AN UPDATE ON RECENT INSURANCE COVERAGE DECISIONS AND THEIR IMPACT ON THE CONSTRUCTION INDUSTRY:

THE POLICYHOLDERS' PERSPECTIVE

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Most headlines in early 2020 related to disputes between insureds and insurers regarding COVID-19-related business losses. The Supreme Court of Texas, however, issued two opinions addressing fundamental duty-to-defend issues. Despite this, questions remain—and litigation will likely continue—as to the standard for evaluating whether an insurer has a duty to defend its insured.

Generally, Texas courts follow the "eight corners" rule in determining whether a duty to defend exists, meaning the review is limited to the "four corners" of the pleading filed against the insured and the "four corners" of the insurance policy.[1] For years, the Supreme Court of Texas was presented with opportunities to adopt an exception to the "eight corners" rule. Though the Court *recognized* on several occasions that *other* courts had applied exceptions in limited circumstances, the Court itself never had formally adopted any exception.[2] One such exception was from the United States Court of Appeals for the Fifth Circuit's 2004 opinion in *Northfield Insurance Co. v. Loving Home Care, Inc.*, where the court held that the use of extrinsic evidence is permitted only when relevant to an independent and discrete coverage issue, not touching on the merits of the underlying third-party claim, *and* when "it is initially impossible to discern whether coverage is potentially implicated" (commonly referred to simply as the "*Northfield* Exception").[3]

A. Background of *Richards*

On March 20, 2020, the Supreme Court addressed the extrinsic evidence issue again in *Richards*.[4] The case came before the Court via certified question from the Fifth Circuit, which sought guidance as to whether a "policy language" exception to the "eight corners" rule exists under Texas law.[5]

The underlying case involved the tragic death of a 10-year-old in an ATV accident at his grandparents' house.[6] The boy was under the temporary care of his grandparents at the time of the accident. Subsequently, the boy's mom sued the grandparents, who sought coverage for the lawsuit from their insurer, State Farm Lloyds. State Farm Lloyds initially agreed to provide a defense, but then filed a declaratory judgment action arguing that exclusions precluded the duty to defend.[7]

The first exclusion was a "motor-vehicle exclusion" that precluded coverage for bodily injury "'arising out of the . . . use . . . of . . . a motor vehicle owned or operated by or loaned to

[1] *Richards v. State Farm Lloyds*, 597 S.W.3d 492, 499–500 (Tex. 2020).

[2] *See, e.g.*, *GuideOne Elite Ins. Co. v. Fielder Rd. Baptist Church*, 197 S.W.3d 305, 308 (Tex. 2006) ("Although this Court has never expressly recognized an exception to the "eight corners" rule, other courts have.")

[3] 363 F.3d 523, 531 (5th Cir. 2004) (emphasis in original).

[4] *Richards*, 597 S.W.3d at 499–500.

[5] *State Farm Lloyds v. Richards*, 784 F. App'x 247, 253 (5th Cir. 2019).

[6] *Richards*, 597 S.W.3d at 495.

[7] *Id.*

any insured.'"[8] The term '"motor vehicle'" was defined to include an "'all-terrain vehicle' . . . owned by an insured and designed or used for recreational or utility purposes off public roads, while off an insured location."[9] The policy defined the term '"insured location' to mean 'the residence premises.'"[10] To support its motion for summary judgment, State Farm Lloyds included a crash report to show that the accident did not occur on the grandparents' premises. State Farm Lloyds also attached admissions by the grandparents that the accident did not occur at their premises.

State Farm Lloyds also relied on an "insured exclusion," which barred coverage for bodily injuries to insureds and defined "insured" to include "you and, if residents of your household: a. your relatives; and b. any other person under the age of 21 who is in the care of a person described above."[11] State Farm Lloyds argued that the child was an "insured" because the grandparents were his joint managing conservators.[12] As proof, State Farm Lloyds submitted a court order from a suit affecting the parent-child relationship ("SAPCR").[13] The grandparents argued in response that the "eight corners" rule prohibited the district court from considering the crash report and the SAPCR order in evaluating whether State Farm Lloyds had a duty to defend.

Over the insureds' objections, the federal district court allowed State Farm Lloyds to rely on the extrinsic evidence it submitted in conjunction with its summary judgment briefing. Finding that the extrinsic evidence established that the policy would not provide coverage—and, thus, there would be no duty to defend—the court ruled in favor of State Farm Lloyds. The district court referenced and relied upon the "policy language" exception to the "eight corners" rule in making its determination.[14] The insureds then appealed to the Fifth Circuit.

Notably, on appeal, State Farm Lloyds made no effort to defend the analysis of the district court.[15] The Fifth Circuit began its analysis by surveying the current jurisprudence regarding the application and scope of the duty-to-defend rule and circumstances where extrinsic evidence was allowed or disallowed in making the defense determination. The Fifth Circuit noted that neither it nor any Texas court had recognized a "policy language" exception to the "eight corners" rule. The Fifth Circuit further noted that, while it and many Texas state and federal courts recognized and applied the *Northfield* Exception, other Texas state courts had declined to even recognize that any exception existed.[16]

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[8] *Id*.

[9] *Id*.

[10] *Id.*

[11] *Id.*

[12] *Id*. at 496.

[13] *Id.*

[14] *Id*.

[15] *Id*. (referencing *State Farm Lloyds v. Richards*, 784 F. App'x 247, 250 (5th Cir. 2019)).

[16] *Id*. at 496–97 (citing *AIX Specialty Ins. Co. v. Shiwach*, No. 05-18-01050-CV, 2019 WL 6888515, at *7 (Tex. App.—Dallas Dec. 18, 2019, pet. denied) ("Although the Fifth Circuit and multiple intermediate appellate courts have

Recognizing that "there is no controlling Texas Supreme Court caselaw determining whether there is a policy-language exception to the "eight corners" rule" and that the issue "involves important and determinative questions of Texas law," the Fifth Circuit certified to the Supreme Court of Texas the question of whether Texas courts should recognize the "policy-language exception to the "eight corners" rule."[17]

B. The Supreme Court of Texas Rejects the "Policy Language" Exception to the "Eight Corners" Rule

In analyzing the certified question, the Court recognized that parties can contract around the "eight corners" rule, but clarified that the question at hand was whether the insurer actually had contracted around the rule by "declining to expressly agree that State Farm Lloyds must defend claims 'even if groundless, false or fraudulent.'"[18] In particular, State Farm Lloyds argued that the "eight corners" rule developed because of the once common "groundless-claims clauses."[19] Because that language is no longer common in liability policies, State Farm Lloyds argued that the "eight corners" rule should change, "no matter how deeply in the law it has become."[20] In response, the Richardses argued that the "eight corners" rule is not dependent upon the presence of the "groundless claims" clause, specifically noting that, in evaluating the duty to defend, the Supreme Court of Texas's analysis never has turned on the presence of such language.[21] Thus, according to the Richardses, "[b]ecause the presence or absence of a groundless-claims clause has rarely, if ever, been important to Texas courts' analysis of the contractual duty to defend, and because Texas courts routinely apply the eight-corners rule without looking for a groundless-claims clause, the . . . federal district court's 'policy-language exception' is erroneous."[22]

The Supreme Court of Texas agreed with Richards, explaining that State Farm Lloyds did not contract away the "eight corners" rule altogether by omitting an "express agreement to defend claims that are 'groundless, false or fraudulent.'" In doing so, the Court recognized that Texas courts of appeal routinely have applied the "eight corners" rule "for many decades, without regard to whether the policy contained a groundless-claims clause."[23] Continuing, the Court noted that, "[g]iven the consistency of Texas appellate decisions on this topic, those who write insurance contracts know courts applying Texas law will employ the eight-corners rule, subject possibly to

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expressly recognized a limited exception to this rule, permitting consideration of extrinsic evidence when relevant only to the coverage issue, the Texas Supreme Court and this Court have not yet done so."); *USAA Texas Lloyd's Co. v. Doe*, No. 04-15-00673-CV, 2017 WL 2791327, at *3 (Tex. App.—Amarillo June 28, 2017, pet. denied) ("The duty to defend is not affected by facts discovered before suit, developed in the course of litigation, or by the outcome of the suit."); *AccuFleet, Inc. v. Hartford Fire Ins. Co.*, 322 S.W.3d 264, 273 (Tex. App.—Houston [1st Dist.] 2009, no pet.) ("We decline to create an exception to the eight corners rule . . . .")).

[17] *Richards*, 784 F. App'x. at 253.

[18] *Richards*, 597 S.W.3d at 497.

[19] *Id*. at 497–98.

[20] *Id.* at 498.

[21] *Id.*

[22] *Id*.

[23] *Id*. at 499.

exceptions such as that found in the Fifth Circuit's *Northfield* decision. We can safely presume their agreements are drafted in light of this understanding."[24]

The Court also specifically recognized that the duty to defend is a "creature of contract" and "'a valuable benefit granted to the insured by the policy.'"[25] Thus, the Court found that the "eight corners" rule is not an amendment to the parties' agreement, but rather a "purpose . . . to effectuate those agreements, to enforce them consistently and predictably so that parties may write their agreement knowing how courts will interpret them."[26] The Court determined that State Farm Lloyds agreed to defend if '"a claim is made or a suit is brought against an insured for damages because of bodily injury . . . to which this coverage applies."'[27] Thus, whether a "claim" has been "made" or a "suit" has been "brought," requires courts to "naturally look first to the claims made, to the suit brought."[28] In other words, according to the Court, "the eight-corners rule merely acknowledges that, under many common duty-to-defend clauses, only the petition and the policy are relevant to the initial inquiry into whether the petition's claim fits within the policy's coverage."[29] The Court noted that "[t]his is how Texas courts have long interpreted contractual duties to defend" and that, "[i]f any party is familiar with the overwhelming precedent to that effect, it is a large insurance company."[30] Consequently, the Court concluded that State Farm Lloyds did not contract around the "eight corners" rule by simply omitting the words "groundless, false or fraudulent," or similar words, from its policy.[31]

In dicta, the Supreme Court of Texas recognized that "it is often the case that the petition states a claim that could trigger the duty to defend, but the petition is silent on facts necessary to determine coverage."[32] While recognizing that some courts have "often allow[ed] extrinsic evidence on coverage issues that do not overlap with the merits in order to determine whether the claim is for losses covered by the policy," the Court declined to express an opinion on that issue, citing to the Fifth Circuit's limited certified question. The Court also specifically reserved "comment on whether other policy language or other factual scenarios may justify the use of extrinsic evidence" in evaluating the duty to defend.

C. Background of *Avalos*

Just a few months after issuing its opinion in *Richards*, the Court evaluated the extrinsic evidence issue again in *Avalos*.[33] In that case, Loya Insurance Company ("Loya") sold an

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[24] *Id.*

[25] *Id*. (quoting *Pine Oak Bldrs., Inc. v. Great Am. Lloyds Ins. Co.*, 279 S.W.3d 650, 655 (Tex. 2009)).

[26] *Id*. 499–500.

[27] *Id.* at 500.

[28] *Id.*

[29] *Id.*

[30] *Id.*

[31] *Id.*

[32] *Id*.

