IN THE SUPREME COURT
OF THE
STATE OF SOUTH DAKOTA

APPEAL NO. 29000

JOSEPH SAPIENZA and SARAH JONES SAPIENZA, M.D.

Plaintiffs,

vs.

LIBERTY MUTUAL INSURANCE COMPANY,

Defendant.

CERTIFICATION OF QUESTION FROM THE UNITED STATES DISTRICT COURT,
DISTRICT OF SOUTH DAKOTA, CENTRAL DIVISION

THE HONORABLE ROBERTO A. LANGE,
UNITED STATES DISTRICT JUDGE

BRIEF OF PLAINTIFFS

JOSEPH SAPIENZA AND SARAH JONES SAPIENZA, M.D.

Angela Beranek Brandt
LARSON • KING, LLP
30 East Seventh Street, Ste. 2800
Saint Paul, MN 55101
(651) 312-6500

Attorney for Plaintiff

Christian A. Preus
BASSFORD REMELE, P.A.
100 South Fifth Street, Ste. 1500
Minneapolis, MN 55402-1254
(612) 376-1649

Jack H. Hieb
RICHARDSON, WYLY, WISE, SAUCK
& HIEB, LLP
One Court Street
Post Office Box 1030
Aberdeen, SD 57402-1030
(605) 225-6310

Attorneys for Defendants

Table of Contents

Table of Authorities

Federal Cases

South Dakota Cases

Foreign Cases

State Statutes

Secondary Sources

Introductory Statement

References to the District Court record attached hereto are denoted by "DR" followed by the appropriate document number. References to the Appendix are denoted by "APP" and the corresponding exhibit and page numbers. Plaintiffs Joseph and Sarah Jones Sapienza are hereinafter referred to as the "Sapeinzas" and Defendant Liberty Mutual Fire Insurance Company will be referred to as "Liberty Mutual."

Jurisdictional Statement

This matter comes to this Court as a certified question from the United States District Court, District of South Dakota, Central Division and arises out of *Sapienza et al. v. Liberty Mutual Fire Insurance Company*, 3:18-cv-03015, before Judge Roberto A. Lange. Certification was sought sua sponte by the district court under SDCL § 15-24A-1, as part of an order issued on May 17, 2019. [APP11] This Court accepted the Certified Question on June 7, 2019 and directed the parties to respond in accordance with SDCL § 15-24A-7.

Statement of the Issue Presented

The Court has agreed to determine the following question:

> Do the costs incurred by the Sapienzas to comply with the injunction constitute covered "damages" under the Policies such that Liberty Mutual must indemnify the Sapienzas for these costs?

The Sapienzas respectfully request this Court to answer the certified question in the affirmative.

Statement of the Case

The Sapienzas commenced this action on September 7, 2018 in South Dakota federal court. [DR at 1.] The case was assigned to the Honorable Judge Roberto A. Lange. The Sapienzas brought claims for breach of contract, breach of good faith and fair dealing, breach of fiduciary duty, and bad faith. [DR at 9-12.] Liberty Mutual moved to dismiss the

Sapienzas' Complaint for failure to state a claim on October 2, 2018. [DR at 278.] On May 17, 2019, the District Court denied in part and granted in part Liberty Mutual's Motion to Dismiss, and certified a question to this Court. [APP1-20] The case has been stayed, pending the resolution of the issue before this Court. [Id.]

Statement of the Facts

This Court is familiar with some of the facts and circumstances that gave rise to the Sapienzas' claims against Liberty Mutual. The Sapienzas moved to Sioux Falls in 2013 after Dr. Sapienza, a pediatric surgeon, took a position at Sanford Health. Shortly thereafter, the Sapienzas purchased a home in the McKennan Park Historic District. [DR at 2.] In 2014, after obtaining the necessary approvals and permits, the Sapienzas began construction on their new home. [DR at 3-4.] In May of 2015, their neighbors, Pierce and Barbara McDowell, filed a lawsuit ("the McDowell lawsuit") in Minnehaha County Circuit Court, seeking injunctive relief and money damages alleging that the Sapienzas' newly constructed home violated certain regulations and ordinances that thereby deprived the McDowells of the use and enjoyment of their home. [DR at 14-22.]

The Policies

Prior to the initiation of the McDowell lawsuit, the Sapienzas contracted with Liberty Mutual for their insurance needs. The Sapienzas and Liberty Mutual entered into two separate insurance contracts (collectively, "the Policies"). The Sapienzas obtained a LibertyGuard Deluxe Homeowners Policy, Policy No. H32-248-993819-21 in effect from August 30, 2014 to August 30, 2015 (the "Homeowners Policy"). Additionally, the Sapienzas obtained a LibertyGuard Personal Catastrophe Liability Policy, Policy No. LJ1-248-932278-214 3, in effect from September 1, 2014 to September 1, 2015 (the "Excess Policy"). [DR at 24-70; 71-87.] Under the Homeowners Policy, Liberty Mutual was required to defend the

Sapienzas in the McDowell lawsuit. The terms of the Homeowners Policy provide that, in the event "a claim is made or a suit is brought against an 'insured' for damages because of 'bodily injury' or 'property damage' caused by an 'occurrence' to which this coverage applies" Liberty Mutual will

> 1. Pay up to [Liberty Mutual's] limit of liability for damages for which the 'insured' is legally liable. Damages include prejudgment interest awarded against the 'insured'

[DR at 40.] The Homeowners Policy defined "property damage" as "physical injury to, destruction of, or loss of use of tangible property" and "occurrence" as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions, which results, during the policy period, in…property damage." [DR at 30.]

The Excess Policy provided different definitions for certain terms throughout the policy. The terms of the Excess Policy require Liberty Mutual to

> "pay all sums in excess of the **retained limit** and up to our limit of liability for damages because of **personal injury** or **property damage** to which this policy applies and for which the **insured** is legally liable."

[DR at 76 (alterations in original).] The Excess Policy provided the following definition for property damage:

> **7. "property damage"** means: (a) injury to or destruction of tangible property; (b) injury to intangible property sustained by an organization as the result of false eviction, malicious prosecution, slander or defamation."

[DR at 76 (alterations in the original).] Neither insurance policy provides a definition of the term damages or the phrase legally liable.

The McDowell Litigation and Appeal

Liberty Mutual took control of and directed the defense of the McDowell Lawsuit. The suit proceeded to trial, and the Circuit Court found in favor of the McDowells and

ordered injunctive relief, requiring the Sapienzas to "bring their residence into compliance with the Administrative Rules of South Dakota and Secretary of the Interior Regulations regarding the requirements for new construction…or rebuild it." [DR at 90.] This extraordinary and unusual remedy was supported by the following findings relevant to this case:

- The violation of certain regulations "resulted in an invasion of [the McDowell's] interest in the private use and enjoyment of the land." [DR at 106.]
- "The value of the McDowells' residence declined and they lost the use of their wood burning fireplace." [Id.]
- "The historic residence and the historic district are not capable of being remedied by monetary judgment." [Id.]
- The harm caused by the Sapienza home was "irreparable and unable to be cured by monetary compensation." [DR at 109.]

After the injunction was issued, Liberty Mutual sent the Sapienzas a reservation of rights letter, informing the Sapienzas that Liberty Mutual believed that "[n]o indemnity coverage is owed" because "the Excess Policy only applies to damages for which the insured is legally liable. The Court's order specifically rejects the award of compensatory damages and instead orders injunctive relief. Such injunctive relief, and any costs associated with complying with the order of injunctive relief, does not constitute damages." [DR at 121.] Despite taking this position, Liberty Mutual continued to direct and fund the appeal of the McDowell lawsuit.

This Court affirmed the Circuit Court's issuance of an injunction in January of 2018. *See McDowell v. Sapienza*, 2018 S.D. 1, 906 N.W.2d 399. In finding in favor of the McDowells, this Court determined that the Sapienza home "not only decreased the market value of the McDowells' home, it interfered with the use and enjoyment of their home" and that "these types of intangible *harms* are often not rectified by pecuniary compensation." *Id.* at ¶ 24 (emphasis added). This Court also affirmed the Circuit Court's factual findings that the

Sapineza home "interfered with the McDowells' private use and enjoyment of their home" and that

> because of the home's proximity and size, the home rendered the McDowells' wood-burning fireplace unusable, it blocked McDowells' natural sunlight, it had a window that looked directly into the window of McDowells' daughter's bedroom and bathroom, it interfered with any privacy in the McDowells' living room, and it generally dominated the McDowells' home.

Id. at ¶ 30. After finding that the record supported the issuance of injunctive relief, this Court recognized that the dispute presented a "difficult case" and that "substantial harm will befall whichever party does not prevail." *Id.* at ¶ 31.

Remand & Demolition

On remand, substantial harm befell the Sapienzas. The Circuit Court ordered the Sapienzas to submit new architectural plans to the Board of Historic Preservation for the City of Sioux Falls ("the Board"). The Sapienzas submitted a new application to the Board. Legal counsel for the McDowells presented a series of written and oral arguments to the Board, prior to and during the hearing. Counsel for the McDowells instructed the Board that the Rules of Civil Procedure, rather than the Board's typical policies or administrative code, must govern the proceeding. Legal counsel retained by Liberty Mutual to defend the Sapienzas did not attend the hearing, and so the Sapienzas were unrepresented. [DR at 4.] The Board denied the Sapienzas' proposed changes to their home and, at the request of the McDowells' counsel, denied the Sapienzas an opportunity to submit any additional proposed changes to address the Board's concerns. The Circuit Court determined that the proposed plan "violates the terms of the Judgment of South Dakota law as it does not remedy or correct the violations of the aforesaid, and the Judgment having been final" ordered a Writ of Execution, directing the "Sheriff of Minnehaha County to remove said home if the same

has not been removed from thirty days" from May 17, 2018. [APP23] The Circuit Court further ordered that the Sapienzas' Supersedeas Bond be forfeited and the funds from the bond be used by the sheriff to demolish their home. [Id.]

On June 7, 2018, pursuant to the writ of execution, the Sapienzas had their home demolished. The price the Sapienzas paid to comply with the orders of this Court and the Circuit Court was in the form of their home. As a consequence of their liability to the McDowells, the Sapienzas incurred costs, including the price of construction of the home, the loss of use of the home, and $60,000 in demolition fees.

Standard of Review

This Court has the power to answer certified questions that "may be determinative of the cause pending in the certifying court and it appears to the certifying court and to the Supreme Court that there is no controlling precedent in the decisions of the Supreme Court of this state." SDCL § 15-24A-1.

The certified question presented here involves the interpretation of an insurance contract. SDCL § 58-11-39 requires that "[e]very insurance contract shall be construed according to the entirety of its terms and conditions as set forth in the policy and as amplified, extended, or modified by any rider, endorsement, or application lawfully made a part of the policy." Insurance policies are contracts and the interpretation of an insurance contract involves a question of law, reviewable de novo. *De Smet Ins. Co. of S.D. v. Gibson*, 1996 S.D. 102 ¶ 5, 552 N.W.2d 98, 99. Whether an insurance contract is ambiguous is likewise a question of law, subject to de novo review. *Ass Kickin Ranch, LLC v. N. Star Mut. Ins. Co.*, 2012 S.D. 73, ¶ 7, 822 N.W.2d 724, 726.

Argument

I. The Plain Meaning Of The Term Damages Unambiguously Includes The Expenses, Costs, Or Charges Associated With Compliance With the Circuit Court's Order

The term damages is not defined by the insurance policies issued by Liberty Mutual. As such, under well-settled South Dakota law, the term must be given its plain and ordinary meaning. "An insurance contract's language must be construed according to its plain and ordinary meaning and a court cannot make a forced construction or a new contract for the parties." *St. Paul Fire and Marine Ins. Co. v. Schilling*, 520 N.W.2d 884, 887 (S.D. 1994). When "the terms of an insurance policy are unambiguous, these terms cannot be enlarged or diminished by judicial construction." *Ass Kickin Ranch*, at ¶ 10. The term damages encompasses both money paid to compensate for harm as well as any expenses, costs, charges, or loss incurred to remedy a harm.

A. The Plain Meaning of Damages Includes Any Cost or Loss that is Incurred as a Result of Liability

The Court may "use statutes and dictionary definitions to determine the plain and ordinary meaning of undefined words in a contact." *Western Nat'l Mut. Ins. Co. v. TSP, Inc.*, 2017 S.D. 72 ¶ 14, 904 N.W.2d 52, 57 (quotation omitted). The plain meaning of damages is broad and includes the narrower, technical definition of the term advocated by Liberty Mutual.

Damage has been defined as "loss due to injury; injury or harm to person, property, or reputation due to injury" as well as "disadvantage" or "expense, cost or charge." *Webster's New International Dictionary* 664 (2nd Ed. 1950). Alternatively, a legal definition for damage defined the term as "estimated reparation in money for detriment or injury sustained; compensation or satisfaction imposed by law for a wrong or injury caused by a violation of a legal right." *Id.* Another source defines the term as any "impairment of the usefulness or

value of person or property; harm." *American Heritage College Dictionary*, 350 (3rd Ed. 1993). While legal damages are defined as "money ordered to be paid as compensation for injury or loss." *Id.* Informally, damages is defined as the "cost; price." *Id.* Yet another strictly legal definition of damages includes only "[m]oney claimed by, or ordered to be paid to, a person as compensation for loss or injury." *Damages*, Black's Law Dictionary, (10th Ed. 2018). These varied definitions indicate that the plain meaning of damages broadly includes any losses, harms, expenses, or costs caused by a specific injury and extends beyond the technical definition of legal damages.

South Dakota statutes recognize that the purpose of insurance is to allow consumers to shift and distribute risk and liability. SDCL § 58-6A-1(7). Liability insurance is designed to insure "against legal liability for…damage to property." SDCL § 58-9-13. Casualty insurance generally "includes insurance against any other kind of loss, damage, or liability properly a subject of insurance[.]" SDCL § 58-9-27. South Dakota law acknowledges that "liability" comes in many different forms and includes "legal liability for damages, including costs of defense, legal costs and fees, and other claims expenses because of injury to a person, damage to the person's property, or other damage or loss to any other person resulting from or arising out of any business…premises, or operations…" SDCL § 58-6A-1(8). It is clear from the plain language of SDCL § 58-6A-1(8) that insurance coverage for "legal liability" for damages includes more than just compensatory damages and extends to any legal costs, fees, or other expenses that are a consequence of liability.

Liberty Mutual advocates a specialized definition that is narrower than the plain meaning of the term. Liberty Mutual failed to specifically define the term in the Policies and cannot now seek to rewrite its policies via judicial construction. Neither policy offers a specific or technical definition of damages. Nor is the term damages prefaced by any

qualifier or limiting language that indicates the term has any special or technical meaning. In fact, the expansive language "[p]ay up to our limit" and "pay all sums[1]" at the beginning of the clause pertaining to Liberty Mutual's obligation to pay damages indicates that Liberty Mutual has an obligation to pay any amount or the whole amount quantity, or number of damages for which the Sapienzas were liable. Further, the "[p]ay up to our limit" and "pay all sums" language does not restrict to whom the payment of sums will be made. Moreover, the phrase "legally liable" in both Policies does not distinguish between a legal obligation to pay money to a third party or a legal obligation in equity, such as an injunction requiring the remedy of some existing wrong. Nothing in the Policies serves to alert or inform the insured that the term damages is meant to be confined to a technical, legal meaning or that damages excludes the costs of complying with court orders.

The Circuit Court determined that the Sapienzas were liable to the McDowells for the harm caused by the noncompliant construction of their home. The Circuit Court expressly found that the Sapienzas "brought the harm" to the McDowells through the construction of their home. And that harm or "injury" to the McDowell home included the loss of use of the McDowell fireplace, the loss of the historical character of the home, and a diminished resale value of the property.

The remedy for these injuries to the McDowell's tangible property came in the form of injunctive relief—requiring the Sapienzas to submit additional plans for approval and eventually for the Sapienzas to pay for the harm done to the McDowells by losing their home. The Sapienzas incurred significant costs and expenses including the lost value of their

[1] "Sum" is defined as "an amount obtained as a result of adding numbers" or "the whole amount, quantity, or number; an aggregate." *American Heritage College Dictionary*, 1359 (3rd Ed. 1993).

newly constructed home and expenses to demolish the home pursuant to the court order. The Sapienzas were found liable to the McDowells and the costs and expenses incurred to remedy the harm constitute damages under the plain and ordinary meaning of the terms of the Policies.

B. This Court has Implicitly Acknowledged that Damages Encompasses the Costs of Complying with Injunctive Relief.

The concept that damages covered by an insurance contract includes both dollars ordered to be paid and expenses incurred as a result of liability is not new. Though not directly addressed, the idea that the insured has a right to be indemnified for the costs associated with complying with a court order has previously been embraced by this Court. In *Taylor v. Imperial Casualty & Indemnity Co.*, 82 S.D. 298, 114 N.W.2d 856 (S.D. 1966), Taylor—the insured—was sued by a third party for nuisance, injunctive relief, and money damages for the insured's improper gasoline storage. An interlocutory injunction was issued, requiring the insured to take action to prevent the leakage of gasoline. In complying with that injunction, the insured employed excavators and dug drainage trenches, incurring costs and expenses. *Id.*

The insurer refused to provide a defense in the first instance and denied any claim to indemnity, asserting that "there was no damages because of injury to property caused by accident in the original action and hence there was no liability under the terms of the policies." *Id.* at 858. The terms of the policies provided that the insurer would pay "all sums which the insured shall become legally obligated to pay as damages because of injury to…property…caused by accident." *Id.* at 857. The insured commenced suit, claiming a right to indemnification for the costs associated with complying with the injunction. *Id.* at 858. The *Taylor* court determined that the insured was entitled to recover the costs of complying with the injunction under the policy, without directly interpreting the term damages. *Id.* at

859. In assuming, without deciding, that the costs of the injunction were included in the definition of damages, the holding in *Taylor* implies that the plain meaning of the term includes such costs.

The terms of the insurance policy at issue in *Taylor* are nearly identical to the terms of the Policies. Like the *Taylor* policy, the Excess Policy requires the insurer to pay "all sums" for which the insured is liable[2] as damages. This Court had no difficulty applying the plain and ordinary meaning of damages in *Taylor*. And this Court should do the same here. The costs and expenses incurred by the Sapienzas as a result of their liability to the McDowells for property damage constitute covered damages under the terms of the policy.

II. South Dakota Law Prohibits A Construction Of The Term Damages That Adopts The Technical Definition

Liberty Mutual offers a purported industry-specialized definition of damages informed by "black letter insurance law" designed to rewrite the terms of the policy. [DR at 198.] Liberty Mutual's proposed definition of damages is in direct conflict with South Dakota's rules of insurance contract interpretation. South Dakota law requires that unambiguous terms receive their plain and ordinary meaning. *See City of Fort Pierre v. United Fire & Cas. Co.*, 463 N.W.2d 845 (S.D. 1990); *Grandpre v. Northwestern Nat'l Life Ins. Co.*, 261 N.W.2d 804 (S.D. 1977); *Strong v. State Farm Mut. Ins. Co.*, 78 N.W.2d 828 (S.D. 1956). This longstanding principal has been reaffirmed as recently as May of 2019. *See James v. State Farm Mut. Automobile Ins. Co.*, 2019 S.D. 31. ¶ 12, 2019 WL 2292359 ("We construe the language of an insurance contract according to its plain and ordinary meaning.") (quotation omitted).[3]

---

[2] "Liable" means "responsible or answerable in law; legally obligated." *Liable*, Black's Dictionary (10th ed., 2018).

[3] The district court seemed to interpret the recently decided *Geidel v. De Smet Mut. Ins. Co. of S.D.*, 2019 S.D. 20, ¶18, 926 N.W.2d 478, 483 as modifying or in some way abrogating this well-established maxim. [APP14.] However, that decision does not contradict or supersede

The rules of contract interpretation developed by this Court do not permit the technical construction of the term damages advocated by Liberty Mutual. As recognized elsewhere, to give the term damages in the Policies "a technical meaning simply by reading [it] 'in the insurance context' would render meaningless [the] law's requirement that words be given their ordinary meaning unless a technical meaning is plainly intended." *Farmland Indus., Inc. v. Republic Ins. Co.*, 941 S.W.2d 505, 510 (Mo. 1997).[4] There is no basis in South Dakota law to give the term damages a technical meaning that only an insurance professional or attorney would understand. Instead, the plain and ordinary meaning of damages must be determined from the point of view of the average insurance consumer in South Dakota.

Importantly, the "black letter" definition offered by Liberty Mutual is anything but well-settled. Numerous federal and state courts have rejected the technical definition of damages advocated by Liberty Mutual, regardless of whether the term damages is unambiguous or ambiguous.[5] The Sapienzas recognize that most courts interpreting the term

---

the well-established rule regarding the interpretation of unambiguous phrases. The *Geidel* court referenced common understanding of the term "accident" in the insurance context but discussed and applied a more detailed and expansive definition of the term from its previous decisions, applying the plain and ordinary meaning of that term: *State Farm Mut. Auto. Ins. Co. v. Wertz*, 540 N.W.2d 636, 639 (S.D. 1995) and *Taylor v. Imperial Cas. and Indemnity Co*, 144 N.W.2d 856, 858 (1966). Nothing in the *Geidel* decision expressly or by implication permits the construction of an insurance policy in accord with the industry or technical definition of the term "damages."

[4] *See also Helena Chem. Co. v. Allianz Underwriters Ins. Co.*, 357 S.C. 631, 638 (S.C. 2004) ("An 'ordinary' meaning of the term [damages] is not a legalistic one dependent on whether the damages are classified as legal versus equitable.").

[5] Compare *Outboard Marine Corp. v. Liberty Mut. Ins. Co.*, 607 N.E.2d 1204, 1215 (Ill. 1992) (collecting cases, determining "damages" to be unambiguous); *Aetna Cas. And Sur. Co. v. Pintlar Corp.*, 948 F.2d 1507, 1513 (9th Cir. 1991) ("[T]he term 'damages,' in common thought, does not distinguish between equitable and nonequitable relief" and a "technical, arcane approach in discerning the meaning of damages under the policies must not be taken."); *Liberty Mut. Ins. Co. v. Those Certain Underwriters at Lloyds*, 650 F.Supp.1553, 1560 (W.D. Penn. 1987) (rejecting the "hypertechnical distinction between damages and equitable relief which has no relevance" because "such terminology is to be construed in accord with the plain meaning of the term and the reasonable expectations of the insured.") with *Lindsay*

damages in other jurisdictions have done so in the context of whether the costs associated with environmental clean-ups are covered damages. Nonetheless, the logic of their holdings should not be limited to that context alone. Each court's analysis of the meaning of the term damages was not tied directly to the language of any particular statute or the specific context of environmental issues.

