IN THE UNITED STATES DISTRICT COURT

FOR THE WESTERN DISTRICT OF WISCONSIN

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U.S. PLASTIC LUMBER, LTD. and
THE EAGLEBROOK GROUP, INC.,

Plaintiffs,

OPINION AND ORDER

02-C-211-C

v.

STRANDEX CORPORATION,

Defendant.

CINCINNATI INSURANCE COMPANY,

Intervening Plaintiff,

v.

STRANDEX CORPORATION,
U.S. PLASTIC LUMBER, LTD., and
THE EAGLEBROOK GROUP, INC.,

Defendants in Intervention.

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This is a civil action for monetary relief in which plaintiffs U.S. Plastic Lumber, Ltd. and The Eaglebrook Group, Inc. seek damages for the alleged breach of their licensing agreement with defendant Strandex Corporation. The dispute arises out of problems that plaintiffs experienced with defendant's formula and process for making a wood fiber and

plastic composite building material that plaintiffs used to manufacture outdoor decks. Jurisdiction is present. 28 U.S.C. § 1332(a)(1).

In an opinion and order dated February 7, 2003, I granted defendant's motion for summary judgment on plaintiffs' claims that defendant breached the license agreement's warranty regarding the performance properties of the licensed process and an implied duty of good faith and fair dealing. However, I concluded that a jury must decide plaintiffs' claim that defendant breached the license agreement's know-how disclosure provision. The case is presently before the court on intervening plaintiff Cincinnati Insurance Company's motions for summary judgment and to stay the underlying proceedings until the summary judgment motion can be decided. In its summary judgment motion, intervenor seeks a declaration that two insurance policies it issued to defendant do not obligate it to defend or indemnify defendant against any of the claims asserted in plaintiffs' amended complaint. I conclude that the policies at issue do not cover the claims asserted in plaintiffs' amended complaint, because plaintiffs seek only to recover economic losses resulting from alleged breaches of the license agreement. Therefore, I will grant intervenor's motion for summary judgment. Because intervenor has prevailed on its motion for summary judgment, I will deny its motion for a stay as moot.

I find from the parties' proposed findings of fact that the following facts are material and undisputed.

UNDISPUTED FACTS

Defendant Strandex Corporation is a Wisconsin corporation with its principal place of business in Wisconsin. Intervening plaintiff Cincinnati Insurance Company is an Ohio corporation with its principal place of business in Ohio.

Intervenor issued a commercial general liability policy to defendant, effective from June 10, 1998 to June 10, 2001, with liability limits of $1 million for each occurrence. The commercial general liability policy specifies that, subject to all other policy provisions and exclusions, intervenor "will pay those sums that the insured becomes legally obligated to pay as damages because of 'bodily injury' or 'property damage' to which this insurance applies." The policy provides that intervenor has "the right and duty to defend any 'suit' seeking those damages." It specifies further that the "insurance applies to 'bodily injury' and 'property damage' only if: (1) the 'bodily injury' or 'property damage' is caused by an 'occurrence' that takes place in the 'coverage territory'; and (2) the 'bodily injury' or 'property damage' occurs during the policy period."

The commercial general liability policy defines the term "property damage" as "a. Physical injury to tangible property, including all resulting loss of use of that property. All such loss of use shall be deemed to occur at the time of the physical injury that caused it; or b. Loss of use of tangible property that is not physically injured. All such loss of use shall be deemed to occur at the time of the 'occurrence' that caused it." The term "occurrence"

is defined by the policy as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions."

Intervenor issued a commercial umbrella liability policy to defendant, effective from June 10, 1998 to June 10, 2001, with liability limits of $10 million for each occurrence and a $10 million aggregate limit.

OPINION

Defendant and intervenor agree that no material questions of fact are in dispute and that it is appropriate to resolve on summary judgment the legal question whether intervenor has a duty under the terms of the commercial general and umbrella liability policies to provide defendant with a defense against plaintiffs' claims. In addition, the parties agree that the commercial general liability policy and the umbrella policy are materially indistinguishable on the question of the existence of a duty to defend. Therefore, if intervenor has no duty to defend defendant under the terms of the commercial general liability policy, it has no duty to do so under the umbrella policy either. Moreover, defendant acknowledges that because the duty to defend is broader than the duty to indemnify, see Elliott v. Donahue, 169 Wis. 2d 310, 320-21, 485 N.W.2d 403, 407 (1992), a determination that intervenor has no duty to defend compels the conclusion that it has no indemnification obligation. Finally, the parties agree that Wisconsin law governs the resolution of this

dispute.

