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INSURANCE LAW UPDATE

By Jennifer Kelley

FIFTH CIRCUIT APPLIES "ENTITLED TO BENEFITS" RULE AND "INDEPENDENT INJURY" RULE IN LIGHT OF TEXAS SUPREME COURT'S *MENCHACA* OPINION, AND REAFFIRMS APPLICABILITY OF TEXAS' "ANTI-STACKING" RULE.

The Fifth Circuit in *Lyda Swinerton Builders, Inc. v. Oklahoma Sur. Co.*, considered a suit between a general contractor and the insurer of its subcontractor alleging that the insurer breached its CGL policy by failing to defend the general contractor in an underlying state court breach of contract and negligence action by the owner of the construction project. 877 F.3d 600 (5th Cir. 2017). The facts of the underlying lawsuit are fairly simple: Lyda Swinerton Builders ("LSB"), a general contractor, was hired to build a ten story office building. LSB hired, in turn, several subcontractors including Willis, a roofing subcontractor. In the subcontract between LSB and Willis, Willis was required to maintain CGL insurance coverage designating LSB as an additional insured with respect to liability arising out of Willis' work under the subcontract. The subcontract included the following indemnification provision:

> TO THE FULLEST EXTENT PERMITTED BY LAW, SUBCONTRACTOR AGREES TO DEFEND, HOLD HARMLESS AND UNCONDITIONALLY INDEMNIFY CONTRACTOR AND OWNER . . . AND ALL PARTIES WHOM CONTRACTOR IS REQUIRED TO INDEMNIFY PURSUANT TO THE TERMS OF THE CONTRACT DOCUMENTS, AGAINST AND FOR ALL LIABILITY, COSTS, EXPENSES, CLAIMS, LIENS, CITATIONS, PENALTIES, FINES, ATTORNEYS' FEES, LOSSES, AND DAMAGES WHICH CONTRACTOR MAY AT ANY TIME SUFFER OR SUSTAIN OR BECOME LIABLE FOR BY REASON OF ANY ACCIDENTS, DAMAGES, OR INJURIES EITHER TO THE PERSONS OR PROPERTY OR BOTH OF CONTRACTOR, OWNER OR SUBCONTRACTOR, OR OF THE WORKERS OF SUCH PARTIES, OR OF ANY OTHER PARTIES, OR TO THE PROPERTY OF ANY PARTY, IN ANY MANNER ARISING OUT OF OR RESULTING FROM SUBCONTRACTOR'S PERFORMANCE OR FAILURE TO PERFORM HEREUNDER, OR FAILURE OR DEFECTS IN MATERIALS OR GOODS SUPPLIED BY OR ON BEHALF OF SUBCONTRACTOR, ~~INCLUDING, BUT NOT LIMITED TO, ANY NEGLIGENT ACT OR OMISSION OR CLAIM INVOLVING STRICT LIABILITY OR NEGLIGENCE PER SE OF CONTRACTOR OR OWNER, THEIR OFFICERS, DIRECTORS, SHAREHOLDERS, EMPLOYEES, AGENTS, CONTRACTOR'S SURETY AND ALL PARTIES WHOM CONTRACTOR IS REQUIRED TO INDEMNIFY PURSUANT TO THE TERMS OF THE CONTRACT DOCUMENTS.~~ (Strikethrough in original).
>
> THE COVERAGE OF ANY INSURANCE POLICY REQUIRED HEREIN OR ACTUALLY CARRIED BY SUBCONTRACTOR SHALL NOT LIMIT THE EXTENT OF SUBCONTRACTOR'S LIABILITY UNDER THE FOREGOING INDEMNITY.

Before signing the subcontract, Willis' President made handwritten changes to the contract, including striking out the portion of the indemnification provision above. LSB did not countersign the subcontract and LSB apparently did not notice or object to Willis' alterations. Willis obtained a CGL policy with a standard insuring agreement. The policy also contained an endorsement identifying LSB and affiliates as additional insureds "but only with respect to liability directly attributable to [Willis'] performance of '[Willis'] work' for [LSB and LSB's parent and affiliates]." *Id.* at 606.

Facts:

In the underlying state court lawsuit, claims were asserted against LSB seeking damages for breach of contract alleging that the project was not timely completed, that it failed to adequately supervise work performed by subcontractors, and for negligence asserting that LSB breached its duty to exercise ordinary care in supervising its subcontractors, causing property damage. LSB filed a third party petition against subcontractors including Willis. The owner's petition against LSB referred to Willis as a third-party defendant but did not expressly identify it as a subcontractor. In a subsequent amended petition, again the owner made specific references to Willis only as "third-party defendant" but not identified by name or as subcontractor. LSB demanded a defense and indemnity from Oklahoma Surety Company, Willis' liability insurer who denied LSB's demand.

