NONPRECEDENTIAL DISPOSITION
To be cited only in accordance with FED. R. APP. P. 32.1

United States Court of Appeals
For the Seventh Circuit
Chicago, Illinois 60604

Argued November 3, 2023
Decided November 25, 2024

Before

THOMAS L. KIRSCH II, *Circuit Judge*

CANDACE JACKSON-AKIWUMI, *Circuit Judge*

DORIS L. PRYOR, *Circuit Judge*

No. 23-1152

CORNICE & ROSE INTERNATIONAL, LLC and JAMES A. GRAY,
Plaintiffs-Appellants,

v.

ACUITY, a Mutual Insurance Company,
Defendant-Appellee.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

No. 21-cv-06112

Nancy M. Maldonado,
Judge.

O R D E R

This case concerns whether an insurance policy requires an insurer to defend an architectural firm against a lawsuit alleging that the firm inadequately designed and oversaw the construction of a building. The district court, interpreting the policy in light of what most appellate courts in Illinois had said about the issue, concluded that the answer was no. Since then, the Illinois Supreme Court has overruled those appellate decisions. *See Acuity v. M/I Homes of Chicago, LLC*, 2023 IL 129087, 234 N.E.3d 97, *reh'g denied* (Jan. 22, 2024). That intervening decision indicates that the insurer owes the architectural firm a duty of defense. We therefore vacate and remand.

I. Factual Background

A. The Underlying Counterclaim and Complaint

Cornice & Rose International, LLC and James Gray—an architectural firm and its owner—designed and oversaw the construction of a building in Iowa.[1] According to the contract between Cornice and the building's owner, Cornice agreed to provide the following services:

1. Prepare drawings illustrating the design of the building.
2. Prepare drawings and specifications "setting forth in detail the quality levels of materials and systems and other requirements for the construction" of the building.
3. Evaluate the project regularly to become "familiar with the progress and quality of … the [w]ork completed" and "to endeavor to guard the [o]wner against the defects and deficiencies in the [w]ork." Cornice, however, was liable only for its own failure to perform and not the failure of construction workers to perform.

Years later, the building's owner and its lender filed a counterclaim against Cornice in an Iowa federal court under several theories, including breach of contract and negligence.[2] The counterclaim alleged that "construction was not complete" and that Cornice "fail[ed] to provide design in accordance with the standard of care," which left the building with a litany of "defects and design problems." For example, the counterclaim alleged that the elevator did not meet the required code and that kitchen cabinets were built so tall that they blocked the windows. It also alleged that a lack of ventilation in the attic space caused the roof sheathing and the trusses to rot, and that a heater Cornice used left residue on surfaces, which meant the owner had to treat those surfaces. These problems—resulting from what the counterclaim termed was "the negligent provision of architectural services"—cost over three million dollars to fix.

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[1] Cornice & Rose International is a Limited Liability Company organized and existing under the laws of the State of Illinois. (Dkt. 1).

[2] *See Cornice & Rose, International, LLC v. Four Keys, LLC*, Case No. 6:20-cv-2097, United States District Court for the Northern District of Iowa. (Dkt. 1-8).

The owner and lender eventually dismissed their counterclaim and sued Cornice in Iowa state court instead. The state court complaint is materially identical to the federal counterclaim.

B. Cornice's Insurance Policy

Cornice did not obtain malpractice insurance. Instead, it acquired successive, annual "commercial general liability" policies from Acuity, an insurance company. These policies covered Cornice during the relevant period and stated that Acuity had a duty to defend Cornice in any suit seeking to recover for "property damage" caused by an "occurrence." The policies defined each term:

1. "[O]ccurrence" meant "an accident, including continuous or repeated exposure to substantially the same general harmful conditions."
2. "Property damage" meant either "[p]hysical injury to tangible property, including all resulting loss of use of that property" or "[l]oss of use of tangible property that is not physically injured."

II. District Court Proceedings

Forty days after the building owner filed its counterclaim, Cornice sued Acuity in federal court based on diversity jurisdiction and sought a declaratory judgment requiring Acuity to defend it under the policies. Cornice also alleged breach of contract, arguing that Acuity was equitably estopped from defending against the breach of contract claim, and sought costs under Section 5/155 of the Illinois Insurance Code. Each party moved for a judgment on the pleadings under Federal Rule of Civil Procedure 12(c).

The district court granted Acuity's motion and denied Cornice's.[3] The court—relying on how most appellate courts in Illinois had interpreted similar policies—concluded that Acuity had no duty to defend Cornice because the Iowa lawsuit did not seek to recover for "property damage" arising out of an "occurrence." The court also determined that Acuity was neither estopped from defending against the breach of contract claim nor liable for costs.

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[3] This initial ruling concerned only whether Acuity had a duty to defend Cornice in the Iowa federal court proceeding. Afterward, the parties agreed that the ruling also applied to the Iowa state court proceeding, leading the district court to enter a judgment deciding the case in favor of Acuity.

