WINTER 2014 NEWSLETTER

INSURANCE LAW UPDATE

By Jennifer Kelley

SUPREME COURT OF TEXAS

***Ewing Construction Company, Inc. v. Amerisure Ins. Co.*, No. 12-0661, 2014 Tex. LEXIS 39 (Tex. Jan. 17, 2014).**

In a decision addressing certified questions from the Fifth Circuit, the Supreme Court of Texas narrowly construed the contractual liability exclusion in a commercial general liability policy and concluded that:

> …a general contractor who agrees to perform its construction work in a good and workmanlike manner, without more, does not enlarge its duty to exercise ordinary care in fulfilling its contract, thus it does not "assume liability" for damages arising out of its defective work so as to trigger the Contractual Liability Exclusion.

In *Ewing*, Ewing Construction contracted with a school district to serve as a general contractor on some renovations and additions to a school. Shortly after the work was completed, the district complained that the tennis courts started cracking and flaking rendering them unusable. Suit was filed and Ewing tendered the defense to its insurance carrier Amerisure. Amerisure denied coverage based in part on the contractual liability exclusion which, in turn prompted Ewing to file a declaratory judgment action in federal court seeking coverage. The district court held that the contractual liability exclusion precluded coverage, the insured appealed and the Fifth Circuit certified questions involving the contractual liability exclusion to the Supreme Court of Texas.

The Supreme Court of Texas observed that the contractual liability exclusion precludes coverage when the insured contractually assumes liability, except when: (1) the insured's liability for damages would exist absent the contract, and (2) where the contract is an insured contract. In this case, the insurer argued that the contractual liability exclusion "means what it says" and the exclusion applies here because the insured contractually agreed to construct the tennis courts in a good and workmanlike manner, and therefore assumed liability for damages. The insured, on the other hand, argued that this case is distinguishable from the Court's decision in *Gilbert Texas Construction, L.P. v. Underwriters at Lloyd's London,* 327 S.W.3d 118 (Tex. 2010), and that the insured's agreement to perform in a good and workmanlike matter did not enlarge any duties it has at common law, and therefore, was not an "assumption of liability" within the meaning of the contractual liability exclusion.

In responding to the first certified question as to whether a general contractor that enters into a contract in which it agrees to perform its construction work in a good and workmanlike manner, without more specific provisions enlarging this obligation, "assumes liability" for damages arising out of the contractor's defective work so as to trigger the Contractual Liability

Exclusion, the Supreme Court of Texas answered "no". Consequently, the supreme court did not need to answer the second question of whether an exception to the exclusion applied.

TEXAS COURTS OF APPEALS

***Simon v. Tudor Ins. Co*., No. 05-12-00443-CV, 2014 Tex. App. LEXIS 1321 (Tex. App.—Dallas Feb. 5, 2014, no pet. h).**

The Dallas Court of Appeals affirmed summary judgment in favor of the insurer based on a wood destroying insect inspection exclusion in the policy, holding that the insured could not have reasonably relied on language in the certificate of insurance.

In *Simon*, the insured performed wood destroying insect ("WDI") inspections as part of its structural pest control business. The insured's 2007 and 2008 commercial liability policies included a WDI exclusion in two separate endorsements. During the 2008 renewal process, the insurance agent, as the insurer's authorized representative, signed a certificate of insurance for the insured that was submitted to the Structural Pest Control Service of the Texas Department of Agriculture. The certificate did not list any categories of pest control work excluded from coverage.

The insured performed a WDI inspection report for a homeowner, who subsequently sued the insured for performing an improper WDI inspection. The insured reported the claim to its insurer, which was denied on the grounds that the policy excluded coverage for that type of claim. The trial court agreed with the insurer and granted summary judgment in its favor.