[33] 610 S.W.3d 878 (Tex. 2020).

automobile liability insurance policy to Karla Flores Guevara. Guevara's husband, Rodolfo Flores, explicitly was excluded from coverage by a named driver exclusion.[34] While moving Guevara's car, Flores collided with another car carrying Osbaldo Hurtado Avalos and Antonio Hurtado (the "Hurtados"). The Hurtados, Guevara, and Flores agreed to tell both the responding police officer and the insurer that Guevara was driving the car rather than Flores.[35]

The Hurtados sued Guevara, asserting that their damages resulted from Guevara's negligent operation of her vehicle. Guevara sought coverage from Loya, which agreed to defend and appointed counsel to represent her. Early in discovery, "Guevara disclosed the lie to her attorney and identified Flores as the driver."[36] In response to this disclosure, Loya cancelled Guevara's scheduled deposition, denied coverage, and withdrew from the defense.[37] The Hurtados subsequently obtained a $450,343.34 judgment against Guevara.[38]

Guevara assigned her rights against Loya to the Hurtados, who then filed suit against Loya for breach of contract for denying coverage to Guevara. Loya filed counterclaims for breach of contract and fraud and sought a declaratory judgment that it owed no coverage and had no duty to defend because Flores, an excluded driver, was driving at the time of the accident. Loya then deposed Guevara, who recanted her initial statement that she, rather than Flores, was driving. Loya moved for summary judgment, asserting that it owed no coverage or duty to defend. Attached to that motion as evidence were excerpts of Guevara's depositions.[39]

The trial court granted summary judgment for Loya, stating at the hearing that the Hurtados were "'asking this Court to ignore every rule of justice and help [them] perpetuate a fraud.'"[40] On appeal to the Court of Appeals of San Antonio, the Hurtados argued that the summary judgment was improper under the "eight corners" rule because Loya had a duty to defend as a matter of law based on the terms of the insurance policy and the face of the pleadings in the underlying suit in which they alleged Guevara was driving at the time of the accident. The court of appeals reversed the trial court's judgment, holding that, "'as logically contrary as it may seem,'" the insurer had a duty to defend under the "eight corners" rule.[41] The case then was appealed to the Supreme Court of Texas.

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[34] *Id.* at 880.

[35] *Id*.

[36] *Id.*

[37] *Id.*

[38] *Id.*

[39] *Id.*

[40] *Id*.

[41] *Id.* (quoting *Avalos v. Loya Ins. Co.*, 592 S.W.3d 138, 145 (Tex. App.—San Antonio)).

D. The Supreme Court of Texas Finds that a Collusive Fraud Exception Exists Under Limited Circumstances

The Court first explained that it had suggested "twice before that collusive fraud by the insured might provide the basis for an exception" to the "eight corners" rule.[42] While the Court did not look to extrinsic evidence in those cases, it determined that the egregious facts and circumstances presented by *Avalos* justified the adoption of a "collusive fraud" exception to the "eight corners" rule.[43] In particular, with respect to "falsity," the Court explained that no dispute existed as to who was actually driving the vehicle that collided with the Hurtados.[44] Likewise, with respect to "collusion," there was no dispute that the Hurtados agreed with Guevara and her husband to make false statements about who was driving in order to trigger Guevara's insurance coverage and Loya's duty to defend.[45] In fact, Guevara's own admissions under oath conclusively established that the Hurtados and Guevaras "conspired to lie about who was driving to trigger insurance coverage."[46]

Recognizing that the "eight corners" rule is a "creature of contract," the Court concluded that the rule "does not bar courts from considering such extrinsic evidence regarding collusive fraud by the insured in determining the insurer's duty to defend."[47] The Court explained that the defense of third-party claims is a "valuable benefit granted to the insured by the policy."[48] While an insurer must defend even "if the third party suing the insured makes allegations that are groundless, false, or fraudulent,"[49] the Court drew a sharp distinction, finding that this rule "applies to fraudulent allegations against the insured *by third parties*" and not fraudulent claims perpetrated by insureds.[50] Continuing, the Court said:

> The insurer has not agreed to undertake, and the insured has not paid for, a duty to defend the insured against fraudulent allegations brought about by the insured itself. Thus, an insurer owes no duty to defend when there is conclusive evidence that groundless, false, or fraudulent claims against the insured have been manipulated by the insured's own hands in order to secure a defense and coverage where they would not otherwise exist.[51]

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[42] *Id*. at 881 (citing *Pine Oak Bldrs., Inc. v. Great Am. Lloyds Ins. Co.*, 279 S.W.3d 650 (Tex. 2009); *GuideOne Elite Ins. Co. v. Fielder Rd. Baptist Church*, 197 S.W.3d 305, 307, 311 (Tex. 2006)).

[43] *Id.* at 882.

[44] *Id.*

[45] *Id.*

[46] *Id.*

[47] *Id*.

[48] *Id*.

[49] *Id*. (citing *Richards v. State Farm Lloyds*, 597 S.W.3d 499–500 (Tex. 2020)).

[50] *Id*.

[51] *Id.*

As a result, the Court held that extrinsic evidence was admissible regarding whether the insured and a third party suing the insured colluded to make false representations of fact in that suit for the purpose of securing a defense and coverage where they would not otherwise exist.[52]

The Court also rejected the Hurtados' contention that an insurer must pursue a declaratory judgment action to determine its duty to defend before withdrawing from the defense of the insured.[53] In reaching this decision, the Court explained that, while it has "encouraged insurers to utilize declaratory judgment actions for prompt resolution of disputes, [it has] not mandated that course."[54] If an insurer has "conclusive evidence" of an insured lying to get coverage, it would—according to the Court—be a waste of judicial resources to require the insurer to seek a judicial determination of coverage.[55] Moreover, the Court reasoned that the fact that "an insurer that breaches its duty to defend by withdrawing can be held liable for substantial damages and attorneys' fees," "will help ensure that an insurer withdraws its defense without first securing a declaratory judgment only in clear-cut cases."[56]

E. Application of *Richards* and *Avalos* in *Young*

On May 12, 2020, the U.S. District Court for the Northern District of Texas issued an opinion in *National Liability & Fire Insurance Company v. Young*, in which it evaluated *Richards*, *Avalos*, and the *Northfield* Exception, all in one.[57] There, the federal district court declined to allow an insurer to rely on extrinsic evidence in evaluating its duty to defend.

In *Young*, John Young d/b/a Rio Restaurant ("Mr. Young") was insured under a business auto policy issued by National Liability & Fire Insurance Company ("National Liability").[58] The policy provided liability coverage for any "auto" that the insured "do[es] not own while used with the permission of its owner as a temporary substitute for a covered 'auto' you own that is out of service because of its: a. Breakdown; b. Repair; c. Servicing; d. 'Loss'; or e. Destruction."[59] The insuring agreement of the policy stated that National Liability would cover all sums that the insured "legally must pay as damages because of 'bodily injury' or 'property damage' to which this insurance applies," and that National Liability has "the right and duty to defend any 'insured' against a 'suit' asking for such damages . . . ."[60]

On February 6, 2019, Gustina Penna ("Penna") was operating a vehicle rented from Enterprise Rent-A-Car to Mr. Young when she was involved in a collision with Rogelio

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[52] *Id*.

[53] *Id.*

[54] *Id*. at 833 (citing *Excess Underwriters at Lloyd's v. Frank's Casing Crew & Rental Tools, Inc.*, 246 S.W.3d 42, 46 (Tex. 2008)).

[55] *Id.*

[56] *Id.*

[57] *Natl'l Liab. & Fire Ins. Co. v. Young*, 459 F. Supp. 3d 796, 799–800 (N.D. Tex. 2020).

[58] *Id.* at 797–98.

[59] *Id.* at 798.

[60] *Id.*

Castellanos. Mr. Castellanos suffered fatal injuries from the collision.[61] A state court lawsuit was filed against Mr. Young, Penna, and another entity where plaintiffs sought damages for negligence and gross negligence arising from the collision.[62]

National Liability subsequently filed a declaratory judgment action in federal court, seeking a judgment that it had no duty to defend or indemnify the defendants in the underlying state-court lawsuit.[63] National Liability conceded that the First Amended Petition in the underlying lawsuit "specifically alleges the vehicle operated at the time of the incident in question was rented temporarily to . . . Young . . . and was being used temporarily as a substitute for one of his permanent vehicles that was being repaired or serviced at the time of the incident."[64] Additionally, there were allegations that Young gave Penna permission to use the vehicle and that she was operating it in connection with her employment by Young's business. Based on this, the court stated:

> Application of the eight-corners rule to this case is therefore straightforward. The First Amended Petition alleges that the vehicle Penna was driving at the time of the accident was a temporary substitute auto within the meaning of the insurance policy. National Liability has not identified any applicable exclusion within the policy's text, and the Court has not located any such exception. Thus, the First Amended Petition implicates the policy's coverage.[65]

Nevertheless, National Liability argued that the rented vehicle that Penna drove at the time of the accident was not covered under the terms of the policy because Young rented the vehicle continuously between August 2018 and February 2019 and because "none of [the insured's] Specifically Described 'Autos' under the Policy were being repaired."[66] In asserting that it was allowed to resort to this extrinsic evidence in assessing the duty to defend, National Liability relied "heavily" on the "policy language" exception that had been proposed by the district court in *State Farm Lloyds v. Richards*.[67] The court summarily rejected this argument in light of the Supreme Court of Texas' opinion from *Richards*: "[T]he omission of a groundless-claims clause from the insurance policy that is at issue here cannot support an exception to the eight-corners rule."[68]

The court then moved to whether the *Northfield* Exception would allow National Liability to introduce extrinsic evidence. In support of its position, National Liability asserted "that the issue of whether the vehicle Penna was driving at the time of the accident 'qualified as a temporary substitute pursuant to the Policy's terms' does not 'overlap with the merits of the Underlying

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[61] *Id.*

[62] *Id.*

[63] *Id*.

[64] *Id*.

[65] *Id*. at 799.

[66] *Id*. at 798.

[67] *Id*. at 799.

[68] *Id.*

Lawsuit or engage the truth or falsity of any substantive facts bearing upon liability.'"[69] The court disagreed, noting that the "facts demonstrate otherwise," and that it was possible to discern from the allegations in the First Amended Petition that coverage was implicated because the vehicle was a "temporary substitute for a covered 'auto.'" As a result, the court found that the *Northfield* Exception did not apply.[70]

Moreover, the court concluded that the "collusive fraud" exception outlined in *Avalos* also was inapplicable. The court recognized:

> National Liability does not allege that the insured . . . conspired to manipulate a groundless, false, or fraudulent claim against National Liability. Rather, National Liability attacks the alleged 'gamesmanship of the underlying plaintiffs in amending their original petition after this coverage action was filed.' [citation omitted]. Moreover, National Liability lacks "conclusive evidence" that any manipulation occurred.[71]

Continuing, the court explained that "[a]rtful pleading, in which National Liability effectively alleges that the plaintiffs in the underlying lawsuit engaged, does not give rise to an exception to the eight-corners rule."[72] Rather, if an insurer knows that the allegations in the underlying pleading are untrue, the insurer has a "duty to establish such facts in defense of its insured, rather than as an adversary in a declaratory judgment action."[73]

F. Commentary

Young addressed *Richards*, *Avalos*, and the *Northfield* Exception. In doing so, the Northern District recognized that the "eight corners" rule remains alive and well and that the use of extrinsic evidence applies only in a narrow set of circumstances. While *Avalos* and the "collusive fraud" exception presented interesting developments in the coverage world, the ruling is not much of a surprise, especially based on the facts and circumstances of the case. The very narrow exception to the "eight corners" rule carved out in that case requires conclusive proof of collusion and insurance fraud by the insured and the third-party claimant.

In *Young*, the Northern District expressly recognized the significant distinction between circumstances where there is collusive fraud and circumstances where there is "artful" pleading. It may be that many insurers have a difficult time meeting the *Avalos* standard to show that collusive fraud should allow introduction of extrinsic evidence. In *Richards*, the Court specifically referred to the *Northfield* Exception (by name) and outlined the narrow circumstances under which courts have applied it in other cases. The Court then declined, once again, to express an opinion on the *Northfield* Exception, noting that it was only addressing the narrow question certified as to

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[69] *Id*. at 801.

[70] *Id.*

[71] *Id*. 801–02 (quoting *Loya Ins. Co. v. Avalos*, 610 S.W.3d 878, 882 (Tex. 2020)).

[72] *Id*. at 802

[73] *Id*. (citing *GuideOne Elite Ins. Co. v. Fielder Road Baptist Church*, 197 S.W.3d 305, 311 (Tex. 2006); *Liberty Surplus Ins. Corp. v. Allied Waste Systems, Inc*., 758 F.Supp.2d 414, 420 (S.D. Tex. 2010)).

whether a "policy language" exception exists. While the Court recognized but expressly declined to analyze the *Northfield* Exception in *Richards*, it did not even mention the *Northfield* Exception in *Avalos*.