For example, in *Minnesota Min. and Mfg. Co. v. Travelers Indem. Co.*, the Minnesota Supreme Court, in answering a certified question, first determined that the term damages "does not have an unambiguous technical meaning in the insurance industry which draws a distinction between actions seeking purely monetary relief and actions seeking injunctive relief." 457 N.W.2d 175, 179 (Minn. 1990). The *Travelers* court determined that the "ordinary understanding of the term 'damages' upon which the insureds could base a reasonable expectation of coverage is the estimated reparation in money for detriment or injury sustained: the compensation or satisfaction imposed by law for a wrong or injury caused by a violation of a legal right." *Id.* (internal quotation omitted). And under that plain and ordinary meaning, the average insured "could reasonably expect the policy to provide coverage for *any economic outlay* compelled by law to rectify or mitigate damage caused by the insured's acts or omissions." *Id.* at 181 (emphasis added). Absent from this analysis is any special consideration of the statutory environmental concerns at issue and should apply with equal force in this context. Moreover, though the environmental cases always involved

---

Mfg. Co. v. Hartford Acc. & Indem. Co., 118 F.3d 1263, 1271 (8th Cir. 1997) (holding that, under Nebraska law, the term "as damages" is ambiguous and adopting interpretation that includes "both legal damages and equitable relief because that interpretation favors the insured."); *A.Y. McDonald Indus., Inc. v. Ins. Co. Of North Am.*, 475 N.W.2d 607, 625 (Iowa 1991) (answering certified question and interpreting the term "damages" in a comprehensive general liability policy to be ambiguous).

sophisticated insurance consumers—large companies—courts still applied the plain and ordinary meaning, as understood by the average person.

Here, the Circuit Court could have awarded compensatory damages on the McDowells' negligence claim or ordered the injunctive relief actually issued. Either way, compliance with the Circuit Court's order would have required the Sapienzas to expend money and incur costs to remedy the property damage caused by the construction of their home. Simply because the Circuit Court issued an equitable remedy does not alter the fact that the Sapienzas were required to incurred costs as a result of their liability for the McDowells' property damage. Under the terms of the Policies, the Sapienzas could reasonably expect any economic outlay, resulting from liability for property damage, to be covered. As such, the costs and expenses associated with the demolition and loss of the use of the Sapienza home are covered as damages under the Policies.

This Court is bound to apply the plain and ordinary meaning of the term damages. The plain meaning of damages, as understood by the average lay person, includes the costs expended in complying with any relief ordered by a court. The Sapienzas request that the certified question be answered in the affirmative.

III. In The Alternative, Liberty Mutual's Technical Definition Of Damages Renders The Policies Ambiguous

The Sapienzas maintain that the term damages is unambiguous and should be afforded its plain and ordinary meaning. At best, Liberty Mutual's technical definition of damages renders the policy ambiguous. A policy is only ambiguous"[i]f, after examining the plain meaning of the whole policy, there is a genuine uncertainty as to which of two or more meanings is correct." *Larimer v. Am. Family Mut. Ins. Co.*, 2019 S.D. 21 ¶ 9, 926 N.W.2d 472, 475 (quotation omitted). And where a policy is ambiguous, this Court is required to adopt "the interpretation most favorable to the insured" *Id.* (quotation omitted). Any ambiguity "is

to be construed *most strongly* against the insurer and in favor of the insured." *Wilson v. Allstate Ins. Co.*, 186 N.W.2d 553, 557 (S.D. 1971)(emphasis added). "However, the court may not seek out a strained or unusual meaning for the benefit of the insured." *Ass Kickin Ranch*, at ¶ 10 (citation omitted).

The interpretation most favorable to the insured is the interpretation in favor of coverage. If the term damages is indeed ambiguous, this Court is required to adopt the interpretation most favorable to the Sapienzas—an interpretation that would provide coverage for the costs and expenses incurred by the Sapienzas in complying with the remedy ordered by the Circuit Court. Public policy favors the interpretation providing coverage where ambiguity exists. After all, to avoid any ambiguity, Liberty Mutual could have specified that damages applied only to legal damages ordered to be paid to third parties and associated with non-equitable remedies. Instead, Liberty Mutual left the term undefined and offers its technical definition after the fact. The Sapienzas are entitled to the benefit of any ambiguity in the policies and Liberty Mutual's decision not to define the term must be construed "most strongly" against them. *Wilson*, 186 N.W.2d at 557.

In the event this Court determines that the technical definition of damages renders the policy ambiguous, the interpretation in favor of coverage must be adopted. The interpretation of the term damages in favor of coverage in this case includes all costs or expenses that are the result of the Sapienzas' liability for the McDowells' property damage. Under this analysis, the certified question must be answered in the affirmative.

Conclusion

The Court should answer the certified question in the affirmative. The Sapienzas purchased insurance expecting coverage for costs incurred as a result of legal liabilities—regardless of whether those costs came in the form of a money judgment or injunctive relief.

Liberty Mutual could have, but did not, offer a technical, narrow definition of the term damages into the Policies. This court must construe unambiguous terms according to their plain and ordinary meaning. If the Court deems the term ambiguous, the Court must adopt the interpretation most favorable to the insured. Under either analysis, the Policies provide coverage for the substantial costs and losses incurred by the Sapienzas as a result of their liability. For these reasons, the Sapienzas respectfully submit that the certified question must be answered in the affirmative.

Dated: July 8, 2019

/s/ Angela Beranek Brandt

Angela Beranek Brandt (#3091)
LARSON • KING, LLP
30 East Seventh Street, Ste. 2800
Saint Paul, MN 55101
(651) 312-6500 | Fax: (651) 312-6618
abrandt@larsonking.com

Attorneys for Plaintiffs

Certificate of Compliance

Under SDCL 15-26A-66(b)(4), I certify that this brief complies with the requirements of the South Dakota Codified Laws. This brief was prepared using Microsoft Word, and contains 4,581 words from the Statement of the Case through the Conclusion. I have relied on the word count of a word-processing program to prepare this certificate.

/s/ Angela Beranek Brandt
Angela Beranek Brandt (#3091)

Certificate of Service

The undersigned certifies that a true and correct copy of the foregoing brief was served electronically upon:

Attorneys for Defendants
Jack H. Hieb
jhieb@rwwsh.com

Christian A. Preus
cpreus@bassford.com

Appendix to Plaintiff's Brief

Table of Contents

UNITED STATES DISTRICT COURT

DISTRICT OF SOUTH DAKOTA

CENTRAL DIVISION

JOSEPH SAPIENZA, and SARAH JONES SAPIENZA, M.D., Plaintiffs, vs. LIBERTY MUTUAL FIRE INSURANCE COMPANY, Defendant.	3:18-CV-03015-RAL OPINION AND ORDER GRANTING IN PART DEFENDANT'S MOTION TO DISMISS AND CERTIFYING QUESTION TO SUPREME COURT OF SOUTH DAKOTA

Plaintiffs, Joseph Sapienza and Dr. Sarah Jones Sapienza, built a house and then had to tear it down to comply with an injunction issued against them in a state court action. The Sapienzas' insurer, Liberty Mutual Fire Insurance Company (Liberty Mutual), defended them in the state court action but refused to indemnify them for the costs of complying with the injunction. The Sapienzas sued Liberty Mutual in this Court, alleging breach of contract and bad faith. Doc. 1. Liberty Mutual moved to dismiss, arguing that the Sapienzas failed to state a claim upon which relief can be granted. Doc. 9. For the reasons stated below, this Court grants in part and denies in part Liberty Mutual's motion to dismiss and certifies a question to the Supreme Court of South Dakota.

I. Facts

In 2013, the Sapienzas purchased a home in the McKennan Park Historic District in Sioux Falls, South Dakota. Doc. 1 at ¶¶ 6–7. They decided to raze the existing house and build a new home on the property. Doc. 1 at ¶ 7. They hired an architect to design the home and submitted a proposal to the Sioux Falls Board of Historic Preservation (the Board). Doc. 1 at ¶¶ 8–9. The Board approved the proposal and the Sapienzas hired a contractor to build their home. Doc. 1 at ¶¶ 9–10.

During construction, the Sapienzas' neighbors, Pierce and Barbara McDowell, became concerned about the size and location of the new home. McDowell v. Sapienza, 906 N.W.2d 399, 403 (S.D. 2018); Doc. 1 at ¶ 11. In early May 2015, the McDowells' lawyer sent the Sapienzas a cease-and-desist letter maintaining that the home violated height and setback regulations. McDowell, 906 N.W.2d at 403. The Sapienzas did not stop construction, so the McDowells sued them in state court in mid-May 2015. Id.; Doc. 1 at ¶ 11.

The McDowells' complaint alleged that the height and proximity of the Sapienzas' home prevented the McDowells from using their fireplace, blocked the natural light the McDowells previously enjoyed, and decreased the value of their home. Doc. 1 at ¶ 11; Doc. 1-1 at 4–5. Count 1 of the complaint sought a permanent injunction requiring the Sapienzas to modify or relocate their house. Doc. 1-1 at 5–6. Count 2, entitled "Negligence," sought this same injunctive relief and, in the alternative, damages. Doc. 1-1 at 6–7. Count 3 alleged that the Sapienzas' home was a nuisance and requested an injunction and damages. Doc. 1-1 at 7–8.

The Sapienzas retained a South Dakota attorney (defense counsel) to defend them against the McDowell suit. Doc. 14 at 2; Doc. 11-1. Defense counsel filed an answer for the Sapienzas on June 12, 2015. Doc. 11-1. The Sapienzas notified their insurer Liberty Mutual of the McDowell suit on August 24, 2015. Doc. 1 at ¶ 18; Doc. 14 at 2; Doc. 1-5 at 3. Liberty Mutual insured the Sapienzas under a Homeowner's Policy and an Excess Policy. Doc. 1 at ¶¶ 12–17; Docs. 1-2, 1-3.

Several sections of these Policies are relevant to the Sapienzas' claims and Liberty Mutual's motion to dismiss. In brief, the Homeowner's Policy required Liberty Mutual to defend and indemnify the Sapienzas against a suit for damages because of "property damage." Section II of the Homeowner's Policy describes the coverage provided:

> **COVERAGE E – Personal Liability**
> If a claim is made or a suit is brought against an "insured" for damages because of "bodily injury" or "property damage" caused by an "occurrence" to which this coverage applies, we will:
> **1.** Pay up to our limit of liability for the damages for which the "insured" is legally liable. Damages include prejudgment interest awarded against the "insured"; and

> 2. Provide a defense at our expense by counsel of our choice, even if the suit is groundless, false or fraudulent. We may investigate and settle any claim or suit that we decide is appropriate. Our duty to settle or defend ends when the amount we pay for damages resulting from the "occurrence" equals our limit of liability.

Doc. 1-2 at 18. The Homeowner's Policy defines "property damage" as "physical injury to, destruction of, or loss of use of tangible property." Doc. 1-2 at 8. The Homeowner's Policy in its exclusions states that "**Coverage E – Personal Liability,** does not apply to: . . . b. 'Property damage' to property owned by the 'insured.'" Doc. 1-2 at 20.

The Excess Liability Policy provides additional coverage to the Sapienzas:

> **COVERAGE – PERSONAL EXCESS LIABILITY**
>
> We will pay all sums in excess of the **retained limit** and up to our limit of liability for damages because of **personal injury** or **property damage** to which this policy applies and for which the **insured** is legally liable.

Doc. 1-3 at 7. The Excess Liability Policy defines "property damage" as "(a) injury to or destruction of tangible property; (b) injury to intangible property sustained by an organization as the result of false eviction, malicious prosecution, libel, slander or defamation." Doc. 1-3 at 7. The Excess Liability Policy "does not apply to: **property damage** to: (1) property owned by any **insured.**" Doc. 1-3 at 8.

Liberty Mutual agreed to defend the Sapienzas from the McDowell suit under a reservation of rights, and defense counsel previously retained by the Sapienzas continued defending the Sapienzas with Liberty Mutual then paying the attorney's fees. Doc. 1 at ¶ 18; Doc. 1-5. Nevertheless, the Sapienzas allege that Liberty Mutual "controlled the defense by, among other things, implementing a Comprehensive Litigation Program, issuing instructions to defense counsel concerning actions to be taken (or not taken), failing to retain an independent expert architect or contractor to offer opinions regarding the home, and refusing to pay for certain activities." Doc. 1 at ¶ 18; Doc. 1-4 at 2.

The McDowell suit went to trial in June 2016. Doc. 1-4 at 2. The state trial judge issued a decision and order in December 2016 granting the McDowells a mandatory injunction against the Sapienzas. The injunction required the Sapienzas to bring their house into compliance with federal and state regulations for

buildings in historic districts or rebuild it. Doc. 1-4 at 2–3, 25, 29. The state trial judge did not order the Sapienzas to pay any monetary damages to the McDowells. Doc. 1-4.

Liberty Mutual sent the Sapienzas a letter in early March 2017 stating that it would "continue to provide a defense to you for the Lawsuit, including any appeal," but that it would not provide any coverage for the "injunctive relief" ordered by the state trial judge. Doc. 1-5 at 2. According to Liberty Mutual, the injunctive relief and the costs of complying with it did not constitute "damages" under the Policies. Doc. 1-5 at 4.

The Supreme Court of South Dakota affirmed the state trial court's order of injunctive relief in early 2018. McDowell, 906 N.W.2d 399. The Court affirmed that regulations concerning construction in historic districts applied to the Sapienzas' house and that the house violated these regulations because it was more than eight feet taller than the permitted height. Id. at 405–06. As to the injunction, the Court held that "[p]ecuniary compensation would not provide adequate relief" for the harm the Sapienzas' home caused to the McDowells and the McKennan Park District. Id. at 407. The Court remanded the case "for further proceedings consistent with" its opinion. Id. at 411.

The Sapienzas allege that after the remand, the state judge ordered them to submit a new application to the Board. Doc. 1 at ¶ 26. The new application included structural changes to the Sapienzas' home to bring it into compliance with the regulations for historical districts. Doc. 1 at ¶ 26. Defense counsel, who had continued to represent the Sapienzas during their appeal to the Supreme Court of South Dakota, did not attend the hearing before the Board. Doc. 1 at ¶ 27. According to the Sapienzas, the Board refused to approve the new application and, based on arguments by the McDowells' lawyer, prohibited the Sapienzas from submitting any future plans for approval. Doc. 1 at ¶ 28.

In May 2018 the state judge issued a writ of execution giving the Sapienzas thirty days to demolish their home. Doc. 1 at ¶ 29. The Sapienzas complied with the writ and incurred in excess of $60,000 in demolition-related expenses. Doc. 1 at ¶ 30.

The Sapienzas sued Liberty Mutual in this Court in September 2018. Count 1 of their complaint is for breach of contract, alleging that Liberty Mutual breached its duty to defend and indemnify them. Doc.

1 at ¶¶ 31–35. Counts 2, 3, and 4 of the Sapienzas' complaint essentially allege that Liberty Mutual's handling of the McDowell suit and refusal to indemnify the Sapienzas constitute bad faith. Doc. 1 at ¶¶ 36–48. Liberty Mutual moved to dismiss under Federal Rule of Civil Procedure 12(b)(6). Doc. 9.

II. Standard of Review

On a motion to dismiss under Rule 12(b)(6), the court must accept a plaintiff's factual allegations as true and make all inferences in the plaintiff's favor, but need not accept a plaintiff's legal conclusions. Retro Television Network, Inc. v. Luken Commc'ns, LLC, 696 F.3d 766, 768–69 (8th Cir. 2012). To survive a motion to dismiss for failure to state a claim, a complaint must contain "a short and plain statement of the claim showing that the pleader is entitled to relief." Fed. R. Civ. P. 8(a)(2). Although detailed factual allegations are unnecessary, the plaintiff must plead enough facts to "state a claim to relief that is plausible on its face." Ashcroft v. Iqbal, 556 U.S. 662, 678 (2009) (quoting Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 570 (2007)). A claim is plausible on its face "when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged," id., "even if it strikes a savvy judge that actual proof of those facts is improbable, and 'that a recovery is very remote and unlikely,'" Twombly, 550 U.S. at 556 (quoting Scheuer v. Rhodes, 416 U.S. 232, 236 (1974)). Still, "conclusory statements" and "naked assertions devoid of further factual enhancement" do not satisfy the plausibility standard. Iqbal, 556 U.S. at 678 (cleaned up) (quotation omitted).

When determining whether to grant a Rule 12(b)(6) motion, a court generally must ignore materials outside the pleadings, but it may "consider matters incorporated by reference or integral to the claim, items subject to judicial notice, matters of public record, orders, items appearing in the record of the case, and exhibits attached to the complaint whose authenticity is unquestioned . . . without converting the motion into one for summary judgment." Dittmer Props., L.P. v. FDIC, 708 F.3d 1011, 1021 (8th Cir. 2013) (internal marks omitted) (quoting Miller v. Redwood Toxicology Lab., Inc., 688 F.3d 928, 931 n.3 (8th Cir. 2012)). Here, the Sapienzas attached to their complaint the McDowell's complaint in state court, both Policies, the state judge's December 2016 decision and order, the March 2017 letter from Liberty Mutual, and the Supreme Court of South Dakota's decision in McDowell v. Sapienza. Among other things, Liberty

Mutual submitted the answer defense counsel filed in the McDowell suit. This Court has considered these documents in ruling on Liberty Mutual's 12(b)(6) motion. These items were either matters of public record, attached to the complaint, or integral to the Sapienzas' claims.

III. Analysis

A. Count 1: Breach of Duty to Defend

The Sapienzas as part of Count 1 of their complaint allege that Liberty Mutual had a contractual duty to defend them against the McDowell suit and that Liberty Mutual breached this duty by failing to provide them with a proper defense. Doc. 1 at ¶¶ 18, 26–28, 32; see also Doc. 14 at 7. Neither party cited—and this Court has not found—any South Dakota case addressing an insurer's liability for an inadequate defense. This Court must therefore "attempt to predict" how the Supreme Court of South Dakota would treat such a claim. Jurrens v. Hartford Life Ins. Co., 190 F.3d 919, 922 (8th Cir. 1999) (citation omitted). In doing so, this Court "may consider relevant state precedent, analogous decisions, considered dicta, and any other reliable data." Id. (cleaned up and citation omitted). Although there is no South Dakota precedent on an insurer's liability for providing an inadequate defense, there is a draft of the Restatement addressing this issue. Because the draft Restatement follows the well-reasoned majority rule and because the Supreme Court of South Dakota has found the Restatements "persuasive in many instances," this Court predicts that the Supreme Court of South Dakota would adopt the Restatement's position on insurer liability for an improper defense. Chem-Age Indus., Inc. v. Glover, 652 N.W.2d 756, 770 (S.D. 2002); see also Hendrix v. Schulte, 736 N.W.2d 845, 848–49 (S.D. 2007) (applying the Restatement); Wildeboer v. S.D. Junior Chamber of Commerce, Inc., 561 N.W.2d 666, 674 n.10 (S.D. 1997) (Sabers, J., dissenting) ("This court frequently consults and employs the Restatements."); Beau Townsend Ford Lincoln, Inc. v. Don Hinds Ford, Inc., 759 F. App'x 348, 353 (6th Cir. 2018) ("[W]e may look to an applicable Restatement . . . for guidance when there is no controlling state law on point [and] the state has indicated that it considers the Restatements to be persuasive authority." (cleaned up and citation omitted)).

The most recent draft of the Restatement provides two scenarios under which the insurer may be liable for providing an inadequate defense:

> (1) If an insurer undertakes to select counsel to defend a legal action against the insured and fails to take reasonable care in so doing, the insurer is subject to liability for the harm caused by any subsequent negligent act or omission of the selected counsel that is within the scope of the risk that made the selection of counsel unreasonable.
> (2) An insurer is subject to liability for the harm caused by the negligent act or omission of counsel provided by the insurer to defend a legal action when the insurer directs the conduct of the counsel with respect to the negligent act or omission in a manner that overrides the duty of the counsel to exercise independent professional judgment.

Restatement of the Law of Liability Insurance § 12 (Am. Law Inst., Revised Proposed Final Draft No. 2, Sept. 7, 2018).[1] To be liable under § 12, then, the insurer itself must have engaged in some misconduct. Indeed, § 12 rejected the rule applied by a minority of states that insurers are vicariously liable for all malpractice by defense counsel they hire. Id. cmts. d, e & reporters' notes d, e; see also George M. Cohen, Liability of Insurers for Defense Counsel Malpractice, 68 Rutgers Univ. L. Rev. 119, 125 n.37 (2015) (stating that a majority of jurisdictions do not hold insurers vicariously liable for the actions of defense attorneys they hire). This minority rule is unnecessary, the Restatement reasoned, because defense counsel is in the best position to prevent harm from his or her own malpractice and because an attorney with adequate liability insurance is just as able as the insurer to spread the risk of loss. Restatement of the Law of Liability Insurance § 12 cmts. d, e. Beyond that, the Restatement explained, a lawyer hired by an insurance company to represent an insured is not an agent of the company such that the company should be held vicariously liable for the lawyer's misconduct. Id. cmt. d & reporters' note d. Instead, the lawyer is an independent contractor who owes the insured a duty to exercise his or her own judgment when representing the insured. Id.; see also St. Paul Fire & Marine Ins. v. Engelmann, 639 N.W.2d 192, 200 n.7 (S.D. 2002) (explaining that "attorneys representing insureds on behalf of carriers owe an undeviating fealty to the insureds").

The Sapienzas hired defense counsel themselves so the issue here is whether Liberty Mutual breached the duty to defend by overriding counsel's independent judgment. According to the Sapienzas'

[1]The Restatement of the Law of Liability Insurance remains in proposed final draft form, but reflects many years of work by the American Law Institute and has been cited and relied upon in various court decisions. See, e.g., Country Mut. Ins. Co. v. Martinez, No. CV-17-02974-PHX-ROS, 2019 WL 1787313, at *13 n.15 (D. Ariz. Apr. 24, 2019); Nat'l Cas. Co. v. W. Express, 356 F. Supp. 3d 1288, 1299 (W.D. Okla. 2018); Selective Ins. Co. of Am. v. Smiley Body Shop, Inc., 260 F. Supp. 3d 1023, 1033 (S.D. Ind. 2017).

complaint, Liberty Mutual breached the duty to defend when it "took control of the defense of the Lawsuit and responsibility for payment of counsel," issued "instructions to defense counsel concerning actions to be taken (or not taken)," failed "to retain an independent expert architect or contractor to offer opinions regarding the home," and refused to "pay for certain activities, all to the ultimate detriment of the Sapienzas." Doc. 1 at ¶ 18. The Sapienzas also allege that Liberty Mutual breached the duty when defense counsel "did not attend" the Board's hearing on the Sapienzas' new application. Doc. 1 at ¶ 27. Liberty Mutual argues that these allegations fail to state a claim because, among other things, the Sapienzas do not allege that Liberty Mutual overrode defense counsel's independent professional judgment and have not adequately alleged that Liberty Mutual's actions caused them damages.

This Court agrees with Liberty Mutual that the Sapienzas' allegations fall short in several respects. To begin with, the Sapienzas' allegations that Liberty Mutual issued "instructions to defense counsel" and refused "to pay for certain activities" are too vague to support the reasonable inference that Liberty Mutual breached the duty to defend. See Braden v. Wal-Mart Stores, Inc., 588 F.3d 585, 594 (8th Cir. 2009) ("[S]ome factual allegations may be so indeterminate that they require further factual enhancement in order to state a claim." (cleaned up and citation omitted)). The Sapienzas do not allege what Liberty Mutual instructed defense counsel to do or for what activities Liberty Mutual refused to pay. Nor have the Sapienzas made any allegations suggesting that Liberty Mutual's instructions and refusal to pay overrode defense counsel's independent professional judgment or caused the Sapienzas harm. In short, the Sapienzas' allegations about instructions to defense counsel and the refusal to pay for certain services constitute "naked assertions devoid of further factual enhancement," and are therefore insufficient to state a claim. Iqbal, 556 U.S. at 678 (cleaned up) (quoting Twombly, 550 U.S. at 557).

