STATE OF MINNESOTA
IN COURT OF APPEALS
A09-179

Grinnell Mutual Reinsurance Company,
Respondent,

vs.

Steven Ripley,
d/b/a Ripley Construction,
Appellant,

John Gieschen, et al.,
Defendants.

Filed December 29, 2009
Affirmed
Lansing, Judge

Dakota County District Court
File No. 19HA-CV-08-2537

Ken D. Schueler, Hilary R. Stonelake, Dunlap & Seeger, P.A., Suite 505, 206 South Broadway, P.O. Box 549, Rochester, MN 55903 (for respondent)

Timothy K. Dillon, Dillon Law Office, 400 West Mill Street, Cannon Falls, MN 55009 (for appellant)

Considered and decided by Hudson, Presiding Judge; Lansing, Judge; and Shumaker, Judge.

U N P U B L I S H E D O P I N I O N

LANSING, Judge

Grinnell Mutual Reinsurance Company sought a declaratory judgment that it had no duty to defend or indemnify its insured, building contractor Steven Ripley, in a homeowners' suit for breach of contract, breach of statutory warranty, and negligent construction. The district court granted summary judgment on the ground that the damages alleged in the homeowners' action were essentially for negligent construction that is not covered under the policy. Because we conclude that the damages sought in the homeowners' suit are clearly excluded by the policy, we affirm.

F A C T S

Steven Ripley, a building contractor, had a commercial general liability (CGL) policy with Grinnell Mutual Reinsurance Company when he built a home for Gregory and Julie Waldvogel in Randolph in 2005. A year and a half later the Waldvogels sued Ripley when water seeped into their home during the spring thaw.

The facts leading up to the Waldvogels' suit are largely undisputed. The Waldvogels bought a lot from a developer and hired Ripley to build a home for them on the lot. After Ripley began construction, he suggested modifying the home design to include a walk-out basement. The Waldvogels agreed and Ripley added the walkout basement. He hired a subcontractor to grade and excavate the lot and to design and install the septic system.

After the subdivision's developer and the Waldvogels' lender expressed concerns about the lot's drainage, Ripley obtained the overall grading plan for the subdivision.

The plan showed that a walkout basement would not be appropriate for the lot based on the current drainage system, but Ripley proceeded with the walkout-basement design. When the city refused to issue an occupancy permit, Ripley wrote a letter ensuring that no flooding would occur so long as drainage was proper for the subdivision as a whole. The Waldvogels moved into the completed house in November 2005.

In the spring of 2007, melting snow pooled in the Waldvogels' back yard and water seeped into the basement of the home. Ripley built a dam of snow to stop the accumulation of water and the Waldvogels used a shop-vacuum and fans to dry out the basement's carpet. The city also provided some pumping services to get rid of water. Ripley visited the house later and stated that the Waldvogels' efforts drying out the carpet had been sufficient to prevent property damage to the interior of the home.

The Waldvogels sued Ripley and the developer of the subdivision. The complaint sought monetary damages from Ripley, based on claims that he negligently constructed the home, breached his contract, and breached a statutory new-housing warranty. Grinnell defended Ripley under a reservation of rights and then filed this action seeking a judgment declaring that it had no duty to defend or indemnify Ripley under the CGL policy. The district court granted Grinnell's motion for summary judgment, and Ripley now appeals.

D E C I S I O N

An insurer has a duty to defend a claim against its insured when any part of the claim is arguably covered by the policy. *Jostens, Inc. v. Mission Ins. Co.*, 387 N.W.2d 161, 165 (Minn. 1986). To support a declaration that the insurer has no duty to defend,

the insurer has the burden to show that all parts of the cause of the action fall clearly outside the scope of coverage. *Id.* at 165-66. The question of duty to defend is determined by "compar[ing] the allegations in the underlying complaint with the relevant language in the insurance policy." *St. Paul Fire & Marine Ins. Co. v. Seagate Tech., Inc.*, 570 N.W.2d 503, 505-06 (Minn. App. 1997).