LSB then sought damages and declaratory relief against Oklahoma Surety for breach of contract based on its failure to defend LSB, violations of Chapter 541 of the Texas Insurance Code, and violations of Texas' prompt payment of claims statute. The district court found that LSB was entitled to a defense in the underlying state court action and OSB therefore owed damages including defense costs; Oklahoma Surety violated the prompt pay statute by breaching its duty to defend; and denied Oklahoma Surety's counter-motion for summary judgment based on Texas' "anti-stacking rule." In addition, the district court ruled that LSB did not prove that it had suffered an independent injury from the denial of benefits and, therefore LSB was not entitled to recover extra-contractual damages in absence of an independent injury. (Notably, the district court's opinion was issued pre-*Menchaca*, and the Fifth Circuit's opinion, post.).

Appeal:

On appeal to the Fifth Circuit, LSB appealed the district court's ruling denying its claim for extra-contractual damages under Chapter 541 of the Texas Insurance Code, and Oklahoma Surety appealed the district court's rulings as to duty to defend, breach of duty, and liability under the prompt payment of claims statute.

1. Additional Insured

Oklahoma Surety argued that the subcontract was not a written contract that entitled LSB to be an additional insured under the additional insured by "written insured contract" endorsement because LSB never countersigned. The Fifth Circuit rejected this argument noting well established Texas law allows a party to assume the tort liability of another even without an enforceable contract. Additionally, Oklahoma Surety argued the subcontract did not confer

additional insured coverage because of the handwritten modifications; the court also rejected this argument because the part of the provision remaining still stated that "Willis agrees to 'unconditionally indemnify' LSB 'to the fullest extent permitted by law' for 'all liability' that LSB incurs for damages 'in any manner arising out of or resulting from [Willis'] performance or failure to perform' under the subcontract." Thus, the Fifth Circuit concluded that LSB was an additional insured for all claims except for those involving strict liability and negligence per se.

2. Duty to Defend

Although the petition did not identify Willis by name, the petition and subsequent amendments alleged that LSB was responsible for "material deficiencies" affecting portions of the project including the roof and roof structures. The Fifth Circuit held that the petition's allegation that LSB failed to "adequately supervise work performed by subcontractors" sufficiently alleged liability attributable to Willis' performance of its work for LSB. As a result, the Fifth Circuit held that "[r]eading the original petition liberally, and resolving any doubts in LSB's favor, there was at least a *potential* that ADP's suit fell within the policy's scope of coverage." *Id.* at 612.

3. Anti-Stacking Rule

"Stacking" refers to "taking policy limits from multiple, but not overlapping, policies potentially covering the same lawsuit and adding those limits together." *Id.* at 614. The Fifth Circuit noted that the Texas Supreme Court has adopted an "anti-stacking rule" that prohibits an insured from stacking multiple consecutive policies when a single claim extends across several distinct policy periods; rather, "the insured's indemnity limit [is] whatever limit applied at the single point in time during the coverage periods of the triggered policies when the insured's limit was highest." *Id.* (quoting *American Physicians Insurance Exchange v. Garcia*, 876 S.W.2d 842, 853-55 (Tex. 1994)). Oklahoma Surety argued that the anti-stacking rule precluded LSB's claims because another insurer insured Willis for some of the years involved in the underlying suit and LSB selected that other insurer to provide a defense and, therefore, allowing LSB to recover defense costs from Oklahoma Surety would effectively allow LSB to "stack" the Oklahoma Surety policy with the other insurer's policy. The Fifth Circuit expressed doubt that the Texas Supreme Court would extend the "anti-stacking rule" which applies to an insurer's indemnity obligation to the defense context; but refused to answer the question outright.

4. Extra-Contractual Damages

In one of the most significant opinions post-*Menchaca*, the Fifth Circuit next addressed LSB's cross-appeal seeking reversal of the district court's denial of extra-contractual damages under the Texas Insurance Code. Traditionally, Texas Law allowed extra-contractual recovery in favor of an insured when an insurer withholds policy benefits even if the insured is unable to show any independent injury beyond the wrongly denied policy benefits. *Vail v. Texas Farm Bureau Mutual Insurance Co.*, 754 S.W.2d 129 (Tex. 1988). While the appeal was pending before the Fifth Circuit, the Texas Supreme Court issued its *USAA Texas Lloyds Co. v. Menchaca* opinion in which the court reaffirmed the Texas "entitled-to-benefits" rule providing that "an insured who establishes a right to receive benefits under an insurance policy can recover

those benefits as 'actual damages' under the [Insurance Code] if the insurer's statutory violation causes the loss of the benefits." *Id.* at 617 (citing *USAA Texas Lloyds Co. v. Menchaca*, -- S.W.3d --, No. 14-0721, 2017 WL 1311752, at *7 (Tex. Apr. 7, 2017), *reh'g granted* (Dec. 15, 2017); as well as the "independent injury rule" which provides that "if an insurer's statutory violation causes an injury independent of the insured's right to recover policy benefits, the insured may recover damages for that injury even if the insured is not entitled to receive benefits under the policy." *Id.* at 617 (citing *Menchaca* at 12).

