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

THE POLICYHOLDERS' PERSPECTIVE

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Notable Cases:

Laura Pendergest-Holt, et al v. Certain Underwriters at Lloyd's of London, 2010 WL 317684 (S.D. Tex. Jan. 26, 2010) (granting preliminary injunction against Underwriters in connection with D&O coverage)

ARM Properties Mgmt. Group v. RSUI Indemnity Co., 2009 WL 1064153 (W.D. Tex. February 23, 2009) (denying motions for summary judgment filed by insurer and reaffirming prior ruling in favor of insured in connection with Hurricane Katrina losses).

Lamar Homes, Inc. v. Mid-Continent Cas. Co., 242 S.W.3d 1 (Tex. 2007) (answering certified questions in favor of policyholder on "property damage," and "occurrence" issues as well as the "prompt payment of claims" act)

Archon Investments, Inc. v. Great American Ins. Co., 174 S.W.3d 334 (Tex. App.—Houston [1st Dist.] Aug 25, 2005, pet denied.) (holding insurer breached the duty to defend against allegations of defective workmanship)

Mt. Hawley Ins. Co. v. Steve Roberts Custom Builders, Inc., 215 F. Supp. 2d 783 (E.D. Tex. 2002) (holding insurer breached duty to defend and, in doing so, violated article 21.55 of the Insurance Code)

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AN UPDATE ON RECENT INSURANCE COVERAGE DECISIONS AND THEIR IMPACT ON THE CONSTRUCTION INDUSTRY: *THE POLICYHOLDERS' PERSPECTIVE*

This paper provides an insurance law update for the 12-month period following the last Construction Law Conference. The cases discussed in this paper focus on insurance law as it pertains to the construction industry. Three cases are highlighted and discussed in detail. The remaining cases briefly are discussed to emphasize the key aspects of their holdings.

I. *D.R. Horton—Texas, Ltd. v. Markel International Insurance Co., Ltd.*, 2009 WL 4728008 (Tex. Dec. 11, 2009)

In *D.R. Horton—Texas, Ltd. v. Markel International Insurance Co., Ltd.*, 2006 WL 3040756 (Tex. App.—Houston [14th Dist.] Oct. 26, 2006, *pet. denied* (Tex. Feb. 13, 2009), *reh'g of pet. for review granted* (Tex. June 26, 2009)), the appellate court found that when an insurer has no duty to defend its insured that necessarily means that no duty to indemnify can exist either. *Id.* at *6. Later, on the same day that the Supreme Court of Texas re-affirmed the application of the "eight corners" rule to the duty to defend in *Pine Oak Builders, Inc. v. Great American Lloyds Insurance Co.*, 279 S.W.3d 650 (Tex. 2009), the Court contemporaneously denied a petition for review in *D.R. Horton*. By denying the petition for review, the Court upheld the court of appeals' holding that no duty to defend means no duty to indemnify. *See D.R. Horton*, 2006 WL 3040756, at *6. On March 2, 2009, a motion for rehearing of the petition for review was filed by D.R. Horton. On behalf of the Texas Association of Builders, the National Association of Homebuilders and the Associated General Contractors of America – Texas Building Branch, the authors filed an amicus brief, addressing only the "no duty to defend, no duty to indemnify" issue. In a rare move, the Court requested a response to the motion for rehearing, withdrew its original denial of the petition for review, granted the petition for review and requested oral argument. On December 11, 2009, the Court issued its opinion in which it reversed the lower court in part, adopted in large part the amici curiae briefing and held that a duty to indemnify can arise even if the duty to defend never is triggered. *See D.R. Horton—Texas, Ltd. v. Markel Int'l Ins. Co., Ltd.*, 2009 WL 4728008 (Tex. Dec. 11, 2009).

A. Background Information

In *D.R. Horton*, the Houston Court of Appeals addressed the duty to defend and extrinsic evidence issue in the context of an additional insured tender. In 2002, James and Cicely Holmes sued D.R. Horton alleging that their house contained latent defects that led to the propagation of toxic mold. The Holmes' petition was silent about D.R. Horton's use of subcontractors to construct the home. In particular, the Holmes' petition did not name any subcontractors, nor did it make any reference to damage caused by any of D.R. Horton's subcontractors. D.R. Horton, however, had extrinsic evidence that demonstrated that the alleged damages to the home were caused, at least in part, by work performed on D.R. Horton's behalf by its masonry subcontractor.