This presents an interesting question: Is the *Northfield* Exception good law? If so, why did the Court not—at the very least—discuss that rule (much less even mention its existence) in *Avalos*, which was the first time the Court actually acknowledged that there are circumstances where extrinsic evidence is admissible in analyzing the duty to defend? The Northern District recognized that, although the Supreme Court of Texas did not address the *Northfield* Exception in *Avalos*, that rule remains binding on Texas federal district courts: "Neither Texas case law nor a change in statutory authority has displaced the Fifth Circuit's *Northfield* [E]xception."[74] It appears that, if the Northern District case is any indication, the *Northfield* Exception will continue to be applied on a narrow basis (at least in federal courts). More importantly perhaps, the "collusive fraud" exception will be applied only in extreme cases.

II. *Mid-Continent Casualty Company v. McCollum Custom Homes, Inc.*, 461 F. Supp. 3d 516 (S.D. Tex. 2020)

In *Mid-Continent Casualty Company v. McCollum Custom Homes, Inc.*, the United States District Court for the Southern District of Texas evaluated a host of exclusions in determining whether an insurer had a duty to defend or a duty to indemnify its insured against an underlying lawsuit relating to the defective construction of a custom home.

A. Background Facts

In 2014, the Mark Family purchased a "spec" home in Houston being constructed by McCollum Custom Homes, Inc. ("McCollum") that cost well over $2,000,000.[75] McCollum was the general contractor for the project as well as the seller. Just over a year after moving into the home, the Mark Family began discovering a number of issues with the home, including "leaking windows; hundreds of drywall, mortar, and brick cracks; and extensive foundation movement."[76] The root cause of these issues, as alleged in the state court petition, is a defective foundation caused by McCollum's failure to take proper account for the effects of the drought Houston experienced from 2011 to 2013.[77] The Mark Family claims that McCollum and its subcontractors inadequately assessed risks relating to the moisture levels in the soil when removing trees from the area and building the home's foundation, and that McCollum failed to follow a drainage plan designed by a third party who was not sued. These failures allegedly caused the physical movement of the home's foundation.[78] This movement in the foundation allegedly caused cracks in the sheetrock, brick, mortar, stucco, tile and concrete floors; water leaks into the home from the roof and windows; the inoperability of doors; and visible displacement of the pool.[79] McCollum tendered

[74] *Id*. at 800.

[75] *Mid-Continent Cas. Co. v. McCollum Custom Homes, Inc.*, 461 F. Supp. 3d 516, 519 (S.D. Tex. 2020).

[76] *Id*. at 519.

[77] *Id.*

[78] *Id.*

[79] *Id.*

the lawsuit to Mid-Continent, who agreed to provide a defense subject to a reservation of rights.[80] Mid-Continent then filed a declaratory judgment action, seeking a ruling that its policy did not provide coverage for the damages sought by the Mark Family.

B. The Court Determines that the "Defective Work" Exclusion Bars Coverage for Damages to the Foundation

Having found that the insuring agreement was met based on the allegations, the court turned to whether any exclusions barred coverage. The first exclusion the court evaluated was the "defective work" exclusion, which stated:

> This insurance does not apply to:
>
> **l. Defective Work**
>
> "Defective Work" includes any and all costs associated with the removal or replacement of the defective, deficient or faulty work.
>
> * * *
>
> "Defective Work" means "Your Work" that is defective, deficient, non-conforming, not in accordance with plans and specifications, fails to satisfy applicable building code(s), fails to meet industry practice standards, is not fit for its intended use, not performed in a workman like manner or is faulty, and is included in the products-completed operations hazard.[81]

The Court concluded that this exclusion barred coverage for the damage to the foundation itself, which was alleged to have been defective, but not to the other items. In particular, the court noted that it was not apparent, "from the face of the [pleading,] that all of the . . . problems [at issue] were themselves 'defective,' 'deficient,' 'faulty,' etc."[82] The Court noted that it was unclear, for example, if the "brick, mortar, and stucco cracks, water leaks from the roof and windows, cracking tile, sheet rock, and concrete floors, doors that could not open or close, and a displaced pool" were simply defective or resulted from the movement of the defective foundation.[83]

C. The Court Determines that the "Earth Movement" Exclusion Bars Coverage for the Remainder of the Damages Sought in the Underlying Lawsuit

The Court then moved to the "earth movement" exclusion, which stated:

> This insurance does not apply to any "bodily injury" or any "property damage", that is directly or indirectly caused by, involves, or is in any way connected or related to any movement of earth, whether naturally occurring or due to manmade or other artificial causes.

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[80] *Id*. at 521.

[81] *Id*. at 526.

[82] *Id.*

[83] *Id.*

> Movement includes, but is not limited to, settlement, cracking, contraction, compaction, compression, consolidation, subsidence, shrinking, expansion, heaving, swelling, caving-in, erosion, vibration, shock, earthquake, landslide, mudflow, wind-driven, freezing, thawing or any other movement of earth, regardless of the cause.
>
> Earth includes, but is not limited to any dirt, soil, terrain, mud, silt, sediment, clay, rock, sand, fill material or any other substances or materials contained therein.[84]

The court explained that the allegations regarding leaks from the window and roof should be considered jointly with the allegations of damages to walls, bricks, roof, windows, door, three types of flooring, and pool, as those were purportedly the result of the home's foundation movement.[85] Mid-Continent argued that the "earth movement" exclusion barred coverage for this "laundry list" of damages because the foundation shifted due to "movement of the earth."[86] In support of its position, Mid-Continent argued that the allegations in the underlying pleading focused on the failure of McCollum and/or its agents "to conduct a proper risk assessment related to the soil before building the home's foundation."[87] In other words, Mid-Continent argued that the "earth moved and took the foundation with it, and the foundation movement allegedly caused the problems in the . . . home."[88] In response, McCollum argued that there were multiple causes of damage to the home and that, while the foundation movement was a "major problem," it was not the *only* problem.[89] Next, relying on *Wilshire Insurance Company v. RJT Construction, LLC*,[90] McCollum also argued that the exclusion should not apply because it did not cause the soil to move.[91]

The court explained that the "duty to defend is not tethered to only the core allegations, but instead all allegations must be considered."[92] In evaluating the pleading as a whole, the court agreed with Mid-Continent that the "earth movement" exclusion barred coverage for the "laundry list" of damages relating to the foundation movement.[93] According to the court, the underlying lawsuit was brought because of the alleged deficiencies of the soil foundation investigation report prepared by McCollum or its subcontractor. The underlying pleading included allegations that the report failed to take account of the effect of a lengthy drought in the Houston area, which led to an inadequate analysis regarding the proper design of the home's foundation.[94] This improper

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[84] *Id*. at 520.

[85] *Id*. at 524.

[86] *Id*. at 526–27.

[87] *Id*. at 527.

[88] *Id.*

[89] *Id.*

[90] 581 F.3d 222 (5th Cir. 2009).

[91] *McCollum*, 461 F. Supp. 3d at 527.

[92] *Id.*

[93] *Id.*

[94] *Id.*

foundation design failed to take into account potential changes in soil content, which subsequently led to foundation movement when the earth shifted.[95] The court concluded, therefore, that when the allegations were read together, the exclusion applied because there were allegations that the foundation movement contributed to and/or caused the defects and damages.[96]

McCollum argued that the exclusion should not apply because there were allegations of damage relating to its failure to follow the drainage plan. The court explained that these allegations directly followed allegations that McCollum did not take proper care when it came to the moisture content of the soil.[97] The court determined that, when read together, the allegations suggested "that McCollum did not take care to properly assess the risks presented by the moisture content of the soil and that this failure was exacerbated by its failure to implement a proper drainage plan."[98] These actions, according to the court, contributed to McCollum building the foundation on soil susceptible to movement, which led to the earth movement and caused the alleged defects and damages.[99]

The court also rejected McCollum's second argument, explaining that the earth movement exclusion in the *RJT Construction* case on which McCollum relied explicitly required that the movement of land result from the operations of the insured or its subcontractor, whereas the exclusion in Mid-Continent's policy barred coverage for any damages relating to movement of the earth "whether naturally occurring or due to man-made or other artificial causes."[100] Thus, the court explained that the "fact that McCollum may not have moved the soil is irrelevant and [did] not trigger a duty to defend."[101]

D. The Court Finds that Mid-Continent has no Duty to Indemnify

Having found that there was no duty to defend based on a combination of the "defective work" and "earth movement" exclusions, the Court then evaluated whether Mid-Continent had a duty to indemnify McCollum.[102] Mid-Continent argued that it had no duty to indemnify because it prevailed on its duty to defend arguments and because "no facts can be developed in the underlying tort suit that will change claims that are fundamentally excluded . . . into covered losses."[103] McCollum responded that a fact question existed as to whether it was responsible for the damages to the pool, so summary judgment on the duty to indemnify was improper.[104] Noting that McCollum had "confuse[d] the issue," the Court explained that, if McCollum is not held

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[95] *Id.*

[96] *Id.*

[97] *Id*. at 528.

[98] *Id.*

[99] *Id.*

[100] *Id.* at 528–29.

[101] *Id*. at 529.

[102] *Id.*

[103] *Id.*

[104] *Id*. at 530.

responsible for the damage to the pool, then it would not have potential liability that would trigger the insuring agreement.[105] On the other hand, if McCollum was responsible for that damage, any coverage for that damage would be excluded by the "earth movement" exclusion. Thus, the Court concluded that, "[i]n either event, Mid-Continent has no duty to indemnify."[106] The Court also concluded that all of the remaining damages for which McCollum could be held liable fell within one of the exclusions that also precluded the duty to defend. As a result, the Court also ruled that Mid-Continent did not have a duty to indemnify as a matter of law.[107]

E. Commentary

Though added by endorsements, the "earth movement" and "defective work" exclusions within the Mid-Continent policy at issue in *McCollum* are becoming more common in commercial general liability policies issued to homebuilders. Both exclusions are relatively broad and preclude coverage for common risks faced in the construction of new homes in Texas. Insurers also have begun to draft these exclusions even more broadly, as evidenced by the distinction in policy language from that in *McCollum* as compared to the similar exclusion at issue in *RJT Construction.* This case also illustrates the fact that insurance policies are contracts and courts will give meaning to the specific wording of exclusions—even when they are enhanced to narrow coverage.

III. *Balfour Beatty Construction, L.L.C. v. Liberty Mutual Fire Insurance Co.*, 968 F.3d 504 (5th Cir. 2020)

In *Balfour Beatty Construction, L.L.C. v. Liberty Mutual Fire Insurance Co.*, the Fifth Circuit evaluated whether coverage was available to an insured under a builders' risk policy for damage to the exterior of glass windows caused by welding slag.[108]

A. Background Facts

TCH Energy Corridor Venture, LLC ("Trammell Crow") was the developer of a commercial office building located in Houston, Texas, known as Energy Center 5 (the "Project"). Trammell Crow selected Balfour Beatty Construction, L.L.C. ("Balfour") as the Project's general contractor. Balfour, in turn, subcontracted with Milestone Metals, Inc. ("Milestone") for the erection of structural steel, stairs, and ornamental steel on the Project. Under Trammell Crow's contract with Balfour, Trammell Crow was required to procure builder's risk insurance for the Project, which it did through Liberty Mutual Fire Insurance Company, and which was in effect from July 10, 2014, to August 10, 2016.[109]

In October 2015, Milestone welded a 2-inch metal plate to external tubing on the eighteenth floor of the Project.[110] Milestone's Safety Director testified that Milestone utilized safety measures

[105] *Id.*

[106] *Id.*

[107] *See id.* at 531.

[108] 968 F.3d 504 (5th Cir. 2020).

[109] *Id*. at 506.

[110] *Id*. at 507.

to avoid damaging the building when installing the plate. On July 12, 2016, Milestone learned that welding slag from the October 2015 welding operations had fallen down the side of the building and damaged the exterior of certain glass windows on lower floors.[111] Trammell Crow, Balfour, and Milestone then tendered a claim to Liberty under the policy.