III. Discussion

On appeal, Cornice contests all three rulings. It argues that Acuity has a duty to defend, that equitable estoppel prevents Acuity from contesting the breach of contract claim, and that Acuity owes costs under the Illinois Insurance Code.

We review the entry of judgment on the pleadings de novo, construing the allegations in the light most favorable to the non-movant. *Federated Mut. Ins. Co. v. Coyle Mech. Supply Inc.*, 983 F.3d 307, 313 (7th Cir. 2020). If it is beyond doubt that the non-movant cannot prove facts sufficient to prevail, we must rule for the movant. *Id.*

In addition, because we are sitting in diversity, we apply state substantive law. *Mathis v. Metro. Life Ins. Co.*, 12 F.4th 658, 661 (7th Cir. 2021). Here, the parties agree that Illinois law controls. This means that our task is to resolve the issues as the Illinois Supreme Court would. *Mashallah, Inc. v. W. Bend Mut. Ins. Co.*, 20 F.4th 311, 319 (7th Cir. 2021).

A. Duty to Defend

Cornice first argues that Acuity has a duty to defend it against the Iowa suit.

To analyze whether a party has a duty to defend under Illinois law, we compare the language in the insurance policies with the allegations in the underlying complaint. *Valley Forge Ins. Co. v. Swiderski Elecs., Inc.*, 860 N.E.2d 307, 314 (Ill. 2006). When doing so, we must liberally construe the allegations in favor of the insured. *Id*. If the complaint alleges facts bringing the suit within or potentially within a policy's coverage, then the insurance company must defend the policyholder. *Id.* at 315. This holds true even when the allegations are false and even when only one of the theories of recovery in the complaint might trigger the duty to defend. *Id.*

Here, the policies require Acuity to defend Cornice against any lawsuit alleging "property damage" stemming from an "occurrence." As we have discussed, the policies define "property damage" as "[p]hysical injury to tangible property" or the loss of use of that property. And the policies define "occurrence" as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions."

Much of the briefing and argument in this case focused on which property was allegedly damaged and how. In particular, the parties considered whether the Iowa

lawsuit simply sought to hold Cornice responsible for the cost of repairing and replacing the work that Cornice had contracted to provide. This approach was understandable. Many appellate courts in Illinois had held that, for damage to constitute "property damage," the property in question must fall "beyond [the scope] of the contractor's work product." *Certain Underwriters at Lloyd's London v. Metro. Builders, Inc.*, 158 N.E.3d 1084, 1096 (Ill. App. Ct. 2019). By the same token, several Illinois courts had held that the need to repair or replace work was the "natural and ordinary consequence" of faulty workmanship rather than an unexpected "accident" capable of constituting an "occurrence." *Id.* at 1093. These interpretations were driven by the idea that commercial general liability policies are meant to protect against freak accidents, not against run-of-the-mill breach of contract claims. *Id.* at 1093, 1095 ("[T]he case law has focused at least as much on the purposes of CGL policies as it has on textual interpretation and application.").

After we held oral argument, the Illinois Supreme Court rejected the above approach. In doing so, it reiterated the long-standing rule that courts must interpret insurance policies not in light of "policy considerations" but in the way that an "average, ordinary, normal, [and] reasonable person" would read them. *M/I Homes*, 234 N.E.3d at 105 (citation omitted).

The Illinois Supreme Court accordingly concluded that "property damage" meant only physical injury to tangible property and no more. *Id.* at 106. If the property "is altered in appearance, shape, color or in other material dimension," that is enough. Under that definition, the complaint in *M/I Homes*, which sought damages to repair the insured's alleged faulty workmanship on a group of townhomes, alleged "property damage." *Id.* It did not make a difference that the damage occurred to property that was within the scope of the insured's project. *See id.*

A similar analysis followed for "occurrence." That term, according to *M/I Homes*, meant only "an unforeseen occurrence, usually of an untoward or disastrous character, or an undesigned, sudden, or unexpected event of an inflictive or unfortunate character." *Id.* at 106–07 (citation omitted). So it encompassed "unintended and unexpected harm caused by negligent conduct." *Id.* In turn, because the contractors in *M/I Homes* did not intend or anticipate the defects or the resulting harm to the townhomes, the damage was caused by an "occurrence." *Id.* at 108. This reasoning tracks how we understood the term "occurrence" in *Prisco Serena Sturm Architects, Ltd. v. Liberty Mut. Ins. Co.*, 126 F.3d 886, 890–91 (7th Cir. 1997).

At our request, the parties have submitted supplemental briefing on how *M/I Homes* affects this dispute. Cornice argues that *M/I Homes* clarified what had been the law in Illinois all along. Acuity concedes that after *M/I Homes*, the Iowa lawsuit potentially includes allegations of "property damage" stemming from an "occurrence" but argues that we should apply the rule of *M/I Homes* only prospectively.

We agree with Cornice that *M/I Homes* makes it clear that Acuity must defend Cornice. To start, the complaint here alleges "property damage" because it seeks to hold Cornice responsible for damaging tangible property. *M/I Homes*, 234 N.E.3d at 106. The most obvious example is the rotted roofing material. This allegation, like the water damage in *M/I Homes*, involved tangible property that had been altered in appearance or in another material dimension. Acuity's counterargument—that Cornice damaged its own project—no longer carries weight.