The Sapienzas' claim about lack of a retained expert suffers from similar problems. Again, the Sapienzas allege that Liberty Mutual "controlled the defense by . . . failing to retain an independent expert architect or contractor to offer opinions regarding the home." Doc. 1 at ¶ 18. This allegation does not plead sufficient facts to draw a reasonable inference that Liberty Mutual breached the duty to defend. See Iqbal, 556 U.S. at 678. Indeed, the Sapienzas do not allege that defense counsel wanted to hire an expert or that

Liberty Mutual overrode defense counsel's professional judgment that an expert was necessary. See Restatement of the Law of Liability Insurance § 12 cmt. e, illus. 5 (explaining that an insurer would not be liable for the failure to hire an expert when defense counsel independently chose not to hire the expert without consulting the insurer). Moreover, nothing in the complaint indicates that the failure to hire an expert hurt the Sapienzas' defense.

The Sapienzas' final claim is that Liberty Mutual breached the duty to defend when defense counsel "did not attend" the Board's hearing on the Sapienzas' new application. Doc. 18 at ¶ 27. The Sapienzas fail to state a claim on this basis because they do not allege that Liberty Mutual engaged in any wrongdoing. That is, the Sapienzas do not allege that Liberty Mutual caused defense counsel to fail to attend the hearing or somehow overrode defense counsel's judgment that his attendance at the hearing was necessary. Absent any such facts, this Court cannot reasonably infer under Eighth Circuit precedent that Liberty Mutual breached the duty to defend. See Braden, 588 F.3d at 594.

This Court recognizes that the Sapienzas make somewhat different assertions about breach of the duty to defend in their brief. In briefing, the Sapienzas assert that Liberty Mutual "directed counsel's course of action through affirmative statements and the refusal to pay for certain activities associated with the case," "failed to allow counsel to retain an independent expert to evaluate the home or make recommendations" and "failed to require or otherwise direct counsel to appear at the court-ordered hearing before the Historic Board." Doc. 14 at 7. Some Eighth Circuit cases suggest that courts may consider allegations in response to a motion to dismiss even if those allegations are not in the complaint. Neudecker v. Boisclair Corp., 351 F.3d 361, 362 (8th Cir. 2003) (per curiam); Pratt v. Corrs. Corp. of Am., 124 F. App'x 465, 466 (8th Cir. 2005) (per curiam); Anthony v. Runyon, 76 F.3d 210, 214 (8th Cir. 1996); see also Danielson v. Huether, 355 F. Supp. 3d 849, 856 n.1 (D.S.D. 2018) (considering factual assertions in a pro se plaintiff's brief on a motion to dismiss). These cases do not help the Sapienzas, however, as the factual assertions in their brief still fall short of stating a claim for breach of the duty to defend.

First, the Sapienzas' additional allegations about Liberty Mutual directing defense counsel's conduct and refusing to pay for certain activities remain too vague to support a reasonable inference that

Liberty Mutual breached the duty to defend. Second, the Sapienzas' allegation that Liberty Mutual "failed to allow counsel to retain an independent expert" comes closer to alleging the necessary misconduct by Liberty Mutual, but still stops short of alleging that Liberty Mutual refused counsel's request to hire an expert or overrode his professional judgment. In any event, the Sapienzas' brief does not include any facts suggesting that the failure to hire an expert caused them damage. Third, the Sapienzas' allegation that Liberty Mutual "failed to require or otherwise direct" counsel to attend the hearing is not a viable theory of breach of the duty to defend. As explained above, courts and the draft of § 12 of the Restatement have rejected the notion that insurers are vicariously liable for any malpractice committed by defense counsel. The authors of the Restatement found no cases "holding a liability insurer liable for the torts of counsel on a theory of apparent authority or negligent supervision." Restatement of the Law of Liability Insurance § 12 reporters' note d. None of the Sapienzas' allegations allow for the plausible inference that Liberty Mutual was so closely involved in the Sapienzas' defense that it could be liable for failing to require or direct counsel to attend the Board hearing.

Rather than dismissing the Sapienzas' breach of the duty to defend claim now, this Court will give the Sapienzas 14 days from the date of this opinion to seek leave to amend their complaint if indeed there is a basis under the facts for a claim for breach of the duty to defend. This approach is more appropriate than immediate dismissal as the Sapienzas may not have contemplated in the absence of settled South Dakota precedent application of the most recent draft of § 12 of the Restatement to dismiss their breach of the duty to defend claim.

B. Count 1: Breach of Duty to Indemnify

The Sapienzas' other claim in Count 1 is that Liberty Mutual breached the terms of the Policies by refusing to indemnify them for the damages resulting from the McDowell suit. Liberty Mutual argues that this claim fails as a matter of law because the costs the Sapienzas incurred to comply with the injunction do not constitute "damages" under the Policies. Both parties cite authority which they claim supports their interpretation of the word "damages."

Liberty Mutual cites several cases in which courts have held that the term "damages" in an insurance contract refers to legal damages rather than claims for equitable relief. See, e.g., Ellett Bros., Inc. v. U.S. Fid. & Guar. Co., 275 F.3d 384, 387 (4th Cir. 2001); Aetna Cas. & Sur. Co. v. Hanna, 224 F.2d 499, 503 (5th Cir. 1955); O'Brien & Assocs. v. Tim Thompson, Inc., 653 N.E.2d 956, 960–61 (Ill. App. Ct. 1995); Ladd Const. Co. v. Ins. Co of N. Am., 391 N.E.2d 568, 571–73 (Ill. App. Ct. 1979). Relying on this "technical" definition, these courts have held that the costs of complying with an injunction do not constitute damages. Ellett Bros., 275 F.3d at 388; Hanna, 224 F.2d at 503; O'Brien, 653 N.E.2d at 960; Ladd, 391 N.E.2d at 571–73.

The Sapienzas, on the other hand, cite a string of cases rejecting the technical definition of damages as inconsistent with the rule that terms in an insurance contract be given their plain and ordinary meaning. See, e.g., Lindsay Mfg. v. Hartford Accident & Indem. Co., 118 F.3d 1263, 1270–71 (8th Cir. 1997); Liberty Mut. Ins. v. Those Certain Underwriters at Lloyds, 650 F. Supp. 1553, 1560–61 (W.D. Pa. 1987); A.Y. McDonald Indus., Inc. v. Ins. Co. of N. Am., 475 N.W.2d 607, 618–21, 625 (Iowa 1991); Minn. Mining & Mfg. Co. v. Travelers Indem. Co., 457 N.W.2d 175, 179–80 (Minn. 1990). The courts in Lindsay, A.Y. McDonald, and Minnesota Mining held that costs the insured incurred when cleaning up environmental contamination constituted "damages," Lindsay, 118 F.3d at 1271; A.Y. McDonald, 475 N.W.2d at 625; Minn. Mining, 457 N.W.2d at 184, while the court in Liberty Mutual found that backpay awarded as part of a class-action lawsuit qualified as "damages," Liberty Mutual, 650 F. Supp. at 1560–61.

The Sapienzas argue that this Court should reject the technical definition of damages because South Dakota law requires that terms in an insurance contract be given their plain and ordinary meanings. Liberty Mutual responds that Lindsay, A.Y. McDonald, and Minnesota Mining are inapplicable because they concerned cleanup costs under environmental protection statutes. According to Liberty Mutual, the remedies available under environmental protection statutes explain the decisions in these cases. See Gen. Star Indem. Co. v. Lake Bluff Sch. Dist. No. 65, 819 N.E.2d 784, 792 (Ill. App. Ct. 2004) ("Statutory schemes designed for environmental protection have a unique nature that blurs the distinction between monetary compensation and the expenditure of money to comply with a mandatory injunction."); id at 794

("The costs of complying with an injunction are considered 'damages' only in special situations, such as . . . environmental litigation . . . ."); see also U.S. Fid. & Guar. Co. v. Ellet Bros., Inc., No. 3:00-3691-24, 2003 WL 22519471, at *6 (D.S.C. Mar. 5, 2003) (concluding that "analysis regarding equitable relief in the [environmental protection statute] context should be limited to those types of actions").

The parties agree that there are no South Dakota cases directly addressing whether the costs of complying with an injunction constitute "damages" under a liability insurance policy. Liberty Mutual argues, however, that the decisions in Public Entity Pool for Liability v. Score, 658 N.W.2d 64 (S.D. 2003), and Dan Nelson Automotive Group, Inc. v. Universal Underwriters Group, No. CIV 05-4044, 2008 WL 170084 (D.S.D. Jan. 15, 2008), support its position.

The Score case involved South Dakota's Public Entity Pool for Liability (PEPL fund) rather than an insurance policy. The issue in Score was whether a state employee who had been sued for negligence could recover attorney's fees incurred in a separate declaratory judgment action the PEPL fund brought to seek a declaration that it had no duty to defend the negligence suit. 658 N.W.2d at 66. The employee argued that the attorney's fees constituted "defense costs" under the PEPL fund's memorandum of coverage. Id. at 70. The Supreme Court of South Dakota disagreed, explaining that while the PEPL fund covered "defense costs," these defense costs had to be "generated by and related to *a claim*," which the memorandum of coverage defined as "any claim or suit for damages." Id. (cleaned up). The Supreme Court of South Dakota concluded that the employee could not recover attorney's fees for the declaratory judgment action because it was not a "claim or suit for damages." Id.

Liberty Mutual contends that Score "implie[s]" that the Supreme Court of South Dakota would hold that the costs of complying with an injunction do not constitute damages. Doc. 12 at 17. As the Sapienzas point out, however, Score was not a typical insurance case. Indeed, the PEPL fund "is not insurance" and state employees do not pay premiums for coverage or have a contractual relationship with the PEPL fund. Score, 658 N.W.2d at 69–70. Moreover, South Dakota's insurance code does not apply to the PEPL fund because subjecting the fund to these "duties and obligations" would "adversely affect the [fund's] ability to provide members cost-effective liability coverage . . . ." Id. at 69 (citation omitted).

Beyond these differences, Score did not consider whether costs associated with an injunction can constitute damages, but only decided that a declaratory judgment action brought to determine the existence of coverage was not a "claim or suit for damages." Thus, while Score may provide some limited insight into how the Supreme Court of South Dakota would rule on the coverage issue here, it is far from controlling or conclusive.

Dan Nelson provides even less insight into how the Supreme Court of South Dakota would decide the issue in this case. The issue in Dan Nelson was whether a petition filed against the plaintiffs by the Iowa Attorney General constituted a civil "suit" for "damages" such that the insurer had a duty to defend. The policy in Dan Nelson defined "damages" as "amounts awardable by a court of law," and its definition of "suit" specifically excluded "equitable actions." 2008 WL 170084, at *6. Relying on the nature of the petition along with the Iowa law on which it was based, this Court concluded that the petition was an equitable action even though one of the requests for relief in the petition was a judgment "for all amounts of money that individual consumers have a right to recover." Id. at *6–8. There is a "significant distinction," this Court explained, "between actions brought by individual consumers and an attorney general's petition alleging violations by Plaintiffs of the Iowa Consumer Fraud Act." Id. at *8. Dan Nelson is too different from this case to be controlling.

The closest this Court came to finding an authoritative South Dakota case is Taylor v. Imperial Casualty & Indemnity Co., 144 N.W.2d 856 (S.D. 1966). The plaintiffs in Taylor sued their insurer to recover expenses they had incurred to comply with an injunction. Id. at 858. These expenses included the cost of digging trenches to prevent gasoline from the plaintiffs' filling tanks from leaking into the surrounding streets and businesses. Id. The plaintiffs' insurance policy provided that the insurer would "pay on behalf of the insured all sums which the insured shall become legally obligated to pay as damages because of injury to or destruction of property, including the loss of use thereof, caused by accident." Id. at 857. The Supreme Court of South Dakota held that the plaintiffs could recover the cost of complying with the injunction without specifically addressing whether these costs constituted "damages" under the insurance policy. Id. at 858–59. Thus, Taylor suggests that the Supreme Court of South Dakota might treat

the costs of complying with an injunction as "damages," but it is not conclusive. The policy in Taylor had different coverage provisions and did not appear to exclude coverage for property damage to property owned by the insured.

A case decided last month by the Supreme Court of South Dakota suggests that the Court might give a technical meaning to a common word like "damages" in an insurance contract. In discussing the term "accident" in an insurance policy, the Supreme Court of South Dakota reasoned: "'Accident' is not defined by the policy. However, the term 'accident' in the insurance context has been commonly viewed as something that causes an 'unexpected' or 'unanticipated' injury or damage." Geidel v. De Smet Farm Mut. Ins. Co. of S.D., #28627, 2019 WL 1590978, at *4 (S.D. Apr. 10, 2019). Geidel is far from controlling here. "Property damage" is defined in the Liberty Mutual Policies, but the policies are silent as to coverage for an injury from complying with an injunction. Though the Policies exclude coverage for property damage to property owned by the insured, Docs. 1-2 at 20, 1-3 at 8, here the insureds were complying with an injunction designed to remedy damage inflicted on the McDowells. See Unigard Mut. Ins. v. McCarty's, Inc., 756 F. Supp. 1366, 1369 (D. Idaho 1988) (limiting application of a similar exclusion "when the insured becomes liable to third parties for events confined exclusively to the insureds' premises"); see also Aetna Ins. v. Aaron, 685 A.2d 858, 866–67 (Md. Ct. Spec. App. 1996).

This Court may certify a question of law to the Supreme Court of South Dakota "if there are questions of law of [the State of South Dakota] involved in any proceeding before the certifying court which may be determinative of the cause pending in the certifying court and it appears to the certifying court and to the Supreme Court [of South Dakota] that there is no controlling precedent in the decisions of the Supreme Court of this state." SDCL § 15-24A-1. It is a question of law whether the costs the Sapienzas incurred to comply with the injunction constitute covered "damages" under the Policies. The answer to this question will be determinative of the Sapienzas' claim that Liberty Mutual breached the insurance contract by refusing to indemnify them for these costs. It also appears that there are no controlling decisions by the Supreme Court of South Dakota on this question. This Court therefore will certify the following question to the Supreme Court of South Dakota: Do the costs incurred by the Sapienzas to comply with the injunction

constitute covered "damages" under the Policies such that Liberty Mutual must indemnify the Sapienzas for these costs?[2]

C. Counts 2 and 3: Bad Faith

The parties refer to Counts 2, 3, and 4 as the Sapienzas' "bad faith claims." The Sapienzas' complaint is not entirely clear about the basis for Counts 2 and 3. Count 2 alleges that Liberty Mutual breached the implied covenant of good faith and fair dealing by placing "its interests above the Sapienzas," engaging "in deceptive and bad faith conduct," withholding and misrepresenting information, acting "contrary to the Sapienzas' justified expectations," and engaging "in subterfuge and evasions." Doc. 1 at ¶ 38. Count 2 "repeat[s] and reallege[s] all of the preceding paragraphs of the Complaint," rather than identifying the particular facts on which the count is based. Count 3, entitled "Breach of Fiduciary Duty," is even more vague. It simply incorporates by reference all the preceding paragraphs, asserts that Liberty Mutual owed the Sapienzas a duty of equal consideration, and alleges that Liberty Mutual's "conduct as more fully described herein constitutes a breach of its fiduciary duties." Doc. 1 at ¶¶ 40–43.

The Sapienzas clarify in their brief that Counts 2 and 3 concern the defense they received in the McDowell lawsuit. Doc. 14 at 14–15. They argue that Liberty Mutual "hindered" their defense and that this constitutes bad faith and a failure to give their interests equal consideration. Doc. 14 at 14–15. As the Sapienzas tell it, this misconduct began once Liberty Mutual determined that it did not have to pay for the costs associated with injunctive relief. Doc. 14 at 14–15; see also Doc. 1 at ¶ 24 (alleging that the Sapienzas and Liberty Mutual had diverging interests once Liberty Mutual issued its denial letter). Liberty Mutual argues that these allegations fail to state a bad faith claim because there has been no breach of the insurance

[2]It is not entirely clear from the Sapienzas' brief and complaint whether they seek to recover not only the cost to demolish the house, but also to build it. The Sapienzas' complaint claims that they incurred in excess of $60,000 in demolition costs, yet generally allege damages of in excess of $75,000 without elaborating on what other damages are sought. Liberty Mutual thinks that the Sapienzas are trying to recover both the building and demolishing costs. See Doc. 12 at 15. If the Sapienzas are seeking to recover for the construction costs as well, that seems to be a novel issue of damages appropriate to address on certification. If the Sapienzas are not seeking benefits under the Policies exceeding demolition costs, then, in light of the failure to state other claims at this time, their case may belong in state court anyway as less than $75,000 exclusive of interest in costs would be at issue under 28 U.S.C. § 1332.

contract and because the Sapienzas have not adequately alleged that Liberty Mutual's conduct caused them damage. Liberty Mutual also argues that Counts 2, 3, and 4 should be treated as first-party bad faith claims rather than third-party claims.

South Dakota law recognizes both first and third-party bad faith claims. Hein v. Acuity, 731 N.W.2d 231, 235 (S.D. 2007). "Third-party bad faith is traditionally based on principles of negligence and arises when an insurer wrongfully refuses to settle a case brought against its insured by a third-party." Id. An insurer commits third-party bad faith when it breaches "its duty to give equal consideration to the interests of its insured when making a decision to settle a case." Id. First-party bad faith, in contrast, "is an intentional tort and typically occurs when an insurance company consciously engages in wrongdoing during its processing or paying of policy benefits to its insured." Id. The oft-repeated test for first-party bad faith claims requires the plaintiff to show "(1) an absence of a reasonable basis for denial of policy benefits, and (2) the insurer's knowledge of the lack of a reasonable basis for denial." Zochert v. Protective Life Ins. Co., 921 N.W.2d 479, 490 (S.D. 2018) (cleaned up and citation omitted). Despite the phrasing of this test, first-party bad faith "can extend to situations beyond mere denial of policy benefits." Dakota, Minn. & E. R.R. v. Acuity, 771 N.W.2d 623, 629 (S.D. 2009) (citation omitted). A first-party bad faith claim in South Dakota may be based on a "failure to comply with a duty under the insurance contract," but still must involve "an insurance company consciously [engaging] in wrongdoing." Id. (citation omitted).

Here, the Sapienzas allege that Liberty Mutual committed a tort by failing to give their interests equal consideration. Doc. 1 at ¶¶ 38, 41–42; Doc. 14 at 13–15. This duty of equal consideration, however, only applies to third-party bad faith claims, i.e. those arising in the settlement context. Indeed, the Supreme Court of South Dakota has always focused on an insurer's unreasonable refusal to settle a claim against its insured when discussing third-party bad faith. See Zochert, 921 N.W.2d at 489; Bertelsen v. Allstate Ins. Co., 796 N.W.2d 685, 700 (S.D. 2011) ("[T]hird party bad faith occurs when an insurer breaches its duty to give equal consideration to the interests of its insured when making a decision to settle a case brought against its insured by a third party." (citation and internal marks omitted)); Hein, 731 N.W.2d at 235 (explaining that third-party bad faith "arises when an insurer wrongfully refuses to settle a case brought

against its insured by a third-party"). And the Court recently explained in Zochert that while it had "recognized a *tort* duty of equal consideration in insurance bad faith cases dealing with the third-party claims process," it was not inclined to apply this duty "outside of the realm of third-party bad faith tort litigation." 921 N.W.2d at 489. According to the Supreme Court of South Dakota, requiring equal consideration in the first-party context—where the insurer does not act like a fiduciary as it does when considering whether to settle a claim by a third party against its insured— "could fundamentally alter the rights and obligations of insureds and insurers contained in the express contractual provisions of the policy." Id. at 489–90. Relying on Zochert, this Court predicted that the Supreme Court of South Dakota would hold that there is no duty of equal consideration in the first-party bad faith context. Lead GHR Enters., Inc. v. Am. States Ins., Civ. 16-5026-JLV, 2019 WL 918253, at *13 (D.S.D. Feb. 25, 2019).

The Sapienzas' claim that Liberty Mutual committed bad faith by "hindering" their defense does not arise in the settlement context and is not a third-party claim. As such, the Sapienzas must satisfy the two-prong test that applies to first-party bad faith claims rather than the "equal consideration" test used in the third-party context.[3] See Restatement of the Law of Liability Insurance § 24 cmts. a, c (explaining that the Restatement limits the equal consideration standard to situations where the insurer has made an unreasonable settlement decision); Stephen S. Ashley, Bad Faith Actions Liability & Damages § 3:1 (updated Sept. 2018) ("An insurer's bad faith refusal to defend involves the denial of a benefit that the policy expressly promises to the insured. One ought, therefore, to determine whether a refusal to defend constitutes bad faith according to first-party bad faith standards . . . ."); William T. Barker & Ronald D. Kent, New Appleman Insurance Bad Faith Litigation, Second Ed., § 17.03 (Matthew Bender, Rev. Ed.)

[3]This Court is treating Counts 2 and 3 as one bad faith claim concerning the alleged inadequate defense the Sapienzas received. Count 3 alleges that Liberty Mutual breached the duty of equal consideration, a duty that does not apply to the Sapienzas' claim. Doc. 1 at ¶ 41. Although Count 3 is entitled "Breach of Fiduciary Duty," the Sapienzas have not adequately plead (and their brief has not addressed) the elements of breach of fiduciary duty. See Chem-Age Indus., Inc. v. Glover, 652 N.W.2d 756, 772 (S.D. 2002) (listing elements of breach of a fiduciary and describing the type of relationship that is necessary to support a fiduciary duty); see also Haanen v. N. Star Mut. Ins., 1:16-CV-01007-CBK, 2016 WL 6237806, at *3 (D.S.D. Oct. 25, 2016) (holding that a "separate tort action for the breach of a fiduciary duty is not recognized in South Dakota when the case involves first party insurance coverage").

("Bad faith breach of the duty to defend is actionable, but under the same standards as delay or denial of any other first-party benefit.").

The Sapienzas cannot meet the first-party bad faith test for essentially the same reasons why they failed to state a claim for breach of the duty to defend. Many of the allegations in the Sapienzas' complaint lack sufficient detail to support the reasonable inference that Liberty Mutual breached any duty it owed to the Sapienzas. In particular, these allegations fail to link Liberty Mutual's conduct to the supposedly deficient defense the Sapienzas received. And other allegations, such as the allegation that Liberty Mutual failed to hire an expert, do not adequately allege that Liberty Mutual's misconduct caused the Sapienzas damages. The Sapienzas' bad faith claim based on Liberty Mutual "hindering" their defense is dismissed for failure to state a claim.

D. Count 4: Bad Faith

Count 4 of the Sapienzas' complaint alleges that Liberty Mutual engaged in bad faith because it did not have a reasonable basis for refusing to indemnify them for damages caused by the McDowell law suit. Doc. 1 at ¶¶ 45–48. To succeed on this first-party bad faith claim, the Sapienzas must show that: (1) Liberty Mutual lacked a reasonable basis for refusing to indemnify them and (2) Liberty Mutual knew of, or recklessly disregarded, the lack of a reasonable basis for this refusal. Zochert, 921 N.W.2d at 490; see also S.D. Network LLC v. Twin City Fire Ins. Co., 4:16-CV-04031-KES, 2017 WL 4233019, at *8–9 (D.S.D. Sept. 22, 2017) (applying this test to a claim that a liability insurer had committed bad faith by refusing to defend and indemnify the insured). An insurer has a reasonable basis for denying benefits if the claim is "fairly debatable" in fact or law. Dakota, Minn. & E. R.R., 771 N.W.2d at 630.

