STATE OF MINNESOTA
IN COURT OF APPEALS
A10-113

Sand Companies, Inc.,
Respondent,
vs.

Gorham Housing Partners III, LLP, et al.,
Defendants,

International Insurance Company of Hannover, Ltd.,
Appellant,

Cincinnati Insurance Companies,
Respondent.

Filed December 21, 2010
Affirmed in part, reversed in part, and remanded
Ross, Judge

Stearns County District Court
File No. 73-CV-07-1885

Thomas G. Jovanovich, Matthew W. Moehrle, Rajkowski Hansmeier, Ltd., St. Cloud, Minnesota (for respondent Sand Companies, Inc.)

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Considered and decided by Minge, Presiding Judge; Toussaint, Judge; and Ross, Judge.

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

ROSS, Judge

This insurance coverage appeal arises from judgments in a successful declaratory judgment action brought by Sand Companies, Inc. (SCI) to establish that one or both of its two insurers were required to indemnify it for costs it incurred while retrofitting a faulty garage sprinkler system. Because we hold that the district court erred by failing to distinguish between the known-injury-or-damage provision in International Insurance Company of Hannover, Ltd.'s policy and the known-loss doctrine, we reverse and remand in part. We affirm the district court judgments on all other issues. On remand, the district court should determine which insurer must indemnify SCI depending on whether Hannover's known-injury-or-damage provision precludes coverage.

FACTS

Gorham Housing Partners hired SCI in 2001 to be the general contractor for its Heritage Park Estates apartment project. SCI subcontracted with Superior Fire to install the apartment's garage sprinkler system. The subcontract required Superior Fire to obtain various kinds of insurance, including general-aggregate and products-completed insurance and to name SCI as an "additional insured" under the policy. At the time it signed the subcontract, Superior Fire was insured by United National under a Commercial General Liability (CGL) insurance policy. But a year later, its United National policy expired and it obtained a replacement CGL policy issued by Hannover. This policy lasted for less than a year, and in August of 2003 it was cancelled for non-

payment of premium. That summer, Superior Fire completed its work on the sprinkler system, and by fall, Heritage Park Estates was substantially complete.

Winter brought pipe breaks. On December 13, 2003, a garage sprinkler pipe froze and burst. The pipe was repaired. On December 18, Ted Lindberg of SCI sent a letter to Greg Schell of Superior Fire expressing his concern that cold weather would lead to more breaks and asking Superior Fire to participate in any repair costs. On January 6, 2004, Hannover issued a new CGL policy to Superior Fire. Two weeks later, on January 20, sprinkler pipes located in the first floor atrium broke, but did not cause other damage. The pipes were repaired. Two days later an elbow pipe located in a third-floor apartment broke, damaging the apartment. In February, a fire protection specialist issued SCI a report listing areas of concern and concluding that "modifications to the design and installation of the sprinkler systems are necessary to bring this installation to minimum code compliance." The following spring, SCI performed and financed a retrofit of the sprinkler system.

Autumn brought litigation. Gorham sued SCI and Superior Fire seeking recovery for out-of-pocket expenses and consequential damages resulting from defective design, construction, and installation of the sprinkler system. In April 2008, a jury made findings on, among other things, liability for the breaks and costs of the repairs. Posttrial motions were argued and pending when SCI commenced a declaratory judgment action, out of which this appeal arose. SCI asked the district court to declare whether Hannover, or its own insurer, Cincinnati, had a duty to indemnify it for expenses from its retrofitting the sprinkler system. All parties in the declaratory judgment action moved for summary

judgment. In the meantime, the district court ruled on Gorham's pending motion for judgment as a matter of law in its lawsuit against SCI. It issued an order for judgment finding Superior 100% negligent for the pipe breaks of December 2003 and January 2004 but not for additional pipe breaks on December 2004 or January 2005.

The district court later ruled on the cross-motions for summary judgment in SCI's declaratory judgment action. It granted summary judgment in favor of SCI and denied summary judgment for Hannover and Cincinnati.