Accordingly, since D.R. Horton required its subcontractors to name it as an additional insured, D.R. Horton tendered the Holmes' lawsuit to the liability carriers for the masonry subcontractor. Those insurers, however, declined to defend D.R. Horton

based on the fact that the Holmes' petition failed to mention the use of, or otherwise reference, any subcontractors. In particular, the additional insured endorsement limited the insurer's liability to those claims arising out of the named insured's (i.e., the masonry subcontractor) work for the additional insured (D.R. Horton).

In the coverage litigation against the additional insured carriers, D.R. Horton sought to introduce extrinsic evidence that the damages to the home were caused by the masonry subcontractor (i.e., the named insured). The trial court refused to permit the use of extrinsic evidence. The court of appeals, while recognizing that D.R. Horton "produced a significant amount of summary judgment evidence that . . . links [the masonry subcontractor] to the injuries claimed by the Holmeses," concluded that the trial court properly excluded the evidence. *D.R. Horton*, 2006 WL 3050756, at *5. In particular, without explaining its basis, the court of appeals side-stepped the extrinsic evidence debate by classifying the evidence before it as relating to *both* coverage and liability. *See id.* at *5 n.11. After ruling that no duty to defend existed, based on a strict "eight-corners" analysis, the court of appeals then ruled that there necessarily can be no duty to indemnify. *Id.* at *6.

B. D.R. Horton Waived Its Extrinsic Evidence Argument

In its opinion, the Supreme Court first noted that D.R. Horton's argument that the court of appeals erred by not recognizing an exception to the "eight corners" rule had been waived. *Id.* at *2. In particular, the Court noted that D.R. Horton did not argue for an exception to the "eight corners" rule in the trial court or in the court of appeals until its second motion for rehearing was filed, following the Court's issuance of its opinion in *GuideOne Elite Insurance Co. v. Fielder Road Baptist Church*, 197 S.W.3d 305 (Tex. 2006). The Court explained that, under Texas' summary judgment rules, issues not raised in the trial court cannot be grounds for reversal on appeal. *D.R. Horton*, 2009 WL 4728008 at *2. And, while D.R. Horton had argued in response to Markel's summary judgment motion that the trial court should apply the "eight corners" rule and liberally construe the underlying petition in its favor, the Court found that that was not the same as challenging the "eight corners" rule or urging an exception to the rule. *Id.* Accordingly, the court refused to disturb the court of appeals' duty to defend ruling in favor of Markel. *Id.*

C. No Duty to Defend Does Not Mean No Duty to Indemnify

Turning to D.R. Horton's second argument, regarding the duty to indemnify, the Court explained that liability policies generally include two duties owed by the insurer to the insured: (1) the duty to defend; and (2) the duty to indemnify. *Id.* Importantly, those "are distinct and separate duties." *Id.* And, as the Court noted in *Farmers Texas County Mutual Insurance Co. v. Griffin*, 955 S.W.2d 81, 82 (Tex. 1997), one duty may exist without the other. *D.R. Horton*, 2009 WL 4728008 at *2. Thus, "the duties enjoy a degree of independence from each other." *Id.* (citations omitted).

Elaborating on their differences, the Court reiterated that the duty to defend "has been strictly circumscribed by the eight-corners doctrine" while the duty to indemnify is controlled by the "facts actually established in the underlying suit." *Id.* at *3 (citing *Pine Oak*, 279 S.W.3d at 656; *GuideOne*, 197 S.W.3d at 310). Thus, while the duty to defend is determined by considering only the factual allegations in the pleadings and the terms of the insurance policy, the

insurer's duty to indemnify its insured "depends on the facts proven and whether the damages caused by the actions or omissions proven are covered by the terms of the policy." *Id.* The Court explained that in order to determine the insurer's duty to indemnify, evidence is necessary in the coverage litigation and that is especially true when the underlying lawsuit is resolved prior to a trial on the merits and no opportunity to develop the evidence existed—as was the case in *D.R. Horton*. Thus, the Court held "that even if Markel has no duty to defend D.R. Horton, it may still have a duty to indemnify D.R. Horton as an additional insured under Ramirez's CGL insurance policy. That determination hinges on the facts established and the terms and conditions of the CGL policy." *Id.*

The Court specifically rejected the insurer's argument that, if the underlying pleadings do not trigger a duty to defend, then proof of all those same allegations likewise could not trigger the insurer's duty to indemnify. *Id.* The Court explained that Markel's reliance on *Griffin* was misplaced because that holding was "fact-specific and cannot be construed so broadly." *Id.* (citing *Griffin*, 955 S.W.2d at 84). The result in *Griffin*, in which "the duty to indemnify [was] justiciable before the insured's liability [was] determined in the liability lawsuit when the insurer ha[d] no duty to defend and the same reasons that negate[d] the duty to defend [] likewise negate[d] any possibility the insurer will ever have a duty to indemnify,"

> was grounded on the impossibility that the drive-by shooting in that case could be transformed by proof of any conceivable set of facts into an auto accident covered by the insurance policy. It was not based on a rationale that if a duty to defend does not arise from the pleadings, no duty to indemnify could arise from proof of the allegations in the petition. These duties are independent, and the existence of one does not necessarily depend on the existence or proof of the other.