Liberty Mutual's decision that the costs of complying with the McDowell lawsuit do not constitute "damages" under the Policies is fairly debatable under the law. As explained above, this Court is certifying a question to the Supreme Court of South Dakota because there are no controlling cases concerning whether expenses associated with an injunction qualify as damages in the insurance context. Moreover, cases on this issue from some other jurisdictions support Liberty Mutual's decision to deny coverage to the Sapienzas. See Ellett Bros., 275 F.3d at 388 (holding that the costs of complying with an injunction do not

constitute damages); Hanna, 224 F.2d at 503 (same); O'Brien, 653 N.E. 2d at 960 (same); Ladd, 391 N.E. 2d at 571–73 (same). Although the Sapienzas cited cases adopting a broader view of damages, these cases merely show that there is a split of authority on the issue, not that Liberty Mutual lacked a reasonable basis for its decision. Indeed, the cases the parties cite provide good arguments both for and against concluding that the costs of complying with an injunction constitute damages recoverable under the Policies.

The Sapienzas contend that it would be premature to dismiss Count 4 because "there is no information in the record regarding Liberty Mutual's investigation of the claim," and such information "is essential to the inquiry into whether or not" Liberty Mutual had a reasonable basis to deny coverage. Doc. 14 at 14. But this Court does not need to know about Liberty Mutual's investigation to conclude that it did not act in bad faith in declining to pay for costs to remove the home. After all, there is no dispute that the state court awarded the McDowells only injunctive relief and did not require the Sapienzas to pay the McDowells any monetary damages. And whether this injunctive relief constituted "damages" under the Policies is a legal question rather than a factual one. Thus, even if Liberty Mutual's investigation somehow was inadequate, it would still have a reasonable basis under South Dakota law for denying coverage for costs the Sapienzas incurred in complying with the injunction. See Anderson v. W. Nat'l Mut. Ins. Co., 857 F. Supp. 2d 896, 905 (D.S.D. 2012) ("[A] failure to investigate, without more, does not constitute bad faith."); 14 Lee R. Russ & Thomas F. Segalla, Couch on Insurance § 207:25 (3d ed. 2011) ("An imperfect investigation, standing alone, is not sufficient cause for recovery where the insurer, in fact, has objectively reasonable basis to deny coverage."). Count 4 of the Sapienzas' complaint is dismissed for failure to state a claim.

IV. Conclusion

For the reasons stated above, it is hereby

ORDERED that Liberty Mutual's Motion to Dismiss, Doc. 9, is granted in part and denied in part, in that the Sapienzas' claims that Liberty Mutual breached the insurance contract by refusing to indemnify them and providing them with an inadequate defense may survive Liberty Mutual's motion to dismiss. If the Sapienzas do not amend their claim that Liberty Mutual breached the insurance contract by providing

them with an inadequate defense within fourteen days, this claim will be dismissed for failure to state a claim. The Sapienzas' bad faith claims—Counts 2, 3, and 4—are dismissed for failure to state a claim. It is further

ORDERED that under SDCL § 15-24A-1, this Court certifies the following question to the Supreme Court of South Dakota:

> Do the costs incurred by the Sapienzas to comply with the injunction constitute covered "damages" under the Policies such that Liberty Mutual must indemnify the Sapienzas for these costs?

It is further

ORDERED that the Clerk of Court shall forward this certification order under official seal to the Supreme Court of South Dakota, under SDCL § 15-24A-5. It is further

ORDERED that this case will be stayed (other than the possible motion to amend the complaint and ruling thereon) while the certified question is pending before the Supreme Court of South Dakota.

DATED this 17th day of May, 2019.

BY THE COURT:

/s/ Roberto A. Lange

ROBERTO A. LANGE
UNITED STATES DISTRICT JUDGE

STATE OF SOUTH DAKOTA) :ss	IN CIRCUIT COURT
COUNTY OF MINNEHAHA)	SECOND JUDICIAL CIRCUIT
PIERCE McDOWELL and BARBARA McDOWELL, Plaintiffs, vs. JOSEPH SAPIENZA, SARAH JONES SAPIENZA, M.D. and CITY OF SIOUX FALLS, Defendants.	CIV. #15-1320 **ORDER**

This matter came before the Court on March 2, 2018 upon the Plaintiffs' Motion to Enforce Injunctive Relief and Judgment. Defendants Joseph and Sarah Sapienza appeared through their counsel, Richard L. Travis. The City of Sioux Falls appeared through its counsel, William C. Garry. The Plaintiffs appeared through their counsel, Scott A. Abdallah and Sara E. Show, and Plaintiff Barbara McDowell appeared personally. The parties also having submitted written argument to the Court. NOW, THEREFORE, the Court having reviewed its memorandum decision dated December 27, 2016, which the South Dakota Supreme Court unanimously upheld in its decision dated January 3, 2018, and having reviewed the arguments of counsel and the record in this matter, it is hereby

ORDERED:

(1) That Defendants Joseph and Sarah Jones Sapienza, M.D. have six (6) weeks from March 2, 2018 to submit renovation plans to the Historic Board of Preservation;

(2) That such renovation plans shall be submitted with a copy of the regulations found in ARSD 24:52:07:04;

(3) That such renovation plans shall be for renovations that will bring the home in conformance with all the requirements in ARSD 24:52:07:04 and with this Court's memorandum decision; and

(4) If plans are not approved rectifying the violations set forth in the Court's memorandum decision, the Court will exercise all remedies available consistent with the judgement of the court.

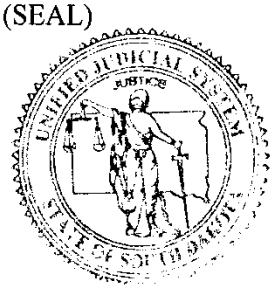
Dated this 7 day of March, 2018.

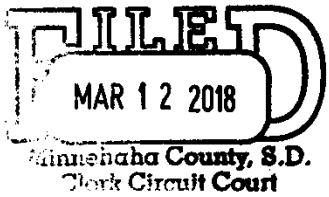
BY THE COURT:

JOHN PEKAS
CIRCUIT COURT JUDGE

Attest: Angelia M. Gries

Clerk of Courts
(SEAL)





STATE OF SOUTH DAKOTA :ss COUNTY OF MINNEHAHA	))	IN CIRCUIT COURT SECOND JUDICIAL CIRCUIT
PIERCE McDOWELL and BARBARA McDOWELL, Plaintiffs, vs. JOSEPH SAPIENZA and SARAH JONES SAPIENZA, M.D., Defendants.		CIV. #15-1320 **WRIT OF EXECUTION**

The Court having entered its Judgment in this matter on March 17, 2017, and said Judgment having been affirmed unanimously by the South Dakota Supreme Court on January 3, 2018, and the Defendants having been ordered to submit an application to the Board of Historic Preservation of the City of Sioux Falls to cure and remedy the violations found with regard to their home at 1323 South Second Avenue in the City of Sioux falls, State of South Dakota, and the Board of Historic Preservation having unanimously found that the home violates the terms of the Judgment of South Dakota law as it does not remedy or correct the violations of the aforesaid, and the Judgment having been final, the Court, pursuant to SDCL 15-18-1, *et seq.*, hereby issues this Writ of Execution to the Sheriff of Minnehaha County to remove said home if the same has not been removed from thirty days from the date of this Writ; and it is further determined by this Court that the Supersedeas Bond of the Defendants dated July 27, 2017, is hereby forfeited and the funds of the same shall be utilized by the sheriff to remove said home if it is not removed in accordance with this Writ and that any remaining funds shall be transmitted to the Plaintiffs in this case.

Dated this 17 day of May, 2018.

FILED
MAY 17 2018
Minnehaha County, S.D.
Clerk Circuit Court

BY THE COURT:

JOHN PEKAS
CIRCUIT COURT JUDGE

ATTEST:

Clerk of Courts
(SEAL)

IN THE SUPREME COURT
OF THE
STATE OF SOUTH DAKOTA
* * * *

JOSEPH SAPIENZA and SARAH JONES SAPIENZA, M.D., Plaintiffs, vs. LIBERTY MUTUAL FIRE INSURANCE COMPANY, Defendant.	ORDER ACCEPTING CERTIFICATION #29000

The United States District Court, District of South Dakota, Central Division having pursuant to the provisions of SDCL Ch. 15-24A, certified questions of South Dakota law, sua sponte, to this Court for determination, said question being set out as follows:

> Do the costs incurred by the Sapienzas to comply with the injunction constitute covered "damages" under the Policies such that Liberty Mutual must indemnify the Sapienzas for these costs?

and the Court having considered the certification order of said Federal Court, now therefore,

IT IS ORDERED that the Court will accept such certification.

IT IS FURTHER ORDERED that the order for transcript, if any, be made upon receipt of this order and the schedule for briefing follow the schedule set forth in SDCL 15-24A-7. The Court designates Plaintiffs to file the first brief.

IT IS FURTHER ORDERED that the original or copies of the record before the certifying court be filed with this Court pursuant to SDCL 15-24A-5.

DATED at Pierre, South Dakota this 7th day of June, 2019.

BY THE COURT:

David Gilbertson, Chief Justice

ATTEST:

Clerk of the Supreme Court
(SEAL)

PARTICIPATING: Chief Justice David Gilbertson, Justices Janine M. Kern, Steven R. Jensen, Mark E. Salter and Patricia J. DeVaney.

IN THE SUPREME COURT
OF THE
STATE OF SOUTH DAKOTA

APPEAL NO. 29000

JOSEPH SAPIENZA and SARAH JONES SAPIENZA, M.D.,

Plaintiffs,

vs.

LIBERTY MUTUAL INSURANCE COMPANY,

Defendant.

CERTIFICATION OF QUESTION FROM THE UNITED STATES DISTRICT COURT,
DISTRICT OF SOUTH DAKOTA, CENTRAL DIVISION

THE HONORABLE ROBERTO A. LANGE,
UNITED STATES DISTRICT JUDGE

BRIEF OF DEFENDANT LIBERTY MUTUAL INSURANCE COMPANY

Jack H. Hieb
Richardson, Wyly, Wise, Sauck
& Hieb, LLC
P.O. Box 1030
Aberdeen, SD 57402-1030
Phone: 605-225-6310

Christian A. Preus, Pro Hac Vice
BASSFORD REMELE, P.A.
100 South 5th Street, Suite 1500
Minneapolis, MN 55402-1254
Phone: 612-333-3000

Attorneys for Defendant Liberty Mutual Insurance Company

Angela Beranek Brandt
Larson, King, LLP
30 East Seventh Street, Ste. 2800
St. Paul, MN 55101
Phone: 651-312-6500

Attorneys for Plaintiffs Joseph Sapienza and Sarah Jones Sapienza, M.D.

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Page

Federal Cases

State Cases

State Statutes

Federal Rules

State Regulations

Other Authorities

JURISDICTIONAL STATEMENT

This Court has jurisdiction to accept a certified question from a United States district court under SDCL § 15-24A-1.

STATEMENT OF LEGAL ISSUE

This Court has accepted the following certified question from the United States District Court, District of South Dakota, Central Division:

> Do the costs incurred by the Sapienzas to comply with the injunction constitute covered "damages" under the Policies such that Liberty Mutual must indemnify the Sapienzas for these costs?

STATEMENT OF THE CASE

This is an insurance coverage case. Sapienzas commenced this action on September 7, 2018, in United States District Court for the District of South Dakota seeking to compel Liberty Mutual to pay for costs they incurred to remove their house in the McKennan Park Historic District of Sioux Falls after they failed to correct violations of building code regulations. The Sapienzas' Complaint alleges breach of contract, including breach of the duty to defend and breach of the duty to indemnify. Sapienzas also alleged breach of the duty of good faith and fair dealing, breach of fiduciary duty, and bad faith.

On October 2, 2018, Liberty Mutual moved to dismiss the Sapienzas' Complaint for failure to state a claim upon which relief can be granted, pursuant to Fed. R. Civ. P. 12(b)(6). On May 17, 2019, the District Court, the Honorable Judge Roberto A. Lange, granted in part and denied in part Liberty Mutual's motion to dismiss. With respect to Liberty Mutual's alleged breach of the duty to

indemnify, the District Court certified to this Court the question presented above. On June 7, 2019, this Court issued its Order Accepting Certification of the question presented by the District Court.

STATEMENT OF THE FACTS

Sapienzas seek indemnity coverage under the *liability sections* of the insurance policies issued by Liberty Mutual for the costs they incurred in removing the house they built in the McKennan Park Historic District of Sioux Falls.

A. Sapienzas' house.

Sapienzas allege they moved to Sioux Falls, South Dakota in 2012, and in 2013 purchased a home in the McKennan Park Historic District of Sioux Falls. (DR 1, at 2, ¶¶ 5-6).[1] They tore down the existing house on the property and planned to build a new house. (*Id*. at 3, ¶ 7). They hired an architect to design the house, and submitted a proposal to the Sioux Falls Board of Historical Preservation. (*Id*. at 3, ¶ 9). They then hired a contractor to build the house. (*Id*. at 3-4, ¶ 10).

Pierce and Barbara McDowell lived adjacent to the lot on which Sapienzas were building the house. As construction progressed, McDowells became increasingly concerned about the proximity and size of Sapienzas' house.

---

[1] Consistent with the Sapienzas Brief, references to the District Court record are denoted by "DR" followed by the docket number and page and references to the Appendix are denoted by "APP" and the corresponding page number.

McDowell v. Sapienza, 2018 S.D. 1, ¶ 7, 906 N.W.2d 399. In May, 2015, after requesting an inspection of their chimney, McDowells were informed by the fire inspector that they could no longer use their fireplace. *Id*. at ¶ 8. The fire inspector noted City ordinance requirements regarding chimneys required them to extend at least two feet above the highest point in any structure located within ten horizontal feet of the chimney and McDowells' use of the chimney would violate the ordinance because of the newly constructed Sapienza home. *Id*. Four days later, on May 8, 2015, McDowells' attorney sent Sapienzas a letter demanding that they cease and desist construction of their house or face legal action. *Id*. at ¶ 9. Sapienzas did not stop construction. *Id*. On May 15, 2015, McDowells initiated their lawsuit against Sapienzas. Sapienzas continued their construction of the house until it was complete in January, 2016. *Id*.

B. McDowell lawsuit.

On May 15, 2015, McDowells initiated a lawsuit against Sapienzas in the Circuit Court, Second Judicial District. The McDowells' complaint advanced three counts against Sapienzas. (DR 1-1, at 2-3, ¶¶ 4-7). Count 1 sought "*Permanent Injunctive Relief*," and specifically sought "a permanent injunction prohibiting further construction inside or outside the Sapienzas' residence until the residence is brought into compliance with the 2013 Shape Places Zoning Ordinance of the City of Sioux Falls and until the home is relocated in such a fashion as to not cause the McDowell home to violate the Residential Code." (DR 1-1, at 6, ¶ 31).

Count 2, entitled "*Negligence*," also sought a permanent injunction, and alternatively sought damages. (*Id*. at 7, ¶ 39). The alleged damages included McDowells' access to natural sunlight that had been significantly blocked, the quiet enjoyment of their property, a decline in the value of their property, and that "they can no longer use their wood fireplace." (*Id*. at 7, ¶ 38).

Count 3 alleged "*Nuisance*," and, similar to Counts 1 and 2, sought an injunction and damages, alleging the same damages as alleged in Count 2, including that they were prevented "from using their wood fireplace." (*Id*. at 8, ¶ 43).

At trial of McDowells' lawsuit, the circuit court, the Honorable John Ryan Pekas, bifurcated the issues and first considered McDowells' claim for injunctive relief. (DR 1-6, at 6-7, ¶ 11, DR 1-4, at 25). After a three-day trial, the circuit court "issued a lengthy memorandum decision indicating it would grant a mandatory injunction requiring Sapienzas to modify their home to comply with the State regulation for historic districts. Sapienzas were also required to modify their home so McDowells could use their fireplace." *McDowell v. Sapienza*, at ¶ 11. The circuit court order specifically held that "the McDowells are entitled to injunctive relief that the Sapienzas must bring their residence into compliance with the Administrative Rules of South Dakota 24:52:07:04 and Secretary of the Interior Regulations regarding the requirements for new construction in historic districts … or rebuild it." (DR 1-4, at 29).

No damages were awarded to the McDowells. (*Id*.).

Sapienzas appealed to this Court, which affirmed the circuit court order granting injunctive relief in favor of McDowells and against Sapienzas. *McDowell v. Sapienza*, at ¶¶ 22, 31[2]. With respect to the relief awarded to McDowells, this Court held that "[p]ecuniary compensation would not provide adequate relief in this case." *Id*. at ¶ 24. This Court further noted that the "types of intangible harm" involved would not be rectified by pecuniary compensation and that because "pecuniary compensation would not afford an adequate relief here, the circuit court was statutorily authorized to issue an injunction." *Id*. This Court also specifically noted that the harm at issue was not limited to harm suffered by McDowells, but was harm to McKennan Park itself, which would not be remedied by payment of money to McDowells. *Id*. at ¶ 26.

This Court affirmed the circuit court order, resulting in a final judgment affording only injunctive relief to the McDowells. *Id*. at ¶ 31.

Sapienzas' Complaint alleges that the "Circuit Court also ordered the Sapienzas to forfeit the appeal bond and the funds be used by the Sheriff to remove the home or transmitted to the McDowells if the home was demolished by the Sapienzas." (DR 1, at 8, ¶ 29). Sapienzas' Complaint fails to note that the circuit court reversed itself and issued an order on August 24, 2018 granting the Sapienzas' Motion for Release of Supersedeas Bond and ordering that "the funds

---

[2] This Court reversed the circuit court, to the extent that it held that Sapienzas had violated a set-back requirement relating to the height of chimneys, agreeing with Sapienzas that their home was not cited in violation of the chimney regulation. (*Id*. at ¶¶ 36-40).

securing said bond, shall be released back to Defendants Joseph Sapienza and Sara Jones Sapienza, M.D." (DR 11-4 at 1).

C. Defense of the McDowell lawsuit and notice to Liberty Mutual.

After being served with the McDowells' complaint on May 13, 2015, Sapienzas retained attorney Richard Travis of May & Johnson, P.C., of Sioux Falls, who filed an Answer on behalf of Sapienzas on June 12, 2015. (DR 11-1). On behalf of Sapienzas, Mr. Travis stipulated to a scheduling order. (DR 11-2). He also was served with amended deposition notices of Sapienzas, scheduling their depositions for July 22, 2015. (DR 11-3).

Sapienzas first gave notice of the McDowells' lawsuit to Liberty Mutual on August 24, 2015. (DR 1-5, at 3). Liberty Mutual agreed to provide a defense to Sapienzas and issued a reservation of rights letter dated November 30, 2015. (DR 1-5, at 2). Instead of retaining panel counsel, Liberty Mutual agreed to allow Sapienzas' retained counsel to continue to represent them and Mr. Travis represented them at the trial before the circuit court (DR 1-4, at 2) and in the appeal to this Court. (DR 1-6, at 2).

Following the issuance of the circuit court's Memorandum Decision and Order, Liberty Mutual provided Sapienzas with an updated coverage position in a letter dated March 7, 2017. (DR 1-5). Liberty Mutual stated to Sapienzas that it would "continue to provide a defense ..., including any appeal of the court's Memorandum Decision and Order." (*Id*. at 1). Liberty Mutual also explained that the insurance policies issued to Sapienzas would "provide no coverage related for

(sic) the injunctive relief set forth in that order." Liberty Mutual continued to maintain a reservation of rights as explained in the letter. (*Id*.) Liberty Mutual's letter identified the specific insurance policy language at issue, discussed the factual background and decision of the circuit court, and explained that injunctive relief does not constitute damages as that term is used in the insurance policies. (*Id*. at 3-8). The letter also attached a copy of certain pages of the insurance policies (*Id*. at 10-27).[3]

D. Insurance policies.

Liberty Mutual issued two insurance policies to Sapienzas, a Homeowners Policy (DR 1, at 4, ¶ 12; DR 1-2) and an Excess Policy (DR 1, at 5, ¶ 15; DR 1-3).

The Homeowners Policy provides, in relevant part:

SECTION II – LIABILITY COVERAGES

COVERAGE E – Personal Liability

> If a claim is made or a suit is brought against an "insured" for damages because of "bodily injury" or "property damage" caused by an "occurrence" to which this coverage applies, we will:
>
> 1. Pay up to our limit of liability for the damages for which the "insured" is legally liable. Damages include prejudgment interest awarded against the "insured"; and
>
> 2. Provide a defense at our expense by counsel of our choice, even if the suit is groundless, false or fraudulent. We may investigate and settle any claim or suit that we decide is appropriate. Our duty to settle or defend ends when the

[3] The copy of Liberty Mutual's March 7, 2017 letter (DR 1-2) attached to Sapienzas' Complaint is complete, but the pages are out of order. Pages 4, 5, 6, and 7 are in reverse order.

amount we pay for damages resulting from the "occurrence" equals our limit of liability.

(DR 1-2, at 18).

DEFINITIONS

* * *

6. "Property damage" means physical injury, to, destruction of, or loss of use of tangible property.

(DR 1-2, at 8).

The Excess Policy provides, in relevant part:

I. DEFINITIONS

* * *

7. "property damage" means: (a) injury to or destruction of tangible property; (b) injury to intangible property sustained by an organization as the result of false eviction, malicious prosecution, libel, slander or defamation.

* * *

II. COVERAGE – PERSONAL EXCESS LIABILITY

We will pay all sums in excess of the **retained limit** and up to our limit of liability for damages because of **personal injury** or **property damage** to which this policy applies and for which the **insured** is legally liable.

(DR 1-3, at 6, 7).

STANDARD OF REVIEW

In analyzing questions certified to it by the federal district court, the South Dakota Supreme Court employs "the same legal standards … that [it uses] when reviewing appellate cases." *In re Certification of a Question of Law from U.S.*

Dist. Court, Dist. of S. Dakota, S. Div., 2014 S.D. 57, ¶ 7, 851 N.W.2d 924, 926. This is true even though the Court "[t]echnically … does not sit as an appellate court" in such cases. *Id.*

The certified question involves interpretation of an insurance policy. "Insurance contract interpretation is a question of law reviewed de novo." *Batiz v. Fire Ins. Exch*., 2011 S.D. 35, ¶ 10, 800 N.W.2d 726, 728.

ARGUMENT

A. Rules of construction and interpretation of insurance policies.

The foundation of insurance coverage analysis involves construction and interpretation of insurance policies. The rules of construction and interpretation of insurance policies are well-established both by statute and common law.

An insurance policy is a contract. *See Fedderson v. Columbia Ins. Grp*., 2012 S.D. 90, ¶ 6, 824 N.W.2d 793, 795, quoting *State Farm Fire & Cas. Co. v. Harbert*, 2007 S.D. 107, ¶ 17, 741 N.W.2d 228, 234. ("The insured's 'rights and obligations' under the 'insurance contract are determined by the language of the contract.'") *See also Ass Kickin Ranch, LLC v. N. Star Mut. Ins. Co*., 2012 S.D. 73, ¶ 9, 822 N.W.2d 724, 727 ("[T]he scope of coverage of an insurance policy is determined from the contractual intent and the objectives of the parties *as expressed in the contract*.") (emphasis added).

Interpretation of insurance contracts is further codified by statute:

> Every insurance contract shall be construed according to the entirety of its terms and conditions as set forth in the policy and as amplified,

> extended, or modified by any rider, endorsement, or application lawfully made a part of the policy.

SDCL § 58-11-39. Application of the statute means that when a term is not expressly defined, the court first looks to see if its "meaning can be determined by reviewing the policy language as a whole." *Zochert v. Nat'l Farmers Union Prop. & Cas. Co.*, 1998 S.D. 34, ¶¶ 6-7, 576 N.W.2d 531, 532. *See also Hemmer–Miller Dev. Co. v. Hudson Ins. Co.*, 59 S.D. 129, 133, 238 N.W. 342, 343 (1931). ("[A]ll the provisions of the policy must be considered and construed together, and the intention ascertained from the language of the policy alone, if possible.")