B. The Coverage Dispute

Liberty conceded that the window damage was a "direct physical loss or damage" that triggered the insuring clause of the policy.[112] Nevertheless, Liberty denied coverage based on the following exclusion:

> 2. "We" do not pay for loss or damage that is caused by or results from one or more of the following:
>
> * * *
>
> c. **Defects, Errors, And Omissions –**
>
> (1) "We" do not pay for loss or damage consisting of, caused by, or resulting from an act, defect, error, or omission (negligent or not) relating to:
>
> a) design, specifications, construction, materials, or workmanship;
>
> * * *
>
> c) maintenance, installation, renovation, remodeling, or repair.
>
> But if an act, defect, error, or omission as described above results in a covered peril, "we" do cover the loss or damage caused by that covered peril.
>
> (2) This exclusion applies regardless of whether or not the act, defect, error or omission:
>
> a) originated at a covered "building or structure"; or
>
> b) was being performed at "your" request or for "your" benefit.[113]

Following the denial of coverage, Milestone and Balfour ultimately replaced the windows for Trammell Crow at a cost of $686,976.88. Milestone and Balfour then filed suit against Liberty.[114] In the coverage litigation, the parties stipulated that the "defects, errors, and omissions" exclusion applied.[115] Instead, the dispute centered on whether the exception to the exclusion restored coverage for the damage to the windows.[116] The district court determined that the

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[111] *Id.*

[112] *Id*. at 508.

[113] *Id*. at 507–08.

[114] *Id*. at 508.

[115] *Id.*

[116] *Id.*

exception did not reinstate coverage under the circumstances of the loss and granted Liberty's motion for summary judgment.[117]

C. The Fifth Circuit Holds that the Exception does not Restore Coverage for the Loss

On appeal, the Fifth Circuit noted that, although the exception does not use the term "ensuing loss," similar exceptions often are referred to as "ensuing loss" provisions that "operate "to provide coverage when, as a result of an excluded peril, a covered peril arises and causes damage."[118] The court determined, however, that the exception did not restore coverage for the loss at issue, as it only would restore coverage "when one (excluded) peril results in a distinct (covered) peril, meaning there must be two separate events for the [e]xception to trigger."[119]

In particular, the Court explained that the question was whether the "an act, defect, error, or omission" "result[ed] in a covered peril." In other words:

> [The] welding operation involved falling slag, which damaged the exterior glass of [the Project]. The welding operation is inseparable from the falling slag; they are not two separate events. The falling slag is not an independent event that "resulted in a covered peril." Instead, the falling slag during the welding operation constituted damage, caused by an act of construction or installation, to the exterior glass. Further, even if the falling slag is separable from the welding operation, it is not a "covered peril." Under the [p]olicy, [the] claim is not covered because it falls within the [e]xclusion.[120]

According to the court, the damage to the exterior glass was caused by the "construction and installation activities, specifically, the falling slag occurring during [the] welding project."[121] Therefore, the exception would restore coverage only if the welding project itself "result[ed] in a covered peril."[122] The court explained that the damage caused by an act of construction is not a "covered peril" because it falls within the exclusion.[123] Thus, the court found that the welding project did not "result in" a separate covered peril; rather, the welding project and attendant falling slag was itself the peril and for which no coverage existed.[124]

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[117] *Id.*

[118] *Id*. at 511.

[119] *Id*. at 511–12.

[120] *Id*. at 512.

[121] *Id.*

[122] *Id.*

[123] *Id*. at 512–13.

[124] *Id*. at 513.

D. The Court Finds that the Policy is not Illusory and that the Insureds Forfeited Arguments that the Policy was Ambiguous

The court next rejected arguments that the policy was illusory.[125] In particular, the court noted that the policy provides coverage under numerous potential factual scenarios, including for damage caused by acts of nature.[126] Further, the policy also potentially would apply in the event of a fire unrelated to construction activities, if a vehicle damaged a pillar of the building, or even if construction-related damage weakened the building and that weakness was later exacerbated by a separate event.[127] Thus, the court concluded that the policy was not illusory.[128]

Next, the court explained that the insureds had forfeited any arguments that the policy was ambiguous because that issue was not presented in their initial pleading or to the district court.[129] Notwithstanding that issue, the court noted that, even if the ambiguity argument had been presented to the court and preserved for appeal, it would not have changed the analysis, as the court determined that the policy "'as written can be given a clear and definite legal meaning."'[130]

E. Commentary

The ensuing loss provision at issue in this case was rather narrow, restoring coverage only when the excluded peril results in loss that is caused by a separate and independent covered peril. While a fairly innocuous decision in light of the policy terms, this decision provides a reminder as to the importance of reviewing insurance policy terms at the time of purchase and considering the issues that might arise in the event of a faulty workmanship related loss. In that regard, although the terms of this particular policy are common, other versions of such exclusions exist with far broader "ensuing loss" exceptions. It is incumbent on the party that seeks coverage to point out the differences between the *specific* language used in exclusions. Otherwise, there is a danger that courts will apply this opinion beyond its intended reach.

IV. *Gonzalez v. Mid-Continent Casualty Co.*, 969 F.3d 554 (5th Cir. 2020)

In *Gonzalez v. Mid-Continent Casualty Company*, the Fifth Circuit held that "property damage" was "deemed to occur" in 2013—during the policy period at issue—because the insured performed his defective work and damaged electrical wires at that time, even though the fire that damaged the home at issue occurred in 2016.[131] As a result, the court ruled that Mid-Continent Casualty Company ("Mid-Continent") had a duty to defend its insured.

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[125] *Id*. at 515.

[126] *Id*.

[127] *Id.*

[128] *Id*. at 516.

[129] *Id*.

[130] *Id*. (quoting *Gilbert Tex. Const., L.P. v. Underwriters at Lloyd's London*, 327 S.W.3d 118, 133 (Tex. 2010)).

[131] 969 F.3d 554, 558 (5th Cir. 2020).

A. Background Facts

Norman Hamilton hired Gilbert Gonzalez ("Gonzalez") to install new siding on his house during the summer of 2013. Gonzalez was insured by a commercial general liability policy issued by Mid-Continent, which was in effect for the initial policy period of July 15, 2012 to July 15, 2013.[132] Gonzalez renewed the policy, but then canceled it effective June 6, 2014.

In December 2016, a fire damaged Hamilton's home. Hamilton and his homeowners' insurance provider sued Gonzalez, alleging that the fire resulted from Gonzalez negligently hammering nails through the home's electrical wiring when he installed the siding in 2013.[133] Gonzalez sought coverage for the underlying lawsuit from Mid-Continent, which denied coverage in its entirety, prompting Gonzalez to file a declaratory judgment action against the insurer. Gonzalez prevailed at the district court on the duty to defend issue and Mid-Continent filed an appeal.[134]

B. The Fifth Circuit Determines that the Requirements of the Insuring Agreement were Met

The court began its analysis as to whether the insuring agreement of the policy was met by the allegations in the underlying pleading. The court focused on the following allegation, which it identified as the "single paragraph" from the underlying pleading that formed the basis of the claims:

> The injuries and damages suffered by Plaintiffs and made the basis of this action arose out of an occurrence on or about December 1, 2016, at the property in question that relates back to construction and/or installation of siding occurring before the date of loss. The property in question had a fire caused by the construction and/or installation of siding by Defendants when Defendants improperly hammered nails through electrical wiring. Defendants were in charge of and oversaw the construction and/or installation of siding at the property in question, and their acts and/or omissions allowed a fire to occur.[135]

According to the Court, this paragraph indicated that, "when Gonzalez installed the siding on Hamilton's house in 2013, he hammered nails through electrical wiring and created a dangerous condition that caused a fire three years later in 2016."[136] The court explained that the allegations that Gonzalez "'improperly hammered nails through electrical wiring"' were sufficient to constitute an "occurrence" or accident.[137] The court further determined that the allegations that Gonzalez pierced the wires was "physical injury" to "tangible property," thus constitute "property

[132] *Id*. at 556.

[133] *Id*.

[134] *Id.*

[135] *Id*. at 557.

[136] *Id.*

[137] *Id*. at 558.

damage" under the policy.[138] The court also found that this "property damage" occurred during the policy period, as there was "no dispute that Gonzalez took all of his actions, including hammering the nails in question, during the policy period."[139]

The court further noted that express allegations existed that the 2016 fire—although occurring after the expiration of the Mid-Continent policies—related back to the construction and installation of the siding in 2013.[140] Referencing the definition of "property damage" ('"[p]hysical injury to tangible property, including all resulting loss of use of that property"') and the language from the policy that '"[a]ll such loss shall be deemed to occur at the time of the physical injury that caused it,'" the court held that the 2016 fire '"shall be deemed'" to have occurred in 2013 when the electrical lines were damaged.[141] In particular, the court stated that, "[b]ecause it is alleged that both the damage to the electrical wires and the fire can be traced to 2013, when the policies were in effect, the property damage alleged in the [underling pleading] took place during the policy period."[142] In support of its holding, the Court referenced the Supreme Court of Texas's opinion from *Don's Building Supply, Inc. v. OneBeacon Insurance Co.*[143] and its prior opinions in *Wilshire Insurance Co. v. RJT Construction, LLC*[144] and *VRV Development L.P. v. Mid-Continent Casualty Co.*,[145] which the Court stated all had one thing in common:

> They focus on the actual, physical damage alleged in the underlying litigation. If the only alleged damage occurred outside of the policy period, then there is no duty to defend (*VRV Development)*. But if any of the alleged damage occurred during the policy period, then the duty to defend attaches (*Don's Building* and *Wilshire*). This case easily falls on the *Don's Building-Wilshire* side of the line.[146]

Accordingly, the insuring agreement was satisfied, and Mid-Continent only could escape its duty to defend if an exclusion applied to negate coverage.

C. The Fifth Circuit Finds that no Exclusions Apply and that it had no Appellate Jurisdiction over the Duty to Indemnify

Turning to exclusions, the court also rejected Mid-Continent's arguments that exclusions j.(5) and j.(6) barred coverage, as those provisions explicitly limited their application to "that particular part" of property on which Gonzalez was working, which was limited, in this case, to

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[138] *Id.*

[139] *Id.*

[140] *Id.*

[141] *Id.*

[142] *Id.*

[143] 267 S.W.3d 20, 29–30 (Tex. 2008).

[144] 581 F.3d 222, 225 (5th Cir. 2009).

[145] 630 F.3d 451, 458 (5th Cir. 2011).

[146] *Gonzalez*, 969 F.3d at 560.

the siding and not the electrical wires.[147] Finally, the court explained that it lacked appellate jurisdiction as to whether a duty to indemnify existed because the district court did enter a final judgment as to that issue.[148]

D. Commentary

This case presents an interesting view on when "property damage" occurs under the terms of the standard commercial general liability policy. In a circumstance where there is a fire loss that happens after the expiration of the policy period, many insurers—like Mid-Continent in this case—simply would deny coverage based on the "actual injury" rule adopted by the Supreme Court of Texas in *Don's Building*. This holding, however, demonstrates the importance of evaluating the particular factual allegations to determine if there is a possibility that the damage may be "deemed to occur" earlier based on the circumstances leading up to and contributing to the loss at issue. That being said, had the Supreme Court of Texas had this case, it is difficult to believe that the same result would have occurred. At the end of the day, the damage to the electrical wires certainly occurred during the 2012-2013 policy on which Mid-Continent held the risk, but the fire damage clearly was separate and distinct (even if the result of the same occurrence) and did not occur "during the policy period" as required by the insuring agreement. In other words, the factual scenario before the court seemed to be one where a single "occurrence" caused distinct "property damage" in multiple policy periods that likely should have been allocated accordingly. Notably, Judge Haynes, a former coverage lawyer and the author of many of the Fifth Circuit's insurance decisions, issued dissent on this very point.

