COURT OF APPEALS
DECISION
DATED AND FILED

May 2, 2017

Diane M. Fremgen
Clerk of Court of Appeals

NOTICE

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A party may file with the Supreme Court a petition to review an adverse decision by the Court of Appeals. *See* WIS. STAT. § 808.10 and RULE 809.62.

Appeal No. 2016AP1343 **Cir. Ct. No. 2014CV1661**

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

COUNTRY WORLD MEDIA GROUP, INC.,

PLAINTIFF,

V.

ERIE INSURANCE COMPANY,

DEFENDANT-RESPONDENT,

COUNTRY WORLD PRODUCTIONS, INC.,

DEFENDANT-APPELLANT,

BEST BUILT, INC., CRAIG A. KASSNER, ACUITY, A MUTUAL INSURANCE COMPANY, VHC, INC. AND VALLEY FORGE INSURANCE COMPANY,

DEFENDANTS.

APPEAL from a judgment of the circuit court for Brown County: KENDALL M. KELLEY, Judge. *Reversed and cause remanded with directions*.

Before Stark, P.J., Hruz and Seidl, JJ.

¶1 STARK, P.J. Country World Productions, Inc., (CWP) appeals a judgment dismissing its insurer, Erie Insurance Company, from this case. The circuit court determined Erie's insurance policy did not cover claims made against CWP by Country World Media Group, Inc., (Media) because the property that Media's complaint alleged was damaged—specifically, "television shows, master copies and field footage"—constituted electronic data and was therefore excluded from the policy's definition of property damage. The court therefore concluded Erie had no duty to defend CWP.

¶2 We conclude Media's complaint arguably alleged damage to both tangible, physical property—that is, the videotapes on which the television shows, master copies, and field footage were recorded—and the intangible electronic data stored on those tapes. Because Erie's policy covers claims for damage to tangible property, Erie had a duty to defend CWP against all of the allegations in Media's complaint. It is undisputed that, if Erie had a duty to defend CWP, it breached that duty by refusing to provide a defense. We therefore reverse the judgment dismissing Erie from this case. We remand for the circuit court to enter a declaratory judgment in CWP's favor on the duty-to-defend issue and to determine the damages CWP is entitled to recover as a result of Erie's breach.

BACKGROUND

¶3 The following facts are taken from Media's complaint and are accepted as true for purposes of this appeal. VHC, Inc., owned premises on

Lawrence Drive in De Pere, Wisconsin. In October 1998, CWP, which was then owned by Timothy Manion, contracted with VHC to lease an office suite (Space #1) in the Lawrence Drive premises. In April 2006, CWP contracted with VHC to lease a larger office suite in the same premises (Space #2).

¶4 On April 14, 2006, CWP moved its operations from Space #1 to Space #2. However, Best Built, Inc., VHC's lease manager for the premises, agreed to allow CWP to use Space #1 for storage until that space was rented by another tenant. From 2007 through 2011, CWP stored "several boxes of television tapes, VHS copies and books" in Space #1.

¶5 In August 2011, Manion sold CWP to a private equity group. Manion remained on CWP's board of directors, acted as a consultant for CWP, and maintained an office in Space #2. The sale of CWP did not include its "television production shows or publishing division." Instead, the "television production and publishing assets were retained by [Media]," which is owned by Manion.

¶6 Following the sale, CWP allowed Media to store items, "including but not limited to television show tapes, cookbooks and videos," in Space #2. In September 2011, CWP employees moved a box of cookbooks and videos to a closet in Space #1. Media continued to store other items, "including television shows, master copies and field footage," at CWP's office in Space #2. In September 2013, CWP employees moved most of Media's remaining property from Space #2 into a closet in Space #1.[1] Manion was not informed the property

[1] At oral argument in the circuit court, Media's counsel described the property that was moved to Space #1 as "eight to nine large boxes" containing "videos" or "TV production series" with a value of "about a million dollars."

was being moved from Space #2 to Space #1 and did not give permission for the move. In January 2014, Manion discovered that the closet in Space #1 was empty, except for a box of cookbooks and videos. He contacted Craig Kassner, the owner of Best Built, who admitted he had ordered Best Built employees to discard the property that had been stored in Space #1 in a dumpster.