Id. In fact, the Court noted that, in *Griffin*, it recognized that sometimes resolving the duty to indemnify must wait until after the underlying litigation is completed because coverage may turn on the facts adjudicated in that lawsuit. *Id.* at *4.

And, while the facts before the Court in *Griffin* allowed a ruling on the duty to indemnify prior to adjudication of the underlying facts, the *D.R. Horton* case was not as clear. Rather, D.R. Horton presented evidence in its response to Markel's motion for summary judgment that showed that D.R. Horton used a masonry subcontractor, Markel's insured, on the home and that the subcontractor's work and repairs allegedly contributed to the defects for which D.R. Horton was sued. Moreover, D.R. Horton presented evidence that the subcontractor had named D.R. Horton as an additional insured on its CGL policy. Thus, with respect to Markel's motion for summary judgment on the duty to indemnify, that evidence raised fact questions that needed to be addressed by the lower court. The Court acknowledged that other terms of the policy or other evidence presented by the insurer or the putative insured could establish or refute the insurer's duty to indemnify. Accordingly, the court affirmed the court of appeals' decision on the duty to defend, albeit for different reasons, and reversed the judgment as to the duty to indemnify, remanding the case to the trial court for proceedings consistent with its opinion. *Id.*

Commentary:

The Court's ruling in *D.R. Horton* is very significant. Since *Griffin*, insurance carriers consistently have attempted to stretch the Court's holding in that case in order to defeat the duty to indemnify whenever the underlying pleadings are insufficient to establish the insurer's duty to defend. In doing so, the carriers—and the courts that agreed with them—pulled indemnity from the insureds even when the *actual* facts would establish the insured's entitlement to indemnity. And, as such, those courts and carriers left insureds at the mercy of the pleadings filed by the underlying plaintiffs. Importantly, by reversing its denial of petition for review in this case, the Court took the opportunity to clarify this important aspect of insurance coverage law while upholding the general principles of Texas insurance law—the duty to defend is governed by a strict "eight corners" rule but the duty to indemnify is governed by the actual facts. In other words, the two duties truly are "separate and distinct."

Notably, a motion for rehearing recently was filed and remains pending before the Court.

II. *Underwriters at Lloyd's of London v. Gilbert Texas Construction, L.P.*, 245 S.W.3d 29 (Tex. App.—Dallas 2007, pet. granted).

Policyholders and insurers alike often struggle with the scope of the "contractually assumed liability" exclusion. In 2007, the Dallas Court of Appeals weighed in on the application of the exclusion and, in doing so, mistakenly equated the exclusion to a breach of contract exclusion. Now, the Supreme Court of Texas has an opportunity to clear the muddied waters in *Underwriters at Lloyd's of London v. Gilbert Texas Construction, L.P.*, 245 S.W.3d 29 (Tex. App.—Dallas 2007, pet. granted).

A. Background Facts

In 1993, the Dallas Area Rapid Transit Authority ("DART") hired Gilbert Texas Construction, L.P. ("Gilbert") as the general contractor for the construction of a commuter rail system in Dallas, Texas. The parties entered into a contract in which their responsibilities were outlined, including, but not limited to, Gilbert's responsibilities with respect to inspection and maintenance of the construction areas and the protection of property belonging to third parties. The contract, by way of example, required Gilbert to "preserve and protect all structures . . . on or adjacent to the work site . . . ." *Gilbert*, 245 S.W.3d at 31.

On May 5, 1995, Dallas experienced unusually heavy rains. At the time, Gilbert was preparing the area in front of a complex of buildings owned by RT Realty, L.P. ("RT Realty") for the installation of rail lines. According to RT Realty, DART and Gilbert had implemented a "storm water pollution prevention plan" that limited the capacity of the storm water drainage inlets in the area around its buildings. Additionally, RT Realty alleged that large piles of dirt, barricades, temporary structures, and construction debris had been left by DART and Gilbert, causing the rain water to be diverted toward RT Realty's buildings and allegedly causing substantial flooding and damage to RT Realty's property. *Id.* at 32.