V. *Colony Insurance Co. v. First Mercury Insurance Co.*, No. 4:18-CV-03429, 2020 WL 5658662 (S.D. Tex. Sept. 22, 2020)

In *Colony Insurance Co. v. First Mercury Insurance Co.*, the Southern District of Texas denied the parties' cross-motions for summary judgment because of the existence of genuine issues of material fact. Nevertheless, the court's ruling included important findings worthy of discussion here.

A. Background

Cambridge Builders & Contractors, LLC ("Cambridge") built an apartment complex in Houston for Archstone Memorial Heights Villages I LLC ("Archstone"). Construction began in 2012 and substantial completion was reached on October 23, 2014. Pertinent to the court's analysis, Cambridge held the following insurance policies provided by First Mercury, Colony, and Navigators Specialty Insurance Co. ("Navigators"):

Policy Period	Primary	Excess
2011-2012	First Mercury	First Mercury
2012-2013	First Mercury	First Mercury
2013-2014	Navigators	First Mercury
2014-2015	Navigators	Colony

[147] *Id*. at 561.

[148] *Id*. at 562.

Each primary policy had a limit of insurance of $1 million while each excess policy had a limit of $10 million.

In 2015, Archstone sued Cambridge, alleging that water damage resulting from defective construction had occurred. Because the alleged damage occurred over multiple years, both First Mercury's and Navigators' primary coverage was implicated, resulting in the two insurers sharing in Cambridge's defense. As excess insurers, First Mercury and Colony also were on notice of the lawsuit.

While Archstone sought between $9 and $11 million in damages, the case ultimately settled for $2.925 million. Both primary insurers paid $500,000 each toward the settlement, but First Mercury, as the excess insurer refused to contribute to settlement, leaving Colony holding the bag for the remaining $1.925 million. First Mercury justified its refusal to participate in settlement under its excess policies by noting that it had not been "provided any evidence or quantifying of any covered damage in the policy's term."

Having warned First Mercury that it would do so, Colony filed suit against First Mercury for reimbursement for its pro rata share of the settlement. Colony asserted claims for contractual and equitable subrogation, arguing that it was entitled to recover from First Mercury on behalf of Cambridge because First Mercury breached the duty to indemnify Cambridge in the liability lawsuit. First Mercury denied any such obligation, arguing that Colony had no right of reimbursement simply because it was unhappy with the amount it chose to pay in settlement. Thus, it moved for summary judgment.

B. Right of Subrogation – Inapplicability of *Mid-Continent v. Liberty Mutual*

At the outset, the court addressed First Mercury's contention that, because Cambridge was fully indemnified by Colony's contribution to settlement of the case, Colony had no right of equitable or contractual subrogation under the Supreme Court of Texas's ruling in *Mid-Continent Casualty Co. v. Liberty Mutual Insurance Co.*[149] The district court, however, disagreed, noting that "much ink has been spilled since *Mid-Continent* was decided,"[150] and the Fifth Circuit has made clear that that decision was limited to its facts. "That is, there can be no recovery under a subrogation theory against a co-primary insurer only when neither insurer disputes coverage and the parties are subject to pro rata 'other insurance' clauses."[151] And, in fact, the Fifth Circuit specifically held in *Amerisure* that contractual subrogation is not precluded "simply because the insured is fully indemnified."[152] Moreover, another reason existed for *Mid-Continent* not applying—First Mercury denied coverage to Cambridge. "If the rule of *Mid-Continent* applied in this situation, it would encourage insurers to deny coverage in the hope that the other insurer pays,

[149] 236 S.W.3d 765, 777 (Tex. 2007).

[150] *Colony Ins.*, 2020 WL 5658662 at *3.

[151] *Id.* (citing *Amerisure Ins. Co. v. Navigators Ins. Co.*, 611 F.3d 299, 306 (5th Cir. 2010)).

[152] *Id.* (citing *Amerisure*, 611 F.3d at 307).

which, from Colony's point of view, is exactly what First Mercury did here."[153] Thus, *Mid-Continent* did not apply.

C. Right of Subrogation – Substantive Analysis

Turning to the substance of Colony's subrogation claim, the court first noted that equitable subrogation applies only when one person, not acting voluntarily, has paid a debt for which another party was liable and which, in equity, should have been paid by that latter party.[154] Thus, Colony could recover only if its payment was involuntary and First Mercury breached its obligation to pay.

On the voluntary payment issue, the court noted that, under Texas law, if an insurer makes a payment in good faith and reasonably believes that payment was necessary to protect its insured, then the payment is not voluntary.[155] Moreover, an excess insurer's payment—like Colony's—is "presumptively involuntary for subrogation purposes."[156] Because First Mercury did not present any evidence to overcome that presumption—and, in fact, the mediator of the case told the excess insurers that they needed to pay under their policies in order for the case to settle.[157] The court also rejected First Mercury's argument that, without a trial and subsequent judgment, there can never be a duty to indemnify, such that both insurers made business decisions—one decided to settle and one did not. The court said that the argument implied that there can never be a duty to indemnify absent a trial, which is not the case.[158]

The court then looked at whether First Mercury should have paid toward settlement, finding that a fact issue existed that precluded summary judgment. In other words, Colony had to establish coverage existed under First Mercury's policy.[159]

First, Colony had to establish that $1 million was paid at the primary level to trigger First Mercury's excess coverage. Colony argued that the loss in question was covered by several consecutive policy periods and, because Texas law prohibits an insured from "stacking" the limits of insurance under consecutive policy periods for a single loss, Colony had to "(1) identify the highest limit of primary coverage and (2) show that this limit was paid by the insurer or insurers whose policies were triggered."[160] The parties agreed that the highest limit of insurance was $1 million, and Colony presented evidence that Navigators and First Mercury each paid $500,000 in settlement. No dispute existed that that $1 million was for covered loss, and the remaining liability

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[153] *Id.* at 4.

[154] *Id.*

[155] *Id.* (citing *Colony Ins. Co. v. Peachtree Constr., Ltd.*, 647 F.3d 248, 256 (5th Cir. 2011)).

[156] *Id.* (quoting *Peachtree Constr.*, 647 F.3d at 256).

[157] *Id.*

[158] *Id.* (citing *Am. Centennial Ins. Co. v. Canal Ins. Co.*, 843 S.W.2d 480, 482–83 (Tex. 1992) (collecting cases that recognized equitable subrogation "to encourage fair and reasonable settlement of lawsuits")).

[159] *Id.* at *5.

[160] *Id.*

of $1,709,657 constituted a loss that exceeded Cambridge's primary insurance layer; thus, the primary coverage was exhausted.[161]

Second, Colony had to establish that loss occurred during First Mercury's policy. To do so, it had to show that the apartment complex was physically damaged before November 7, 2014 as a result of an event attributable to Cambridge. Colony presented emails that showed that water leaks caused physical damage to the complex. Thus, even though fact issues existed as to *how* those leaks occurred, that was sufficient evidence of damage during First Mercury's excess policy.

Third, because the emails did not establish damage in excess of $1 million—the amount necessary to trigger the excess policy—Colony pointed to the excess policy's language that stated that it covered "'[i]njury or damage' which occurs during the Policy period . . . [and] includes any continuation, change or resumption of that 'injury or damage' after the end of the Policy period."[162] As such, the court found that the policy covered damage that occurred before November 7, 2014 and also any continuation of that damage that occurred after November 7, 2014. Within the evidence presented by Colony to support the amount of damages were expert reports that put First Mercury on notice that "experts found damage in 2016 and 2017 that could support a continuation or resumption of the damage reported during First Mercury's 2013–14 policy period."[163] Those documents were enough to create a fact issue as to how damage occurred and when it began, which the court held should be decided at trial.

Finally, because Colony had met its burden to show coverage under First Mercury's excess policy, the burden shifted to First Mercury to establish that an exclusion applied to negate coverage.[164] In that regard, First Mercury relied on exclusions j.(5) and j.(6) to disclaim coverage, arguing that its policy only covered damage that occurred after Cambridge completed its work, which it claimed occurred on October 23, 2014 based on a final certificate of occupancy. Colony countered that temporary certificates of occupancy were issued as early as February 2014 and evidence existed that the property was turned over to the property manager in March 2014. According to the court, a fact issue existed as to when Cambridge was "performing operations." Because First Mercury did not meet its burden to establish the exclusion applied, the insurer was not entitled to summary judgment and, therefore, the court denied the motion.[165]

D. Commentary

Although the summary judgment motion was denied in this case, the court made some important rulings along the way. First and foremost, the court again shut down any argument that *Mid-Continent v. Liberty Mutual* bars an insurer's subrogation claims in situations in which one insurer denies coverage and another accepts coverage, doing the right thing to settle the case on its insured's behalf. The court also made clear that excess insurers that pay to protect their insureds do so involuntarily. Further, when a loss that is the result of a single "occurrence" causes damage

[161] *Id.* at *6.

[162] *Id.* at *7.

[163] *Id.*

[164] *Id.*

[165]

that occurs over multiple policy periods, the payment of a single limit of insurance at the primary level—however shared by those insurers—is sufficient to trigger excess coverage even if the consecutively issued primary policies are not exhausted in full. And, finally, the policy language in the excess policy issued by First Mercury should be enforced as written; thus, while damage has to occur during the insurer's policy period, coverage is not limited to only the damage during the policy period but also to the continuation of any such damage in later policy years. Of course, like primary insurers that can share a single limit across their consecutively issued policies, excess insurers are entitled to the same ability to allocate among *their* consecutively issued excess policies.

VI. *Siplast, Inc. v. Employers Mutual Casualty Co.*, No. 3:19-CV-1320-E, --- F. Supp. 3d ---, 2020 WL 5747869 (N.D. Tex. Sept. 25, 2020)

In *Siplast, Inc. v. Employers Mutual Casualty Co.*, the Northern District of Texas evaluated coverage issues arising out of a defective roofing and waterproofing membrane system on properties in New York.[166] Though the court found that the insuring agreement of the policies was triggered by the damages alleged, the court also ruled that the "damage to your product" and "damage to your work" exclusions barred coverage for the damages sought by the underlying plaintiffs.[167]

A. Background

Siplast, Inc. ("Siplast") is a developer and manufacturer of roofing and waterproofing systems and was insured by Employers Mutual Casualty Company ("EMCC") under CGL policies effective during the consecutive annual policy periods from January 1, 2012 to January 1, 2017.[168] In October 2018, the Archdiocese of New York, Cardinal Spellman High School, and the Catholic High School Association (collectively "the Archdiocese") filed a lawsuit against Siplast and Vema Enterprises ("Vema") in New York. In that lawsuit, the Archdiocese alleged that it purchased a Siplast Roof System that Vema installed at its Cardinal Spellman High School property in 2012.[169] The roof system was covered by a "Siplast Roof/Membrane Guarantee" (the "Siplast Guarantee").[170]

Under the Siplast Guarantee, Siplast guaranteed to the Archdiocese that the new roof membrane and system installed at the school would '"remain in a watertight condition for a period of 20 years, commencing with the date hereof; or SIPLAST will repair the Roof Membrane/System at its own expense.'"[171] The Siplast Guarantee was delivered by Vema to the Archdiocese.

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[166] 2020 WL 5747869, at *3.

[167] Id. at *5–6.

[168] *Id*. at *1.

[169] *Id.*

[170] *Id.*

[171] *Id*. at *3.