In light of the Texas Supreme Court's *Menchaca* holding, therefore, the Fifth Circuit concluded that because LSB was entitled to a defense from Oklahoma Surety as a benefit of the policy, if Oklahoma Surety's statutory violations (e.g. misrepresentation of the coverage afforded by the policy) caused LSB to be deprived of that defense benefit, LSB is legally entitled to recover the resulting defense costs as actual damages under Chapter 541 of the Texas insurance code without limitation from the independent injury rule. *Id.* at 618.

5. Prompt Payment of Claims Statute

Finally, the Fifth Circuit addressed Oklahoma Surety's argument that the 18% penalty provided by Section 542.060(a) of the Texas Insurance Code accrues only until the date of final judgment, not until the date the final judgment is actually paid. The Fifth Circuit noted that the prompt payment of claims statute does not expressly state when the 18% penalty stops accruing. The Fifth Circuit reaffirmed its earlier position that the penalty accrues only until the judgment is entered. However, because the opinions of the district court and the Fifth Circuit vacated the trial court's judgment, there was not yet a final judgment. Thus, Oklahoma Surety was required to pay the 18% per annum penalty until the time that a new judgment was entered on remand in accordance with the Fifth Circuit's opinion.

TEXAS INTERMEDIATE APPELLATE COURT ADDRESSES INTERACTION AND ENFORCEMENT OF "OTHER INSURANCE" PROVISION IN UNINSURED/UNDERINSURED MOTORIST PORTION OF TWO IDENTICAL AUTOMOBILE INSURANCE POLICIES.

In *Elwess v. Texas Farm Bureau Mut. Ins. Co.*, the Eastland Court of Appeals addressed an insured's argument that "other insurance" provisions in Uninsured/Underinsured Motorist Coverage forms have been invalidated by the Texas Supreme Court in all cases. . -- S.W.3d --, No. 11-15-00286-CV, 2017 WL 6559654, at *4 (Tex. App.—Eastland Dec. 21, 2017, no pet.). The Eastland Court of Appeals rejected this argument noting that although the Texas Supreme Court has held that an "other insurance" provision may be invalid where "the provision prevents the claimant from recovering the actual damages caused by an uninsured/underinsured motorist" (*Id.* at *3 (citing *Stracener v. United Services Auto. Ass'n*, 777 S.W.2d 378, 380 (Tex. 1989); *Texas & P. Ry. Co. v. Roberts*, 481 S.W.2d 798, 799–800 (Tex. 1972))) this rule does not invalidate "other insurance" clauses in all circumstances involving uninsured/underinsured motorist coverage. Rather, an "other insurance" provision is not invalid where it does not prevent an injured plaintiff from recovering his actual damages caused by the uninsured/underinsured motorist, such as in *Elwess*, where the injured plaintiff actually did recover in excess of his actual damages from other insurance policies providing coverage for the accident.

TEXAS COURT OF APPEALS FOLLOWS *BRAINARD* AND REFUSES TO IMPOSE LIBILITY ON UIM INSURER WHO CONSENTED TO INSURED'S POLICY-LIMIT SETTLEMENT WITH LIABILITY CARRIER WHERE THERE WAS NO JUDGMENT ESTABLISHING LIABILITY.

In *Weber v. Progressive County Mutual Ins. Co*., No. 05-17-00163-CV, 2018 WL 564001, (Tex. App.—Dallas, January 26, 2018, mem. op.), a Progressive insured was injured in a motor vehicle accident and with Progressive's consent, she settled her claim with the other motorist's insurer for the $30,000 policy limit. The insured then demanded the policy limit of her UIM coverage ($100,007) with Progressive, claiming she had over $150,000 in medical expenses. Progressive offered the insured $30,000, which she rejected. The insured sued Progressive and Progressive' claim representative for breach of contract and for violations of the Texas Insurance Code. The defendants responded with special exceptions, asserting in part that the insured's claims were premature until she obtained a judgment establishing the liability of the other driver and the amount of her damages, and that the "exhaustion doctrine" was not recognized in Texas and therefore, the insured failed to state a viable cause of action. The trial court sustained the special exceptions and dismissed the insured's claims with prejudice. The Dallas Court of Appeals affirmed the dismissal because (1) the insured's claim for breach of contract was premature under *Brainard v. Trinity Universal Insurance Co*., 216 S.W.3d 809 (Tex. 2006) even though the insurer consented to the insured's liability settlement, and (2) the insured's claim under the theory of the "exhaustion doctrine" failed to state a viable cause of action.

In *Brainard*, the Texas Supreme Court ruled that a "UIM insurer is under no contractual duty to pay benefits until the insured obtains a judgment establishing the liability and underinsured status of the other motorist." *Brainard*, 216 S.W.3d at 818. Further, "neither a settlement with nor an admission of liability from the underinsured motorist establishes UIM coverage, because a jury could find that the underinsured motorist was not at fault or award damages that do not exceed the [underinsured motorist's] liability insurance." *Id*. Based on *Brainard*, the court held that the insured failed to present a contract claim because the petition did not allege that she had obtained a judgment against the other driver, and therefore, she failed to establish the existence of a duty owed by the defendants. Progressive's consent to the insured's liability settlement did not alter that requirement that she obtain a judgment.