On appeal from summary judgment, we determine whether there are any genuine issues of material fact and whether the district court erred in its application of the law. *Thommes v. Milwaukee Ins. Co.*, 641 N.W.2d 877, 879 (Minn. 2002). Coverage issues and the interpretation of policy language are questions of law, reviewed de novo. *Jenoff, Inc. v. N.H. Ins. Co.*, 558 N.W.2d 260, 262 (Minn. 1997). If the policy language is unambiguous, we apply its plain and ordinary meaning. *Thommes*, 641 N.W.2d at 880.

The determination of coverage in this litigation turns on the nature of the relief that the Waldvogels, as homeowners, are seeking in the underlying action. We begin, therefore, with the complaint. In the complaint's prayer for relief, the Waldvogels seek a "money judgment" against Ripley "for damages . . . as described above [in the complaint]." The damages that are "described above" are listed under the three claims against Ripley. In its negligence claim, the complaint seeks a money judgment for "re-construction and the installation of appropriate surface water drainage improvements . . . to prevent future flooding." The breach-of-contract claim describes the breach as constructing the home on property not suitable for a walkout basement, and seeks a money judgment to "re-construct a portion of their home and septic system, and/or install appropriate storm surface water drainage systems to protect their home

from flooding." And the final claim, for breach of statutory warranty, seeks a money judgment "for the cost to remedy the defect or breach or the reduction in the value of the dwelling."

The money judgment that the Waldvogels seek in the underlying action is therefore a claim for repair costs, replacement costs, improvement costs, or for the diminished value of the home. On its face, the complaint attributes these damages to defects in the design or construction of the home. Although the complaint describes the flood that occurred in February 2007, it does not attribute its claim for damages to costs resulting from the flood. That is, the Waldvogels allege that costly alterations are necessary, not as a result of the flood, but because the house was defectively constructed in the first place. The complaint alleges that the alterations are required to prevent future flooding, not to pay for the costs of the past flooding.

Having identified the damages that the underlying action seeks, we turn to the language of the policy. Ripley's policy with Grinnell promises payment for covered sums that he "becomes legally obligated to pay as damages because of . . . 'property damage.'" The coverage includes defense in any suit seeking these monetary damages. "Property damage" means "physical injury to tangible property, including all resulting loss of use of that property." It also includes "loss of use of tangible property that is not physically injured."

The injuries that the Waldvogels allege are arguably within the definition of "property damage" under the policy. As a result of the litigation, Ripley could become obligated to pay for "physical injury to tangible property." A defective septic-system

installation could constitute a physical injury to the house to which the system attaches, and could cause lost use of the house. In the same way, the walkout basement incorporated into a lot that is not suited for it can be a physical impairment of the lot and house, and cause lost use when the design flaw makes it likely that water will accumulate and seep into the house. The other defects could also arguably be property damage as defined by the policy.

Having established that the damages that the Waldvogels seek in their suit are arguably property damages, we now turn to the policy's exclusions to determine Grinnell's obligation. Provision 2(j)(5) of the policy excludes coverage for damages based on "'[p]roperty damage' to [] [t]hat particular part of real property on which [the insured] . . . or subcontractors working directly or indirectly on [the insured's] behalf are performing operations, if the 'property damage' arises out of those operations."

This type of exclusion incorporates the concept of the "business-risk" doctrine. *See Knutson Constr. Co. v. St. Paul Fire and Marine Ins. Co.*, 396 N.W.2d 229, 233 n.5, 234-35 (Minn. 1986) (listing similar exclusions). Under the doctrine, a contractor's liability "to make good on products or work which is defective . . . [or] to completely replace or rebuild the deficient product or work . . . is not what the [CGL] coverages . . . [are] designed to protect against." *Bor-Son Bldg. Corp. v. Employers Commercial Union Ins. Co.*, 323 N.W.2d 58, 63 (Minn. 1982) (quotation omitted); *see also Knutson*, 396 N.W.2d at 235 (stating that CGL policy "does not provide coverage for claims of defective materials and workmanship giving rise to a claim for damage to the property itself which is the subject matter of the construction project").

