COURT OF APPEALS
DECISION
DATED AND FILED

September 8, 2010

A. John Voelker
Acting Clerk of Court of Appeals

Appeal No. 2009AP1629

Cir. Ct. Nos. 2004CV11186
2005CV1054

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

3303-05 MARINA ROAD, LLC AND RICK A. MICHALSKI,

PLAINTIFFS-APPELLANTS,

V.

WEST BEND MUTUAL INSURANCE COMPANY,

DEFENDANT-RESPONDENT,

ZENNETT PROPERTIES, LLC AND EUGENE BENNETT,

DEFENDANTS.

APPEAL from a judgment of the circuit court for Milwaukee County: THOMAS R. COOPER, Judge. *Affirmed.*

Before Curley, P.J., Fine and Brennan, JJ.

¶1 BRENNAN, J. 3303-05 Marina Road, LLC and Rick A. Michalski (collectively "Michalski" unless otherwise noted) appeal from a judgment, which

dismissed Michalski's claims against West Bend Mutual Insurance Company ("West Bend"). Michalski asserts that in denying coverage the trial court erred by: (1) failing to consider whether Michalski suffered a "loss of … Covered Property" commencing during the policy period and (2) applying an objective knowledge standard to the known loss doctrine. For the reasons which follow, we affirm the trial court.

BACKGROUND

¶2 The facts set forth are those that appear undisputed by the parties, included only to provide background information, and those found by the trial court following a bench trial.

¶3 This case arises out of a real estate transaction between Marina Road (owned by Michalski) and Zennett Properties, LLC ("Zennett Properties"). Zennett Properties was the prior owner of a 35-unit apartment complex located at 3303-05 Marina Road in South Milwaukee ("the Property").

¶4 Zennett Properties listed the Property for sale, and in July 2003 Michalski made an offer to purchase the Property for $2.1 million. Michalski's offer to purchase initially included the right to a professional inspection. However, because of the demand for real estate at that time, Michalski was told it would be four to six weeks before the Property could be professionally inspected. According to the trial court's findings of fact:

> When … Michalski was unable to get an inspector, discussions were had between [Michalski] and [Zennett Properties] as to whether the offer to purchase would terminate, or whether … Michalski[] would waive the inspection provision.
>
> … Michalski … indicated that he was concerned that he would lose the [P]roperty to somebody else. He

> made the economic decision to waive the inspection, and made a walk-thr[ough] inspection on his own sometime prior to closing. [Michalski] testified that he did look in one attic area, but did not have a light; the attic was dark, and he did not see anything that caused him concern.
>
> [Michalski] was only allowed access to three units of the 35[-]unit building, based upon the representation by the seller that he was unable to gain access from the tenants of the other units.… Michalski saw nothing of concern in the three units he observed, and he further conducted a walk-around inspection of the exterior of the building.

¶5 The trial court found that Michalski testified "forthrightly and truthfully," and the court accepted Michalski's assertion that he did not observe any damage to the Property before purchase. However, the trial court also found that Michalski "did not carefully look [or] carefully observe, and was primarily concerned with completing the deal" and that water intrusion on the Property was "clearly observable with careful inspection" at the time Michalski purchased the Property. On October 29, 2003, Michalski purchased the Property. Within thirty days of purchasing the Property, "Michalski became aware of water intrusion issues on the [P]roperty."

¶6 On November 29, 2004, Michalski notified West Bend, his property insurer, of the damage to the Property. West Bend conducted an investigation and determined that the damages claimed commenced prior to Michalski's purchase of the Property. Consequently, West Bend denied coverage for damages alleged by Michalski on grounds that those damages were not covered under Michalski's insurance policies with West Bend ("the Policies").

¶7 On December 27, 2004, Michalski filed suit against Zennett Properties and its principals, and Shorewest Realtors, Inc., asserting claims for fraud, strict responsibility misrepresentation, and intentional misrepresentation,

among others, in connection with concealment of the pre-existing damages to the Property. The parties eventually settled those claims.

¶8 On February 1, 2005, Michalski filed suit against West Bend, alleging that West Bend had breached its obligation to provide coverage for the damages to the Property under the terms of the Policies and did so in bad faith. West Bend timely answered the complaint. In its affirmative defenses, West Bend asserted that the damages claimed by Michalski were precluded under various provisions in the Policies. West Bend did not assert the known loss doctrine as a defense.

¶9 The trial court conducted a bench trial from February 23, 2009, through March 23, 2009. After ten days of testimony, the trial court issued a written decision dismissing Michalski's complaint against West Bend. The trial court's decision was based on its finding that damages to the Property pre-existed the policy period. Michalski appeals.

¶10 Additional facts are included in the discussion section as necessary.