The insured also argued her petition stated a viable claim against the defendants under the Texas Insurance Code under the "exhaustion doctrine" which she argued entitled UIM claimants to UIM bodily injury benefits upon (1) an agreement by insurer with insured; (2) providing the insurer with a judgment of damages by legal proceeding; or (3) a settlement or judgment exhausting the policy limits of all liability policies. The court held that adoption of the doctrine would directly conflict with *Brainard's* holding that a settlement is not sufficient to impose contractual liability on a UIM insurer to pay benefits. The court stated that "[w]hatever the virtues of a contrary rule might be, as an intermediate court, we are bound to follow the rule laid down in *Brainard* unless and until the supreme court reconsiders or revises it."

CERTIFICATE OF SUBSTANTIAL COMPLETION DOES NOT FULFILL SURETY'S OBLIGATIONS UNDER PERFORMANCE BOND.

In *Wolfe City, Texas v. American Safety Cas. Ins. Co.*, No. 06-17-00075-CV, 2018 WL 792108 (Tex. App.—Texarkana Feb. 9, 2018), the Texarkana court of appeals held that a certificate of substantial completion on a construction project was not enough to relieve the contractor's surety of its obligations under a performance bond. In *Wolfe City*, a construction company (M&M) contracted to install an automatic water meter system in Wolfe City. American Safety provided a performance bond to the contractor. When most of the work had been completed, the city's engineer on the project signed a certificate of substantial completion. Afterward, the City began to have significant problems with the meter system.

In the resulting lawsuit, American Surety moved for and won summary judgment in the trial court on the ground that the certificate of substantial completion absolutely relieved it of any duty under the performance bond. American Surety also won a no-evidence summary judgment on the ground that there was no evidence the problems which occurred after the certificate of completion was signed were the result of any construction defect rather than a design defect in the products supplied under the project's specifications. The court of appeals disagreed with respect to both rulings.

Under the terms of its bond, American Safety bound itself to perform M&M's contract with the City if M&M failed to do so. In addition, the bond specifically incorporated the terms of the contract. A surety's liability under a performance bond issued to secure performance of a construction contract is determined by examining the underlying contract. Thus, American Safety was only liable to the City under its bond if M&M breached the contract. Therefore, in order to determine whether there was evidence showing that M&M failed to perform under the contract and whether American Safety owed the City any obligation under its bond, the court had to examine the relevant terms of the contract.

The contract expressly specified that M&M's obligation to complete the work in accordance with the contract was absolute, and that a certificate of substantial completion would not release M&M from its obligations. The contract also expressly provided that M&M (and by extension, the surety company) was required to correct problems discovered within one year of substantial completion. Based on the contract's terms and the evidence presented by the parties, the court found the summary judgment evidence produced by the City was evidence that M&M breached the contract by failing to properly supervise, direct, and inspect the installation of the meters, failing to provide and install a fully functioning system, and by failing to repair or replace the defects discovered in its work.

American Safety argued that a surety may rely on a certificate of substantial completion as a final discharge of its liability on its performance bond, citing cases regarding the one-year statute of limitations to bring suit on a performance bond. The court held that those cases did not stand for the proposition that a certificate itself is the equivalent to full performance of the contract. To the contrary, in *Wolfe City*, the contract expressly imposed additional duties on the contractor (and by extension, on the surety company) to correct problems discovered within one year of substantial completion.

Having concluded the certificate of substantial compliance was not definitive proof of full performance of the contract, the court of appeals also reversed American Safety's no-evidence summary judgment. The court held there was some evidence the contractor had breached its contract because of the numerous problems discovered after the certificate was signed, and which the contractor had an obligation to correct. The contract exonerated the contractor of any responsibility for a design defect in the project resulting from the negligence of the city or the engineer, and the contractor argued that because the project specifications required the contractor to use a specific brand of meters, the defects in those meters were the city's fault and not the contractor's. However, the contract provided that the contractor was responsible for supervising all work performed by subcontractors, and the subcontractor who provided the defective meters was under the contractor's supervision.

COURT RELIES ON EIGHT-CORNERS RULE TO FIND NO DUTY TO DEFEND.

In *Dorvin D. Leis of Texas, Inc. v. Ohio Casualty Ins. Co. d/b/a Liberty Mutual Co*., No. 05-17-00548-CV 2018 WL 850931 (Tex. App. – Dallas Feb. 14, 2018), the Dallas Court of Appeals affirmed summary judgment in favor of the insurer (Liberty), concluding that based on the "eight-corners" rule, Liberty did not have a duty to defend its insured under a CGL policy. The underlying lawsuit involved allegations by a pro se litigant (Saleh) which alleged Leis discriminated against Saleh, who is Muslim or Arab, because Leis did not return Saleh's calls or e-mails regarding a malfunctioning thermostat. Leis requested Liberty provide a defense to the Saleh litigation but Liberty refused. Leis retained counsel who obtained dismissal of Saleh's lawsuits, incurring attorney's fees and costs. After the Saleh litigation was dismissed, Leis sued Liberty for breach of contract and for violations of the Texas Insurance Code.