The exclusion in 2(j)(5) squarely applies to defects that are attributable to Ripley and his subcontractors. The Waldvogels' lot and home are "that particular real property on which [Ripley and his subcontractors were] performing operations." The construction defects are clearly alleged to have arisen out of these operations. The Waldvogels sought damages based on construction defects, and those damages are excluded from coverage. *See Knutson*, 396 N.W.2d at 235 (applying earlier version of exclusion 2(j)(5)).

Ripley challenges exclusion from coverage on two different grounds. First, he argues that the flood occurred long after his construction and his subcontractors' construction ceased. For 2(j)(5) to exclude coverage, commentators generally agree that the property damage for which relief is sought has to have occurred while the insured's operations were ongoing. *See* Theodore J. Smetak et al., *Minnesota Commercial General Liability Insurance Policy: Annotated* 79 (2008) (stating that exclusion applies to property damage arising out of insured's or subcontractors work "while they are performing [the] work").

It is undisputed that the flood occurred after construction operations had ceased. But the property damage at issue in this appeal is defective construction, which necessarily occurred while construction operations were ongoing. The complaint demonstrates that flood-related property damage is not the source of the relief that the Waldvogels seek. They seek repair, replacement, improvement, or lost value based on defects, all of which occurred during construction.

It is, of course, possible that damage could have occurred because of the flood if parts of the lot, home, or the home's contents had been further damaged, or if the

Waldvogels had lost the use of the home and incurred monetary damages for the lost use. But the record indicates that the flood did not cause damage to the home or lot or otherwise exacerbate the alleged construction defects. The allegations in the complaint referred to the flood as *evidence* of defects, but not an independent source of monetary damages.

Second, Ripley argues for coverage under an exception to the "your work" exclusion in the policy. The "your work" exclusion—exclusion 2(l)—denies coverage for "'property damage' to 'your [the insured's] work' arising out of it or any part of it and included in the 'products-completed operations hazard [(PCOH)].'" As relevant to Ripley's argument, the PCOH includes all property damage occurring away from the insured's premises and arising out of the insured's completed work. Ripley concedes that this exclusion would apply insofar as his own defective work caused property damage, but relies on the exception to the exclusion, which states that coverage is not excluded "if the damaged work or the work out of which the damage arises was performed on [the insured's] behalf by a subcontractor." Ripley averred by affidavit that the Waldvogel's property damage was caused by the grading, excavation, and improper septic design, work that was performed by one of his subcontractors.

We agree that, if this exclusion applied, there would likely be an issue of fact on whether the flood arose out of Ripley's work or the subcontractor's work. *See SCSC Corp. v. Allied Mut. Ins. Co.*, 536 N.W.2d 305, 313 (Minn. 1995) (stating that insurer has burden to show that excluded cause overrides covered, direct cause), *overruled on other grounds by Bahr v. Boise Cascade Corp.*, 766 N.W.2d 910 (Minn. 2009). And if the

complaint included monetary damages based on flood-related property damage, the causation issue would be material to whether the monetary damages were covered under this exclusion. The monetary damages sought by the Waldvogels, however, are based exclusively on the alleged construction defects themselves, not on the flood. Thus, the "your work" exclusion, and its exception, is inapplicable. Provision 2(j)(5) excludes coverage for all defect-related damages, and that exclusion applies whether or not the defects are attributable to a subcontractor.

Because the claims by the Waldvogels are not arguably covered by the policy, summary judgment absolving Grinnell of its duty to defend or indemnify Ripley was appropriate.

Affirmed.