In considering the provisions of the policy, "[w]e ascribe to contract language plain and ordinary meaning." *Opperman v. Heritage Mut. Ins. Co.*, 1997 S.D. 85, ¶ 4, 566 N.W.2d 487, 490. But the "plain and ordinary" meaning is *not* determined by isolating certain words to examine every possible definition:

> To understand their meanings, these terms ought to be measured with their companions: … Under the canon of *noscitur a sociis*, words take import from each other. … This maxim of interpretation is "wisely applied where a word [or phrase] is capable of many meanings in order to avoid the giving of unintended breadth" to contract provisions.

Id. at ¶¶ 6, 7, citing *Jarecki v. G. D. Searle & Co.*, 367 U.S. 303, 307, 81 S. Ct. 1579, 1582, 6 L. Ed. 2d 859, 862–63 (1961) (other citations omitted). In *Opperman*, for example, the court determined the meaning of the terms "process" and "warehouse" by applying their "common, industry usage" rather than the expansive number of different possible dictionary definitions. *Id.*

Moreover, it is long-established law that the plain and ordinary meaning rule does not permit courts to engage in "forced construction, or to make a new contract for the parties." *Stene v. State Farm Mut. Auto. Ins. Co*., 1998 S.D. 95, ¶ 14, 583 N.W.2d 399, 402, quoting *St. Paul Fire & Marine Ins. v. Schilling*, 520 N.W.2d 884, 887 (S.D. 1994). "Insurance contracts warrant reasonable interpretation, in the context of the risks insured, without stretching terminology." *Opperman*, 1997 SD 85 at ¶ 4, citing *State Farm Mut. Auto. Ins. Co. v. Vostad*, 520 N.W.2d 273, 275 (S.D. 1994). "Essentially, this means that when the terms of an insurance policy are unambiguous, these terms cannot be enlarged or diminished by judicial construction." *Am. Family Mut. Ins. Co. v. Elliot*, 523 N.W.2d 100, 102 (S.D. 1994).

"Ambiguity in an insurance policy is determined with reference to the policy as a whole and the plain meaning and effect of its words." *Batiz v. Fire Ins. Exch*., 2011 S.D. 35, ¶ 10, 800 N.W.2d 726, 729 (citation omitted). Ambiguity exists "when application of rules of interpretation leave a genuine uncertainty as to which of two or more meanings is correct." *Standard Fire Ins. Co. v. Cont'l Res., Inc.*, 2017 S.D. 41, ¶ 13, 898 N.W.2d 734, 738 (citation omitted). Ambiguity in a policy "must be construed most strongly against the insurer and in favor of the insured." *Wilson v. Allstate Ins. Co*., 85 S.D. 553, 557, 186 N.W.2d 879, 881 (1971). But the uncertainty must be real and not manufactured or contrived: "insurance policies must be subject to a reasonable interpretation and not one that amounts to an absurdity." *Vostad*, 520 N.W.2d at 275. *See also Prokop v. N. Star*

Mut. Ins. Co., 457 N.W.2d 862, 864 (S.D. 1990) (courts are to look to the "natural and obvious import of the language, without resorting to subtle and forced construction for the purpose of either limiting or extending their operation.") The fact that the parties differ as to the contract's interpretation does not create an ambiguity. *Zochert v. Nat'l Farmers Union Prop. & Cas. Co.*, 1998 S.D. 34, ¶ 5, 576 N.W.2d 531, 532. "Rather, a contract is ambiguous only when it is capable of more than one meaning when viewed objectively by a reasonably intelligent person who has examined the context of the entire integrated agreement." *Coffey v. Coffey*, 2016 S.D. 96, ¶ 9, 888 N.W.2d 805, 809.

Finally, Sapienzas seek indemnity coverage under the liability coverage section in their Homeowners Policy; they are not seeking first-party property coverage. (*See* Brief of Plaintiffs Joseph Sapienza and Sarah Jones Sapienza, M.D. at pp. 7, 12). This liability coverage is separate and distinct from first-party property insurance for damage to a homeowners' own property.

> It is necessary to keep in mind the basic distinction between liability insurance and property insurance. Property insurance generally insures against specified risks or damage to property owned by, or placed in the care or custody of, the insured. *Liability insurance, in contrast, covers the liability of the insured for property damage to property that is not owned by, or in the care or custody of, the insured*. In fact, this requirement of nonownership is often expressly stated in the policy.

Property damage; nonowned property, 12 *Couch on Ins.* § 172:26 (emphasis added).[4]

B. Insurance policy language – applying the rules of construction and interpretation.

The Sapienzas' Homeowners Policy states in the Insuring Agreement that coverage is provided for a suit "*brought against an 'insured' for damages because of … 'property damage'* caused by an 'occurrence' to which this insurance applies, …." (DR 1-2, at 18) (emphasis added). The Insuring Agreement also provides that Liberty Mutual will pay up to its limit of liability "*for the damages* for which the 'insured' is legally liable." (*Id*).[5] Further "[d]amages include prejudgment interest *awarded against the 'insured.'*" (*Id*.).

Thus, for a claim to fall within the scope of the Insuring Agreement, the claim must be "brought against an 'insured.'" Further, the claim against the insured must be "for damages because of … 'property damage.'" If there is a claim against an insured for "damages because of … 'property damage,'" then Liberty Mutual will pay "for the damages" up to the limit of liability. By using the definite article "the" to modify "damages" in subparagraph 1 of the Insuring

---

[4] Consistent with the explanation in *Couch*, both the Homeowners Policy and the Excess Policy exclude coverage for damage to property owned by the insured. (DR 1-2, at p. 20; DR 1-3, at p. 8).

[5] The Insuring Agreement of the Excess Policy issued by Liberty Mutual to Sapienzas, which applies in excess of the Homeowners Policy, similarly applies to "liability for damages because of … **property damage** to which this policy applies and for which the **insured** is legally liable." (DR 1-3, at 7).

Agreement, "the damages" necessarily refers to the "damages because of … 'property damage'" referenced in the immediately-preceding sentence of the Insuring Agreement. Accordingly, "the damages" covered under the Insuring Agreement are the damages because of property damage alleged in the claim "against an 'insured.'" "The damages" are the damages of the plaintiff for which the insured is legally liable.

That is the nature of liability coverage – to pay the damages to another party for which the insured is legally liable, subject to other provisions in the insurance policy.

McDowells' complaint alleged, in part, that because of the location and height of Sapienzas house, McDowells "can no longer use their wood fireplace." (DR 1-1, at 7, ¶ 38). The term "property damage" is defined to include "loss of use of tangible property." (DR 1-2, at p. 8). Thus, the McDowells' complaint included allegations "against [Sapienzas] for damages because of … 'property damage' …" to McDowells' house.

Because the McDowells' complaint alleged that McDowells suffered "damages because of … 'property damage' …," the Insuring Agreement of the Homeowners Policy was satisfied. For this reason, Liberty Mutual agreed to provide a defense to Sapienzas against the McDowells' lawsuit.

The McDowells' lawsuit also, alternatively, sought a temporary and permanent injunction. Indeed, the injunctive relief was the primary relief sought by McDowells in their lawsuit. Count 1 of the McDowells' complaint sought

"*Permanent Injunctive Relief*," "prohibiting further construction inside or outside the Sapienzas' residence until the residence is brought into compliance with the 2013 Shape Places Zoning Ordinance of the City of Sioux Falls and until the home is relocated …." No damages are sought in Count 1. (DR 1-1 at 6, ¶ 31). Count 2 of the McDowells' complaint also sought a permanent injunction, and sought damages alternatively. (*Id*. at 7, ¶ 39). Count 3 also sought an injunction, and alternatively damages. (*Id*. at 8, ¶ 43).

As the McDowells' lawsuit proceeded, it became clear the sole relief sought was injunctive relief. The McDowells did not seek any award of damages at trial and the circuit court did not award damages. (DR 1-4, at 29). On appeal, this Court did not address issues of damages, but instead considered whether the injunctive relief granted by the circuit court was authorized and within the discretion of the circuit court. *McDowell v. Sapienza*, at ¶¶ 23-31. Accordingly, once this Court issued its Opinion on January 3, 2018, the possibility of damages being awarded in favor of McDowells and against Sapienzas was no longer a part of the lawsuit. The case was purely one of injunctive relief. [6]

---

[6] There is an important distinction between an insurer's *duty to defend* and its *duty to indemnify* under a liability policy, which applies here. An insurer's duty to defend and its duty to indemnify are separate and independent duties. *North Star Mut. Ins. v. Korzan, et al*., 2015 S.D. 97, ¶ 15, 873 N.W.2d 57 (2015). "Importantly, '[a]n insurer's duty to defend is distinct from–and broader than–its duty to indemnify.'" *Geidel v. De Smet Farm Mut. Ins. Co. of South Dakota,* 2019 S.D. 20, ¶ 8, ___ N.W.2d ___, quoting *Lowry Construction & Concrete, LLC v. Owners Ins. Co.*, 2017 S.D. 53 ¶ 8, 901 N.W.2d 481. The duty to defend need only arguably appear on the face of the pleadings. *Demaray v. De Smet Farm*

The award of injunctive relief is not an award "for damages because of … 'property damage'" as required by the Insuring Agreement of the Homeowners Policy and Excess Policy. There were no damages awarded to McDowells because of property damage to their home. Instead, the relief McDowells pursued and awarded in the lawsuit was for injunctive relief. The injunctive relief did not result in any damage award to McDowells because of any property damage to McDowells' property. Instead, McDowells sought, and the circuit court granted, "a mandatory injunction requiring Sapienzas to modify their home to comply with the State regulation for historic districts. Sapienzas also were required to modify their home so that McDowells could use their fireplace." *McDowell v. Sapienza*, at ¶ 11. Thus, Sapienzas did not become legally liable for damages to McDowells because of property damage. Instead, the Sapienzas were required to make modifications to their own property.

By characterizing the term "damages" as including injunctive relief and resulting costs, Sapienzas are asking this Court to "indulge in forced construction, or to make a new contract for the parties." *Hemmer-Miller Dev. Co. v. Hudson*

Mut. Ins. Co., 2011 S.D. 39, 801 N.W.2d 284 at ¶ 8. If even one claim is covered by the policy, an insurer must defend. *Korzan, et al.*, at ¶ 15. The duty to indemnify, however, "arises only on a showing that the insured contingency occurred." *St. Paul Fire and Marine Ins. Co. v. Engleman*, 2002 S.D. 8, at ¶ 8, 639 N.W.2d 192. Thus, while Liberty Mutual had a *duty to defend* Sapienzas because of the possibility that coverage could exist based on allegations in McDowells' complaint, Liberty Mutual had no *duty to indemnify*, because the relief ultimately awarded did not constitute "damages" for which the insured was legally liable as required by the insuring agreements of the insurance policies.

Ins. Co. of New York, 59 S.D. 129, 131, 238 N.W. 342 (1931). Sapienzas' effort to enlarge the scope of the Insuring Agreement, and particularly the meaning of the word "damages" and the context in which it is used throughout the insurance contracts, is not a reasonable interpretation of the policy language, and accordingly must be rejected. *Opperman v. Heritage Mut. Ins. Co.*, 1997 S.D. 85, ¶ 4, 566 N.W.2d 487.

C. South Dakota law regarding damages.

"The sole object of compensatory damages is to make the ***injured party*** whole." *Hulstein v. Meilman Food Indus., Inc.*, 293 N.W.2d 889, 891 (S.D. 1980) (emphasis added), citing *Ralston Purina Co. v. Jungers*, 86 S.D. 583, 588, 199 N.W.2d 600, 604 (1972). Although this Court has not yet directly addressed the specific issue of whether costs associated with injunctive relief can constitute "damages" under a liability insurance policy, this Court has addressed analogous circumstances. *Public Entity Pool for Liability (PEPL) v. Score, et al.*, 2003 S.D. 17, 658 N.W.2d 64 (2003). In *Score*, two state employees, who had been sued for negligence, sought payment from the Public Entity Pool for Liability (PEPL fund) for attorney's fees and costs incurred in defending the liability lawsuit against them. The PEPL fund brought a declaratory action seeking a declaration it had no obligation to defend the employees in the liability lawsuit. *Id.* at ¶ 3. The employees argued that, in addition to providing coverage for their legal expenses incurred in the liability lawsuit, the PEPL fund's Memorandum of Liability Coverage applied to the "defense costs" incurred in the declaratory judgment

action. *Id*. This Court rejected this argument, noting that the defense obligation under the Memorandum provided that the "defense costs" must be "generated by and related to … a claim." This Court noted that the Memorandum provided that the PEPL fund would "defend any claim or suit for damages …." A "claim or suit for damages" did not include a suit for declaratory judgment. *Id*. at ¶ 14.

Although the PEPL fund is not an insurance policy, it has been characterized as a self-insurance pool. *Id*. at ¶ 10. Further, similar to an insurance policy, the agreement is interpreted according to the rules of contract law that rely on the intent of the parties and the contract itself. *Id*. at ¶ 13. Thus, the reasoning and holding in *Score* apply to the case at hand, supporting the conclusion that a claim for injunctive relief is not a claim "for damages."

Similarly, in *Dan Nelson Automotive Group, Inc. et al v. Universal Underwriters Group*, 2008 WL 170084 (D. S.D.), the court addressed the issue of whether an Attorney General's petition for equitable relief constituted a civil action for damages. After considering caselaw from various other jurisdictions, the court held that there is a significant distinction between an action brought by an individual consumer for damages and an attorney general's petition seeking equitable relief. The court specifically rejected the argument that the potential of a money judgment in the form of restitution or disgorgement constituted a suit for damages. *Id*. at 7-8, *citing City of Fort Pierre v. United Fire and Casualty Company*, 463 N.W.2d 845, 848 (S.D. 1990) (civil penalties prayed for by federal

government for intentionally violating Clean Water Act were punitive in nature and did not constitute a suit for damages requiring insurer to defend).

Further, whether a claim for injunctive relief constitutes a claim for damages was directly addressed by the court in *Headley v. St. Paul Fire & Marine Ins. Co.*:

> The Headleys' claim against Midland for injunctive relief pursuant to SDCL 34A–10 is not covered under any policy of insurance issued to Midland by St. Paul. St. Paul is not obligated to defend Midland against any such claim, as it is not for a sum of money which Midland may be obligated to pay under the terms of the policy's coverage.

712 F. Supp. 745, 749 (D. S.D. 1989). The language of the St. Paul insurance policy at issue in *Headley* is described as applying to all sums the insured "was legally obligated to pay as damages arising out of bodily injury or property damage," and as such is fundamentally the same as the language in the Insuring Agreement of the Homeowners Policy and Excess Policy.

The reasoning of this Court in *Score*, along with the holdings in *Dan Nelson Automotive Group* and *Headley* lead to the conclusion that injunctive relief and associated costs do not fall within the Insuring Agreement of the Homeowners Policy or the Excess Policy. Sapienzas advocate an unreasonable and overbroad interpretation of the term "damages" that fails to consider these cases and improperly applies or disregards the basic rules of construction and interpretation that this Court has consistently applied to insurance policies.

D. Case law from other jurisdictions overwhelmingly holds that the term "damages" in a liability insurance policy does not include injunctive relief.

A substantial majority of courts have held that injunctive relief – outside the environmental clean-up context – does not constitute "damages" as the term is used in an insuring agreement in a liability insurance policy.[7]

---

[7] *See, e.g.*, Windt, Allan D., "Duty to defend administrative proceeding or suit seeking injunctive relief," 1 *Insurance Claims and Disputes* § 4:16 (6th ed.) ("Apart from the context of pollution claims, courts have, in general, held that the cost of compliance with an injunction is not regarded as a sum payable as damages.") *See also O'Brien and Associates, PC v. Tim Thompson, Inc.*, 247 Ill. App. 3d 472, 653 N.E.2d 956 (1995) (lawsuit seeking injunction requiring insureds to alternatively, reconstruct the house or pay off the mortgage plus interest and fees, could not be characterized as seeking "damages"); *Nationwide Ins. Co. v. King*, 673 F. Supp. 384, 387 (S.D. Cal. 1987) (injunction requesting injunctive relief from homeowners' association restriction on window air conditioners not compensatory damages); *State Farm Fire and Cas. Co. v. Nat'l Research Ctr. for College and University*, 445 F.3d 1100 (8th Cir. 2006) (order that insured stop making misrepresentations and make clear and conspicuous disclosures did not constitute "damages" under liability policy); *City of Thief River Falls v. United Fire and Casualty Co.*, 336 N.W.2d 274 (Minn. 1983) (liability policy providing coverage for "damages" did not apply to suit seeking to compel initiation of condemnation proceedings); *Ellett Bros., Inc. v. United States Fidelity and Guarantee Co.*, 275 F.3d 384, 387 (4th Cir. 2001) *cert denied* 123 S. Ct. 94 (2002) (proposed fund to monitor gun dealers was "forward-looking, prospective relief— not compensation for past injuries" and therefore was not covered "damages"); *Fallon McElligott, Inc. v. Seaboard Sur. Co.*, 607 N.W.2d 801, 805 (Minn. Ct. App. 2000) (no duty to defend suit seeking injunctive relief for copyright infringement in absence of claim for damages); *Bullock v. Maryland Casualty Company*, 85 Cal. App. 4th 1435, 102 Cal. Rptr.2d 804 (2001) ("[W]hile an [injunctive] order compelling compliance with [an ordinance] might be 'mitigative' in some broad societal sense, the mitigation would be prophylactic, not remedial, and thus outside the zone of coverage."); *Seaboard Sur. Co. v. Ralph Williams' Nw. Chrysler Plymouth, Inc*., 81 Wash. 2d 740, 747, 504 P.2d 1139, 1143 (1973) (suit by attorney general for injunctive relief rather than "redress for private individuals" did not seek damages); *Green v. Heritage Mut. Ins. Co.*, 655 N.W.2d 147, 153 (Wis. App. 2002); (Equitable relief, in the form of an injunction

> In common usage, the plural noun "damages" has a specific meaning in a legal context, such as here, where a "legal obligation" is involved. The Oxford English Dictionary defines "damages," when used in "law," as "[t]he value, estimated in money, of something lost or withheld; the sum of money claimed or adjudged ***to be paid in compensation*** for loss or injury sustained." .... Similarly, Black's Law Dictionary defines the term as "[m]oney claimed by, or ordered to be paid to, a person ***as compensation*** for loss or injury." ... Therefore, paying a sum as "damages" pursuant to a legal obligation is not equivalent to paying any sum that is legally owed or legally required to be paid. Rather, "damages" has a more specific meaning, indicating ***a sum that is claimed by another***, or ordered to be paid, as remediation for something lost or as compensation for injury.

Elec. Motor & Contracting Co., Inc. v. Travelers Indem. Co. of Am., 235 F. Supp. 3d 781, 789 (E.D. Va. 2017) (emphasis added; internal citations omitted). *See also Patrons Oxford Mut. Ins. Co. v. Marois,* 573 A.2d 16 (Me. 1990) ("The word 'damages' is not ambiguous in the insurance context. Black letter insurance law holds that claims for equitable relief are not claims for 'damages' under the liability insurance contracts"); *Jones v. Farm Bureau Mut. Ins. Co*., 172 Mich. App. 24, 29, 431 N.W.2d 242, 245 (1988) (suit seeking "abatement of a nuisance" was for injunctive relief only, and did not constitute "sums which the insured shall become legally obligated to pay as damages"); *Harris Corp. v. Travelers Indem.*

---

or otherwise, does not constitute "damages" within the meaning of an insurance policy providing liability coverage.)*; Moore v. State Farm Mut. Auto. Ins. Co*., 520 F. Supp. 2d 815, 826 (E.D. La. 2007) (no coverage for injunctive relief sought by insurance company against agent "[b]ecause the plain language of the … policy provides coverage only for 'sums which the Insured shall become legally obligated to pay as damages"); *State Farm Fire & Cas. Co. v. Metro. Mgmt*., No. 1:07CV00176HGKSC, 2007 WL 4157148, at *11 (D. Haw. Nov. 23, 2007) (relief sought included order to terminate management contract and turn over records; this was equitable relief for which coverage was not available).

Co., No. 96-166-CIV-ORL-19A, 1998 WL 1657171, at *7 (M.D. Fla. Mar. 19, 1998) ("the phrase 'for damages' must be read to modify the phrase 'all sums.' Otherwise, the phrase 'for damages' would be rendered meaningless"). Under a "plain, ordinary and popular meaning" analysis,

> we cannot agree with the plaintiff that words and phrases such as "in law", "in equity", "legally", and "damages" are so confusing and ultra-technical as to defy understanding and interpretation by those who have need for policies of insurance such as the one issued in the instant case.

Ladd Const. Co. v. Insurance Co. of N. Am., 391 N.E. 2d 568, 573-74 (Ill. App. 1979). [8]

Even when the term "damages" could conceivably be ambiguous, courts do not automatically hold that injunctive relief constitutes "damages." *See Cutler-Orosi United School District v. Tulare County School District Liability/Property Self Insurance Authority, et al,* 31 Cal. App. 4th 617, 630, 37 Cal. Rptr. 2d 106, 113 (1995) (injunctive relief outside the environmental clean-up context is traditionally "prospective and prophylactic," and construing "damages to include

---

[8] *See also, Pennsylvania County Risk Pool, et al v. Northland Ins.*, 2009 WL 506369 (M.D. Penn.) (in the context of insurance policy interpretation, claims for declaratory relief, injunctive relief, and restitution do not constitute claims for monetary damages, citing *Bowen v. Massachusetts*, 487 U.S. 879, 893 (1988)); *Feed Store, Inc. v. Reliance Ins. Co.*, 774 S.W.2d 73, 75 (Tex. App. 1989), writ denied (Oct. 25, 1989) (where complaint alleged a tort but did not specifically request money damages, prayer for "such other and further relief" did not constitute suit for damages, also citing *Bowen v. Massachusetts*, 487 U.S. at 893 (1988)).

such costs would effectively strike the 'as damages' qualification from the policy language").

Indeed, the requirement to pay for "damages" "is a far cry from the cost to unsuccessful litigants of complying with an injunctive decree." *Aetna Cas. & Sur. Co. v. Hanna*, 224 F.2d 499, 503 (5th Cir. 1955) In *Hanna*, the insured was ordered to remove "fill dirt, rocks and boulders" that were encroaching on neighboring land, and to "build a bulkhead or other effective restraining wall" to prevent future encroachment. *Id.* at 501. The initial suit against the insureds did not seek damages, although damages were sought later for noncompliance with the injunction (although they were not granted because the insured eventually complied). The Fifth Circuit held that the insured's liability insurance "clearly … covers only payments to third persons," and did not provide coverage "against mandatory injunctive orders;" noting that to hold that coverage existed would "wholly ignore large portions of the context in which words are used." *Id. See also Maryland Cup Corp. v. Employers Mut. Liab. Ins. Co. of Wisconsin*, 81 Md. App. 518, 526, 568 A.2d 1129, 1133 (1990), citing *Desrochers v. New York Cas. Co.*, 99 N.H. 129, 106 A.2d 196, 198 (1954) (noting that a significant number of cases hold that damages have "an accepted technical meaning in law" as recompense to third parties for "injuries sustained" and holding that cost of compliance with an injunction does not constitute damages.)