The district court held that SCI is entitled to indemnification for its costs by at least one of its insurers. Specifically, it held as follows:

- SCI was obligated by its contract with Gorham to repair the sprinkler system.
- SCI was an "additional insured" under Hannover's policy.
- Hannover's policy was in effect at the time of some of the occurrences.
- SCI was also insured under Cincinnati's policy.
- SCI's repairs and retrofits are damages because of "property damage" as defined in both Hannover and Cincinnati's policies.
- The pipe breaks were "occurrences" as defined in both the Hannover and Cincinnati policies.
- Exclusions (*l*), (m), and (n) do not bar coverage under either policy.
- Cincinnati's policy was secondary to Hannover's, which was primary.

The district court also concluded that fact issues remained regarding whether the known-loss doctrine would exclude coverage and whether SCI obtained the necessary consent from Hannover to do the retrofit work.

The district court entered its findings of fact, conclusions of law, and order for judgment in the Gorham-SCI-Superior Fire trial. In relevant part, the court found that Superior Fire was responsible for the December 2003 pipe break, that no party was responsible for the December 2004 and January 2005 pipe breaks, and that Gorham was responsible for the January 22, 2004, pipe break. It also held that $314,629.17 would compensate SCI for the reasonable cost of repair work of the garages.

The district court then held a trial on remaining fact issues in SCI's declaratory judgment action. Three witnesses testified: Greg Miller, president of Superior Fire, Leo Sand, chairman of SCI, and Ted Lindberg, SCI's project manager for the Heritage Park project. On November 19, 2009, the district court determined that the known-loss doctrine did not bar coverage under Hannover's policy and that the consent provisions in Hannover's policy also did not bar coverage.

Hannover and Cincinnati both appeal from summary judgment and the posttrial judgment in the declaratory judgment action.

D E C I S I O N

Hannover and Cincinnati both appeal from the summary judgment order and the final judgment. Generally, any challenge to the denial of a summary judgment motion based on the existence of factual issues becomes moot once the jury reaches a verdict on that factual issue. *Bahr v. Boise Cascade Corp.*, 766 N.W.2d 910, 918 (Minn. 2009).

But we have recently clarified that when the denial of summary judgment is based on a question of law, the denial can be reviewed in an appeal from the judgment. *Schmitz v. Rinke*, 783 N.W.2d 733, 744 (Minn. App. 2010), *review denied* (Minn. Sept. 21, 2010).

We apply the following standard of review to all of the issues raised in this appeal. With respect to the legal issues resolved at summary judgment, we review de novo "whether there are any genuine issues of material fact and whether the district court erred in applying the law." *Wanzek Constr., Inc. v. Employers Ins. of Wausau*, 679 N.W.2d 322, 324 (Minn. 2004). With respect to our review of the declaratory judgment, we apply a clearly erroneous standard as to factual findings and review the district court's legal conclusions de novo. *Onvoy, Inc. v. ALLETE, inc.*, 736 N.W.2d 611, 615 (Minn. 2007). We review de novo the interpretation of particular provisions of the insurance policies and their application to the facts. *Franklin v. W. Nat'l Mut. Ins. Co*., 574 N.W.2d 405, 406 (Minn. 1998). And in doing so, "words are to be given their natural and ordinary meaning and any ambiguity regarding coverage is construed in favor of the insured." *Am. Family Ins. Co. v. Walser*, 628 N.W.2d 605, 609 (Minn. 2001).

I

We first address whether SCI is an additional insured under Superior Fire's insurance policy with Hannover. The "additional insured" provision in the contract between Hannover and Superior Fire provides that the policy "is amended to include as an insured any person or organization . . . to whom [Superior Fire is] obligated by valid written contract to provide such coverage."

Hannover claims that it is required to insure SCI only while Superior Fire's work was in progress but not after it was completed. It rests its argument on *Seward Housing*, in which the supreme court held that the insurer of a subcontractor was required to include the contractor as an additional insured only while the subcontractor's work was in progress. *Seward Housing Corp. v. Conroy Bros. Co.*, 573 N.W.2d 364 (Minn. 1998). But *Seward* is not on point. The subcontractor there was required to purchase only general liability insurance, not completed-operations coverage. *Id.* at 367. Here, Superior Fire was obligated by contract to provide insurance for SCI after the work was completed. Paragraph seven of its subcontract with SCI specifically required Superior Fire to obtain both general liability insurance and completed-operations insurance. Based on the plain meaning of these two relevant contract provisions, we hold that SCI was an additional insured under Superior Fire's policy with Hannover.