Liberally construing Saleh's pleadings, the Court of Appeals found that Saleh alleged in the first lawsuit that he was damaged when Leis failed to communicate with him because his name indicated he is Muslim or Arab. Saleh asserted Leis discriminated against him because of his race, religion, or ethnic background, which caused him to suffer damages. In the second lawsuit, Saleh alleged he was damaged because Leis conspired with others to file a false return of service. Saleh made no allegation that he suffered bodily injury, sickness or disease or physical injury or loss of use of tangible property. The Court concluded that neither the discrimination alleged by Saleh nor conspiracy to file a false return of service constituted an allegation of bodily injury or property damage and to reach the conclusion Leis urges "would require us to read facts into the pleadings or imagine factual scenarios that might trigger coverage, which we may not do." Because Saleh's petitions did not allege bodily injury or property damage, Liberty did not have a duty to defend.

GENERAL CONTRACTOR WAS NOT ENTITLED TO THE EXCLUSIVE REMEDY DEFENSE UNDER THE WORKERS' COMPENSATION ACT BECAUSE THE SUBCONTRACTOR WAS ACTUALLY THE ENTITY "PROVIDING" THE COVERAGE.

In *Halferty v. Flextronics America*, LLC, 13–16–00379–CV, 2018 WL 897979 (Tex. App. – Corpus Christi Feb. 15, 2018), a workers' compensation case, the issue presented was whether a general contractor (Flextronics) was entitled to the exclusive remedy defense in a

common law negligence action filed against it by an injured subcontracted employee, Patrick Halferty.

The facts showed that Flextronics entered into an agreement with Titan to perform various IT work at a Flextronics facility and in the agreement, Titan agreed to "provide, pay for and maintain in full force and effect" workers' compensation insurance "in compliance with statutory limits in the respective state/country where work was being performed by Titan." Titan contracted with another entity (Outsource) to assist in installing networking cabling at the premises. It was undisputed that Titan and Outsource complied with the workers' compensation provision of the agreement to cover all their employees on the project, including Halferty, who was an employee of Outsource. Halferty was injured on the job and sued Flextronics for negligence and gross negligence, alleging an employee of Flextronics caused his personal injuries.

Flextronics filed a traditional motion for summary judgment, arguing that it was entitled to the Texas Workers' Compensation Act's exclusive remedy defense, which would bar Halferty's claim against it, because as the general contractor, it served as Halferty's employer for purposes of the Act. The trial court granted the motion and the appeal followed.

On appeal, Halferty argued that Flextronics is not entitled to summary judgment because it did not "provide" workers' compensation insurance coverage to him that would entitle Flextronics to the exclusive remedy defense. In response, Flextronics argued that Flextronics did provide coverage to Halferty pursuant to its agreement with Titan. The Court of Appeals framed the issue as: under Texas Labor Code section 406.123(a), did Flextronics "provide" workers' compensation insurance to Halferty as an employee of Outsource?

The Court of Appeals discussed the Act's process by which a general contractor qualifies for immunity from common-law tort claims brought by the employees of its subcontractors known as the "exclusive remedy" defense, citing Texas labor Code § 408.001(a) ("Recovery of workers' compensation benefits is the exclusive remedy of an employee covered by workers' compensation insurance coverage or a legal beneficiary against the employer or an agent or employee of the employer for the death of or a work-related injury sustained by the employee."). The first step of the process is that the general contractor and subcontractor must enter into a written agreement under which the general contractor provides workers' compensation insurance coverage to the subcontractor and the employees of the subcontractor. This agreement makes the general contractor a statutory employer of the subcontractor's employees for purpose of the workers' compensation laws. As the statutory employer, the general contractor is entitled to immunity from common-law tort actions brought by the subcontractor's employees, and a covered employee's exclusive remedy for work-related injuries is workers' compensation benefits.

With respect to the Flextronics/Titan contract, the contract specifically obligated Titan to "provide, pay for and maintain in full force and effect" workers' compensation insurance for their employees and "any and all subcontractors, or anyone directly or indirectly employed by any of them...." Thus, the obligation to obtain workers' compensation coverage began with Titan—not with Flextronics. The contract did not place any onus on Flextronics to ensure that

subcontracted employees, like Halferty, were covered i.e. there was nothing in the contract whereby Flextronics assured that the coverage remained in place. Flextronics did not pay for the workers' compensation insurance coverage nor was it required to purchase or pay for workers' compensation insurance. Aside from the contractual mandate that Titan "provide, pay for and maintain" workers' compensation insurance, nothing in the contract assured that coverage remained in place if the workers' compensation policies were terminated. The contract required that Titan furnish to Flextronics copies of the certificates of insurance but required nothing more.

