's allegations, the "your work" exclusion in the Bis-Pak form and the "contract" exclusion in the E&O form preclude coverage for the allegations. Accordingly, we affirm the order of the circuit court declaring that Acuity does not have a duty to defend E&A.

By the Court.—Order affirmed.

Not recommended for publication in the official reports.