¶7 Media filed the instant lawsuit in November 2014, naming as defendants CWP, Best Built, Kassner, VHC, and their respective insurers. The complaint alleged claims for breach of contract and negligence against CWP. The complaint further alleged that, as a result of CWP's conduct, Media had "sustained damages equal to the value of the Property which will be determined at the time of trial."[2]

¶8 During the relevant time period, CWP had a commercial general liability (CGL) insurance policy through Erie. On December 18, 2014, one day after it was served with Media's summons and complaint, CWP informed Erie of Media's lawsuit and asked Erie to provide CWP with a defense. During a December 29, 2014 phone call, an Erie representative informed CWP it would not provide coverage for Media's claims and CWP could hire its own lawyer to defend against the claims at its own expense. The following day, Erie sent CWP an email confirming that Erie "would not answer the lawsuit on behalf of [CWP] or provide a defense."

¶9 Erie answered Media's complaint on its own behalf on January 2, 2015, and asserted a "cross-claim/counterclaim for declaratory judgment against

[2] The complaint uses the term "the Property" to refer to the discarded "television shows, master copies and field footage."

all parties," which alleged Erie's policy did not give rise to a duty to defend or indemnify CWP. Erie subsequently moved for declaratory and summary judgment, arguing, among other things, that its policy did not provide coverage for Media's claims against CWP because Media's complaint alleged a loss of "electronic data," which the Erie policy expressly excluded from its definition of the term "property damage." CWP opposed Erie's motion and moved for a declaratory judgment that Erie had a duty to defend CWP and breached that duty by refusing to provide a defense.

¶10 While the coverage dispute between CWP and Erie was being litigated, Media settled with CWP. Accordingly, the circuit court entered an order dismissing Media's claims against CWP on December 23, 2015. On April 27, 2016, the court issued a written decision addressing the coverage issue. The court concluded Erie's policy did not give rise to a duty to defend CWP against Media's claims because the policy "was clearly written to exclude claims for property damage related to electronic data." The court therefore granted Erie's motion for declaratory and summary judgment, denied CWP's motion for declaratory judgment, and dismissed Erie from the case. CWP now appeals.

DISCUSSION

¶11 We independently review a grant of summary judgment, using the same methodology as the circuit court. ***Hardy v. Hoefferle***, 2007 WI App 264, ¶6, 306 Wis. 2d 513, 743 N.W.2d 843. Summary judgment is appropriate if there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. WIS. STAT. § 802.08(2) (2015-16). "Whether to grant a declaratory judgment is addressed to the circuit court's discretion." ***State Farm Fire & Cas. Co. v. Acuity***, 2005 WI App 77, ¶6, 280 Wis. 2d 624, 695 N.W.2d 883. However,

when the exercise of that discretion turns on the interpretation of an insurance policy, which is a question of law, we conduct an independent review. ***Id.***

¶12 Our goal in interpreting an insurance policy is to give effect to the parties' intent. ***American Family Mut. Ins. Co. v. American Girl, Inc.***, 2004 WI 2, ¶23, 268 Wis. 2d 16, 673 N.W.2d 65. We construe a policy as it would be understood by a reasonable person in the position of the insured. ***Id.*** We enforce unambiguous policy language as it is written, but we construe ambiguous policy language against the insurer and in favor of coverage. ***Marnholtz v. Church Mut. Ins. Co.***, 2012 WI App 53, ¶10, 341 Wis. 2d 478, 815 N.W.2d 708. Policy language is ambiguous if it is reasonably susceptible to more than one interpretation. ***Id.***

¶13 Liability insurance policies impose two distinct duties on the insurer: a duty to defend and a duty to indemnify. ***Gross v. Lloyds of London Ins. Co.***, 121 Wis. 2d 78, 84, 358 N.W.2d 266 (1984). In this appeal, only the duty to defend is at issue—CWP argues the circuit court erroneously determined Erie had no duty to defend CWP against Media's claims. CWP further argues Erie breached its duty to defend by refusing to provide a defense for CWP. As a result, CWP contends Erie is liable for both the cost of CWP's settlement with Media and the attorney fees CWP incurred to defend itself against Media's claims. *See* ***Newhouse v. Citizens Sec. Mut. Ins. Co.***, 176 Wis. 2d 824, 837-38, 501 N.W.2d 1 (1993) (A party aggrieved by an insurer's breach of the duty to defend may recover all damages that naturally flow from the breach, including the amount of the judgment or settlement against the insured and the costs and attorney fees the insured incurred in defending the suit.).