The insured's sole argument on appeal was that the trial court erred in concluding that it could not have reasonably relied on the representations made by the insurer and its agent in the certificate of insurance submitted to the Department of Agriculture, which did not identify any exclusions to coverage. The Dallas Court of Appeals disagreed, noting that the evidence established that the insured expressly acknowledged in all applications for insurance that the insurance for which the insured applied did not include coverage for liability arising from WDI inspections. The appellate court further noted that the plain language of both the original and renewal policies clearly excluded coverage for such inspection services in the applicable endorsements. Finally, the appellate court emphasized that the certificate of insurance specifically stated (1) that the certificate neither affirmatively nor negatively amends, extends or alters the coverage afforded by the polices scheduled herein; and (2) that the certificate is furnished for information only, confers no rights on the holder and is issued with the understanding that the rights and liabilities of the parties will be governed by the original policies as they may be lawfully amended from time to time. The Dallas Court of Appeals, therefore, concluded that the insured could not have reasonably relied on the language in the insurance certificate. Accordingly, summary judgment in favor of the insurer was affirmed.

***Seabright Insurance Company v. Lopez*, No. 04-12-00863-CV, 2014 Tex. App. LEXIS 905 (Tex. App.—San Antonio Jan. 29, 2014, no pet. h).**

The San Antonio Court of Appeals held that the "coming-and-going rule," which excludes travel between work and home from the course and scope of employment in a worker's

compensation claim, did not apply to exclude a claim by the beneficiaries of a worker who was residing in employer-provided lodging and driving an employer-provided vehicle at the time of the accident.

In *Lopez*, the decedent's wife sued for workers' compensation benefits after her husband was killed in a motor vehicle accident while driving from his hotel to a job site 40 miles away. The contested case hearing officer, the appeals panel, and the trial court all sided with the wife, ruling that the husband was killed while acting in the course and scope of his employment.

The San Antonio Court of Appeals agreed, noting that the coming-and-going rule generally excludes from workers' compensation coverage travel between work and home, but that an exception to the rule arises when the transportation is paid for by the employer. The appellate court, however, recognized that employer-provided transportation is not dispositive and, therefore, it examined the summary judgment record for additional course-and-scope evidence.

Crucial to the appellate court's resolution of the appeal was the fact that the husband was not only driving a vehicle provided by his employer, but that he was also working away from home. The jobsite was located roughly 450 miles from the husband's residence, and he was given a per diem that he used to stay at a hotel 40 miles from the jobsite. The appellate court deemed the hotel to be "de facto employer-provided housing," and noted that the husband would not have been in the vicinity of the accident but for his work. The evidence in the case, therefore, was sufficient to establish, as a matter of law, that the husband was acting in the course and scope of his employment, and therefore his wife was entitled to recover worker's compensation benefits because of his death.

***Mid-Continent Casualty Company v. Castagna,* 410 S.W.3d (Tex. App.—Dallas 2013, pet. filed).**

The Dallas Court of Appeals held that the proper analysis when applying the actual injury rule to determine whether an insurer has a duty to indemnify its insured is to look for evidence of the date when the injury occurred and not when the injury was discovered.

In *Castagna*, the insurer issued commercial general liability policies to its insured, a residential homebuilder, in 2001, 2002, 2003 and 2006. The homebuilder entered into a contract of sale with a homeowner, which was closed in late 1999. The homeowner subsequently sued the homebuilder for foundation defects, and the case underwent arbitration. The insurer defended the homebuilder during the arbitration, and ultimately an arbitration award was entered in favor of the homeowner. The homeowner then filed suit to enforce the arbitration award against the insurer.

On appeal, the homeowner argued that that the insurer was obligated to pay the final judgment confirming the arbitration award because the damages awarded were covered under the 2001, 2002, and 2003 policies. The insurer, on the other hand, argued that there was no insurance coverage under the policies because the homebuilder was not insured during the policy periods in which the alleged damage occurred, and that there was no evidence that there was an occurrence or property damage prior to 2006 that would have triggered coverage.

The Dallas Court of Appeals addressed and rejected, in relevant part, the insured's argument regarding when the property damage "occurred". The appellate court defined the meaning of "occurred", noting

> [t]he policy asks when the damage happened, not whether it was manifest, patent, visible, apparent, obvious, perceptible, discovered, discoverable, capable of detection, or anything similar. Occurred means when *damage* occurred, not when discovery occurred.