Further, the possibility that monetary damages could have been awarded by a court through its inherent power to award damages not otherwise sought does

not create liability coverage for an award of injunctive relief. For example, in *General Star Indemnity Co. v. Lake Bluff School District No. 65*, the Appellate Court of Illinois considered whether the insurer had a duty to defend against a family's federal court lawsuit seeking to place their disabled child in a regular education classroom and reimburse their costs for medical evaluations and other educational services. The insurer and school district filed cross-motions for declaratory judgment as to the insurer's duty to defend against the parents' lawsuit (which was ultimately unsuccessful). *Lake Bluff Sch. Dist. No. 65*, 354 Ill. App. 3d 118, 120, 819 N.E.2d 784, 787 (2004). The court held that the relief sought by the parents did not constitute compensatory damages:

> The crux of the…analysis is that it would be improper to speculate as to whether a court would award monetary damages where none were sought. To do so in this case would alter the parties' responsibilities under the insurance contract by rendering almost meaningless the policy provision requiring that the suit seek "damages" from the insured. The underlying complaint's general prayer for relief is not a request for monetary damages, and we may not speculate whether the federal court would have awarded such damages absent such a request.

Id. at 123–24, 790. *See also Morgan, Lewis & Bockius LLP v. Hanover Ins. Co., 929 F. Supp. 764, 773 (D.N.J. 1996)* (Where "all claims for money damages" were dismissed prior to trial, and the "sole issue tried … related to injunctive relief," the insurer should not have been responsible for fees and costs for trial); *see also York Golf & Tennis Club v. Tudor Ins. Co.*, 2004 ME 52, 845 A.2d 1173, 1177 (potential for damages not sufficient to create duty to defend).

E. Environmental insurance coverage claims.

Some courts have distinguished environmental contamination claims from the widely-held rule that injunctive relief does not constitute "damages" under a liability insurance policy.[9] In the environmental contamination context, some courts have held that distinguishing compensatory damages from payments made as part of equitable relief is not so simple, particularly where the injured party could have done the work itself and then sued for monetary damages. *See, e.g.*, *Coakley v. Maine Bonding & Cas. Co.*, 136 N.H. 402, 414, 618 A.2d 777, 784 (1992); *New Castle Cty. v. Hartford Acc. & Indem. Co*., 673 F. Supp. 1359, 1366 (D. Del. 1987) ("This interpretation of the word "damages" finds support in cases that consider cleanup costs due to pollution.") (collecting cases). *See also Utica Mut. Ins. Co. v. Bausch & Lomb, Inc.*, 91 Md. App. 1, 11, 603 A.2d 1241, 1246 (1992), *aff'd in part, modified in part*, 330 Md. 758, 625 A.2d 1021 (1993) ("There is a considerable body of case law in federal as well as in state courts on the question as to whether cleanup costs are damages covered by a CGL policy.") (collecting cases).

The reason environmental cases are different is that the "statutory schemes designed for environmental protection have a unique nature that blurs the

---

[9] With respect to environmental contamination claims, "Courts are by no means uniform in the resolution of this dispute." *Aetna Cas. and Sur. Co., Inc. v. Pintlar Corp.*, 948 F.2d 1507, 1511 (9th Cir. 1991) (listing cases). *See also*, *Patrons Oxford Mutual Insurance Company v. Marois*, 573 A.2d 16 (Me. 1990) (listing cases and concluding insured's expense to clean up groundwater contaminated by leaking gas tanks not liability for damages).

distinction between monetary compensation and the expenditure of money to comply with a mandatory injunction." *Gen. Star Indemn. Co. v. Lake Bluff Sch. Dist. No. 65*, 354 Ill. App. 3d 118, 126, 819 N.E.2d 784, 792 (2004). Thus, the "costs of complying with an injunction are considered 'damages' only in special situations, such as the environmental litigation …." *Id*. at 124. In the environmental contamination context, claims are asserted against an insured for payment of cleanup costs for property damage to another party's property. *Aetna Cas. and Sur. Co., Inc. v. Pintlar Corp.*, 948 F.2d 1507, 1514 (9th Cir. 1991). Sapienzas are not seeking coverage for environmental contamination. And more fundamentally, they are not seeking coverage for damage to another party's property. No damages were awarded in favor of McDowells to pay for any damage to the McDowells' property; to the contrary, the relief granted was that Sapienzas were to bring their house into compliance with applicable building code regulations or remove the house.

All the cases relied upon by the Sapienzas to support their contention that "damages" include injunctive relief, except one,[10] are environmental cleanup

---

[10] The non-environmental case cited by Sapienzas is *Liberty Mut. Ins. Co. v. Those Certain Underwriters at Lloyds*, 650 F. Supp. 1553, 1560 (W.D. Pa. 1987), which has no application to this case. At issue in *Liberty Mutual v. Lloyds* was whether back pay (in the form of money) awarded to an employment discrimination plaintiff constituted damages or equitable relief. The language of the insuring agreement at issue was much broader than the language at issue here, providing coverage for "damages, direct or consequential, and expenses, all as more fully defined by the term 'ultimate net loss' on account of (1) personal injuries." *Id.* Sapienzas' Homeowners Policy and Excess Policy involves more-typical narrower

cases: *See Outboard Marine Corp. v. Liberty Mut. Ins. Co.*, 154 Ill. 2d 90, 607 N.E.2d 1204, 1216 (1992) (polluted water cleanup involving CERCLA claims); *Minnesota Min. & Mfg. Co. v. Travelers Indem. Co.*, 457 N.W.2d 175 (Minn. 1990) (claim under Minnesota Environmental Response and Liability Act); *Aetna Cas. & Sur. Co. v. Pintlar Corp.*, 948 F.2d 1507, 1513 (9th Cir. 1991) (CERCLA response costs); *Helena Chem. Co. v. Allianz Underwriters Ins. Co.*, 357 S.C. 631, 594 S.E.2d 455 (2004) (cleanup of soil polluted by chemicals as required under the Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA)); *Farmland Indus., Inc. v. Republic Ins. Co.*, 941 S.W.2d 505 (Mo. 1997) (environmental response costs under CERCLA and state statute); *Lindsay Mfg. Co. v. Hartford Acc. & Indem. Co.*, 118 F.3d 1263 (8th Cir. 1997) (cleanup of contaminated aquifer under CERCLA and Nebraska Environmental Protection Act).

Significantly, jurisdictions relied upon by Sapienzas that have addressed the issue, have also held – in non-environmental cases – that injunctive relief does not constitute "damages" under a liability insurance policy. Sapienzas ignore this case law.

Sapienzas rely upon the Illinois case *Outboard Marine Corp. v. Liberty Mut. Ins. Co.*, 154 Ill. 2d 90, 607 N.E.2d 1204, 1216 (1992). But they fail to

---

language providing coverage "for damages because of … 'property damage" caused by an 'occurrence' …." *Liberty Mutual v. Lloyds* does not support Sapienzas' contention that the costs to remove their house constitute damages covered under the Insuring Agreements of Sapienzas' policies.

acknowledge that Illinois courts have held and continue to hold – outside the environmental cleanup context – that injunctive relief does not constitute damages. *See Ladd Const. Co. v. Insurance Co. of N. Am.*, 391 N.E. 2d 568, 573-74 (Ill. App. 1979); *O'Brien & Assocs., P.C. v. Tim Thompson, Inc*., 274 Ill. App. 3d 472, 478, 653 N.E.2d 956, 960 (1995) (noting "the unique nature of environmental statutes" and distinguishing *Outboard Marine*); *Illinois State Bar Ass'n Mut. Ins. Co. v. Burkart*, 2015 IL App (4th) 140936-U, ¶ 66.

Similarly, Sapienzas rely upon the Minnesota case *Minnesota Min. & Mfg. Co. v. Travelers Indem. Co*., 457 N.W.2d 175 (Minn. 1990). But they fail to note that Minnesota courts also have repeatedly held in non-environmental cases that equitable or injunctive relief is not "damages." *See, e.g., Kroschel v. City of Afton*, 524 N.W.2d 719 (Minn. 1994) (claims for declaratory relief and civil penalty were not claims seeking "damages"); *City of Maple Lake v. Am. States Ins. Co*., 509 N.W.2d 399 (Minn. Ct. App. 1993) (condemnation proceeding for taking lakefront property is not action for "damages"); *Gen. Cas. Co. of Ill. v. Four Seasons Greetings*, No. A04-518, 2004 WL 2987796, at *12 (Minn. Ct. App. Dec. 28, 2004) ("no duty to defend claims for injunctive relief, unless the possibility of damages also exists"); *Fallon McElligott, Inc. v. Seaboard Sur. Co.*, 607 N.W.2d 801, 805 (Minn. Ct. App. 2000) (same). *See also TJB Companies, Inc. v. Maryland Cas. Co.,* 504 N.W.2d 476, 477 (Minn. 1993) ("The remedies of rescission and damages are mutually exclusive, and to characterize [rescission of a real estate contract] as a 'near equivalent' of damages is not only to rewrite the

policy and alter the insuring intent, but also to change the long-standing meaning of rescission in Minnesota.") Sapienzas also ignore that the Minnesota Supreme Court in *Minnesota Mining* distinguished other Minnesota cases seeking relief other than damages. In particular, the court discussed *City of Thief River Falls v. United Fire & Cas. Co*., 336 N.W.2d 274 (Minn. 1983), in which it was held that a writ of mandamus was not an action seeking "damages." 475 N.W.2d at 179. Accordingly, in *City of Thief River Falls* no indemnity coverage was available, because the money paid "was not paid to compensate the claimant for injury." *Id*.

CONCLUSION

The vast majority of courts that have addressed the issue – outside the environmental contamination context – have held that injunctive relief does not constitute "damages" as that term is used in the insuring agreement of a liability insurance policy. This conclusion is consistent with the insurance policy language and properly applies the basic rules of insurance contract construction and interpretation.

Liberty Mutual requests this Court answer the certified question in the negative and hold that the costs incurred by Sapienzas to comply with the injunction do not constitute covered "damages" under the insurance policies issued by Liberty Mutual to Sapienzas.

Dated this 26th day of July, 2019.

RICHARDSON, WYLY, WISE, SAUCK & HIEB, LLP

By: /s/ Jack H. Hieb

1 Court Street
Aberdeen, SD 57402-1030
Telephone: (605) 225-6310
jhieb@rwwsh.com

and

BASSFORD REMELE, *A Professional Association*

Christian A. Preus, Pro Hac Vice
100 South Fifth Street, Suite 1500
Minneapolis, Minnesota 55402-1254
Telephone: (612) 333-3000
cpreus@bassford.com
Attorneys for Defendant Liberty Mutual Fire Insurance Company

CERTIFICATE OF COMPLIANCE

The undersigned hereby certifies that this Brief complies with SDCL 15-26A-66(4). This Brief is 30 pages long, exclusive of the Table of Contents, Table of Authorities, Certificate of Compliance and Certificate of Service, is typeset in Times New Roman (12 pt.) and contains 7,935 words. The word processing software used to prepare this Brief is Microsoft Word.

Dated this 26th day of July, 2019.

RICHARDSON, WYLY, WISE, SAUCK & HIEB, LLP

By: /s/ Jack H. Hieb

1 Court Street
Aberdeen, SD 57402-1030
Telephone: (605) 225-6310
jhieb@rwwsh.com

CERTIFICATE OF SERVICE

The undersigned, one of the attorneys for Defendant Liberty Mutual Fire Insurance Company, hereby certifies that on the 26th day of July, 2019, a true and correct copy of BRIEF OF DEFENDANT LIBERTY MUTUAL FIRE INSURANCE COMPANY was transmitted via electronic mail to:

Ms. Angela Beranek Brandt
Ms. Caryn A. Boisen
Larson King
ABrandt@LarsonKing.com
CBoisen@LarsonKing.com

Mr. Robert C. Riter
Riter, Rogers, Wattier & Northrup
R.Riter@RiterLaw.com

and the original and two copies were mailed by first-class mail, postage prepaid, to Ms. Shirley Jameson-Fergel, Clerk of the Supreme Court, Supreme Court of South Dakota, State Capitol Building, 500 East Capitol Avenue, Pierre, SD 57501-5070. An electronic version of the Brief was also electronically transmitted in Microsoft Word format to the Clerk of the Supreme Court.

Dated this 26th day of July, 2019.

RICHARDSON, WYLY, WISE, SAUCK & HIEB, LLP

By: /s/ Jack H. Hieb

1 Court Street
Aberdeen, SD 57402-1030
Telephone: (605) 225-6310
jhieb@rwwsh.com

IN THE SUPREME COURT
OF THE
STATE OF SOUTH DAKOTA

APPEAL NO. 29000

JOSEPH SAPIENZA and SARAH JONES SAPIENZA, M.D.

Plaintiffs,

vs.

LIBERTY MUTUAL INSURANCE COMPANY,

Defendant.

CERTIFICATION OF QUESTION FROM THE UNITED STATES DISTRICT COURT,
DISTRICT OF SOUTH DAKOTA, CENTRAL DIVISION

THE HONORABLE ROBERTO A. LANGE,
UNITED STATES DISTRICT JUDGE

AMICUS CURIAE BRIEF OF COMPLEX INSURANCE CLAIMS LITIGATION ASSOCIATION and NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

Laura A. Foggan, Pro Hac Vice
Crowell & Moring LLP
1001 Pennsylvania Ave. NW
Washington, DC 20004
Phone: 202-624-2774

Robert C. Riter
Riter, Rogers, Wattier &
Northrup, LLP
319 S. Coteau – P.O. Box 280
Pierre, SD 57501-0280
Phone: 605-224-5825

Attorneys for the Complex Insurance Claims Litigation Association & National Association of Mutual Insurance Companies

Jack H. Hieb
Richardson, Wyly, Wise,
Sauck & Hieb, LLC
P.O. Box 1030
Aberdeen, SD 57402-1030
Phone: 605-225-6310

Christian A. Preus, Pro Hac Vice
Bassford Remele, P.A.
100 South 5th Street, Suite 1500
Minneapolis, MN 55402-1254
Phone: 612-333-3000

Attorneys for Defendant Liberty Mutual Insurance Company

(Continued on next page)

Angela Beranek Brandt
Larson, King, LLP
30 East Seventh Street, Ste. 2800
St. Paul, MN 55101
Phone: 651-312-6500

Attorneys for Plaintiffs Joseph Sapienza
And Sarah Jones Sapienza, M.D.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Other Authorities

JURISDICTIONAL STATEMENT

This Court has jurisdiction to accept a certified question from a United States district court under SDCL § 15-24A-1.

STATEMENT OF THE ISSUE PRESENTED

On May 17, 2019, the United States District Court for the District of South Dakota certified the following question to the Supreme Court of South Dakota:

> Do the costs incurred by the Sapienzas to comply with the injunction constitute covered "damages" under the Policies, such that Liberty Mutual must indemnify the Sapienzas for these costs?

This Court accepted the Certified Question on June 7, 2019. CICLA and NAMIC submit that the Court should answer this question in the negative.

STATEMENT OF THE CASE AND FACTS

CICLA and NAMIC incorporate by reference the statements of the case and facts set forth in Defendant Liberty Mutual Insurance Company's brief.

STANDARD OF REVIEW

The South Dakota Supreme Court applies the same standard of review to certified question cases as it does to appellate cases. *In re Certification of a Question of Law from U.S. Dist. Court, Dist. Of SD, S. Div.*, 2014 S.D. 57, ¶ 7, 851 N.W.2d 924, 926.

INTEREST OF AMICUS CURIAE

The Complex Insurance Claims Litigation Association ("CICLA") is a trade association of major property and casualty insurance companies. CICLA's member companies have entered into insurance contracts in South Dakota and throughout the nation containing provisions similar or identical to those at issue in this appeal. Therefore, CICLA is vitally interested in the judicial interpretation of these coverage provisions and, because of its members' extensive experience, can provide a unique

perspective on the issues presented. CICLA believes the proper interpretation of insurance contracts serves the public interest, as well as that of policyholders and insurers.

The National Association of Mutual Insurance Companies ("NAMIC") is the oldest property/casualty insurance trade association in the country, with more than 1,400-member companies representing 41 percent of the total market. NAMIC supports regional and local mutual insurance companies on main streets across America and many of the country's largest national insurers. NAMIC member companies serve more than 170 million policyholders and write more than $253 billion in annual premiums. Members account for 54 percent of homeowners, 43 percent of automobile, and 35 percent of the business insurance markets. Through NAMIC's advocacy programs, it promotes public policy solutions that benefit NAMIC member companies and the policyholders they serve.

ARGUMENT

The Court should answer the certified question in the negative. Liberty Mutual Insurance Company's ("Liberty Mutual's") liability insurance policies, subject to their terms, conditions, limitations, and exclusions, covered "damages" because of "bodily injury" or "property damage," not orders of specific injunctive relief such as that granted in this matter. Liberty Mutual issued primary and excess homeowners' liability coverage to the Sapienzas. The primary policy provides, in relevant part:

> If a claim is made or a suit is brought against an "insured" *for damages* because of 'bodily injury' or 'property damage' caused by an 'occurrence' to which this coverage applies, we will:
>
> > 1. Pay up to our limit of liability for the *damages* for which the "insured" is legally liable. Damages include prejudgment interest awarded against the "insured."

(emphasis added). The excess policy provides, in pertinent part:

> We will pay all sums in excess of the retained limit and up to our limit of liability *for damages* because of personal injury or property damage to which this policy applies and for which the insured is legally liable.

(emphasis added).

The specific injunction entered against the Sapienzas plainly does not constitute covered "damages" under the plain language of the policies. The Sapienzas were ordered to "bring their residence into compliance with the Administrative Rules of South Dakota and Secretary of the Interior Regulations regarding the requirements for new construction…or rebuild it." [DR at 90.] "Damages" means compensatory damages a court awards for bodily injury or property damage to third parties. As later discussed herein, courts have uniformly agreed that this accepted, legal meaning of the term "damages" does not encompass injunctive relief, or costs of complying with injunctive relief, that are not compensatory awards of damages to third parties. If the insurance contract were intended to impose the obligation now urged by the Sapienzas, it could easily have substituted broader language, or omitted the term "damages." It did not, and the specification of coverage for damages because of "bodily injury" or "property damage" is the crux of such liability insurance: it protects insureds from traditional tort liability awards compensating third parties for their injuries.

The Sapienzas' costs to comply with equitable injunctive relief requiring them to bring their home into compliance with applicable regulations or rebuild it are not "damages" in any sense of that term. The costs incurred to demolish the home did not compensate the Sapienzas' neighbors for past injuries; it was not money awarded to their

neighbors at all.[1] Rather, the costs were expended to comply with specific relief ordered to correct the Sapienzas' own noncompliance with applicable law in the construction of their home. This relief is not covered by the Liberty Mutual policies.

If liability insurers were required to indemnify policyholders for this type of injunctive relief, they would be subject to speculative, open-ended liabilities that would upset the predictability and risk-evaluation necessary for sound underwriting practices. The approach urged by the Sapienzas is so sweeping that it could extend liability insurance to virtually all costs of complying with regulations — since the avoidance of possible injury is surely a consistent objective and result of all such actions. Moreover, as in most such situations, there is no nexus between the cost of correcting the Sapienzas' violation of historic district construction rules and the measurement of harm to their neighbors. Recognizing all of these considerations, courts have long held that "damages" under third-party liability insurance does not encompass specific injunctive relief or other non-damages remedies. This Court should affirm that same conclusion under South Dakota law.

I. Under the plain language of the insurance policies and long-established law, insurance contracts covering suits for "damages" do not afford coverage for other forms of relief such as equitable injunctions.

Liberty Mutual agreed in its policies, subject to its terms and conditions, to pay up to the limits of liability "for *damages* for which the 'insured' is legally liable." (emphasis

[1] In fact, in affirming the award of injunctive relief, this Court noted that an award of damages would not provide adequate relief for the harm to the neighbors and the McKennen Park District from the construction of a home more than eight feet taller than permitted by regulations governing construction in historic districts. The relief entered was not designed to estimate the monetary value of harm to any third party; it was an equitable remedy addressing the violation of the historic district regulations which protect not just the Sapienzas' immediate neighbors but also the character of the neighborhood.

added). This language both defines and circumscribes the insurer's potential obligation to the policyholder. The insurer only agrees to pay those sums owed by the policyholder as "damages" on account of legal liability to third-parties. The agreement does not extend to other, typically equitable, forms of relief. It does not encompass any and all obligations the policyholder may incur in any underlying suit. Rather, the insurer's agreement under the policy reflects the essential character of liability coverage for damages awarded to third parties, *i.e.*, covering damages at law awarded to third parties because of "property damage" or "bodily injury."

Here, in the neighbors' suit, this Court specifically found that monetary damages at law would be an inadequate remedy. Instead of a monetary award to the third-party plaintiffs, the Court affirmed the trial court's grant of equitable relief — an injunction directing the Sapienzas to bring their house into compliance with applicable regulations or rebuild it. On remand, the Sapienzas were ultimately directed to demolish their home because there was no plan to bring it within the historic district regulations. No legal damages were awarded, as no pecuniary compensation was paid to a third-person for his or her prior loss or injury. Under the clear policy terms, this kind of equitable relief does not constitute "damages" and, therefore, is not covered by the Liberty Mutual policies. Liberty Mutual did not undertake to protect the Sapienzas from their non-compliance with regulations.

A. "Damages" is a form of legal relief providing compensation for past harms; it does not encompass equitable, injunctive relief.

Under South Dakota law, an insurance policy's "language must be construed according to its plain meaning." *Northland Ins. Co. v. Zurich Am. Ins. Co.*, 2007 S.D. 126, ¶ 13, 743 N.W.2d 145, 148. While "[t]he language … is to be construed liberally in

favor of the insured," this rule of construction applies "only when the language of the contract is ambiguous." *Id*. Further, the rules of construction under South Dakota law do not mean "that the court may seek out a strained or unusual meaning for the benefit of the insured." *Olson v. U.S. Fidelity & Guar. Co.*, 1996 S.D. 66, ¶ 6. 549 N.W.2d 199, 200.[2] If a term is not ambiguous,[3] the court will interpret the term in accordance with its plain meaning. *See N. Star Mut. Ins. Co. v. Peterson*, 2008 S.D. 36, ¶ 10, 749 N.W.2d 528 (interpreting the term "auto accident" in auto liability policy in accordance with its plain meaning, even where the parties disagreed on the meaning, "without resorting to an ambiguity analysis").

Here, this Court must interpret "damages" in accordance with its plain meaning and effect, considering its common usage in insurance policies of the kind at issue. Although courts elsewhere have long held that "damages" does not encompass specific injunctive relief, such as the order against the Sapienzas here, South Dakota has not ruled on this precise issue. South Dakota courts have held that suits for declaratory relief are not a claim or suit for damages, *see Public Entity Pool for Liability (PEPL) v. Score, et al.*, 2003 S.D. 17, 658 N.W.2d 64, and that an attorney general's petition for violation of

---

[2] Only where policy provisions "are fairly susceptible of different interpretations" will "the interpretation most favorable to the insured … be adopted." *Kremer v. Am. Family Mut. Ins. Co.*, 501 N.W.2d 765, 767-68 (S.D. 1993) (quoting *Prokop v. N. Star Mut. Ins. Co.*, 457 N.W.2d 862, 864 (S.D. 1990)).