Following a rainstorm in November 2016, officials at the high school observed water damage in ceiling tiles throughout the school.[172] The Archdiocese notified both Vema and Siplast of the water damage and potential leaks. In mid-November 2016, Siplast acknowledged receipt of the claims and advised the Archdiocese that the high school should contact a designated Siplast roofing contractor to address the damage and leak. Despite repair work by Siplast's designated contractor, the high school continued to suffer from additional leaks and water damage.[173]

On February 27, 2017, Siplast met with the Archdiocese's representatives about a possible repair plan for the school roof. Siplast apparently admitted there were problems with the roof that needed to be addressed, so Siplast scheduled a meeting with Vema representatives, which took place on March 24, 2017.[174] Vema informed the Archdiocese that the leaks and any damage created thereby were the sole responsibility of Siplast under the Siplast Guarantee. In May 2017, Siplast told the Archdiocese that it would engage a contractor to repair the leaks. In a June 9, 2017 letter, Siplast characterized its earlier repair attempts as "temporary" and advised it would not honor the Siplast Guarantee with respect to any permanent improvements of the roof.[175]

Thereafter, a consultant hired by the Archdiocese "performed an exhaustive inspection and survey of the water penetration issues involving the roofing system."[176] In a December 2017 report, the consultant noted "significant issues with both the workmanship and the materials that were compromising the entire roof membrane and system."[177] In its suit, the Archdicese alleged that the roofing membrane and system had failed of its essential purpose and the only way to remediate the issue was to replace the failed membrane and system with a new one at a cost of approximately $5 million.[178]

B. The Coverage Dispute

Siplast notified EMCC of the lawsuit. EMCC denied coverage, prompting Siplast to file a declaratory judgment action.[179] EMCC argued that it had no duty to defend or indemnify Siplast because Siplast had not met its burden to demonstrate that the Archdiocese sought damages because of any "occurrence."[180] EMCC contended that Siplast's failure to honor its guarantee was not an accident; rather, it was a voluntary and intentional act that was done with deliberate and purposeful intent.[181] In response, Siplast argued that the Archdiocese asserted claims based on an "occurrence" because it alleged that its damages resulted from faulty work and products.

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[172] *Id.*

[173] *Id.*

[174] *Id.*

[175] *Id.*

[176] *Id.*

[177] *Id.*

[178] *Id.*

[179] *Id.*

[180] *Id*. at *4.

[181] *Id.*

According to Siplast, its failure to honor its guarantee is irrelevant to the issue of whether there was an "occurrence," as any breach of the guarantee did not actually cause water to leak into the school or result in "property damage."[182]

C. The Court Determines that the Allegations Trigger the Insuring Agreement

Each party relied on the Supreme Court of Texas's opinion in *Lamar Homes, Inc. v. Mid-Continent Casualty Co.*[183] to support its respective position.[184] EMCC argued that, unlike in *Lamar Homes*—where the underlying plaintiff sought damages because of faulty work and products—the allegations against Siplast demonstrate that its liability is for purposeful refusal to honor its guarantee.[185] Siplast, on the other hand, argued that *Lamar Homes* involved allegations similar to those made by the Archdiocese (*i.e.*, the school sustained damage because of faulty work and products) and that the Archdiocese made no allegations that Siplast expected or intended any damage at issue.[186] The court agreed with Siplast on this issue, explaining that "[t]he origin of the property damage the underlying plaintiffs allege is defects with the workmanship and materials that comprised the roof membrane and system."[187]

D. The Court Determines that Exclusions Preclude Coverage for the Damages Sought in the Underlying Pleading

The court, however, noted that, while there were allegations of "property damage" caused by an accident or "occurrence," this did "not end the inquiry."[188] Rather, EMCC asserted that various "business risk" exclusions unambiguously precluded coverage. In particular, EMCC relied on exclusions that bar coverage for "'[p]roperty damage' to 'your product' arising out of it or any part of it" and for "'[p]roperty damage' to 'your work' arising out of it and any part of it and included in the 'products-completed operations hazard.'"[189]

In reviewing the exclusions, the court explained that a CGL policy generally protects the insured when its work damages someone else's property.[190] EMCC contended that Siplast was not being sued for damage to any property other than its own work and products and that the Archdiocese was simply seeking to recover from Siplast only the cost of a replacement roofing system, not any damage that resulted to the school from the defective roof.[191] Siplast responded

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[182] *Id.*

[183] 242 S.W.3d 1, 4 (Tex. 2007).

[184] *Siplast*, 2020 WL 5747869, at *5.

[185] *Id.*

[186] *Id.*

[187] *Id.*

[188] *Id.*

[189] *Id.*

[190] *Id*. at *6 (citing *Wilshire Ins. Co. v. RJT Constr., LLC,* 581 F.3d 222, 226 (5th Cir. 2009)).

[191] *Id.*

that the underlying pleading "clearly" alleged property damage to the interior of the high school.[192] In particular, Siplast noted that school officials noticed water damage to the ceiling tiles and that the school suffered from "additional leaks and water damage."[193] According to Siplast, because this interior damage to the school is separate from any damage to the Siplast materials on the school roof, EMCC was unable to meet its burden to show that the exclusions applied.

The Court rejected Siplast's argument, noting as follows:

> [A]lthough the underlying complaint mentions damage to school property other than the Siplast roofing products, the Archdiocese does not make any allegations from which the Court can conclude that it has made a claim to recover from Siplast for any damage to the building caused by the leaky roof that is separate from the damage to Siplast's product. It has sued Siplast solely based on its failure to replace the roof as required by the Siplast Guarantee. Siplast guaranteed that if the roof did not remain watertight for a period of 20 years, it would repair the Roof Membrane/System at its own expense. The Archdiocese alleges that due to Siplast's breach, it will be forced to replace the roof well in advance of that 20-year mark at a cost of "approximately $5,000,000. It does not allege that Siplast's breach caused it other damages. The "your work" exclusion precludes coverage for the cost of repairing Siplast's own work.[194]

Consequently, the court concluded that EMCC had no duty to defend Siplast because of the exclusions. Next, the court held that "[b]ecause there is no duty to defend under the policies, there is also no duty to indemnify."[195] Finally, the court dismissed all of Siplast's claims against EMCC for violations of the Texas Insurance Code.

E. Commentary

The holdings from this case are a bit confusing. First, based on the court's analysis, it appears that no dispute existed that interior portions of the building sustained water damage. As the interior of the building was not part of Siplast's scope of work, that damage presumably would be the exact type of damage (resulting damage to property other than the work performed by the insured) that courts recognize as covered by a standard CGL policy. Interestingly, the court then pivots and says that there are no allegations that the damages sought were separate and apart from the work that Siplast performed. Instead, the court found that the allegations related solely to the damages associated with the defective roofing system, not for damages because of water staining of the interior. Accordingly, it appears the court may have gone a bit too far in its interpretation of the exclusions as it relates to the allegations in the pleading.

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[192] *Id.*

[193] *Id.*

[194] *Id.*

[195] *Id.*

Second, the court unequivocally stated that, because there was no duty to defend, there also was no duty to indemnify. The Supreme Court of Texas explicitly has held otherwise.[196] The case was appealed to the Fifth Circuit on October 23, 2020, so it will be interesting to see how the case turns out on appeal. Stay tuned . . . .

VII. *American Guarantee and Liability Insurance Co. v. ACE American Insurance Co.*, 983 F.3d 203 (5th Cir. 2020)

In our "Cases to Watch" section from our paper last year, we noted that the Fifth Circuit was set to review the opinion issued by the Southern District of Texas in *American Guarantee and Liability Insurance Co. v. ACE American Insurance Company*.[197] In that case, the Southern District of Texas evaluated and concluded that a primary insurer breached its *Stowers* duties in rejecting settlement demands prior to and during trial.[198] On appeal, the Fifth Circuit affirmed, holding that ACE breached its *Stowers* duty to accept the settlement offer made during the underlying trial.[199]

A. Background Facts

While riding his bicycle, Mark Braswell ("Braswell") hit the back of a stopped landscaping truck owned by The Brickman Group Ltd., LLC ("Brickman").[200] Braswell sustained fatal head injuries as a result of the collision. Suit was filed against Brickman and the driver of the truck. Brickman was insured by a primary insurance policy issued by ACE and an excess policy issued by American Guarantee.

Leading up to the underlying trial, Brickman's counsel believed that Brickman had a strong liability case. In attempting to evaluate the potential settlement value of the case, jury research was conducted that yielded two critical conclusions: (1) it was important for Brickman to provide at trial that the truck that Braswell hit did not stop short, and (2) that the truck was legally parked.[201] Upon review of this information, American Guarantee's case manager valued the matter as "risk neutral" and assigned a potential settlement value of no more than the $2 million primary layer of the ACE policy. In fact, no one on the defense team believed that a verdict in excess of $2 million was likely.[202]

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[196] *D.R. Horton-Tex., Ltd. v. Markel Int'l Ins. Co., Ltd.*, 300 S.W.3d 740, 741 (Tex. 2009) ("We hold that the duty to indemnify is not dependent on the duty to defend and that an insurer may have a duty to indemnify its insured even if the duty to defend never arises."); *see Colony Ins. Co. v. Peachtree Constr., Ltd.*, 647 F.3d 248, 253 (5th Cir.2011) (recognizing as erroneous the conclusion of many courts that because the duty to defend is broader than the duty to indemnify, there can be no duty to indemnify absent a duty to defend); *Indian Harbor Ins. Co. v. KB Lone Star, Inc.*, No. H-11-CV-1846, 2012 WL 3866858, at *6 (S.D. Tex. Sept. 5, 2012) ("Therefore the duty to indemnify usually is not justiciable until after the underlying litigation is resolved because coverage may turn on facts that are proven even if they are not pled.").

[197] 413 F. Supp. 3d 583 (S.D. Tex. 2019).

[198] *Id*. at 597.

[199] *Am. Guarantee and Liab. Ins. Co. v. Ace Am. Ins. Co.*, 983 F.3d 203, 206, 214 (5th Cir. 2020).

[200] *Id*. at 206.

[201] *Id*. at 207.

[202] *Id.*

On the eve of trial, the Braswells' counsel made the first of three settlement offers, asking for $2 million. ACE countered with $500,000, which the Braswells rejected. Once the case went to trial, "[e]vents quickly turned against Brickman."[203] The judge excluded evidence that Brickman's truck was legally parked; allowed Braswell's widow to testify about a "stop-short" statement made by a Brickman employee; and allowed Braswell's widow to testify about her daughter's psychological trauma, self-harm, suicide attempts, and hospitalization, all caused by her father's death.[204] The case ultimately was submitted to the jury. Before the jury reached a verdict, the Braswells' counsel made two more settlement demands. First, he orally offered Brickman a high/low of "$1.9MM to $2.0MM with costs."[205] ACE believed this offer was outside of its settlement valuation, as the inclusion of "costs" would push the final settlement value beyond its $2 million policy limit. Brickman rejected the offer.[206]

Then the Braswells' counsel emailed a third offer to Brickman's counsel, renewing the prior offer of $2 million and explaining that the offer expired when the jury announced its verdict.[207] Brickman rejected that offer, causing the Braswells to withdraw all offers.[208] The next day the jury returned a verdict of nearly $40 million. After deducting 32% for Mark's comparative negligence, the trial court rendered judgment against Brickman for nearly $28 million. The Braswells and Brickman eventually settled for nearly $10 million, of which American Guarantee paid nearly $8 million. American Guarantee sued ACE, arguing that, because ACE violated its *Stowers* duty to accept one of the three offers within the primary limits, ACE was required to pay for the amount of the settlement paid for by American Guarantee.[209]

In the coverage litigation, the district court determined that ACE did not breach its *Stowers* duty by rejecting the first offer, but that it had breached its *Stowers* duty in declining the second and third offers.[210] ACE then appealed to the Fifth Circuit.

B. The Fifth Circuit Affirms the Holding of the District Court that ACE Breached its *Stowers* Duty with Respect to the Third Demand

The Fifth Circuit first noted that the second offer by the Braswells did not meet the requirements of *Stowers* because the offer was ambiguous as to the total amount sought.[211] As to the third demand, however, the Fifth Circuit affirmed the judgment of the district court that ACE breached its *Stowers* duty by refusing to settle the case at that time.[212] ACE contended that the

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[203] *Id.*

[204] *Id.*

[205] *Id.*

[206] *Id.*

[207] *Id*. at 207–08.

[208] *Id*. at 208.

[209] *Id*.

[210] *Id.*

[211] *Id*. at 209.