The appellate court therefore reviewed the arbitration record and concluded that there was more than a scintilla of evidence that the homeowner witnessed the development of cracks as early as 2001 and that the cracks progressed through 2007.

Specifically, the appellate court noted that there was evidence in the underlying arbitration that in 2001, the homeowner discovered a hairline crack in her residence. The homeowner notified the homebuilder about the crack and the homebuilder inspected and repaired the crack. The hairline crack came back again sometime in 2002 or 2003. The homeowner notified the homebuilder, who again repaired and painted over the crack. The homebuilder informed the homeowner that the crack was the result of normal house "settling." Severe cracks appeared in the residence in the spring of 2007. The homeowner was unable to close or lock her back doors, bathroom door, wine cellar door, and other doors. Based on this evidence, the appellate court concluded that there was some evidence that the property damage commenced in 2001 and progressed through late 2006 to early 2007.

THE FIFTH CIRCUIT

Molly Properties v. Cincinnati Insurance Co., No. 13-50567 2014, U.S. App. LEXIS 2358 (5th Cir. Feb. 7, 2014).

The Fifth Circuit Court of Appeals held that an insurer's failure to give notice of cancellation to the mortgagee does not affect cancellation unless the terms of the policy provide otherwise.

In *Molly Properties*, an insured filed suit against its insurer for breach of contract after the insurer denied the insured's fire claim for nonpayment of premiums. The insured did not dispute that the insurer notified the insured that its policy would be cancelled for non-payment of premiums. However, the insured argued that the policy was not cancelled at the time of the fire because the insurer failed to give notice of the cancellation to the mortgagee on the property. The Fifth Circuit, disagreed, holding that unless the terms of the policy provide otherwise, a policy cancellation is not affected by the failure of the insurer to give notice of cancellation to the mortgagee. The Fifth Circuit, therefore, concluded that because the policy at issue did not condition the cancellation of coverage on notification to the mortgagee, the issue of whether the insurer gave notice to the mortgagee was irrelevant as to the insured's loss of coverage.

The Fifth Circuit also held that the insured could not recover as a third-party beneficiary to an agreement between the insurer and the mortgagee. The appellate court stated that any promise by the insurer to provide a cancellation notice to the mortgagee was made for the benefit

of the mortgagee, not the insured. Consequently, the Fifth Circuit affirmed the trial court's decision to grant summary judgment in favor of the insurer.

***Star-Tex Resources, L.L.C. v. Granite State Insurance Co.*, 2014 WL 60192 (5th Cir. (Tex.) January 8, 2014)**

The Fifth Circuit applied its limited exception to the eight-corners rule to conclude that an insurer did not have a duty to defend or indemnify its insured.

In *Star-Tex Resources*, an intoxicated employee was driving a car on an auto auction lot when the vehicle the employee was driving struck a pedestrian employee, pinning the pedestrian between two vehicles and causing serious injury. Suit was filed against the employer and the responsible employee. The employer and responsible employee sought coverage under the employer's commercial general liability policy. The insurer denied coverage based on the policy's auto-exclusion. The insureds then filed a declaratory judgment action seeking a declaration that the insurer had a duty to defend them in the lawsuit. The trial court granted summary judgment in favor of the insurer.

On appeal, the Fifth Circuit discussed Texas' relatively strict version of the eight-corners analysis with regard to the duty to defend. The appellate court noted that the injured employee's petition only alleged in part that he was "seriously injured in an automobile collision caused by the negligence of…" the employee who was "under the influence of alcohol or drugs at the time of the collision." The Fifth Circuit observed that the petition did not say whether the employee was operating the vehicle, directing traffic, or working in some other capacity when the accident occurred. The Fifth Circuit, therefore, applied the limited exception to the eight-corners rule that it had previously adopted (that has not officially been adopted or rejected by the Texas Supreme Court), which permits the use of extrinsic evidence "only when relevant to the independent and discrete coverage issue, not touching on the merits of the underlying third-party claim", and concluded that the auto-exclusion did in fact apply. Accordingly, summary judgment in favor of the insurer was upheld.