¶14 The duty to defend hinges on the nature, not the merits, of the plaintiff's claim. ***Wausau Tile, Inc. v. County Concrete Corp.***, 226 Wis. 2d 235, 266, 593 N.W.2d 445 (1999). It is determined by comparing the allegations in the plaintiff's complaint to the terms of the insurance policy. ***Fireman's Fund Ins. Co. v. Bradley Corp.***, 2003 WI 33, ¶19, 261 Wis. 2d 4, 660 N.W.2d 666. An insurer has a duty to defend its insured if the allegations contained within the four corners of the complaint would, if proved, result in a covered loss. ***Id.***

¶15 "We use a three-step process when comparing the underlying complaint to the terms of the policy in duty to defend cases." ***Water Well Sols. Serv. Grp. v. Consolidated Ins. Co.***, 2016 WI 54, ¶16, 369 Wis. 2d 607, 881 N.W.2d 285. First, we determine whether the policy provides an initial grant of coverage for the allegations set forth in the plaintiff's complaint. ***Id.*** If so, we next consider whether any of the policy's exclusions preclude coverage. ***Id.*** If an exclusion applies, we then consider whether an exception to that exclusion reinstates coverage. ***Id.*** "If coverage is not restored by an exception to an exclusion, then there is no duty to defend." ***Id.*** However, if the policy "provides coverage for at least one of the claims in the underlying suit, the insurer has a duty to defend its insured on all the claims alleged in the entire suit." ***Id.***

¶16 Here, the Erie policy's insuring agreement provides, in relevant part:

> We 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. We will have the right and duty to defend the insured against any "suit" seeking those damages. However, we will have no duty to defend the insured against any "suit" seeking damages for "bodily injury" or "property damage" to which this insurance does not apply.

¶17 The policy defines "property damage" as:

> a. Physical injury to tangible property, including all resulting loss of use of that property …; or
>
> b. Loss of use of tangible property that is not physically injured ….

The definition of property damage then states that, "[f]or the purposes of this insurance, electronic data is not tangible property." The policy further provides that, as used in the definition of "property damage," "electronic data" means

> information, facts or programs stored as or on, created or used on, or transmitted to or from computer software, including systems and applications software, hard or floppy disks, CD-ROMs, tapes, drives, cells, data processing devices or any other media which are used with electronically controlled equipment.

¶18 In summary, the Erie policy provides an initial grant of coverage for "property damage"—that is, physical injury to or loss of use of tangible property, which does not include "electronic data." In addition, the policy contains an exclusion stating its coverage for bodily injury and property damage liability does not apply to "[d]amages arising out of the loss of, loss of use of, damage to, corruption of, inability to access, or inability to manipulate electronic data."[3]

¶19 The parties dispute whether the loss of the content stored on Media's discarded tapes constitutes covered "property damage" under the Erie policy. Erie asserts the "television shows, master copies and field footage" that were stored on the tapes qualify as "electronic data" because the policy's definition of that term "encompasses any and all data that is used with electronically controlled

[3] This exclusion contains a definition of "electronic data" that is identical to the one set forth above. *See supra* ¶17.

equipment." Because the policy specifies that electronic data is not tangible property, Erie argues the loss of the tapes does not satisfy the policy's definition of property damage and coverage for that loss is also barred by the electronic data exclusion.

¶20 Conversely, CWP argues that, correctly interpreted, the policy's definition of "electronic data" includes only data or information that is "stored as or on, created or used on, or transmitted to or from computer software." CWP argues there is no evidence in the record that the content of the lost tapes "had any connection at all with computer software." In the alternative, CWP argues the policy's definition of "electronic data" is ambiguous as to whether a connection with computer software is required. As such, CWP asserts the definition should be construed against Erie and in favor of coverage. *See* ***Marnholtz***, 341 Wis. 2d 478, ¶10. CWP further argues the circuit court impermissibly expanded the electronic data exclusion when it stated the policy was "clearly written to exclude claims for property damage *related to* electronic data." (Emphasis added.)