[3] A term is not ambiguous just because it is not defined in the policy. *See N. Star Mut. Ins. Co. v. Peterson*, 2008 S.D. 36, ¶ 9, 749 N.W.2d 528. Rather, "[a]mbiguity is created when the language in an insurance contract is 'fairly susceptible to two constructions.'" *Id.* at ¶ 10 (quoting *Nat'l Sun Indus., Inc. v. South Dakota Farm Bureau Ins. Co.*, 1999 S.D. 63, ¶ 18, 596 N.W.2d 45). Whether a term is ambiguous is "determined with reference to the policy as a whole and the plain meaning and effect of its words." *Id.*; *see also McElgunn v. CUNA Mut. Group*, 2009 WL 1578481, at * 2 (D.S.D. May 29, 2009).

the Iowa Fraud Act was an action for equitable relief, not a civil petition for damages. *See Dan Nelson Auto. Group, Inc. et al v. Universal Underwriters Group*, 2008 WL 170084 (D. S.D. Jan 15, 2008). In another case involving an underlying claim for injunctive relief as well as damages, the Court did not address the meaning of the term "damages" in the policy. Rather, it determined whether leaks and the escape and seepage of gasoline were caused by an "accident" under the policy. *Taylor v. Imperial Cas. & Indem. Co.*, 82 S.D. 298, 304, 144 N.W.2d 856, 859 (1966). Thus, South Dakota precedent leaves the question before the Court unanswered, to be resolved by common usage, the policy itself, and South Dakota principles of interpretation.

"Damages" has a specific meaning in its general usage, which is reinforced in the context of liability insurance coverage.[4] It refers to a compensatory award to a third party for past injuries or wrongs. "Damages" is "the compensation for which the law will award for an injury done, … [i]n its common usage," it "is the estimated money equivalent for detriment or injury sustained." 25 C.J.S. *Damages* § 1 (1966 & Supp. 2001). Put differently, "damages" are a compensatory amount awarded to substitute for bodily injury or property damage that a third-party sustained. Equitable injunctive relief is completely different: the costs of such relief are *not* meant to equate to, or substitute for, a third party's past injury, because the relief is granted when an award of damages is inappropriate or unavailable — *i.e.*, there is no basis for compensating the purported injured party. *Travelers Ins. Co. v. Ross Elec. Of Washington, Inc.*, 685 F. Supp. 742, 744

[4] Here, the Liberty Mutual policies insure against "damages for which the 'insured' is legally liable" – making clear in context of the policy that what is insured against is third-party liability for "damages" in the legal sense of the term. If the terms in an insurance contract were not to be interpreted in their accepted, legal sense, then neither insurers nor insureds could reliably determine their respective rights and duties.

(W.D. Wash. 1988) ("Generally, '[o]ne of the essential functions of equity is to anticipate and prevent injury where the damage would be irreparable or inadequate… Damages, on the other hand, are traditionally viewed as a monetary substitution for a loss in value.") (citations omitted).

The Sapienzas' effort to escape this clear meaning of "damages" amounts to the flawed contention that every court order to pay money should be treated as insured "damages." This argument is baseless. The United States Supreme Court has repeatedly held that not all monetary awards constitute awards of damages. *E.g., Curtis v. Loether*, 415 U.S. 189 (1974) (refusing to hold all monetary relief must necessarily be "legal" relief); *Mitchell v. Robert De Mario Jewelry, Inc.*, 361 U.S. 288 (1960) (order for reimbursement of lost wages is within the equity power of the court); *Porter v. Warner Holding Co.*, 328 U.S. 395 (1946) (order for recovery and restitution of illegal rent payments is a proper equitable order).

All three types of remedies – damages, equity (typically, an injunction), and restitution – may require payment of money.[5] Those three remedies differ fundamentally, however.[6] Only the award of damages aims at compensation. The damages award is distinguished from other money awards that are not aimed at compensation. D. Dobbs, *Handbook on the Law of Remedies* 136 (1973). Indeed, the amount of a monetary award may differ dramatically depending on the nature of the relief awarded. Thus, a claim for

[5] *See, e.g.*, D. Dobbs, *Handbook on the Law of Remedies* XIII (1973) (field of remedies comprises damages, equity and restitution).

[6] *E.g., United States v. Long*, 537 F. 2d 1151, 1153 (4th Cir. 1975) (distinguishing monetary damages from equitable monetary relief; holding monetary relief in the form of restitution to be equitable relief), cert. denied, 429 U.S. 871 (1976); *see generally* D. Dobbs, *Handbook on the Law of Remedies*, 1-3, 13-16 (1973).

restitution, directed to the improper gain of the defendant, may substantially differ from the measurement of damages aimed at estimating the injury to the plaintiff.

"Damages" thus consist solely of those sums awarded to compensate third parties for actual injuries caused by the policyholder. Other courts have recognized that this compensatory aspect of damages is reflected in the term's common usage in insurance policies. *See, e.g., Aetna Cas. & Sur. Co. v. Hanna*, 224 F.2d 499, 503 (5th Cir. 1955) ("Damages" are "only payments to third persons when those persons have a legal claim for damages…"); *Hayes v. Md. Cas. Co.*, 688 F. Supp. 1513, 1514 (N.D. Fla. 1988) ("[T]he word 'damages' as used in an insurance agreement of this kind is meant in its ordinary legal sense — compensation in money imposed by law for loss or injury."); *Md. Cas. Co. v. Armco, Inc.*, 822 F.2d 1348, 1353 (5th Cir. 1987) ("Damages is a form of substitutional redress which seeks to replace the loss in value with a sum of money.").

Recognizing that coverage for liability in "damages" due to third-party injury means an award to compensate a third party for harm comports with the policy provisions as a whole. The policies do not broadly agree to pay all amounts the policyholder must pay to comply with a court order or law, but rather limit the insurer's agreement to pay "damages" because of "bodily injury" or "property damage." The Sapienza's reading would render the term "damages" mere surplusage, because any obligation to pay would be covered. The limitation implied by employment of the phrase "'to pay . . . for the damages'" would be obliterated.

Under its South Dakota principles of interpretation, common usage, and the policy terms, "damages" means the award of monetary compensation for a third party's "bodily injury" or "property damage." Liberty Mutual agreed to protect its insured from

traditional tort liability awards, compensating third parties for their injuries, not to pay any amount a policyholder might incur to comply with a court order of any kind.

B. The injunction requiring the Sapienzas to demolish their house is a form of equitable relief, not covered "damages."

An award of injunctive relief, such as that provided here, is not an award of "damages" to a third person to compensate for injury to that party, as the policies require. The Sapienzas were never legally obligated to pay damages; they did not pay any money to the claimants. Ultimately, because the Sapienzas were unable to bring their home into compliance with applicable regulations, they were ordered to demolish the home. Thus, the Sapienzas incurred costs in having their home demolished to comply with the injunction. This clearly was not an award of money to the neighbors calculated to compensate them for past harms.[7]

That the Sapienzas will incur costs to comply with the injunction does not transform this award of specific performance into an award of damages to a third party. Because no damages were awarded in favor of the claimants, Liberty Mutual does not have any duty to indemnify the Sapienzas. *See Ellett Bros., Inc. v. U.S. Fidelity & Guar. Co.*, 275 F.3d 384, 388 (4th Cir. 2001) (requests for monetary relief "in the form of restitution, disgorgement, civil penalties, attorney's fees, cost of suit, and … contribution to a fund" did not constitute "damages" under the policy because they were equitable remedies, as opposed to "compensation of the plaintiff's loss").

[7]The policyholders emphasize that they seek coverage for the costs of complying with an injunction entered due to claims of impingement on and loss of use of their neighbors' property. But "damages" consist of compensatory relief awarded to the third party, whereas rebuilding or demolishing a house can only help prevent *future* injury and has no compensatory element.

II. Enforcing the "damages" limitation is important to the insurance system.

If the unambiguous limitation on coverage for "damages" were ignored, as the policyholder urges, it would undermine the certainty and predictability necessary to the insurance mechanism. Recognizing that awards of damages are the estimated amount of money that is necessary to compensate a third-party for injury provides important boundaries on the risk assumed. Ignoring the "damages" limitation and requiring insurers to pay for the costs of specific injunctive relief designed to prevent future harm would create the prospect of open-ended liability. It would also undermine the reliability of the underwriting criteria that insurers use to evaluate and price risks and estimate their exposures, because what policyholders might spend in complying with injunctions is speculative and discretionary. Thus, seeking to equate the costs of injunctive relief with the award of compensation for harm actually sustained is plainly wrong.

The parties contracted for insurance covering damages, not speculative costs of injunctive relief. The scope of coverage is confined to actual injuries susceptible to quantification. That limitation preserves insurers' ability to project overall loss. Insurers do not assume the risk of all payments that policyholders may become obligated to pay to third parties. They assume specified risks in exchange for premiums, which are calculated based on awards of compensation for actual injury or damage.

Insurance is an important social mechanism, but a delicate one. Insurers are not guarantors against the consequences of all unfortunate events. Instead, insurers are "risk spreaders," whose function is to equalize the known, but unpredictably distributed, costs of liability assessments in a litigation-based society. By evaluating and distributing risks in this fashion, insurance allows individuals and organizations to engage in socially useful activities that would be impossible to undertake if the associated risks had to be

borne alone. *See generally*, Robert E. Keeton & Alan I. Widiss, *Insurance Law*, 12-13 (1988). For obvious reasons, a fundamental premise of this process is that the insurer is willing to accept the transfer of liability only for risks that are both defined and bounded.

The imposition of liability for the costs of complying with an equitable injunction, the value of which is divorced from any valuation of the actual harm imposed, despite clear insurance contract limitations, would invade insurer surplus substantially, and distort the insurance mechanism. Courts have recognized that the costs of these unforeseen liabilities would ultimately be shifted to all consumers of insurance. When courts abandon well-settled principles of insurance law, they diminish the ability of insurers to make useful actuarial predictions. Underwriters, in turn, are forced to pass on the costs of the resulting uncertainty to all consumers of insurance. Thus, courts have found that the failure to enforce insurance contracts as written can adversely affect the price and availability of insurance coverage for those who lack the resources to self-insure. *See Garvey v. State Farm Fire & Cas. Co.*, 770 P.2d 704, 711 (Cal. 1989) (disregarding policy terms would "requir[e] ordinary insureds to bear the expense of increased premiums necessitated by the erroneous expansion of their insurers' potential liabilities").

III. South Dakota should follow black-letter insurance law across the country in recognizing that injunctive relief does not constitute "damages."

A large body of law across the country recognizes the fundamental difference between covered damages and uncovered injunctive relief. Ignoring the weight of that authority, the policyholders rely on cases in which some courts found that environmental regulatory statutes equated costs to pay for cleanup with costs to comply with an

injunction compelling cleanup. *Amici* submit those cases were not correctly decided, but in any event their rationale is inapplicable here.

Courts across the country have long held that the costs incurred by policyholders to comply with equitable injunctions do not trigger liability insurers' coverage obligations. Their rulings make clear that the term "as damages" in insurance policies unambiguously does *not* encompass injunctive relief. *See, e.g., Ellett Bros., Inc. v. U.S. Fidelity & Guar. Co.*, 275 F.3d 384, 387 (4th Cir. 2001) ("[T]here is nothing in the contract … that evidences an intention to include equitable, in addition to legal, claims for relief… the term 'damages,' … does mean legal damages only, and therefore does not extend to claims for equitable relief"); *Jones v. Farm Bureau Mut. Ins. Co.*, 431 N.W.2d 242, 243-45 (Mich. Ct. App. 1988) ("injunctive relief" in the form of abatement of a nuisance "was not a form of 'damages' within the meaning of the insurance policy," because "the word 'damages' as used in the policy" was "clear and unambiguous."); *Aetna Cas. & Sur. Co. v. Hanna*, 224 F.2d 499, 502-03 (5th Cir. 1955) (costs of compliance with injunction to remove boulders from property, and maintain structure to restrain current and prevent future encroachment were not "damages" under liability policy; to construe the policy to provide coverage for "mandatory injunctive orders" would "do violence to its plain and unambiguous provisions"); *Elec. Motor & Contracting Co, Inc. v. Travelers Indem. Co. of Am.*, 235 F. Supp.3d 781 (E.D. Va. 2017) (finding the phrase "legally obligated to pay as damages" unambiguous, "adopt[ing] the plain meaning of the phrase," and concluding that 'damages' means "some claim, order, or adjudication has directed the insured to pay a sum … as compensation or remediation for a loss or injury").

In addressing the scope of insurance coverage, these courts recognize that damages compensate for past harms, whereas injunctions provide prospective relief. *See Bullock v. Md. Cas. Co.*, 102 Cal. Rptr. 2d 804, 811 (Cal. Ct. App. 2001) (no coverage for costs incurred from injunction to convert building, because relief was "prospective only, and … thus the functional equivalent of traditional injunctive remedies, not compensatory damages"; such an injunction "would not compensate anyone for harm already inflicted … Its sole function would be to avert *future* harm from the *future* displacement of residents.") (emphasis in original); *Garden Sanctuary, Inc. v. Ins. Co. of N. Am.*, 292 So.2d 75, 76 (Fla Dist. Ct. App. 1974) (liability policy "[c]learly … covers only payments to third persons when those persons have a legal claim for damages against the Insured," finding no coverage for costs of complying with injunction to restore and maintain an improperly demolished cemetery); *Moore v. State Farm Mut. Auto Ins. Co.*, 520 F. Supp.2d 815, 825 (E.D. La. 2007) (policyholder was not covered because underlying complaint only sought injunctive and declaratory relief, not "damages"); *Cutler-Orosi Unified School Dist. v. Tulare Cty. School Districts Liability/Prop. Self-Ins.-Auth.*, 37 Cal. Rptr. 2d 106, 113 (Cal. Ct. App. 1994) (declaratory and injunctive relief under the Voting Rights Act "retain[ed] their traditional character as prospective and essentially prophylactic methods of preventing the future reoccurrence of past illegal actions," so the word "damages" in the policy did not encompass the relief sought).

These decisions show the strong authority supporting the conclusion that liability policies covering "damages" do not cover injunctive relief. As a recent federal district

court ruling explained in analyzing whether the costs of complying with an injunction were recoverable as damages under a liability policy:

> … paying a sum as "damages" pursuant to a legal obligation is not equivalent to paying any sum that is legally owed or legally required to be paid. Rather, "damages" has a more specific meaning, indicating a sum that is claimed by another, or ordered to be paid, as remediation for something lost or as compensation for injury.

Elec. Motor & Contracting Co, Inc. v. Travelers Indem. Co. of Am., 235 F. Supp.3d 781, 789 (E.D. Va. 2017).

By contrast to the authority cited above, the Sapienzas rely on cases evaluating coverage for federal and state environmental regulatory schemes which *amici* submit are wrongly decided[8] and whose rationale in any event cannot be applied here.[9] The cases cited by the Sapienzas reasoned that CERCLA and comparable state statutes themselves equate the costs of injunctive relief compelling a defendant to clean up hazardous waste with what the government could recover if it undertook the cleanup itself[10] — that the government's choice of remedy is somewhat arbitrary. *See AIU Ins. Co. v. Super. Ct.*, 799 P.2d 1253, 1259, 1269 (Cal. 1990) (stating that CERCLA and similar environmental cleanup statutes "authorize alternative remedies … that are relatively interchangeable" in reaching its conclusion finding coverage for injunctive relief under CERCLA); *United*

---

[8] Some courts have ruled that mandated cleanup costs in the environmental context do *not* constitute indemnifiable damages under liability policies. *See. e.g., Patrons Oxford Mut. Ins. Co. v. Marois*, 573 A.2d 16 (Me.1990).

[9] See *Gen. Star. Indemn. Co. v. Lake Bluff Sch. Dist.*, 819 N.E.2d 784, 794 (Ill. Ct. App. 2004).

[10] CERCLA permits the government to choose between recovering costs it expends for cleanup or obtaining an injunction requiring the defendant to incur the costs of cleaning up a hazardous waste site.
(Continued...)

States Aviex Co. v. Travelers Ins. Co., 336 N.W.2d 838, 843 (Mich. Ct. App. 1983); *Bullock*, 102 Cal. Rptr. 2d at 808 (distinguishing environmental injunctions in part, because "they appeared to be the functional equivalent of reimbursing publicly-incurred costs, and an insured would not expect coverage to depend on the prosecuting agency's fortuitous choice of remedies").[11]

Thus, even if the environmental cases cited by the policyholders reached the correct result under CERCLA and similar statutory schemes (and *amici* submit they did not), their rationale does not apply here. Whether CERCLA equates an injunction requiring the defendant to incur the costs of cleaning up with the costs the government itself would expend for cleanup is beside the point. The Sapienzas' costs to comply with the order to remove the home for violating historic district regulations are decidedly different from a compensatory damages award for third-party harm. Their arguments seeking to negate the "damages" requirement on the facts here cannot stand.

---

[11] In fact, one case relied on heavily by the policyholders, *Minn. Min. & Mfg. Co. v. Travelers Indem. Co.*, 457 N.W.2d 175, 179 (Minn. 1990), specifically distinguished cases seeking general claims for injunctive relief from environmental contamination cases. The court decided that the cleanup claims asserted by the government against the policyholder should be considered damages under the specific facts — "the insureds [were] under a legal obligation to provide compensation to an injured third party," the state, so "the costs associated with cleaning up the contamination are *more aptly characterized* as consequential damages flowing from the direct damage caused to the environment." 457 N.W.2d at 182 (emphasis added). And, some of the same jurisdictions finding coverage for cleanup compelled under CERCLA have agreed that costs of complying with traditional orders of injunctive relief do not qualify as "damages." *Compare Outboard Marine Corp. v. Liberty Mut. Ins. Co.*, 607 N.E.2d 1204 (Ill. 1992) (finding "damages" encompassed injunctive claims brought by the government under environmental statutes) with *Ladd Construction Co. v. Ins. Co. of N. Am.*, 391 N.E.2d 568 (Ill. Ct. App. 1979) (holding "damages" does not encompass traditional injunctive relief).

CONCLUSION

This Court should answer the certified question in the negative, and hold that the costs incurred by the Sapienzas to comply with the injunction do not constitute covered "damages" under the insurance policies issued by Liberty Mutual.

Dated this 29th day of July, 2019.

Riter, Rogers, Wattier, & Northrup, LLP

By: /s/

319 S. Coteau – P.O. Box 280
Pierre, SD 57501-0280
Telephone : (605) 224-5825
RRiter@riterlaw.com

and

Crowell & Moring LLP

Laura A. Foggan, Pro Hac Vice
1001 Pennsylvania Ave. NW
Washington, DC 20004
Phone: (202) 624-2774
LFoggan@crowell.com

Attorneys for the Complex Insurance Claims Litigation Association & National Association of Mutual Insurance Companies

CERTIFICATE OF COMPLIANCE

Under SDCL 15-26A-66(b)(4), I certify that this brief complies with the requirements of the South Dakota Codified Laws. The brief was prepared using Microsoft Word, is 19 pages, and contains 4,921 words, exclusive of the Table of Contents, Table of Authorities, Certificate of Compliance, and Certificate of Service. I have relied on the word count of a word processing program to prepare this certificate. Dated this 29th day of July, 2019.

Riter, Rogers, Wattier,
& Northrup, LLP

By: /s/

319 S. Coteau – P.O. Box 280
Pierre, SD 57501-0280
Telephone : (605) 224-5825
RRiter@riterlaw.com

CERTIFICATE OF SERVICE

The undersigned certifies that a true and correct copy of the foregoing brief was served electronically upon:

Attorneys for Plaintiffs

Angela Beranek Brandt
Caryn A. Boisen
Larson King, LLP
30 East Seventh Street, Ste. 2800
Saint Paul, MN 55101
abrandt@larsonking.com
cboisen@larsonking.com

Attorneys for Defendants

Jack H. Hieb
Richardson, Wyly, Wise, Sauck & Hieb, LLC
P.O. Box 1030
Aberdeen, SD 57402-1030
jhieb@rwwsh.com

Christian A. Preus, Pro Hac Vice
Bassford Remele, P.A.
100 South 5th Street, Suite 1500
Minneapolis, MN 55402-1254
cpreus@bassford.com

The undersigned certifies that the original and two copies were hand delivered to Ms. Shirley Jameson-Fergel, Clerk of the Supreme Court, Supreme Court of South Dakota, State Capitol Building, 500 East Capitol Avenue, Pierre, SD 57501-5070 on the 29th day of July, 2019. An electronic version of the Brief as also electronically transmitted in Microsoft Word format to the Clerk of the Supreme Court.

Dated this 29th day of July, 2019.

Riter, Rogers, Wattier, & Northrup, LLP

By: /s/

319 S. Coteau – P.O. Box 280
Pierre, SD 57501-0280
Telephone : (605) 224-5825
RRiter@riterlaw.com

IN THE SUPREME COURT
OF THE
STATE OF SOUTH DAKOTA

APPEAL NO. 29000

JOSEPH SAPIENZA and SARAH JONES SAPIENZA, M.D.

Plaintiffs,

vs.

LIBERTY MUTUAL INSURANCE COMPANY,

Defendant.

CERTIFICATION OF QUESTION FROM THE UNITED STATES DISTRICT COURT,
DISTRICT OF SOUTH DAKOTA, CENTRAL DIVISION

THE HONORABLE ROBERTO A. LANGE,
UNITED STATES DISTRICT JUDGE

REPLY BRIEF OF PLAINTIFFS

JOSEPH SAPIENZA AND SARAH JONES SAPIENZA, M.D.

Angela Beranek Brandt
LARSON • KING, LLP
30 East Seventh Street, Ste. 2800
Saint Paul, MN 55101
(651) 312-6500

Attorney for Plaintiff

Order Accepting Certification filed June 7, 2019

Christian A. Preus
BASSFORD REMELE, P.A.
100 South Fifth Street, Ste. 1500
Minneapolis, MN 55402-1254
(612) 376-1649

Jack H. Hieb
RICHARDSON, WYLY, WISE, SAUCK
& HIEB, LLP
One Court Street
Post Office Box 1030
Aberdeen, SD 57402-1030
(605) 225-6310

Attorneys for Defendants

Table of Contents

Table of Authorities

Federal Cases

South Dakota Cases

Foreign Cases

Introduction

South Dakota law requires that terms in insurance contracts be given their plain and ordinary meaning. Where there is a genuine uncertainty as to which of two or more meanings of a term is correct, the policy is ambiguous. Cornelius v. Nat'l Cas. Co., 2012 S.D. 29, ¶ 6, 813 N.W.2d 167 (2012). Where a term is ambiguous, the meaning most favorable to the insured must be adopted. At issue here is the meaning of the term damages in the insurance policies ("the Policies") issued by Liberty Mutual to the Sapienzas. The plain and ordinary meaning of damages in those Policies includes any and all losses, costs, and expenses the insured incurs as a result of legal liability for property damage. The Sapiezas incurred significant losses, costs, and expenses as a result of their liability to the McDowells for the damage to the McDowell property caused by the construction of the Sapienza home. These losses, costs, and expenses qualify as damages under the terms of the Policies and include the cost of demolition and the total loss of the value of the home.

Liberty Mutual invites this Court to make a significant departure from South Dakota precedent and ascribe a technical definition of damages that is narrower than the plain and ordinary meaning of the term, as understood from the standpoint of the average insurance consumer. Similarly, Amici Curiae the Complex Insurance Claims Litigation Association and the National Association of Mutual Insurance Companies (collectively "the Amici") urge this Court to apply a "damages limitation" not found in the plain language of the policy, based on purported black letter insurance law. At best, these technical interpretations inject ambiguity into the policies, requiring a reading of the Policies that is most favorable to the Sapienzas and in favor of coverage. Regardless of whether the term damages in the policies

at issue here is ambiguous or unambiguous, the Certified Question must be answered in the affirmative.