II

We next address whether SCI's costs to retrofit the sprinkler system are covered under the insurance policies. Both Hannover and Cincinnati claim that the retrofit does not address "damages" that were the result of an "occurrence" covered under their respective policies. We first address Hannover's arguments.

Hannover's policy states that the insurance "applies to . . . 'property damage' only if: (1) the . . . 'property damage' is caused by an 'occurrence' that takes place in the 'coverage territory'; and (2) the . . . 'property damage' occurs during the policy period. Hannover claims that all damages stemmed from either the December 13, 2003, pipe

break or the faulty pipe design, both of which occurred before the inception of its policy, and it maintains that the January pipe breaks were not occurrences.

We first address whether the January pipe breaks were occurrences. The policy defines "occurrence" as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." "Accident" is not defined in the policy, but has been held to mean "an unexpected, unforeseen, or undesigned happening or consequence from either a known or unknown cause." *Hauenstein v. St. Paul-Mercury Indem. Co.*, 242 Minn. 354, 358–59, 65 N.W.2d 122, 126 (1954).

The district court found that "based on the testimony of all three witnesses, none of the parties knew until after the January 2004 pipe breaks that the pipe bursts would continue to occur until repaired." Based on this finding, we hold that the January pipe breaks were accidents, and therefore, occurrences; they were unexpected, unforeseen, and undesigned happenings or consequences from another cause.

We next address whether Hannover's policy covers damages stemming from multiple occurrences, at least one of which occurred before the start of the policy. Minnesota law follows the "actual injury rule" such that a "liability policy is 'triggered' if the complaining party . . . is actually damaged during the policy period, regardless of when the underlying negligent act occurred" and that "an insurer is on the risk . . . if, during the period of one of its policies, there is property damage." *Wooddale Builders v. Maryland Cas. Co.*, 722 N.W.2d 283, 292 (Minn. 2006). And "[t]his is true even though an excluded cause may have also contributed to the loss." *Henning Nelson Constr. Co. v. Fireman's Fund Am. Life Ins. Co.*, 383 N.W.2d 645, 653 (Minn. 1986). The supreme

court has concluded that "there is no reason for the insured's coverage, or the insurers' obligations, to be diminished simply because the damages arise from a series of events rather than a single discrete occurrence." *Wooddale*, 722 N.W.2d at 296.

It is undisputed that the pipes broke several times and that some of the breaks occurred in January, while Hannover's policy was in effect. It is also undisputed that at least one of the January pipe breaks damaged the building. Following *Wooddale*, as long as one or more occurrences leading to the retrofit occurred during Hannover's policy period, Hannover is liable.

We turn to Cincinnati's arguments. Cincinnati argues that the retrofit does not address "property damage" that was the result of an "occurrence" under its policy, but for different reasons. First, it claims that it is not required to indemnify SCI for the cost to retrofit the sprinkler system because the faulty system is not "property damage." Second, it argues that at the time the retrofit was made, there was no "occurrence" because the pipes that had broken were already fixed.

With regard to Cincinnati's first argument, the supreme court has defined "damages because of property damage" to include "damages which are causally related to an item of 'property damage.'" *Federated Mut. Ins. Co. v. Concrete Units, Inc.*, 363 N.W.2d 751, 757 (Minn. 1985). And Cincinnati's policy defines property damage in part, as "[p]hysical injury to tangible property." There is no dispute that the pipe breaks caused physical injury to tangible property. They damaged the building and the pipes themselves. The breaks therefore constitute property damage. And the district court found that the retrofit was "causally related" to the damage from the pipe breaks. We are

not convinced by Cincinnati's contention made during its oral argument that "the costs to retrofit the system are related to the fact that it was defectively designed and installed in the first instance" and not related to the pipe breaks, because the causal connection between the pipe burst and the retrofit was a factual finding, and we will not disturb factual findings absent clear error. *Onvoy, Inc.*, 736 N.W.2d at 615. We hold that the damages, which the district court held were causally related to an item of property damage, are "damages because of property damages" under Cincinnati's policy.

The supreme court's holding in *Federated Mutual* is instructive. The supreme court there held that the damages caused by defective concrete were property damage. 363 N.W.2d at 756–57. The court did not directly discuss the issue of whether the damaged concrete itself was "property damage," but because it held that an exclusion for property damage excluded coverage of the costs of the concrete, the court must have assumed the concrete was property damage. *Id.* at 755–57 (citing to exclusion (n), which excludes "*property damage* to the named insured's products" (emphasis added)).