In Wisconsin, an insurer's "duty to defend exists when it is merely arguable that the policy in question provides coverage." Red Arrow Products Company, Inc. v. Employers Insurance of Wausau, 233 Wis. 2d 114, 124, 607 N.W.2d 294, 298 (Ct. App. 2000). In other words, an "insurer has a duty to defend if the existence of coverage is fairly debatable." Id. The existence of a duty to defend is determined by reference to the language of the insurance policy and the allegations in the plaintiff's complaint. "An insurer has a duty to defend its insured if the complaint alleges facts that, if proven, would give rise to liability under the policy." Atlantic Mutual Insurance Co. v. Badger Medical Supply Co., 191 Wis. 2d 229, 236, 528 N.W.2d 486, 489 (Ct. App. 1995). "[T]he allegations in the complaint must state a claim or cause of action for the liability insured against; otherwise there is no duty to defend." Id. at 242, 528 N.W.2d at 491. Any doubt about the duty to defend is resolved in the insured's favor. Shorewood School Dist. v. Wausau Insurance Cos., 170 Wis. 2d 347, 364, 488 N.W.2d 82, 87 (1992).

The parties agree that their dispute hinges on the commercial general liability policy's property damage provision, rather than the provision covering bodily injury. Under the terms of the policy, intervenor must "pay those sums that the insured becomes legally obligated to pay as damages because of . . . 'property damage,'" but only if the "'property damage' is caused by an 'occurrence.'" "Property damage" is defined in relevant part as "[p]hysical

injury to tangible property." An "occurrence" is "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." Therefore, the relevant question is whether plaintiffs' amended complaint states a cause of action for physical injury to tangible property resulting from an accident. Defendant argues that the amended complaint does just that, because in it plaintiffs allege that materials made using defendant's licensed process "expanded, cracked, warped and otherwise deteriorated," causing plaintiffs to pay out significant sums to resolve warranty claims from their customers who used decking materials manufactured by plaintiffs using the licensed process and whose decks failed. See Am. Compl. at ¶ 17. Therefore, defendant argues it is entitled to coverage because it may ultimately be held liable for accidental, that is, unintentional, physical injury to tangible property.

Defendant's argument is foreclosed by the Wisconsin Supreme Court's decision in Wausau Tile, Inc. v. County Concrete Corp., 226 Wis. 2d 235, 593 N.W.2d 445 (1999), a case strikingly similar to this one. In that case, the plaintiff was a manufacturer of concrete paving blocks for sidewalks. It had contracted with the defendant to provide the cement for the blocks. The plaintiff sued the defendant for breach of contract and negligence because it alleged that the blocks it had installed for its customers had suffered "excessive expansion, deflecting, curling, cracking and/or buckling" as a result of problems with defendant's cement formula. Among other things, the plaintiff alleged that the cracked blocks caused it to incur

substantial expenses in resolving its customers' warranty claims. Id. at 241-43, 593 N.W.2d at 449-50. The court concluded first that the damages the plaintiff sought in compensation for the warranty claims it was forced to pay were purely economic losses that could not be recovered under a tort theory such as negligence. Id. at 252-53, 593 N.W.2d at 454. The defendant's insurance company then sought a declaration that it had no duty to defend its insured against the plaintiff's remaining breach of contract claims. The court examined the language of the applicable insurance policy, which is identical in all material respects to the language of the insurance policy at issue in this case. Id. at 267-68, 593 N.W.2d at 459-60 & n.18 (noting that policy applied to "property damage," defined as physical injury to tangible property, arising out of an "occurrence," defined as an accident). The court concluded that the term "'property damage' under the plain language of the policy" did not cover the economic losses plaintiff was seeking to recover under its breach of contract theory, including the funds it had expended to resolve its customers' warranty claims. Id. The court noted also that it was undisputed that "breach of a contract or warranty is not a covered 'occurrence' under the [insurance company's] policy." Id. at 269, 593 N.W.2d at 460.