STANDARD OF REVIEW

¶11 Michalski's assertions require us to construe the Policies to determine whether they provide coverage for the water intrusion on the Property. In doing so, we accept the trial court's findings of fact unless they are clearly erroneous. *See* WIS. STAT. § 805.17(2) (2007-08).[1] The interpretation of an insurance contract is a question of law that we review *de novo*. ***Danbeck v.***

[1] All references to the Wisconsin Statutes are to the 2007-08 version unless otherwise noted.

American Family Mut. Ins. Co., 2001 WI 91, ¶10, 245 Wis. 2d 186, 629 N.W.2d 150. Consequently, we may affirm the trial court on different grounds. *See* ***Mercado v. GE Money Bank***, 2009 WI App 73, ¶2, 318 Wis. 2d 216, 768 N.W.2d 53.

¶12 An insurance policy is to be construed so as to give effect to the parties' intentions. ***Danbeck***, 245 Wis. 2d 186, ¶10. We interpret policies "as they would be understood by a reasonable person in the position of the insured." ***American Family Mut. Ins. Co. v. American Girl, Inc.***, 2004 WI 2, ¶23, 268 Wis. 2d 16, 673 N.W.2d 65. The contract's words are to be given their common and ordinary meaning, and when the policy language is plain and unambiguous, we enforce the contract as written and without resorting to the rules of construction or principles of case law. ***Danbeck***, 245 Wis. 2d 186, ¶10. If the contract language is ambiguous, i.e., if it is susceptible to more than one reasonable interpretation, the language is construed in favor of coverage. ***Id.*** But "we do not interpret insurance policies to provide coverage for risks that the insurer did not contemplate or underwrite and for which it has not received a premium." ***American Girl***, 268 Wis. 2d 16, ¶23.

¶13 We follow a three-step procedure when determining whether a policy affords coverage. *See* ***id.***, ¶24. The only step necessary for us to address here is the first, during which "we examine the facts of the insured's claim to determine whether the policy's insuring agreement makes an initial grant of coverage." *See* ***id.*** Because we conclude that the Policies here do not make an initial grant of coverage for the water intrusion on the Property, we need not outline the additional steps. *See* ***id.*** ("If it is clear that the policy was not intended to cover the claim asserted, the analysis ends there.").

DISCUSSION

I. Loss Commencing During the Policy Period

¶14 The trial court determined that there was no coverage under the Policies' language because the "damage" to the Property occurred before the policy period began. Michalski does not challenge this finding but argues that under the Policies' "loss" language, he is entitled to coverage and that the trial court erred in not addressing that language. Michalski argues that the financial detriment he suffered as a result of the water intrusion on the Property amounted to a "loss" commencing during the policy period within the terms of the Policies. Because we conclude that the Policies' grant of coverage for "direct physical loss of … Covered Property" does not include "financial detriment" and that Michalski's arguments to the contrary ignore basic principles of contract construction and common sense, we affirm the trial court.

¶15 West Bend maintained two insurance contracts in effect at times material to Michalski's claim and action. The first was a businessowners' insurance policy in effect from May 7, 2003, through May 7, 2004. By an endorsement effective on October 29, 2003, Marina Road was added as an insured, and the Property was added as a "described premises." (Capitalization omitted.) A second insurance contract, also a businessowners' policy, was in effect from May 7, 2004, through May 7, 2005. The Policies each set forth the following language regarding coverage:

> **A. Coverage**
>
> We will pay for direct physical loss of or damage to Covered Property[2] at the premises described in the Declarations caused by or resulting from any Covered Cause of Loss.
>
> ….
>
> **3. Covered Causes of Loss**
>
> Risks of Direct Physical Loss unless the loss is:
>
> **a.** Excluded in Section **B.**, Exclusions; or
>
> **b.** Limited in Paragraph **A.4.**, Limitations[]
>
> ….
>
> **F.** Property General Conditions
>
> ….
>
> **4.** Policy Period, Coverage Territory
>
> Under this form:
>
> **a.** We cover loss or damage commencing:
>
> **(1)** During the policy period shown in the Declarations[] ….

¶16 Michalski does not challenge the trial court's definition of "[c]ommence[]" to mean "begin[] or start." In other words, the parties agree that by the plain language of the Policies, the Policies only cover "physical loss of or damage to Covered Property" beginning after the Property was added to the

[2] The trial court found that the Property was a Covered Property under the Policies. West Bend does not argue otherwise on appeal.

Policies by the October 23, 2003 endorsement. Michalski also does not challenge the trial court's conclusion that any water "damage to" the Property commenced prior to the policy period. Instead, Michalski claims that the trial court erred in not determining that a "loss of" the Property commenced during the policy period.