FEDERAL DISTRICT COURTS

***Walker v. Nationwide Property and Casualty Insurance Co.*, NO. 1:12-CV-1124-JRN, 2014 U.S. Dist. LEXIS 6683 (W.D. Tex.).**

The Western District of Texas – Austin Division granted summary judgment in favor of an insurer, holding that 1) post-loss misrepresentations are not actionable absent evidence they were the producing cause of damages, and 2) expert testimony *is necessary* to determine whether an insurer's investigation was reasonable.

In *Walker*, the insured owned a residence in Austin and made a claim on his insurance alleged that his extensive foundation movement was the result of multiple plumbing leaks that had been discovered in his drain line. The insurer investigated and retained an engineer who concluded the foundation movement was the result of other causes, not plumbing leaks. The insured did not dispute that the Dwelling Foundation Endorsement limited his coverage to 15% of his Dwelling coverage and was limited solely to the foundation damage. Instead, the insurer argued that the HO-542-A policy itself provided coverage for any cracking of walls, floors, and

ceilings where the damage *ensued* from foundation movement caused by a plumbing leak. The insured also alleged the insurer's adjuster misrepresented the coverage to him during the investigation.

The district court dismissed the insured's policy interpretation arguments and ruled the policy itself, without the endorsement, excludes coverage for plumbing leak damage. In addition, the district court held that the Dwelling Foundation Endorsement only applies to damage to the foundation itself, and only in an amount equal to 15% of the Coverage A (Dwelling) limit of liability. The district court then turned to the insured's alleged extra-contractual claims and dismissed all of them. Importantly, the district court concluded that the alleged post-loss misrepresentations made by an insurance carrier or its adjusters are *not* actionable under the Texas Insurance Code or the DTPA *absent* evidence that the alleged misrepresentations were the producing cause of damages. Finally, when addressing the insured's affidavit, which provided his opinion as to why the insured failed to conduct a reasonable investigation, the district court held that an insured's opinion on whether an insurance carrier violated the Texas Insurance Code by failing to pay a claim without conducting a reasonable investigation is irrelevant and thus inadmissible when the insured is not an expert on insurance investigations.

***Vanliner Ins. Co. v. DerMargosian*, No. 3:12-CV-5074-D, 2014 U.S. Dist. LEXIS 3841 (N. D. Texas Jan. 13, 2014).**

The Northern District of Texas—Dallas Division answered "yes" to the question of whether a claimant who is not yet a judgment holder may be involuntarily joined to the insurer's declaratory judgment action. However, the district court did not answer the question of whether the claimant ***must*** be joined.

In *Vanliner*, there was an underlying suit in which customers sued a moving company for mishandling a packing and moving job. The customers retained the moving company to pack and move specific belongings to Dubai, while leaving others unpacked at their home in Texas. The moving company allegedly failed to accurately follow instructions, and mistakenly packed a pistol, which was shipped to Dubai with their other household goods. As a result, one of the customers was arrested in Dubai for possession of the pistol, incarcerated, and forced to stand trial.

Upon being sued, the moving company sought defense and indemnity from its insurer. The insurer subsequently filed a declaratory judgment suit seeking a declaration that it did not have a duty to defend or indemnify its insured. The insurer also named the customers as defendants. The customers, however, moved for dismissal, arguing they were not proper parties to the declaratory judgment action because they were not in contractual privity with the insurer, the insurer was not a party to the underlying suit, and that the insurer was not asserting any claims directly against them in the declaratory judgment action.

The district court observed that an injured claimant is a third-party beneficiary under a liability policy. While the claimant cannot directly enforce the policy until it holds a judgment against the insured, the insurer can nevertheless obtain a pre-judgment ruling on its duty to defend its insured, and can also obtain a pre-judgment ruling on its duty to indemnify in some circumstances. The district court also noted that a declaratory judgment obtained by the insurer is

binding on a third-party beneficiary if that beneficiary is joined as a party to the action. The district court, therefore, refused to dismiss the customers, concluding that the customers had a material and immediate interest in the question of the insurer's contractual duties, and that there was an actual controversy among all of the parties.