[212] *See id.* at 214.

third demand did not generate a *Stowers* duty to settle because Braswell's widow was making claims on her own and on behalf of her minor children, thus creating potentially adverse interests and requiring that any settlement to be contingent on court or guardian ad litem approval.[213] The Fifth Circuit noted that no Texas court had addressed this issue, so it was required to make an *Erie* guess.[214] The court found no evidence in the record that the settlement offer was more favorable to Braswell's widow than her children or that she was operating with interests adverse to those of her children.[215] In light of that, and the fact that ACE presented no evidence that Braswell's widow intended to place her interests before those of her children, the court found that, while the trial court *could* have appointed a guardian ad litem, the failure to do so did not mean that the settlement otherwise required third-party approval that could constitute a "condition" on the settlement.

ACE also contended that the district court erred in concluding that ACE violated its settlement duty with respect to the third offer because the court did not consider the fact that the trial court's adverse rulings in the underlying lawsuit "were likely to be reversed on appeal."[216] As the Fifth Circuit explained:

> In other words, although the trial went poorly for ACE and its decision to reject the Braswells' final settlement offer may appear unreasonable, ACE was not actually negligent since the trial court's "errors" likely rendered the judgment reversible on appeal. The evidence underlying the district court's factual findings cannot support its judgment, ACE argues, because the district court did not consider ACE's appellate prospects.[217]

Unfortunately for ACE, this argument was not considered by the district court because ACE did not actually assert it in the lower court. Thus, ACE was precluded from raising this "novel legal theory for the first time on appeal."[218] Nevertheless, the court further explained that even if it were to evaluate the *Stowers* issue on this basis, the evidence in the record was "clearly sufficient to support the bench trial verdict [of the district court] that '[a] reasonable insurer would have reevaluated the settlement value of the case [and accepted the Braswsells' third offer].'"[219]

C. Commentary

Just as the district court emphasized, the Fifth Circuit focused on the fact that ACE remained stubbornly stagnant in its evaluation of the value of the case, even in light of significant negative developments in the trial of the underlying matter. The key issues required for the defense—as developed through jury interviews—were compromised early in the trial process, yet ACE still did not take advantage of the opportunity to resolve the case within its limits. ACE had

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[213] *Id*. at 210.

[214] *Id*.

[215] *Id*. at 212.

[216] *Id*. at 213.

[217] *Id.*

[218] *Id.*

[219] *Id.*

an interesting theory that its evaluation of the case was affected by the possibility that the underlying verdict would be overturned on appeal. ACE failed to raise that issue at the district court level, thereby waiving the right to argue the theory on appeal. Even so, the Fifth Circuit left no doubt that, even had that theory been preserved for the appeal, it would not have carried the day because of the negative developments that occurred during the underlying trial. This presents an interesting issue. If an insured is in a bad venue where all the rulings are going against it, does that put more pressure on the insurer to settle the case in the face of a *Stowers* demand even if the trial court rulings are questionable? The Fifth Circuit seems to suggest the answer is "yes."

VIII. *Latray v. Colony Insurance Co.*, No. 07-19-00350-CV, 2021 WL 97204 (Tex. App.—Amarillo Jan. 11, 2021, no pet. h.)

In *Latray v. Colony Insurance Co.*, the Court of Appeals of Amarillo evaluated whether the "occurrence" requirement of a standard insuring agreement of a CGL policy was met with respect to damages resulting from the insured's dumping of materials following demolition of a building.[220]

A. Background

The City of Kosse hired Clifton Boatright ("Boatright") to demolish the town's old high school.[221] Under the terms of the agreement, Boatright was to remove and dispose of debris resulting from the demolition. Boatright also was required to obtain liability insurance to cover the demolition operations. David Garrett ("Garrett"), a friend of Boatright's and a long-time tenant on land owned by W.L. Roberts ("Roberts"), asked Boatright if he could take some of the debris to use for purposes of erosion control. According to Boatright, he mistakenly believed the property on which Garrett wished to place the debris belonged to Garrett when, in fact, the property belonged to Roberts.[222] Neither Garrett nor Boatright sought Roberts' permission before placing the debris on the property, placing brick and metal rebar on the property.

By the end of the project, Garrett and Boatright had placed forty tons of debris on the Roberts' property. When Roberts discovered the debris on his property, he filed suit against Boatright for illegal dumping and damage to his land. Roberts subsequently obtained a judgment against Boatright for $50,000, plus court costs. After the judgment became final, the court also issued a Turnover Order, thereby appointing Michelle Latray ("Latray") as a receiver, to take possession of non-exempt property for the purpose of liquidating that property for the benefit of Boatright's judgment creditors.[223]

After the judgment against Boatright was returned and the Turnover Order was issued, Latray submitted the judgment to Colony, who had issued a commercial general liability policy to Boatright prior to the demolition project. Colony denied coverage, prompting Latray to file a lawsuit. Colony filed a motion for summary judgment, relying primarily on the position that,

[220] No. 07-19-00350-CV, 2021 WL 97204 (Tex. App.—Amarillo Jan. 11, 2021, no pet. h.).

[221] *Id*. at *1.

[222] *Id.*

[223] *Id.*

"because Boatright's actions were intentional, the policy did not cover Boatright's acts and thus, [Colony] had no duty to defend nor [*sic*] indemnify."[224] Latray countered with its own motion for partial summary judgment, arguing that, although Boatright's conduct was intentional, his alleged negligence was "accidental" because he was operating under the misconception that he had authority to dump the debris on Roberts' property.[225] The trial court granted Colony's motion for summary judgment and denied Latray's motion for partial summary judgment.

B. The Court Finds that there is no "Occurrence"

In first evaluating the duty to defend, the court explained that the "property damage" must have allegedly resulted from an "occurrence" as gleaned from the "eight corners" of the pleading and the policy.[226] The court relied heavily on *Curb v. Texas Farmers Insurance Co.*,[227] which is a 2005 unpublished opinion issued by the Eastland Court of Appeals.[228] In *Curb*, a high school student and his friends strung fishing line around the courtyard at school with the intent of luring and then making their friends trip over the line.[229] The students eventually forgot about the line, and the next night, a teacher left the building and tripped over the line sustaining significant injuries.[230] She sued the student and his father, who tendered the lawsuit under the father's homeowners' insurance policy. The insurer denied coverage and coverage litigation ensued. The trial court found that there was no coverage because the conduct in question was intentional.[231] Because of that, there was no "accident" and, thus, no coverage for the damages alleged in the underlying pleading. On appeal, the appellate court agreed, finding liability did not arise as the result of an accident because the teacher had alleged that the student's acts were exactly what he intended to do.[232] To be accidental, according to the court, the "effect could not reasonably have been anticipated from the conduct that produced it, and the insured 'cannot be charged with the design of producing'" the effect.[233] Thus, because the injury caused by the student was of the type that would "ordinarily follow" from his conduct "and the injuries could be 'reasonably anticipated from the use of the means, or an effect[,]'" the homeowners' insurer had no duty to defend the student.[234]

Moving to the present case, the court explained that the situation presented was like that in *Curb*. The policy defined the term "occurrence" as "an accident, including continuous or repeated

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[224] *Id.*

[225] *Id.*

[226] *Id*. at *3.

[227] No. 11–03–00406–CV, 2005 WL 1405744 (Tex. App.—Eastland June 9, 2005, no pet.).

[228] *Latray*, 2021 WL 97204, at *3.

[229] *Id*. at *4 (citing *Curb*, 2005 WL 1405744, at *1).

[230] *Id.*

[231] *Id*. (citing *Curb*, 2005 WL 1405744, at *3).

[232] *Id*. (citing *Curb*, 2005 WL 1405744, at *3).

[233] *Id*. (citing *Curb*, 2005 WL 1405744, at *3).

[234] *Id*. (citing *Curb*, 2005 WL 1405744, at *4).

exposure to substantially the same general harmful conditions."[235] Though not defined, Texas courts have found that an injury is accidental if "from the viewpoint of the insured, [it is] not the natural and probable consequence of the action or occurrence which produced the injury; or in other words, if the injury could not reasonably be anticipated by [the] insured, or would not ordinarily follow from the action or occurrence which caused the injury."[236] Thus, the court found that two factors bear on the determination of whether an insured's action constitutes an accident: (1) the insured's intent and (2) the reasonably foreseeable effect of the insured's conduct.[237]

Roberts alleged in his pleading that "Boatright clearly intended to move the debris to the Roberts' property and leave it there. Because the damage to the property was the very presence of the debris on the property, the damages were a reasonably foreseeable result of Boatright's intentional conduct."[238] The court further found that the damages sought by Robert "were of a type that ordinarily flowed from the conduct, not damages of an accidental nature."[239] Additionally, the court explained that, contrary to Latray's contention, the mere assertion of negligence is not sufficient to trigger a duty to defend as the focus of the analysis is on the factual allegations in the pleading as opposed to the legal theories asserted.[240] Thus, the court held that, as a matter of law, "the placement of the debris on the property was no accident and, therefore, no 'occurrence' under the terms of the policy."[241] Because there was no occurrence, there was no coverage and, as such, no duty to defend.

Latray also argued that there was a fact question as to whether Boatright's actions were negligent as opposed to intentional.[242] In resolving this issue, the court explained that there are two lines of cases in Texas addressing the matter. The first line of cases, the "*Maupin* line," relates to whether there is coverage for claims against an insured for damage caused by the insured's intentional torts.[243]

In *Maupin*, the insured allegedly acted intentionally, wrongfully, and willfully, when it took fill material from the claimants' property without their consent.[244] Maupin had contracted with a third party for the purchase of fill material. After removing about 5,744 cubic feet of the material from the property, it was determined that the third party was not the owner but rather a

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[235] *Id.*

[236] *Id*. (quoting *Lennar Corp. v. Great Am. Ins. Co.*, 200 S.W.3d 651, 663 (Tex. App.—Houston [14th Dist.] 2006, pet. denied) (citing *Mid-Century Ins. Co. v. Lindsey*, 997 S.W.2d 153, 155 (Tex. 1999)).

[237] *Id*. (citing *Lennar Corp*., 200 S.W.3d at 663).

[238] *Id.*

[239] *Id.*

[240] *See id.*

[241] *Id.*

[242] *Id.*

[243] *Id*. at *5 (citing *Argonaut Sw. Ins. Co. v. Maupin*, 500 S.W.2d 633, 635 (Tex. 1973); *Gehan Homes, Ltd. v. Emps. Mut. Cas. Co.*, 146 S.W.3d 833 (Tex. App.—Dallas 2004, no pet.); *Federated Mut. Ins. Co. v. Grapevine Excavation*, Inc., 197 F.3d 720, 723 (5th Cir. 1999)).

[244] *Id*. (citing *Maupin*, 500 S.W.2d at 634).

tenant-in-possession.[245] While Maupin argued there was no intent to injure the landowners and that the removal of the material from the property was done under the authority of a contract, the court found that intent was irrelevant.[246] Rather, the court noted that the damage complained of was the removal of the large amount of material from property without the owners' consent. Maupin "did exactly what they intended to do."[247] Maupin's act in trespassing on the property did not constitute an accident, and the fact that Maupin was unaware of the true owner of the property had "no bearing upon whether the trespass was caused by accident. [Maupin's] acts were voluntary and intentional, even though the result or injury may have been unexpected, unforeseen and unintended."[248] Consequently, the court determined there was "no coverage under the policy for damages caused by mistake or error as to the ownership of the property in question."[249]

The second line of cases comes from a decision by the Supreme Court of Texas in *Massachusetts Bonding & Insurance Co. v. Orkin Exterminating Co.* ("*Orkin*"),[250] where the Court held that the term "accident" included negligent acts causing damages that were "'undesigned and unexpected.'"[251] Subsequent cases citing to *Orkin* have held that there can be an "accident" or "occurrence" when there are damages that are unexpected, unforeseen, or undesigned as a result of an insured's intentional but negligent behavior.[252] The court cited to one case interpreting the second line of cases, *Hallman v. Allstate Insurance Co.*,[253] where the court explained:

> There is not an accident when the action is intentionally taken and performed in such a manner that it is an intentional tort, regardless of whether the effect was unintended or unexpected. However, there is an accident when the action is intentionally taken but is performed negligently and the effect is not what would have been intended or expected had the deliberate action been performed non-negligently.[254]

Rejecting application of the second line of cases, the court concluded that Boatright intended to move the debris onto the Roberts' property and he intended to leave it there. The court noted that no allegations existed that Boatright was negligent in the performance of those acts. Rather, the damage sustained was the consequence of the simple presence of the debris on the Roberts' land.[255] The court found that the situation presented an almost mirror image of the facts at issue in *Maupin*. The court also determined that there was no indication that Boatright's

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[245] *Id*. (citing *Maupin*, 500 S.W.2d at 635).