¶17 Michalski's "loss of" argument is three-fold. First, he argues that because the term "loss" is not defined in the Policies that it is ambiguous and that the word "or" between "loss of" and "damage to" indicates the phrases have two different meanings. Second, he turns to several outside sources to define the phrase "loss of" and ultimately concludes that "loss of" within the meaning of the Policies was meant to include "financial detriment." And finally, because he defines "loss of" as "financial detriment," Michalski attempts to persuade us that "as a matter of simple logic, [he] could not have any 'loss' [financial detriment] on the Property before he purchased the Property," meaning that "the very earliest Michalski's loss [financial detriment] could have possibly commenced is at the moment he closed on the Property—which is when the [Policies] went into effect."

¶18 We disagree with Michalski's assertion that the phrase "loss of" is ambiguous. The Policies clearly state that they cover "direct physical loss of" the Property. The common and ordinary meaning of the word "physical" is "of or related to natural or material things as opposed to things mental, moral, spiritual, or imaginary," *see* WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 1706 (1993); *see also* ***Danbeck***, 245 Wis. 2d 186, ¶10, while the common and ordinary meaning of the word "loss" is "'the state or fact of being destroyed or placed beyond recovery,'" *see* ***RTE Corp. v. Maryland Casualty Co.***, 74 Wis. 2d 614, 624, 247 N.W.2d 171 (1976) (citation omitted); *see also* ***Danbeck***, 245 Wis. 2d 186, ¶10. That is to say, by including the word "physical" before "loss of …

Covered Property" the parties intended that the Policies cover material or tangible destruction of the Property, not financial detriment resulting from a hasty investment. In suggesting that the Policies define "loss of" as "financial detriment," Michalski ignores the word "physical" in its entirety.

¶19 We do agree with Michalski's assertion that the word "or" means that the Policies define "loss of" and "damage to" differently. *See* ***Hull v. State Farm Mut. Auto. Ins. Co.***, 222 Wis. 2d 627, 638, 586 N.W.2d 863 (1998) ("The meaning of 'or' is plain: 'or' is a connector of alternative choices in a series."). Because they are defined differently, Michalski urges us to conclude that even if "damage" commenced prior to the start of the policy period, his "loss," which he defines as financial loss, commenced during the policy period. While we agree that the Policies' plain language provides two possible bases for coverage—namely, direct physical "damage" and "loss"—we do not agree, for the reasons stated above, that coverage is available here for the "financial loss" Michalski seeks.

¶20 Moreover, to define "physical loss of" the Property to include financial detriment, as Michalski requests, would convert the Policies into warranties on the Property, requiring West Bend to underwrite the risks Michalski took when he purchased the Property. There is no evidence that West Bend agreed to undertake that risk. In fact, the trial court explicitly found that the Policies were "not intended by the parties to be a warranty of the condition of the [P]roperty." And Michalski has not argued that the finding of fact is erroneous.

II. Known Loss Doctrine

¶21 Michalski spends the great majority of his brief arguing that "the trial court erred by applying an objective knowledge standard to the known loss

doctrine." (Uppercasing omitted.) "The known loss doctrine is a common law defense to insurance coverage according to which insurers are not obligated to cover losses that are already occurring when the coverage is written or [that] have already occurred." ***American Family Mut. Ins. Co. v. Bateman***, 2006 WI App 251, ¶26, 297 Wis. 2d 828, 726 N.W.2d 678 (citations and internal quotation marks omitted; brackets in ***Bateman***).

¶22 Because we previously concluded that the Policies do not make an initial grant of coverage for the water intrusion on the Property, we need not address the merits of this argument. *See* ***American Girl***, 268 Wis. 2d 16, ¶24. However, we do so briefly only to note that not only did West Bend not assert the known loss doctrine as a defense,[3] we fail to see where the trial court relied on the doctrine in its decision to dismiss Michalski's claims against West Bend. To the contrary, the trial court based its decision on its conclusion that any damage to the Property did not commence during the policy period, holding as follows:

> There was much evidence and testimony as to the length of time of the existence of the damages throughout the building. Some were in existence longer than others, but this Court is satisfied that the building had extensive water damage throughout, and this Court is satisfied the evidence supports the proposition that the water damage was in existence prior to … Michalski's purchase of the property in October of 2003.

Nowhere here or anywhere else does the trial court reference the known loss doctrine. And to the extent the trial court referenced Michalski's failure to professionally or adequately inspect the Property prior to purchase, we conclude

[3] Michalski admits as much in his reply brief, in which he states that "West Bend argues the substance of the known loss doctrine (if not the form)."

those references were mere dicta. In any event, our conclusion that the plain language of the Policies excludes coverage is dispositive, regardless of whether any comments from the trial court imply that it considered the known loss doctrine.

By the Court.—Judgment affirmed.

Not recommended for publication in the official reports.