Argument

I. The Term Damages Includes Any Loss, Cost, or Expense Resulting From Legal Liability.

Liberty Mutual complains that giving the term damages its plain and ordinary meaning would enlarge the scope of the policies and result in a forced construction of the policies. [R.Br. at 16-17.] Both Policies require Liberty Mutual to pay damages for which the Sapienzas are "legally liable." [DR at 40; 76.] Absent from either policy is any specific definition of damages that indicates that the policies only covered money ordered to be paid directly to the plaintiff. Further, there is no language in the policy provisions themselves that indicates that the term damages applies solely to money damages, compensatory damages, or only to damages ordered to be paid to a third party. In the absence of any such limiting language, the plain and ordinary meaning of the term damages extends to any economic outlay resulting from the insured's liability. Liberty Mutual's after-the-fact attempt to ascribe a narrow, technical meaning to the term must be rejected.

Liberty Mutual seeks to narrow the definition of the term damages under the canon of *noscitur a sociis* and based on an unreasonable reading of the term "the" in the Homeowners Policy. Both of these arguments imply, at minimum, that the term damages is ambiguous. First, even assuming that the statutory canon of construction *noscitur a sociis* can or should be invoked to interpret any insurance policy,[1] applying the canon would render the

[1] The Sapienzas maintain that the term damages is unambiguous and therefore there is no need to resort to canons of construction. While the canons of construction are normally reserved to interpret statutes, it appears that this interpretive canon has been invoked at least three times to interpret contracts. See Wright v. GGNSC Holdings, LLC, 2011 S.D. 95 at p. 24 n.7, 808 N.W.2d 114 (2011) (referencing canon in context of arbitration agreement.);

Policies ambiguous. In general, where the language at issue is "clear, certain, and unambiguous, there is no reason for construction and [a] Court's only function is to declare the meaning of the [language] as clearly expressed." State ex rel. Dep't of Transp. v. Clark, 2011 S.D. 20, P 5, 798 N.W.2d 160 (2011); see also Salzer v. Barff, 2010 S.D. 96 P 5, 792 N.W.2d 177 (2010) (finding "no cause to invoke canons of construction where the language [at issue] is clear."). Simply put, absent ambiguity, there is no reason to resort to any canon of construction.

Further, the doctrine of *noscitur a sociis* may only be invoked where "any particular word is *obscure or doubtful* of meaning, taken by itself, its obscurity or doubt may be removed by reference to associated words and the meaning of a term may be enlarged or restrained by reference to the whole clause in which it is used." State v. Douglas, 70 S.D. 20316 N.W.2d 489 (S.D. 1944) (emphasis added). The term damages need not be enlarged or restrained as it is unambiguous. Its plain meaning clearly encompasses any loss, cost, or expenses the insured incurs as a result of legal liability. By invoking the canon of *noscitur a sociis*, Liberty Mutual has essentially agreed that the term damages is of obscure or doubtful meaning, rendering it ambiguous. As such, the term cannot be limited under *noscitur a sociis* as Liberty Mutual contends. Instead, any ambiguity "must be construed most strongly against the insurer in favor of the insured." Wilson v. Allstate Ins. Co., 85 S.D. 553, 557, 186 N.W.2d 879 (1971).

Next, Liberty Mutual attempts to claim that the term damages was limited to only money damages, ordered to be paid to third parties, by virtue of the Homeowners' Policy's use of the "definite article 'the' to modify 'damages.'" [R.Br. at 13.] In doing so, Liberty

---

Opperman v. Heritage Mut. Ins. Co., 566 N.W.2d 487 (S.D. 1997) (insurance policy); Brookings Mall, Inc. v. Captain Ahab's, Ltd., 300 N.W.2d 259 (S.D. 1980) (lease agreement).

Mutual seemingly ignores the scope of the inquiry before this Court, which is whether the costs and losses associated with complying with injunctive relief "constitute covered 'damages' under the Policies." [APP 11.] More importantly, Liberty Mutual's attempt to draw a distinction between the term damages and the phrase "the damages" falls flat. The word "the" does not change the meaning of the provision in any way nor is the phrase "the damages" used consistently throughout the polices.[2] Section II, Coverage E, subsection 1 requires Liberty Mutual to pay "the damages" that result from liability. "The damages" that resulted from liability here were the losses, costs, and expenses the Sapienzas incurred as a result of their liability to the McDowells for the property damage caused by their home's violation of the historic regulations. Liberty Mutual asks the Court to read "the damages" as "the damages of the plaintiff for which the insured is legally liable." [R.Br. at 14.] But the Court is not permitted to rewrite Liberty Mutual's policy to the detriment of the Sapienzas and all other consumers.

Liberty Mutual had the opportunity to include such language in their policies and chose not to. Liberty Mutual cannot now claim that the average insured would read "the damages" to mean only damages payable to the plaintiff. As understood from the position of the average consumer of insurance "the damages for which the 'insured' is legally liable" means all losses, costs, and expenses resulting from liability, not exclusively money to be

[2] Liberty Mutual's interpretation of "the damages" is even less compelling when other damages provisions of the policies are examined. The phrase "the damages" is used in one sentence in the Homeowners Policy. Within Subparagraph 1, the policy dispenses with the definite article "the" and provides that "Damages include prejudgment interest award against the 'insured…'" [DR 40.] Elsewhere in the Homeowners Policy, Liberty Mutual agrees to pay for "damages resulting from the occurrence" [DR at 40], as well as referring to its obligation to pay "all damages resulting from any one 'occurrence.'" [DR at 43.] And the phrase "the damages" does not appear, in any form, in the Excess Policy, which provides that Liberty Mutual will pay for "damages because of…property damages…for which the insured is legally liable." [DR at 76.]

paid to the plaintiff.[3] As such, the term damages must be given its plain and ordinary meaning and cannot be narrowed based on the plain language of the policy.

II. South Dakota Precedent Favors a Plain Meaning Interpretation of the Term Damages

The parties agree that there is no South Dakota case directly interpreting the term damages in an insurance policy. The Sapienzas, and the certification order, both point to Taylor v. Imperial Cas. & Indem. Co., 82 S.D. 298, 144 N.W.2d 856 (1966) as the most analogous situation. In Taylor, the court found in favor of an insured who sought indemnity for costs and expenses associated with complying with injunctive relief. There, as here, the insured was sued for damages, nuisance, and injunctive relief. Id. The insurer declined to defend Taylor and refused to provide any indemnity. Id. Taylor was ordered to "take affirmative action" to correct the nuisance and "incurred expenses in doing so and in effecting a settlement in the action against them." Id. at 302. This Court unanimously determined that the insured was entitled to recover the costs associated with complying with injunctive relief in the underlying case under nearly identical policy language. The result here should be the same. The losses, costs, and expenses incurred by the Sapienzas as a result of their liability to the McDowells for property damage constitute covered damages under the terms of the policy.

Liberty Mutual makes no attempt to distinguish Taylor from the case at bar.[4] Instead, Liberty Mutual drags out the same unavailing arguments it made to the federal court. Liberty

[3] Similarly, the interpretation of damages offered by the Amici, drawing a distinction between different types of monetary awards based on the legal remedies under which the awards are offered falls flat. The Policies themselves do not discuss *remedies* and instead require payment of "all damages for which the insured is legally liable." The Policies do not limit coverage based on legal remedies, and nor should this Court.

[4] For their part, the Amici attempt to limit Taylor to court's interpretation of the term "accident" within the meaning of the policy at issue and rely on the same inapplicable South

Mutual relies on Public Entity Pool for Liability (PEPL) v. Score, 2003 S.D. 17, 658 N.W.2d 64 (2003) despite the fact that that PEPL "is not insurance" and is explicitly excluded from "laws regulating traditional insurance companies." Id. at ¶ 10. The facts of Score, like the PEPL fund, are not analogous to the facts of this case or the policies at issue. At no point does the Score court address injunctive relief, the duties of an insurance company, or the meaning of the term damages. Score is inapplicable.

Similarly, Dan Nelson Auto. Grp., Inc. v. Universal Underwriters Grp., 2008 WL 170084 (D.S.D. 2008) has no real bearing on this case. There, the court was tasked with determining whether "an attorney general's petition alleging violations by Plaintiffs of the Iowa Consumer Fraud Act" fell within the insurance policy's "Customer Complaint Defense" provision. Id. at *8. The language of the policy in Dan Nelson expressly defined damages as "amounts awardable by a court of law" and excluded "equitable actions" from its definition of "suit." Id. at *6. Unlike the policy at issue in Dan Nelson, the policies issued by Liberty Mutual contained no such limiting language. Dan Nelson provides no guidance on the meaning of damages in the policies at issue here or the recoverability of costs associated with injunctive relief.

Finally, Liberty Mutual cites to Headley v. St. Paul Fire & Marine Ins. Co., 712 F.Supp. 745 (D.S.D. 1989) for support for its technical interpretation of damages. Headley offers little guidance. In Headley, the Headleys commenced suit against a water company for damages resulting from discharge of water onto their property. The company tendered defense to its insurance company, who denied coverage. Id. The Headleys commenced a

---

Dakota cases discussed by Liberty Mutual. While the main issues decided by the Court in Taylor involved the interpretation of the terms "accident" and "insured," the court assumed, without deciding, that the cost of compliance with injunctive relief were covered damages under the policy. Taylor, more so than PEPL or Dan Nelson, presents the best analogy and parallel to the Certified Question before this Court.

declaratory judgment action against the insurers, seeking a determination of the scope of the coverage of the various policies. Id. The district court determined that the discharge of water was not an occurrence under the terms of the policy, that it began prior to the effective dates of the policy, and that there was no duty to defend against the Headley's claim for injunctive relief. Id. At no point did the Headley court construe or consider the meaning of the term damages in the policy. Nor does the Headley court's order include the exact language of the policies at issue. And unlike Headley, there is no contention that the occurrence that gave rise to the Sapienzas' claims occurred outside the effective term of the policy. Headley is hardly analogous to the present situation.

Here, like in Taylor, the Sapienzas were required to undertake affirmative actions and incurred significant losses as a result of their liability to the McDowells. Those affirmative actions—tearing down their newly constructed home in its entirety—resulting in significant losses, costs, and expenses which constitute damages under the express terms of the policy.

III. There is No Uniform Consensus on the Meaning of the Term Damages in the Context of Injunctive Relief.

Liberty Mutual and the Amici vastly overstate the number of courts that have considered and interpreted the meaning of the term damages in the context of injunctive relief. As evidenced by the wealth of case law on both sides of the issue, there is no uniform consensus amongst foreign jurisdictions regarding the meaning of the term damages or even a general consensus as to whether that term is ambiguous or unambiguous. Given this lack of uniformity, this Court should follow its own interpretative guidelines in answering the Certified Question. To the extent that foreign decisions are helpful to this inquiry, they support a plain meaning interpretation of the term damages.

First, Liberty Mutual and the Amici rely on cases that expressly apply the "accepted technical meaning in law" of the term damages. Aetna Cas. and Sur. Co. v. Hanna, 224 F.2d

499, 503 (5th Cir. 1955). While other jurisdictions, including Florida and the Fifth Circuit, may accept the technical meaning of damages, South Dakota precedent precludes that result.[5] In South Dakota, terms in an insurance contract must be given their plain and ordinary meaning. Ass Kickin Ranch, LLC v. N. Star Mut. Ins. Co., 2012 S.D. 73, ¶ 7, 822 N.W.2d 724, 726. To adopt the technical meaning would be to misconstrue and circumvent South Dakota law. See Farmland Indus., Inc. v. Republic Ins. Co., 941 S.W.2d 505, 510 (Mo. 1997) (applying Missouri law). Likewise, to draw an arbitrary distinction between legal and equitable relief—a distinction not found in the language of the policies and one that would not be understood to be implied by the plain language—would be to rewrite the Policies in favor of Liberty Mutual. See Helena Chem. Co. v. Allianz Underwriters Ins. Co., 357 S.C. 631, 638 (S.C. 2004) ("An 'ordinary' meaning of the term [damages] is not a legalistic one

[5] Liberty Mutual and the Amici discuss Elec. Motor and Contracting Co., Inc. v. Travelers Indem. Co. of Am., 235 F.Supp.3d 781, 788 (E.D.Va. 2017) as support for their technical definition of "damages." However, the language of the policy at issue in Elec. Motor and the language of the Policies issued by Liberty Mutual is substantially different. In Elec. Motor, the court interpreted the phrase "legally obligated to pay as damages" rather than the language at issue in the present Policies: "damages for which the insured is legally liable." [DR 1-2 at 18; DR 1-3 at 6-7]. The Policies do not include any language regarding the insured's direct payment obligation or the "to pay" language found in Elec. Motor. As discussed elsewhere, the Policies issued by Liberty Mutual encompass far more than just the satisfaction of a judgment and extend to any economic outlay caused by liability for property damage.

Moreover, the Elec. Motor court determined that it unambiguously required the insurer to cover payments "when some claim, order, or adjudication has directed the insured to pay a sum, pursuant to a binding legal obligation, as compensation or remediation for a loss or injury." Id. at 789. Here, the sum the Sapienzas were directed to pay, pursuant to the binding legal obligation set forth in the circuit court's order, as remediation for the McDowell's injury, was not directly fixed by the circuit court. The "sum" the Sapienzas were directed to pay was the cost of the demolition of their home and the loss of the total value of the home. Had the Sapienzas failed to voluntarily comply with the demolition order, the circuit court directed that the Sapienzas pay the entirety of their appellate bond to effectuate demolition. The Sapienzas were required to expend money to comply with the legally binding obligation set forth by the circuit court. Such expenditures constitute covered damages under the language of the Policies and the logic of Elec. Motor.

dependent on whether the damages are classified as legal versus equitable."). No South Dakota authority supports an interpretation of the term damages "in the insurance context" or according to any industry-friendly technical meaning. To give words in the Policies a technical meaning by simply reading them in the insurance context would render meaningless the years of South Dakota precedent requiring that words be given their plain and ordinary meaning.

Second, contrary to the overly broad characterizations advanced by the Amici and Liberty Mutual, there is no support for the claim that all forms of injunctive relief fall outside the meaning of damages under an insurance policy. The injunctive relief at issue here required the Sapienzas to undertake affirmative actions and incur losses, expenses, and costs to remedy property damage they caused to a third party. Unlike a situation where a party is simply enjoined from continuing on a certain course of conduct, the Sapienzas were required to undertake an affirmative action to remedy specific damage. For example, in State Farm Fire & Cas. Co. v. Nat'l Research Ctr. For Colleges and University Admissions, the court determined that an injunction that required the defendant to "stop making misrepresentations and make clear and conspicuous disclosures" did not constitute damages as it was "not designed to compensate anyone." 445 F.3d 1100, 1104 (8th Cir. 2006). Here, the injunction issued by the Circuit Court was designed to correct the harm done to the McDowells and restore the historic character of the neighborhood. Moreover, unlike the injunction at issue in Nat'l Research Ctr., where the injunction required the defendant to refrain from engaging in offensive conduct, the injunction issued by the Circuit Court required the Sapienzas to undertake affirmative acts to remedy the damage caused by their

home.[6] The remedy ordered by the Circuit Court required the Sapienzas to incur costs in demolishing their home and forfeit the substantial sums expended to construct the home in the first place. Contrary to Liberty Mutual's assertions, there is no broad consensus that all forms of injunctive relief are distinct and independent of damages resulting from liability. Where injunctive relief requires a party to undertake specific affirmative actions, the losses, costs, and expenses associated with those actions constitute damages resulting from liability.

Third, Liberty Mutual mischaracterizes the subsequent treatment of damages case law that arises in the environmental remediation context. Illinois has considered whether costs associated with injunctive relief constitute damages multiple times and the results have not been consistent. In Ladd Construction Co. v. Ins. Co. of N.Am., 391 N.E.2d 568 (Ill. App. Ct. 1979), an Illinois Court of Appeals drew a bright line distinction between suits seeking equitable relief and those seeking damages, determining that damages must be "remedial rather than preventive, and in the usual sense are pecuniary in nature." Id.

Over a decade later, the Illinois Supreme Court determined that the plain meaning of damages "does not distinguish between legal compensatory damages or the costs of complying with a mandatory injunction" and covers economic consequences associated with complying with a remedy for an injury to another, regardless of whether those consequences are "compelled by a court of law in the form of compensatory damages or by a court of

[6] Other courts have recognized that "[c]osts incurred to prevent future occurrences that may cause damage to property or life may be considered property damage as well." Big-D Const. Corp. v. Take it for Granite Too, 917 F.Supp.2d 1096, 1109 (D. Nev. 2013) (citing Desert Mountain Props. Ltd v. Liberty Mut. Fire Ins. Co., 236 P.3d 421, 437-32 (Ariz. Ct. App. 2010) (phrase "legal obligation to pay means any obligation enforceable by law, including, for example, an obligation created by statute, contract, or the common law."). Here, the Sapienzas' compliance with the injunction was a measure taken to prevent additional property damage to the McDowells—the continued violation of historic regulations and impingement on the McDowell property and the costs and expenses incurred were a product of the legal obligation to demolish their home created by the Circuit Court's Order.

equity in the form of compliance with mandatory injunctions." Outboard Marine Corp. v. Liberty Mutual Ins. Co., 607 N.E.2d 1204, 1216 (Ill. 1992). The Outboard court, without explanation, declined to follow Ladd and did not distinguish or overrule the previous decision from the lower court. Subsequent intermediate Illinois appellate courts have limited Outboard's holding to the environmental context, but the Illinois Supreme Court has yet to expressly narrow its decision to that context alone. Without any Illinois Supreme Court precedent expressly limiting the Outboard decision, its plain language interpretation of the term damages retains its persuasive value.

Likewise, Liberty Mutual attempts to blur the lines between cases involving injunctive relief and those involving extraordinary writs. In Minnesota, the "term 'damages' refers to compensation for an injury caused by a violation of a legal right. Whether the relief sought is legal or equitable does not alter the meaning of the word." City of Maple Lake v. American States Ins. Co., 509 N.W.2d 399, 404 (Minn. App. 1993) (citing Minn. Mining & Mfg. Co. v. Travelers Indem. Co., 457 N.W.2d 175 (Minn. 1990)). Even under this broad definition of damages, a lawsuit seeking a writ of mandamus does not constitute a suit or claim for damages because a writ of mandamus seeks "the performance of a legally required act" by a unit of government. City of Thief River Falls v. United Fire & Cas. Co., 336 N.W.2d 274, 276 (Minn. 1983). Thief River Falls and other cases involving writs of mandamus are plainly inapplicable to this case, as the relief sought by the McDowells included a claim for damages at the outset and was seeking redress of a private wrong amongst private citizens. In Thief River Falls, the claim against the city sought a writ to compel the city to undertake a condemnation proceeding. Id. Thief River Falls is distinguishable because it involved different types of claims asserted against different classes of insureds, under different policies. And unlike Thief River Falls, the property damage at

issue here—the damage to the McDowell home and the historic character of the McKennan Park neighborhood—required the Sapienzas to incur losses, costs, and expenses to restore the McDowell property, and the neighborhood as a whole, to its previous condition. Under the plain language of the policy, these losses, costs, and expenses were the kind of economic consequences from liability that the average insurance customer could reasonably expect were covered.

IV. Construing the Term Damages in Accordance with its Plain and Ordinary Meaning Safeguards the Rights of Consumers and Members of the General Public.

The Amici reference the importance of "enforcing the 'damages' limitation" to the insurance industry as a whole and contend that construing the policies in accordance with their plain and ordinary meaning will "invade insurer surplus" and shift additional costs to insurance consumers. [AC.Br. at 11-12.] The proposed "damages limitation," in the absence of any limiting language in the policy itself, conflicts with the plain meaning of the term damages and defies the understanding and expectations of any layperson purchasing an insurance policy. The language of the policies, to the average South Dakotan, provides coverage for all financial consequences of liability to third parties resulting from personal injury or property damage. The policies themselves do not put any insurance consumer—sophisticated or otherwise—on notice that coverage extends only to sums ordered to be paid to the prevailing litigant. In the absence of any express exclusion for all other forms of damages, no "damages limitation" can be read into the policies. After all, insurers bear the burden of establishing that an exclusion applies or a claim falls outside the scope of the policy. See Berkley Regional Specialty Ins. Co. v. Dowling Spray Serv., 2015 S.D. 35, ¶ 22, 864 N.W.2d 505 (insurer bears burden of establishing exclusion); Auto-Owners Ins. Co. v. Hansen Housing, Inc., 2000 S.D. 13, ¶ 10, 604 N.W.2d 504 (insurer bears burden of proof

on all affirmative defenses to coverage). Here, to adopt the "damages limitation" offered by the Amici would be to rewrite the terms of the Policies, and indeed many other liability policies in South Dakota to impose a limitation on coverage that was not expressly included as an exclusion or apparent from the plain language of the Policies issued to the Sapienzas. To do so would be to supply an exclusionary provision not bargained for by the insurer or disclosed to the insured.

Further, affording the term damages its plain and ordinary meaning will not automatically pass along additional costs to insurance consumers. First, the unique circumstances of this case are unlikely to be widely applicable. The unique costs of compliance of injunctive relief incurred by the Sapienzas and the facts and circumstances surrounding the McDowell lawsuit are unlikely to have wide applicability or give rise to an inordinate amount of similar insurance claims. A far more likely result than a rise in insurance premiums would be for insurers to include the express exclusion sought by Liberty Mutual and the Amici. As discussed above, Liberty Mutual, and all other insurers providing liability insurance policies to consumers in South Dakota, are free to define the terms in their policies. Like any other policy exclusion, to receive the benefit of a technical definition of damages, insurers need only provide that definition to remove any ambiguity and all doubt regarding coverage of damages. This Court should not reform the Policies in favor of a technical definition where no such definition was expressly provided for by the Policies.

Conclusion

The Court should answer the certified question in the affirmative. The Sapienzas purchased insurance expecting coverage for losses and costs incurred as a result of legal liabilities—regardless of whether those losses and costs came in the form of a money judgment or injunctive relief. The plain and ordinary meaning of damages includes the

losses, costs, and expenses associated with complying with the injunctive relief ordered by the Circuit Court. South Dakota precedent precludes the Court from adopting the technical definition of damages offered by Liberty Mutual and the Amici. At best, the technical definition of damages gives rise to an ambiguity and requires an interpretation most favorable to the insured—an interpretation in favor of coverage. For these reasons, the Sapienzas respectfully submit that the certified question must be answered in the affirmative.

Dated: September 17, 2019

/s/ Angela Beranek Brandt

Angela Beranek Brandt (#3091)
LARSON • KING, LLP
30 East Seventh Street, Ste. 2800
Saint Paul, MN 55101
(651) 312-6500 | Fax: (651) 312-6618
abrandt@larsonking.com

Attorneys for Plaintiffs

Certificate of Compliance

Under SDCL 15-26A-66(b)(4), I certify that this brief complies with the requirements of the South Dakota Codified Laws. This brief was prepared using Microsoft Word, and contains 4,635 words from the Introduction through the Conclusion. I have relied on the word count of a word-processing program to prepare this certificate.

/s/ Angela Beranek Brandt
Angela Beranek Brandt (#3091)

Certificate of Service

The undersigned certifies that a true and correct copy of the foregoing brief was served electronically upon:

Attorneys for Defendants
Jack H. Hieb
jhieb@rwwsh.com

Christian A. Preus
cpreus@bassford.com

/s/ Angela Beranek Brandt
Angela Beranek Brandt (#3091)