The same is true for "occurrence." The underlying lawsuit alleges that Cornice negligently designed the building. Nowhere does it claim that Cornice intended or expected the defects. As a result, the supposedly inadequate work that Cornice performed counts as an "accident." *Id.* at 107–08; *accord Prisco Serena Sturm Architects, Ltd.*, 126 F.3d at 890–91. Once again, Acuity's response—that faulty work is not an accident—has been rejected by the Illinois Supreme Court.

Finally, we reject Acuity's position that *M/I Homes* is an outlier case that falls outside the presumption of retroactive application because the case changed the law. *See Tzakis v. Maine Twp.*, 181 N.E.3d 812, 818 (Ill. 2020) (listing factors to consider when deciding whether to override the presumption that an opinion applies retroactively). Rather than changing the law, *M/I Homes* reiterated the long-standing principle that contracts are to be interpreted as written. *M/I Homes*, 234 N.E.3d at 105. At most, it clarified Illinois law and abrogated decisions that interpreted insurance policies based on their generic purpose instead of their text. *See id.*

For these reasons, we conclude that the Iowa counterclaim alleges "property damage" caused by an "occurrence," meaning Acuity must defend Cornice against the suit.[4]

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[4] Acuity asserts in its post-argument supplemental briefing that we should consider two policy exclusions that bear on its duty to defend, or at least remand for the district court to consider these exclusions. We decline this invitation because the argument is waived. *See Sullivan v. Flora, Inc.*, 63 F.4th 1130, 1137–39 (7th Cir. 2023). Acuity has never before argued that the exclusions apply. On the contrary,

B. Equitable Estoppel

Under Illinois law, when a complaint alleges facts within or potentially within the coverage of an insurance policy, the insurer must either defend against the suit or seek a declaratory judgment stating that it need not do so. *Standard Mut. Ins. Co. v. Lay*, 989 N.E.2d 591, 596 (Ill. 2013). If the insurer fails to take either of these steps within a "reasonable time," it cannot turn around and say that it acted in accordance with the policy. *Korte Constr. Co. v. Am. States Ins.*, 750 N.E.2d 764, 770 (Ill. App. Ct. 2001). Whether the insurer sought a declaration within a reasonable time depends on the circumstances of each case. *First Chicago Ins. Co. v. Molda*, 36 N.E.3d 400, 419 (Ill. App. Ct. 2015).

Cornice argues that estoppel applies because the underlying counterclaim alleged facts potentially within its insurance coverage and Acuity never sought a declaratory judgment. Although the complaint does involve allegations that the insurance policies might cover, Cornice did not give Acuity a reasonable amount of time to seek a declaratory judgment before filing this action.

Cornice sued just forty days after notifying Acuity of the Iowa lawsuit. While the raw amount of time is not dispositive because each case must be judged on its own facts, requiring Acuity to seek a declaratory judgment within thirty-nine days would be at odds with the delays other courts have considered reasonable. *See, e.g.*, *Nautilus Ins. Co. v. Bd. of Directors of Regal Lofts Condo. Ass'n*, 764 F.3d 726, 733 (7th Cir. 2014) (in applying Illinois law the Court concluded that waiting five months was reasonable); *Westchester Fire Ins. Co. v. G. Heileman Brewing Co.*, 747 N.E.2d 955, 965 (Ill. App. Ct. 2001) (concluding that waiting six months was reasonable). In addition, Acuity moved for a judgment on the pleadings in this case—arguing that it did not have a duty to defend—just two months after Cornice sued. *See L.A. Connection v. Penn-Am. Ins. Co.*, 843 N.E.2d 427, 264–66 (Ill. App. Ct. 2006) (concluding that an insurer discharged its duty to defend by, within four months of denying coverage, filing a cross claim for declaratory relief in a suit initiated by the insured). Considering the facts of this case, we cannot say that Acuity waited an unreasonable amount of time to ask a court to rule that it need not defend Cornice.

Acuity admitted below Cornice's allegation that, "[n]one of the Acuity Policies contain an exclusion barring coverage for any property damage in any way arising out of professional services rendered by C&R."

C. Section 5/155 of the Illinois Insurance Code

Lastly, Cornice invokes Section 5/155 of the Illinois Insurance Code, which allows a party to recover costs for a "vexatious and unreasonable delay" in settling a claim. 215 ILCS 5/155. A delay is permissible if a genuine dispute exists over the scope of the coverage. *TKK USA, Inc. v. Safety Nat. Cas. Corp.*, 727 F.3d 782, 793 (7th Cir. 2013). Because Acuity presented legitimate arguments, especially considering the state of Illinois case law at the time, it did not engage in a vexatious or unreasonable delay.

IV. Conclusion

For these reasons, we VACATE the judgment of the district court regarding Acuity's duty to defend. We AFFIRM in all other respects. And we REMAND for further proceedings consistent with this order.