¶21 Ultimately, we need not resolve the parties' dispute over whether the content of the discarded tapes constitutes electronic data under the Erie policy. Even if we assume, for purposes of this appeal, that the tapes' content does qualify as electronic data, Erie nevertheless had a duty to defend CWP. As noted above, Media's complaint alleged the loss of "television shows, master copies and field footage." The complaint further alleged that the loss was caused by CWP's negligence and breach of an oral contract with Media and that, because of CWP's actions, Media had sustained damages "equal to the value of the Property which will be determined at the time of trial." Construed liberally, these allegations assert an entitlement to damages for both the loss of the intangible data contained on the tapes and the loss of the tapes themselves. *See* ***Water Well Sols.***, 369

Wis. 2d 607, ¶15 (When assessing an insurer's duty to defend, we liberally construe the allegations in the underlying complaint and assume all reasonable inferences from those allegations.). The loss of the physical tapes constitutes property damage, as the policy defines that term, and is therefore covered.[4] Because the Erie policy "provides coverage for at least one of the claims in the underlying suit," Erie had a duty to defend CWP "on all the claims alleged in the entire suit." *See* ***id.***, ¶16.

¶22 Erie argues Media's attorney conceded in the circuit court that Media was seeking damages only for the loss of the ideas and footage contained on the discarded tapes, not for the loss of the tapes themselves. This argument fails for two reasons. First, when assessing an insurer's duty to defend, we may consider only the allegations within the four corners of the plaintiff's complaint and may not consider extrinsic evidence. ***Id.***, ¶15. Statements made in the circuit court by Media's attorney are therefore irrelevant.

¶23 Second, even if we could consider Media's counsel's statements, the record does not support a finding that counsel conceded Media was seeking

[4] Erie does not argue on appeal that the loss of the physical tapes does not constitute covered property damage under the policy. In particular, Erie does not dispute CWP's contention that the tapes are "tangible physical items that have value." *See* ***Charolais Breeding Ranches, Ltd. v. FPC Sec. Corp.***, 90 Wis. 2d 97, 109, 279 N.W.2d 493 (Ct. App. 1979) (unrefuted arguments are deemed conceded). Instead, Erie argues Media did not seek damages for the loss of the physical tapes. We reject that argument, for the reasons explained below. *See infra* ¶¶22-32.

In the circuit court, Erie raised additional arguments in support of its position that its policy did not cover Media's claims against CWP. Specifically, Erie argued Media's negligence claim was barred by the economic loss doctrine and its breach of contract claim did not allege an "occurrence," as the policy defines that term. Erie also argued coverage was barred under the policy's exclusions for expected or intended injury and damage to personal property in the care, custody, or control of the insured. The circuit court rejected these arguments, and Erie does not renew them on appeal as alternative bases to affirm the circuit court's decision.

damages only for the loss of the ideas and footage contained on the discarded tapes. During a hearing on the coverage issue, counsel for VHC's insurer asserted Media had conceded it was "only seeking the value for the actual destroyed tapes" and was not "seeking the economic damages or the ideas." In response, Media's attorney stated:

> I do want to clarify for purposes of this tangible and intangible property argument, I don't want to be—[there] to be some confusion *that all that [Media] is asking for are eight to nine boxes of six dollar videotapes*. That's not what I'm conceding. But what I'm conceding is we're not seeking the value of somebody's thoughts or impressions that gave rise to what went on the videotapes, but we are seeking the value of what's on the videotapes. Not the ideas that went into creating those videotapes. So I don't want later to come back and have there been a record that I'm conceding that the value of these boxes is six dollar videotapes contained in them, so that's not the case.

(Emphasis added.) Contrary to Erie's assertion, these statements do not amount to a concession that Media was only seeking to recover for the loss of the tapes' content. Rather, counsel's statements made clear that Media's alleged losses were not confined to the physical property, which supports a conclusion that Media was seeking damages for *both* the loss of the content and the loss of the physical tapes themselves.