The Court of Appeals held that "to seek the exclusive remedy defense, section 406.123(a) requires a general contractor to do something more than simply passing the onus of obtaining coverage to the subcontractor." For example, the contract between Flextronics and its subcontractors could have provided for an alternate insurance plan in which Flextronics would provide coverage in the event that its subcontractors failed to obtain insurance; or, Flextronics could have built enforcement mechanisms into its contract with subcontractors—such as withholding payment, or deducting insurance premium costs—that would trigger in the event that the subcontractors failed to provide coverage to its employees. The court concluded that based on the record, Flextronics was not entitled as a matter of law to the protections and benefits of the exclusive remedy defense because it did not "provide" workers' compensation benefits to Halferty.

AUSTIN COURT OF APPEALS AFFIRMS *CROCKER* HOLDING, CONCLUDING NO DUTY TO DEFEND OR INDEMNIFY WHERE NO TENDER BY INSURED.

In *Egly v. Farmers Ins. Exchange*, 03-17-00467-CV, 2018 WL 895043 (Tex. App. – Austin, Feb. 15, 2018), the undisputed facts showed that Ismael Hernandez was involved in a collision with Egly while driving a vehicle insured under an automobile liability policy issued by Farmers. Egly sued Hernandez for negligence. Hernandez never notified Farmers of the suit. However, Egly's attorney sent several messages to Farmers informing them of the suit. In one message, Egly's attorney warned Farmers that Egly would obtain a default judgment against Hernandez if no answer was filed. Farmers sent messages to Hernandez inquiring about the case, but Hernandez never responded to those messages. Egly obtained a default judgment against Hernandez. He then sued Farmers, seeking payment of the default judgment as a third-party beneficiary to the vehicle's insurance policy. Farmers filed a traditional motion for summary judgment, arguing that it had established as a matter of law that it had no duty to defend the suit against Hernandez, and therefore no duty to pay Egly, because Hernandez never informed Farmers of the suit as required by the policy. The trial court rendered a final summary judgment in Farmers' favor, which was affirmed on appeal.

The Austin Court of Appeals relied on Texas Supreme Court precedent (*National Union Fire Insurance Co. of Pittsburgh, PA v. Crocker*, 246 S.W.3d 603, 609 (Tex. 2008)) which explained that an insurer who has actual knowledge of a suit is not required to defend its insured when the insured has not informed the insurer of the suit or asked the insurer for representation. The Court of Appeals quoted from *Crocker* which stated "[m]ere awareness of a claim or suit does not impose a duty on the insurer to defend under the policy; there is no unilateral duty to act unless and until the additional insured first *requests* a defense—a threshold duty that the insured fulfills under the policy by notifying the insurer that the insured has been served with process

and the insurer is expected to answer on its behalf." In *Egly*, Hernandez never notified Farmers that he "expect[ed] the insurer to interpose a defense" or was "looking to the insurer to provide a defense." Therefore, Farmers had no duty to defend against Egly's suit.

EASTERN DISTRICT OF TEXAS REAFFIRMS THAT A SETTLEMENT IS NOT A "JUDGMENT" THAT LEGALLY ENTITLES AN INSURED TO RECOVER UNDER HIS UNDERINSURED MOTORIST COVERAGE.

In *Adedpipe v. Safeco Ins. (a Liberty Mut. Co.)*, a United States District Court for the Eastern District of Texas issued a memorandum opinion concluding that a policyholder-plaintiff was not entitled to recover damages under his underinsured motorist coverage following settlement with the underlying defendant. -- S.W.3d --, No. 4:17-CV-347, 2018 WL 295428 (E.D. Tex. Jan. 4, 2018). The policyholder-plaintiff, insured by Safeco Insurance, was struck by another vehicle, causing personal injuries. The third-party driver had an automobile liability insurance policy with State Farm at the time of the accident. The Safeco insured settled the underlying lawsuit with State Farm, with Safeco's consent, receiving $30,000.00, the third-party driver's policy limit. In the subsequent coverage action for UIM benefits, the Safeco Insured sought to recover from his insurer, arguing that the damages he sustained in the collision greatly exceeded the amount of damages he received from State Farm in the settlement.

Safeco argued that the policyholder-plaintiff was not legally entitled to recover under his UIM policy because the policyholder-plaintiff did not obtain a judgment against the third-party driver, which was a condition precedent to coverage under the UIM policy. Safeco moved to dismiss the policyholder-plaintiff's claims on this basis. The District Court granted the motion to dismiss because without a legal judgment establishing liability and damages, Safeco had no legal duty to pay damages under the UIM Policy and could not, therefore, be held liable for breach of contract. Relying on well-established Texas law, the District Court found that the settlement with State Farm did not constitute a legal judgment establishing liability of the third-party driver. As such, the district court also dismissed claims under the Texas prompt payment statute and the Texas Deceptive Trade Practices Act.