This case is on all fours with Wausau Tile. Economic loss is "the loss in a product's value which occurs because the product 'is inferior in quality and does not work for the general purpose for which it was manufactured and sold.'" Id. at 246, 593 N.W.2d at 451 (citation omitted). As in Wausau Tile, there can be little doubt that economic losses are

what is at stake in this case. Plaintiffs allege in their amended complaint that materials made with the defendant's process and formula were of inferior quality and not suitable for the purpose of building outdoor decks. On the basis of these allegations, plaintiffs asserted claims for breach of two of the license agreement's express provisions and for breach of the implied duty of good faith that Wisconsin law reads into every contract. Specifically, plaintiffs maintain that much like the paving blocks in Wausau Tile, the decking materials made with defendant's formula expanded, cracked and warped. Like the plaintiff in Wausau Tile, plaintiffs seek to recoup the money they paid to their customers to resolve warranty claims resulting from defendant's alleged breach of contract. It should come as little surprise, then, that the standard commercial general liability policy at issue in this case does not obligate intervenor to defend such a claim. The Wisconsin Supreme Court determined explicitly in Wausau Tile that the specific policy language upon which defendant relies does not give rise to a duty to defend a breach of contract claim seeking purely economic losses to compensate for the cost of resolving the warranty claims of third parties. Id. at 267-68, 593 N.W.2d at 460.

The state court underscored this conclusion subsequently in Wisconsin Label Corp. v. Northbrook Prop. & Cas. Ins. Co., 233 Wis. 2d 314, 607 N.W.2d 276 (2000). It noted that commercial general liability policies are intended to insure against

> the possibility that the goods, products or work of the insured, once relinquished or

> completed, will cause bodily injury or damage to property other than to the product or completed work itself, and for which the insured may be found liable. The insured, as a source of goods or services, may be liable as a matter of contract law to make good on products or work which is defective or otherwise unsuitable because it is lacking in some capacity. This may even extend to an obligation to completely replace or rebuild the deficient product or work. This liability, however, is not what the coverages in question are designed to protect against. The coverage is for tort liability for physical damages to others and not for contractual liability of the insured for economic loss . . . .

Id. at 330, 607 N.W.2d at 283 (citations omitted); see also Jacob v. Russo Builders, 224 Wis. 2d 436, 448, 592 N.W.2d 271, 276 (Ct. App. 1999). In determining whether a duty to defend exists, "it is the nature of the claim alleged against the insured that is controlling." Shorewood, 170 Wis. 2d at 364, 488 N.W.2d at 87. The amended complaint makes clear that the claims at issue in this case sound in contract and seek damages for economic loss. "A CGL policy is not a performance bond; it provides coverage 'for tort damages but not for economic loss resulting from contractual liability.'" Wisconsin Label, 233 Wis. 2d 314, 343, 607 N.W.2d at 289 (citation omitted). Defendant notes the court's observation in Wisconsin Label that "as a general proposition, CGL policies may sometimes cover economic losses." Id. at 342, 607 N.W.2d at 289. However, the court went on to note that this would be true "only when the policy language creates coverage for such losses." Id. In Wausau Tile, 226 Wis. 2d at 267-68, 593 N.W.2d at 460, the court held that the specific policy language at issue in this case does not create such coverage. Accordingly, I conclude that intervenor has no duty to provide defendant with a defense against plaintiffs' claims. Because

intervenor has no duty to defend, it has no obligation to indemnify defendant for any liability it may incur. See Elliott, 169 Wis. 2d at 320-21, 485 N.W.2d at 407. Because intervenor has prevailed on its summary judgment motion, its motion to stay will be denied as moot.

ORDER

IT IS ORDERED that intervening plaintiff Cincinnati Insurance Company's motion for summary judgment is GRANTED and it is DECLARED that intervenor has no duty to defend defendant Strandex Corporation against the claims in plaintiffs U.S. Plastic Lumber, Ltd.'s and The Eaglebrook Group, Inc.'s amended complaint in this case and has no duty to indemnify defendant for any liability arising from those claims. Intervenor's motion for a stay of the underlying proceedings is DENIED as moot.

Entered this 19th day of February, 2003.

BY THE COURT:

BARBARA B. CRABB
District Judge