¶24 Erie also cites several cases dealing with the distinction between tangible and intangible property. However, none of these cases convince us that Media's complaint, liberally construed, does not seek damages for the loss of the tangible tapes in addition to their intangible content.

¶25 Erie first cites ***Janesville Data Center, Inc. v. DOR***, 84 Wis. 2d 341, 267 N.W.2d 656 (1978), and ***Bullock v. Statistical Tabulating Corp.***, 549 S.W.2d 166 (Tex. 1977). Both of those cases involved companies that were "engaged in

the business of transferring to keypunch cards and magnetic tapes data furnished by [their] customers which [their] customers wish[ed] to use in computers." ***Janesville Data Ctr.***, 84 Wis. 2d at 342; *see also* ***Bullock***, 549 S.W.2d at 167. The issue in each case was whether the companies' sale of the cards and tapes to their customers constituted the sale of tangible property and was therefore subject to retail sales tax. ***Janesville Data Ctr.***, 84 Wis. 2d at 343; ***Bullock***, 549 S.W.2d at 166. Both courts acknowledged that the cards and tapes were tangible property. ***Janesville Data Ctr.***, 84 Wis. 2d at 346; ***Bullock***, 549 S.W.2d at 169. However, in ***Janesville Data Center***, our supreme court determined the sale of the cards and tapes was not subject to sales tax because the "essence" of the transaction was "the purchase of coded or processed data, an intangible." ***Janesville Data Ctr.***, 84 Wis. 2d at 346. The ***Bullock*** court similarly concluded the "true object" of the transaction was "not the data processing card … but the purchase of coded or processed data, an intangible." ***Bullock***, 549 S.W.2d at 168.

¶26 Based on ***Janesville Data Center*** and ***Bullock***, Erie argues "the essence of Media's claim for property damages is the loss of the ideas and concepts which are intangible property." Loss of the ideas and concepts contained on the tapes is certainly one item for which Media's complaint seeks to recover damages. However, as explained above, when liberally construed, the allegations in Media's complaint also seek to recover for the loss of the physical tapes themselves. Notably, ***Janesville Data Center*** and ***Bullock*** were not duty-to-defend cases, and the courts in those cases were therefore not bound by the four corners rule and the requirement that we liberally construe the allegations in a plaintiff's complaint when determining whether an insurer had a duty to defend its insured. *See* ***Water Well Sols.***, 369 Wis. 2d 607, ¶15. Rather, the ***Janesville Data Center*** and ***Bullock*** courts relied on the principle that "ambiguity and doubt"

about the applicability of a tax must be resolved in favor of the taxpayer. ***Janesville Data Ctr.***, 84 Wis. 2d at 345; *see also* ***Bullock***, 549 S.W.2d at 169. For this reason, we do not find Erie's citations to ***Janesville Data Center*** and ***Bullock*** persuasive on the issue of whether Media's complaint alleged property damage under the Erie policy—that is, physical injury to or loss of use of tangible property.

¶27 Erie's citation to ***Lucker Manufacturing v. Home Insurance Co.***, 23 F.3d 808 (3d Cir. 1994), is similarly unavailing. There, Lucker Manufacturing produced an anchoring system called an "LMS" that was to be used in off-shore oil drilling. ***Id.*** at 810. Before the LMS was assembled, Lucker discovered a defect in one of its components—specifically, castings produced by Grede Foundries, Inc. ***Id.*** Because of the defect, Lucker was forced to increase the safety precautions it took in manufacturing the LMS in order to ensure the final product would not be defective. ***Id.*** Lucker subsequently sued Grede to recover the cost of the increased safety precautions, and Grede's CGL insurer denied coverage for Lucker's claim. ***Id.***