[246] *Id*. (citing *Maupin*, 500 S.W.2d at 635).

[247] *Id*. (quoting *Maupin*, 500 S.W.2d at 635).

[248] *Id*. (quoting *Maupin*, 500 S.W.2d at 635).

[249] *Id*. (quoting *Maupin*, 500 S.W.2d at 635).

[250] 416 S.W.2d 396 (Tex. 1967)

[251] *Latray*, 2021 WL 97204, at *6 (quoting *Orkin*, 416 S.W.2d at 400).

[252] *Id.*

[253] 114 S.W.3d 656 (Tex. App.—Dallas 2003), *rev'd on other grounds*, 159 S.W.3d 640 (Tex. 2005)

[254] *Latray*, 2021 WL 97204, at *6 (quoting *Hallman*, 114 S.W.3d at 660–61).

[255] *Id*.

intentional acts were performed negligently, which would potentially trigger the *Orkin* line of cases.[256] Thus, the court concluded that there was no "occurrence" and, thus, no coverage under the Colony policy.[257]

C. Commentary

The distinction between the *Maupin* line of cases and the *Orkin* line of cases appears to be clear as mud. *Maupin* suggests that any damages resulting from an intentional tort are not accidental in nature (which seems clear), while the *Orkin* line suggests that there can be accidental damage from an insured's "intentional, but negligent behavior." Thus, had Boatright negligently demolished the high school and mistakenly dumped the debris in a location where he was not supposed to, would the analysis of the court have gone down the *Orkin* line and the outcome of the case been different? The court seemed to suggest this in its analysis because it acknowledged that Boatright performed his demolition work properly and then dumped the debris exactly where he intended (albeit at a place where the recipient had no right to allow for the debris to be dumped). Further in that regard, consider the fact that the Eastern District of Texas followed *Orkin* in holding, in 2002, that an insured's construction of a driveway that encroached on a neighboring property was an "occurrence" because, although the construction was intentional, the encroachment was accidental—a seemingly analogous factual scenario. *Latray* is akin to a professional sports team wearing a retro uniform. While the *Maupin* / *Orkin* distinction was very common in case law during the 90's, the analysis was subsumed within the Court's opinion in *Lamar Homes, Inc. v. Mid-Continent Casualty Co.*[258] Since that time, it has been rare to see a court go back to the analysis.

IX. Honorable Mention

A. *United Specialty Insurance Co. v. Farmers Insurance Exchange*, Nos. 13-19-00127-CV and 13-19-00128-CV, 2020 WL 6343341 (Tex. App.—Corpus Christi Oct. 29, 2020, no pet.)

In *United Specialty Insurance Co. v. Farmers Insurance Exchange*, the court evaluated several issues, including the *Stowers* Doctrine, enforcement of a settlement agreement, *res judicata*, and whether additional insured coverage was available for a bodily injury claim.[259] For purposes of this paper, we focus on the court's analysis of the additional insured provisions in the policy at issue. The court held that, for purposes of establishing additional insured coverage, the named insured must have agreed in writing to provide such coverage to the purported additional insured prior to the loss.

On August 26, 2014, Alonzo Cantu Construction, Inc. ("Cantu"), a general contractor, accepted a written subcontract bid from Wasp Construction, LLC ("Wasp") under which Wasp

[256] *Id*. at *6–7.

[257] *Id*. at *7.

[258] 242 S.W.3d 1 (Tex. 2007).

[259] 2020 WL 6343341, at *6,

agreed to perform water and sewer improvements.[260] Wasp had a "business owners policy" issued by Farmers Insurance Exchange ("FIE"). Cantu had a commercial general liability policy issued by United Specialty Insurance Company ("USIC"). Wasp's FIE policy included an "additional insured" provision, which extended coverage as follows: '"Any person or organization for whom you are performing operations is also an insured, if you and such person or organization have agreed in writing in a contract or agreement that such person or organization be included as an additional insured on your policy."'[261] At the time Wasp began working on the excavation project, however, Cantu was not a named additional insured under Wasp's policy. The contract also did not have a provision—at that time—requiring Wasp to procure additional insured coverage in favor of Cantu.

On August 30, 2014, a Wasp employee was installing underground pipes when he was crushed by collapsing dirt, rendering the employee a paraplegic. On September 9, 2014, the employee filed suit initially against only Wasp, but later amended his petition to include claims against Cantu.[262] On October 9, 2014, Wasp signed a subcontracting agreement with Cantu, which itself stipulated was "made this 12th day of September, 2014"—two weeks after the accident. The parties, however, disputed the date that the subcontracting agreement took effect. The subcontract included indemnification and insurance provisions, compelling Wasp to add Cantu as an additional insured under its FIE policy.[263]

USIC filed a declaratory judgment action, seeking a ruling that FIE was responsible for defending Cantu as an additional insured under the FIE policy. In evaluating the issue, the court noted that there was no dispute that no written agreement was in existence prior to the accident that required Wasp to provide additional insured coverage for Cantu.[264] USIC argued, however, that Cantu qualified as an additional insured because (1) Wasp and Cantu had an oral agreement prior to the accident that eventually was memorialized in written form, and (2) the FIE policy required only that a written contract exist, which did between Wasp and Cantu.[265] In response, FIE countered that the additional insured provision limited coverage to those that were required to be added as an additional insured by written contract executed prior to the loss and that the oral agreement was ineffective to meet the requirements of the policy.[266]

The court noted that the additional insured provision unambiguously limited FIE's obligations to Wasp and those entities with whom Wasp directly contracted in writing to provide additional insured coverage.[267] Moreover, while FIE's interpretation implicitly required that a written agreement be executed before an event for coverage occurred, that position was one that

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[260] *Id*. at *1.

[261] *Id.*

[262] *Id.*

[263] *Id.*

[264] *Id*. at *5.

[265] *Id.*

[266] Id. at *6

[267] *Id.*

many courts around the country have adopted.[268] Accordingly, the court agreed with FIE's position that the written contract had to have been executed in writing prior to the loss.[269]

Many additional insured endorsements require that a written contract between the named insured and the purported additional insured be executed prior to a loss. This case now suggests that, even without such language, considerations must be given to the purpose of insurance and that it is not intended to insure against the already burning building.

B. *Travelers Casualty Insurance Company of America v. Mediterranean Grill & Kabob Inc.*, No. SA-20-CA-0040-FB, --- F. Supp. 3d ---, 2020 WL 6536163 (W.D. Tex. Nov. 4, 2020)

In *Travelers Casualty Insurance Co. of America v. Mediterranean Grill & Kabob Inc.*, the Western District of Texas evaluated the number of occurrences under a commercial general liability policy.[270] The insured operates a restaurant in San Antonio, Texas. Between August 29 and September 1, 2018, nearly 200 cases of food poisoning from salmonella bacteria were reported in San Antonio, all after patrons (the "Claimants") ate at the insured's restaurant.[271] The food poisonings gave rise to seven lawsuits (the "Claims"), each of which alleged the insured was negligent in the manufacture and preparation of the food and that the insured's negligence was a proximate cause of the food poisonings.

Travelers Casualty Insurance Company of America ("Travelers") was the primary insurer at the time of the food poisonings and provided commercial general liability coverage subject to a $1 million "per occurrence" limit and a $2 million "aggregate" limit.[272] Some of the Claims associated with the food poisonings settled, with Travelers paying out approximately $450,000 of its $1 million "per occurrence" limit. Travelers offered the remainder of the $1 million limit to settle the remaining 124 Claims, but that offer was rejected. Travelers then filed a declaratory judgment action, seeking a determination that the food poisoning cases were all a single "occurrence," such that Travelers would be liable only for the remainder of its $1 million "per occurrence" limit. If, on the other hand, the food poisonings constituted 124 separate occurrences, as defendants contended, Travelers would have to pay over $1.5 million to exhaust the aggregate limit.[273]

The court concluded that the food poisoning cases were a single "occurrence" and that Travelers' exposure was limited to $1 million. In reaching this determination, the court explained that the definition of "occurrence" is an "an accident, including continuous or repeated exposure to the same general harmful conditions."[274] Under Texas law, "the proper focus in interpreting

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[268] *Id.*

[269] *Id*. at *7.

[270] No. SA-20-CA-0040-FB, --- F. Supp. 3d ---, 2020 WL 6536163 (W.D. Tex. Nov. 4, 2020).

[271] *Id*. at *1.

[272] *Id.*

[273] *Id.*

[274] *Id*. at *2.

'occurrence'" is on the events that cause the injuries and give rise to the insured's liability, rather than on the number of injurious effects."[275] The court noted that several events "caused" a pause or interruption in the injuries in the underlying lawsuits, including when the insured closed each night, as well as each time a new batch of food was prepared. Nevertheless, only one cause gave rise to the insured's liability, and that was the insured's allegedly contaminated food.[276] Thus, under the "cause" analysis, the court concluded that "there was a single, continuous event that both allegedly caused the injuries in the underlying suits, and gave rise to [the insured's] liability. Therefore, the food poisonings were a single 'occurrence' under the policy."[277]

The court specifically rejected the defendants' argument that the interruption in the business operations during the course of the negligent conduct equated to multiple occurrences.[278] According to the Court, "although there were events distinguishable in time and/or space, the insured's negligence was one proximate, uninterrupted and continuing cause which resulted in all of the alleged injuries and damage."[279] The court also rejected arguments that there were multiple occurrences because the parties did not know which products actually were contaminated but likely were from multiple sources.[280] Rather, the court again focused on the fact that while, the exact source of the contamination was unknown, the origination of the contamination was the restaurant itself.[281] The court concluded that the Claims at issue were the result of a single, proximate cause: the insured's contaminated food.

Though this case involved a claim for food poisoning, an argument can be made that the analysis carries over to the construction industry when evaluating the "occurrence" issue in the context of a defective construction coverage dispute. In particular, the analysis of the court from this case suggests that the focus of whether there is one or multiple occurrences should depend on the liability-causing event as opposed to any other factors. Thus, if one contractor on a project performs defective work that affects multiple phases and buildings, that defective work potentially is the "single, proximate cause" of the loss and should constitute a single "occurrence." The law in Texas continues to develop on this issue.

C. *Mt. Hawley Insurance Co. v. JBS Parkway Apartments, LLC*, No. 7:18-CV-00092-DC (W.D. Tex. Dec. 30, 2020)

In an unpublished decision, the Western District of Texas granted an insurer's motion for summary judgment and denied the judgment creditors' motion for partial summary judgment. *See Mt. Hawley Ins. Co. v. JBS Parkway Apts., LLC*, No. 7:18-CV-00092-DC (W.D. Tex. Dec. 30, 2020). The central issue in the case was the burden an insured or a judgment creditor has to allocate damages in an arbitration proceeding or subsequent to an arbitration proceeding between covered

[275] *Id*. (quoting *H.E. Butt Grocery Co. v. Natl'l Union Fire Ins. Co.*, 150 F.3d 526, 530 (5th Cir. 1998)).

[276] *Id.*

[277] *Id.*

[278] *Id*. at *3.

[279] *Id*. at *4 (citing *Foust v. Ranger Ins. Co.*, 975 S.W.2d 329, 335 (Tex. App.—San Antonio 1998, writ denied)).

[280] *Id.*

[281] *Id.*

and uncovered damages and, in particular, how much evidence needs to be presented at the summary judgment stage. Ultimately, the court granted summary judgment to the insurer because of its belief that the judgment creditors did not establish sufficient covered damages during any of the three policies issued by Mt. Hawley. The Fifth Circuit likely will have an opportunity to further elaborate on these issues on appeal.