The district court also noted established Texas law regarding the issue of settlement with consent, noting that "insurers are not foreclosed or otherwise estopped from arguing that an insured is not entitled to coverage under a UIM policy by virtue of approving a third-party settlement under Texas state law." *Id.* (citing *In re State Auto Prop. & Cas. Ins. Co.*, 348 S.W.3d 499, 502 (Tex. App.—Dallas 2011, pet. struck)). Although an insurer may consent to the insured's settlement with a third party, that consent does not constitute a judgment on the merits. As a result, the condition precedent in the Safeco UIM policy requiring a judgment against the third-party was not satisfied and the policyholder-plaintiff's claims were dismissed.

SOUTHERN DISTRICT OF TEXAS DEMONSTRATES THE NEED FOR CLARITY IN COVERAGE DENIAL LETTERS.

In *Ekhlassi v. Nat'l Lloyds Ins. Co.*, a United States District Court for the Southern District of Texas issued a memorandum opinion concluding that an insured's first party lawsuit against its insurer under a privately written flood insurance policy was barred by the applicable

one-year statute of limitations. *Ekhlassi v. Nat'l Lloyds Ins. Co.*, -- S.W.3d --, No. CV H-17-1257, 2018 WL 341887 (S.D. Tex. Jan. 9, 2018). The insured, Ali Ekhlassi held a flood insurance policy with National Lloyds Insurance Company, underwritten by the Federal Emergency Management Agency ("FEMA"). As Part of the National Flood Insurance Program, National Lloyds policy was a Standard Flood Insurance Policy.

Between May 23 and May 25, 2015, severe storms caused heavy flooding in parts of Houston. This flooding damaged Ekhlassi's home when five to six feet of floodwater filled his unfinished basement garage for two days. In May, 2015, immediately after the flood, Ekhlassi reported his loss to National Lloyds. National Lloyds sent an insurance adjuster to inspect Ekhlassi's property, estimating the total covered losses to be $3,768.15. On October 6, 2015, National Lloyds sent Ekhlassi a letter stating it could not remit payment of the $3,768.15 until it received sworn proof of loss, informing Ekhlassi he had 240 days from the date of loss to provide a sworn proof of loss. The letter also notified Ekhlassi that National Lloyds was denying payment for "any building and contents items not subject to direct physical loss by or from flood" and "all non-covered items located below the lowest elevated floor of your post-FIRM elevated building."

On December 28, 2015, Ekhlassi provided a sworn proof of loss stating an amount of $274,940.05. On January 11, 2016, National Lloyds sent Ekhlassi a second letter rejecting the proof of loss, stating it would only pay the previously determined amount of $3,768.25, and referring Ekhlassi to the October 6 denial letter for the basis for denial. A year later, on January 11, 2017, Ekhlassi sued National Lloyds alleging breach of contract, violations of Chapters 541 and 542 of the Texas Insurance Code, and violations of the Texas Deceptive Trade Practices Act. Under the National Flood Insurance Program, policyholders have a one-year statute of limitations to challenge a denial of coverage by filing suit. *See* 42 U.S.C. § 3072. National Lloyds moved for summary judgment based on the statute of limitations arguing that limitations began to run with the initial October 6, 2015 denial letter; Ekhlassi argued the January 11, 2016 letter was the true date of denial, starting the clock for the suit. The October 6, 2015 denial letter stated:

> The Independent Adjuster's final report indicates there were no visible signs of covered flood damage to the subfloor and flooring of the first elevated floor. We are denying payment for any building and contents items not subject to direct physical loss by or from flood, pursuant to the Standard Flood Insurance Policy.
> . . .
> In accordance with the Standard Flood Insurance Policy, we are denying payment for all non-covered items located below the lowest elevated floor of your post-FIRM elevated building . . . .

The letter also stated: "[i]f you do not agree with our decision to deny your claim, in whole or in part, Federal law allows you to appeal that decision within 60 days of the date of this denial letter." The January 11 letter rejected Ekhlassi's attempt to increase his payment by submitting proof of loss for the full amount, and referenced the October letter directly, stating: "[p]lease refer to the denial letter dated October 6, 2015 for what Federal law allows under the Standard Flood Insurance Policy and for the reasons of denial for damages that have been

claimed." The District Court concluded that the October 6 letter was clearly a denial letter; it referred to itself as a denial letter and made clear that National Lloyds was denying the majority of Ekhlassi's claim at that time. Thus the statute of limitations began to run on October 6, 2015 and Ekhlassi's claims were time barred.

FEDERAL COURT FINDS ALLEGATIONS AGAINST EMPLOYEE ADJUSTER SUFFICIENTLY ALLEGED TEXAS INSURANCE CODE VIOLATIONS AND REMANDS CASE TO STATE COURT.

In *Sarkar Investments, Inc. d/b/a Palace Inn – Tomball v. Travelers Property Casualty Company of America*, No. 4:17-CV-03061, 2018 WL 706471 (S.D. Tex. February 5, 2018**)**, a federal district court in Houston analyzed the allegations against an employee adjuster and held that the allegations were sufficient to state a cause of action against the adjuster under the Texas Insurance Code, which defeated diversity jurisdiction, requiring that the case be remanded to state court. In *Sarkar Investments*, the insured presented a claim for wind, hail and water damage alleging a 2015 storm damaged the insured's property. Travelers assigned its adjuster (Carr) who was responsible for retaining experts, investigating and adjusting the claim. Unhappy with Carr's findings and determinations regarding the damage, the insured brought suit in state court against Travelers and Carr. Travelers removed the case to federal court alleging that the adjuster was improperly joined to defeat diversity jurisdiction. The insured, believing they had sufficiently stated causes of action against Carr, filed a motion to remand the case to state court.