¶28 On appeal, the Third Circuit concluded the insurer had no duty to defend or indemnify Grede because Lucker's complaint did not allege a loss of use of "tangible property." ***Id.*** The court reasoned that "tangible property" is "property that can be felt or touched, or property capable of being possessed or realized." ***Id.*** at 818. The court further observed that, at the time Grede's insurer denied coverage, it knew "that the LMS itself had not physically existed at the time Grede's casting failed but was only in the design stage." ***Id.*** at 810. The court rejected Lucker's argument that a design becomes tangible property when it is reduced to a tangible medium, such as a blueprint or computer disk. ***Id.*** at 819. Instead, the court agreed with the insurer that "where the real value of a design is

in the idea, not in the physical plans that memorialize it, any loss in value of the design represents a loss in the value of the idea, which is not a loss of use of tangible property." ***Id.***

¶29 ***Lucker Manufacturing*** is distinguishable because, in that case, there was no allegation the insured's actions had physically damaged or caused a loss of use of the tangible medium on which the design for the LMS was stored. Here, in contrast, Media's complaint alleges that as a result of CMT's actions, tangible tapes containing intangible footage were discarded. Media's complaint seeks damages for the "value" of the discarded property. We have already determined that these allegations, liberally construed, allege damage to both the tangible tapes and their intangible content.

¶30 Finally, Erie cites ***Schaefer/Karpf Productions v. CNA Insurance Cos.***, 76 Cal. Rptr. 2d 42 (Cal. Ct. App. 1998). Schaefer produced a Christmas television special for children. ***Id.*** at 43. Scholastic, Inc., ordered 32,500 videotapes of the program from Schaefer, which contracted with The Video Company (TVC) to duplicate the program onto videotapes. ***Id.*** TVC duplicated the program onto tapes it had purchased from Matrix Video Duplication Corporation, some of which tapes had previously been used by a distributor of pornographic films. ***Id.*** After Scholastic sold approximately 25,000 copies of the Christmas program, it became apparent that the previous adult content had not been fully deleted from some of the tapes, such that, when the Christmas program ended, the tapes displayed explicit material. ***Id.*** Scholastic therefore recalled the tapes and refused to pay Schaefer. ***Id.*** at 43-44.

¶31 Schaefer subsequently sued TVC and Matrix, asserting claims for breach of contract, negligence, and breach of warranty. ***Id.*** at 44. CNA Insurance

Company, which insured both TVC and Matrix, refused to provide a defense, asserting its policies did not cover Schaefer's claims. ***Id.*** The California Court of Appeal ultimately agreed with CNA, concluding CNA had no duty to defend TVC and Matrix because Schaefer's complaint did not allege physical injury to, or loss of use of, "tangible property." ***Id.*** at 46, 49. The court reasoned:

> The only tangible property involved in this case was the videotapes themselves and, assuming they were defective by reason of containing pornographic material, then they were defective when Schaefer purchased them. The tapes did not cause injury through linkage to any tangible property of Schaefer's. They did not harm the "master tape" of the Pageant; it could still be used to make as many more copies of the Pageant as Schaefer wanted. Even if the defective tapes injured Schaefer's profits or its goodwill, these are intangibles not covered by a CGL policy.

Id. at 46. The court further concluded the Christmas program itself, separate from the videotapes, did not constitute "tangible property." ***Id.*** at 47-49.

¶32 ***Schaefer/Karpf Productions*** expressly recognized that videotapes are tangible property, separate from their intangible content. Thus, it actually supports our conclusion that Erie had a duty to defend CWP against Media's claims because Media's complaint alleged a covered loss—that is, damage to the videotapes themselves. Moreover, unlike the insurer in ***Schaefer/Karpf Productions***, Erie cannot escape a conclusion that it had a duty to defend by claiming the tapes were already defective when the loss occurred.

¶33 For the reasons explained above, we conclude Media's complaint contained allegations that, if proven, would result in a covered loss under Erie's policy. Erie therefore had a duty to defend CWP against each of the claims alleged in Media's complaint. *See* ***Water Well Sols.***, 369 Wis. 2d 607, ¶16. It is undisputed on appeal that, assuming Erie had a duty to defend CWP, it breached

that duty by refusing to provide a defense. We therefore reverse the judgment dismissing Erie from this case. We remand for the circuit court to enter a declaratory judgment in CWP's favor on the duty-to-defend issue and to determine the damages CWP is entitled to recover as a result of Erie's breach.

By the Court.—Judgment reversed and cause remanded with directions.

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