Cincinnati's reliance on *Thermex v. Fireman's Fund Ins. Cos.*, 393 N.W.2d 15 (Minn. App. 1986) is misplaced. In *Thermex*, we stated that "replacement costs related to defective work and materials, does not fit within the policy definition of property damage." 393 N.W.2d at 17. But we specifically noted that the complaint "does not allege that Thermex's faulty workmanship caused any physical damage to the building," *id.*, and that therefore, "this case is distinguishable from cases in which an insurer was held obligated to defend its insured for faulty workmanship which caused physical damage." *Id.* *Thermex* does not control because here, there is no allegation that the

sprinkler system was a result of defective work or materials; it was a design defect and accident, and the sprinklers in this case did cause physical damage to the property when the pipes broke. This case fits squarely within the line of cases from which *Thermex* was distinguished.

We now turn to Cincinnati's other argument—that the damages were not the result of an "occurrence" because the sprinkler system was restored to operation. Cincinnati relies on *Bright Wood Corp. v. Bankers Standard Ins. Co*., 665 N.W.2d 544, 549 (Minn. App. 2003), *review denied* (Minn. Sept. 24, 2003), for the proposition that damage "because of repairs deliberately undertaken" is not an occurrence. Contrary to Cincinnati's characterization, the *Bright Wood* court never held that there was no occurrence. The damages at issue in *Bright Wood* were the costs of replacing a particular component in its windows that was not up to specifications. *Id.* at 548. The installation of a faulty window component *was* an occurrence, which necessitated its replacement. *Id*. The court denied coverage not because there was no occurrence but because of an exclusion. *Id*. Cincinnati misreads the *Bright Wood* court's statement that "[t]he resulting damage is not an accidental occurrence." *Id.* at 549. This statement refers to the "incidental damage to the finish, hardware, and weather-stripping" that was incurred when replacing the portion of the window that was defective. *Id.* at 548. The incidental damage to other parts of the window (that were damaged only because of the window replacement—the cost of which was excluded by the "your work exclusion") was not covered because the replacement was not an occurrence. *Id*. at 549.

Bright Wood adds only that incidental damages caused by the retrofit here would not qualify as damages arising out of an occurrence because the retrofit is not an occurrence. But all costs related to the retrofit arise out of the separate occurrence of the pipe break. It is therefore unnecessary to decide whether the retrofit itself is an occurrence. Cincinnati offers no other reason to disregard the district court's finding that the pipe bursts were "occurrences" as defined by the policy.

III

We turn to whether the CGL policies require the insurers to indemnify SCI without a judicial finding of liability. Hannover and Cincinnati claim that SCI was never legally obligated to pay for the retrofit because the trial court did not find Superior Fire or SCI at fault for the January 2004 pipe breaks. Hannover offers no caselaw to support its position. Cincinnati relies on *St. Paul Fire and Marine Ins. Co. v. A.P.I., Inc*., 738 N.W.2d 401, 409 (Minn. App. 2007), *review denied* (Minn. Dec. 11, 2007), for the broad proposition that "[a] duty to indemnify arises when the insured is legally obligated to pay damages as a result of a judgment or settlement." But *St. Paul Fire* is a statute-of-limitations case. *Id*. We merely held that the statute of limitations begins when the judgment is entered. *Id*. We did not declare that a judicial finding of liability is required to trigger the CGL policy.

The district court held that the contract between SCI and Gorham created a legal obligation to pay because the contract stated, "the Contractor shall be responsible to the Owner for acts and omissions of the Contractor's . . . subcontractors and their agents and employees." The district court's holding is supported by the plain language of the

insurance policy, which merely states the term, "legal obligation." *See Am. Family Ins. Co.*, 628 N.W.2d at 609 ("When interpreting an insurance contract, words are to be given their natural and ordinary meaning and any ambiguity regarding coverage is construed in favor of the insured."); *cf. Waznek*, 679 N.W.2d at 324 (stating that Wanzek was "forced" by its contract with the city to replace stones for a swimming pool after its subcontractor filed for bankruptcy).