The insured alleged that Carr engaged in the following unfair practice: "Not attempting in good faith to effectuate a prompt, fair, and equitable settlement of an insurance claim submitted in which liability has become reasonably clear" under Tex. Ins. Code § 541.060(a)(2). Defendants argued that the insured failed to allege sufficient specific facts against Carr that would lead to Carr's individual liability under state law. The court held that the weight of authority in Texas is that adjusters may be found individually liable under Texas Insurance Code § 541.060. Therefore, if the Complaint sufficiently alleged a valid claim against Carr individually, remand was appropriate. The court analyzed the pleadings, observing several, specific allegations against Carr such as assertions of a biased investigation, retaining biased experts, overlooking wind and hail damage, underestimating and misrepresenting "the actual cost to repair or replace the under scoped wind and hail damage…particularly with respect to the necessary costs of materials, labor, taxes, and contractor overhead and profit" and similar allegations. The court concluded that the insured's allegations "contain adequate detail to reach the threshold of facial plausibility and thus to state a claim on which relief can be granted" against the adjuster under Tex. Ins. Code § 541.060(a)(2)(A)." Therefore, federal diversity jurisdiction was defeated and the case was remanded to state court.

ALLEGATIONS OF CONTROL WERE SUFFICIENT TO TRIGGER AN INSURANCE CARRIER'S DEFENSE OBLIGATION UNDER AN EMPLOYER'S LIABILITY POLICY.

R.M. Personnel, Inc. v. Liberty Mutual Fire. Ins. Co., No. A-16-CA-01030-SS, 2018 WL 935397, at *1 (W.D. Tex. Feb. 16, 2018), involved a dispute over insurance coverage involving an accident at a commercial construction site in El Paso, Texas, where Luis Alberto Rodriguez

fell fifty feet down an elevator shaft resulting in severe personal injuries. Mr. Rodriguez filed suit against RMP and others and obtained a judgment against RMP in the amount of $3,485,000. The lawsuit before the federal court concerned whether Liberty had a duty to defend RMP in the *Rodriguez* Lawsuit. At the time of Mr. Rodriguez's accident, RMP was insured under a workers' compensation and employer's liability policy issued by Liberty. After being served in the *Rodriguez* Lawsuit, RMP sought coverage from Liberty, requesting a defense. Liberty denied coverage, claiming Mr. Rodriguez's petition alleged no employment relationship between RMP and Mr. Rodriguez as required by the Policy. In RMP's motion for partial summary judgment, RMP asked the Court to determine whether Liberty owed a duty to defend RMP in the *Rodriguez* Lawsuit.

Applying the eight-corners rule to Mr. Rodriguez's latest pleading, the court observed Mr. Rodriguez alleged "RMP provided personnel and safety training and agreed to provide safety equipment to personnel it provided" on the construction site. Mr. Rodriguez also alleged "RMP controlled the scope of the work to be performed by workers its assigned to the site, including [Mr. Rodriguez]; undertook responsibility for and controlled the training received by workers it assigned to the site, including [Mr. Rodriguez]; and undertook responsibility for and controlled the safety equipment provided to workers it assigned to the site, including [Mr. Rodriguez]." In addition, Mr. Rodriguez expressly alleged he "was in the course and scope of his employment" at the construction site when the accident occurred.

Based on those allegations, the court concluded the facts alleged in Mr. Rodriguez's petition potentially stated a cause of action covered by the Policy, and that Liberty had a duty to defend RMP in the *Rodriguez* lawsuit.

> "First, Mr. Rodriguez alleged RMP 'provided personnel' to the construction site. From such a statement, it is possible to conclude Mr. Rodriguez was an employee of RMP. Other factual allegations strengthen that conclusion. Specifically, Mr. Rodriguez alleged he was one of the workers RMP assigned to the construction site, trained, and provided with safety equipment. Furthermore, Mr. Rodriguez indicated RMP controlled the scope of his work. As a worker's status as employee depends on whether the employer has the right to control the person's work, the allegation RMP controlled Mr. Rodriguez's work supports concluding Mr. Rodriguez was RMP's employee. *Limestone Prod. Distribution, Inc. v. McNamara*, 71 S.W.3d 308, 312 (Tex. 2002) ("The test to determine whether a worker is an employee rather than an independent contractor is whether the employer has the right to control the progress, details, and methods of operations of the work."). Coupled with Mr. Rodriguez's allegation he 'was in the course and scope of his employment' when the accident occurred, it is reasonable to conclude Mr. Rodriguez asserted claims as an RMP employees for bodily injuries occurring in the course and scope of his employment."