IV

Because we have concluded that the costs to retrofit the sprinkler system are covered under both policies, we now address whether any of the exclusions in Hannover's policy are applicable. Hannover claims that the so-called "business-risk" exclusions, which are exclusions (*l*), (m), and (n), bar coverage. It also urges us to read these exclusions such that "your work" refers to Superior Fire's work. We agree with this interpretation because "your" is defined in the contract as the named insured, and Superior Fire is the named insured.

Taken together, these exclusions purportedly prevent coverage for property damage to, arising out of a defect in, or costs to repair or replace any of Superior Fire's work. But because an overriding, coverage-granting, additional-insured endorsement that specifically provides for coverage for SCI "with respect to liability for . . . 'property damage' arising solely out of [Superior Fire's work]" also applies, and this coverage-granting provision explicitly "modifies" the insurance provided, we hold that the business-risk exclusions do not apply.

We therefore do not discuss the other bases on which we might reach the same conclusion.

V

We next address whether the district court erred by interpreting Hannover's known-injury-or-damage provision under the known-loss doctrine. In relevant part, the known-injury-or-damage provision states that the "insurance applies to . . . 'property damage' only if . . . [p]rior to the policy period, no insured . . . knew that . . . 'property damage' had occurred, in whole or in part." Hannover claims that the parties were aware of the damage after the first pipe burst and that, therefore, this exclusion precludes coverage.

In its order denying summary judgment, the district court held that whether the parties knew the pipe bursts would continue until repaired was a material fact issue. At trial, the district court considered the December 18 letter sent from SCI to Superior Fire advising that future cold weather will bring additional line breaks and water damage, and it received the conflicting testimony of three witnesses. It found that "based on the testimony of [the] witnesses, none of the parties knew until after the January 2004 pipe breaks that the pipe bursts would continue to occur until repaired. Therefore, *the known loss doctrine* does not apply to bar Hannover's coverage." (Emphasis added.)

We hold that the district court erred by construing the known-injury-or-damage provision as if it were incorporating the known-loss doctrine. The known-loss doctrine is a common law concept based on the idea that insurance cannot be issued for a loss in which there is no longer any risk. *Waseca Mut. Ins. Co. v. Noska*, 331 N.W.2d 917, 924–

25 n. 6 (Minn. 1983). The supreme court has said that "where the loss has occurred prior to the application for insurance, the relevant question is . . . whether the parties, particularly the insured, knew of the loss at the time of application, since the knowledge would be nearly conclusive evidence as to bad faith." *Id.* It is therefore a fraud-based defense. *Domtar, Inc. v. Niagra Fire Ins. Co.*, 563 N.W.2d 724, 737 (Minn. 1997). But the issue in this case was not whether a fraud prevents coverage; it was whether a particular provision in the contract barred coverage.

Our holding is consistent with *Wooddale*, where the supreme court, in trying to determine which insurers were liable, interpreted the plain language of some of the insurers' policies and determined that "the terms of the policies at issue prevent an insurer from becoming liable for damages to a home during the insurer's policy period, if the property damage was 'expected' from Wooddale's standpoint before the policy period began." 722 N.W.2d at 292. The court then discussed how its determination is "supported by the rationale behind the known loss doctrine." *Id.* But although it was "supported" by the rationale behind the known-loss doctrine, the court did not construe the provision in accordance to the known-loss doctrine. *Id.* It construed it according to its own *terms*. *Id.*

Our holding is also consistent with a recent Southern District of New York decision construing an identical known-injury-or-damage provision, *Travelers Cas. & Surety Co. v. Dormitory Auth.-State of New York*, ___ F. Supp. 2d ___, 2010 WL 3001729 (S.D.N.Y. 2010). In *Travelers*, the court stated:

> [T]he known-loss doctrine is a 'common law concept' that courts read into insurance policies in order to prevent an insured from recovering for loss or damage that the insured already knew about at the time it procured insurance. The doctrine reflects, in essence, a public policy judgment that a party should not be able to purchase insurance to cover losses that one has already incurred. The known-loss doctrine applies in the *absence* of a known-injury-or-damage provision in the contract itself.

Id. at *10. We find *Travelers* to be persuasive. Because the district court did not determine whether the known-injury-or-damage provision, as written, bars coverage, we remand that issue to the district court.

Affirmed in part, reversed in part, and remanded.