RT Realty filed a lawsuit against DART, Gilbert, and others alleging claims including violations of the Texas Transportation Code, violation of the Texas Water Code, nuisance, and trespass. In its lawsuit, RT Realty claimed that it was a third-party beneficiary of the contract between DART and Gilbert and, further, that it was damaged by Gilbert's purported breach of contract. *Id.*

Gilbert's primary insurer, Argonaut Insurance Company, defended Gilbert in the litigation without even reserving its rights. Its excess insurer, Underwriters at Lloyd's of London ("Underwriters"), issued several reservation of rights letters outlining its position as to indemnity coverage for the RT Realty lawsuit. In particular, with regard to the breach of contract claim, Underwriters questioned whether a breach of contract constituted an "occurrence" as that term is defined under the Underwriters' policies. During the underlying litigation, and while maintaining the position that a breach of contract did not constitute an "occurrence," Underwriters insisted that Gilbert move for summary judgment, asserting a lack of subject matter jurisdiction by virtue of governmental immunity. The trial court concluded that Gilbert was entitled to governmental immunity by virtue of its contract with DART and that RT Realty had failed to state tort claims that fell within the limited waiver of governmental immunity permitted by the Texas Tort Claims Act. Accordingly, the trial court signed an order granting Gilbert's motion for summary judgment based on governmental immunity and dismissed all of the claims against Gilbert *with the exception of* the breach of contract claim. *Id.*

Approximately three weeks later, Underwriters issued a new letter in which it claimed that there was "no coverage for the breach of contract claims against Gilbert" because (i) the primary policy had an exclusion for property damage for which the insured is obligated to pay damages because of the assumption of liability in a contract or agreement; (ii) the excess policy excludes coverage for failure to perform obligations under a contract; (iii) the excess policy covers only tort liability, not liability for breach of contract; and (iv) a breach of contract does not constitute an "occurrence." *Id.*

Subsequent to receiving Underwriters' letter, Gilbert settled the breach of contract claim with RT Realty. And, despite the fact that Gilbert's primary insurer had tendered its full policy limits, Underwriters refused to indemnify Gilbert for any portion of the damages Gilbert paid in settlement. *Id.*

B. The Declaratory Judgment Action and Appellate Court Decision

As a result, Gilbert filed the instant action against Underwriters alleging, *inter alia*, claims for breach of contract, violations of the Texas Insurance Code, and waiver and estoppel. Gilbert and Underwriters cross-moved for summary judgment on the issue of coverage and the breach of contract claim. The trial court denied Underwriters' motion and granted Gilbert's, concluding that coverage existed under the excess policies. Gilbert recovered the amount it paid to RT Realty to settle the underlying lawsuit and also recovered attorneys' fees, pre-judgment interest and post-judgment interest. The trial court, however, dismissed Gilbert's claims for waiver and estoppel, as well as Gilbert's claims for violations of the Texas Insurance Code. *Id.* at 32–33.

On appeal, Underwriters argued that the trial court erred because no coverage existed for the breach of contract claim. On cross-appeal, Gilbert alleged that the trial court erred in failing to hold that Underwriters had waived its policy defenses or was estopped from denying coverage under the excess policies. Gilbert also contended that the trial court erred by granting summary judgment in favor of Underwriters in connection with the claims under the Texas Insurance Code. *Id.* at 33.

At the outset, the court of appeals noted that the excess liability policies at issue were "following form" policies, thus providing the same coverage as the primary policies. Contained within the primary policy was an exclusion for "contractually assumed liability," which provides that coverage does not exist for "bodily injury or property damage for which the insured is obligated to pay damages by reason of the assumption of liability in a contract or agreement." *Id.* at 34. The court of appeals found that the exclusion applied on its face because the claims against Gilbert in the underlying action "were based on Gilbert's assumption of liability in its contract with DART to repair property damage to third-party property." *Id.*

The appellate court, with barely any discussion of the exclusion itself, then turned to one of the two exceptions to the exclusion that provides that the exclusion does not apply to liability for damages "that the insured would have in the absence of the contract or agreement." *Id.* Gilbert claimed that the claims against it fit squarely into that exception. *Id.* The court of appeals disagreed. It found that "[w]here the contract adds nothing to the insured's liability and the liability assumed under the contract is coextensive with the insured's liability under the law, the exclusion does not apply." *Id.* And, although, the court recognized that the liability Gilbert assumed under the contract could be classified as general tort liability, the court could not "say that the contract adds nothing to Gilbert's liability under the law." *Id.* The court noted that the trial court had found that Gilbert was immune from tort liability, so its only liability arose by virtue of what it assumed under the contract with DART. In other words, the court said:

> But for the contract, all claims made by RT Realty against Gilbert would have been barred by governmental immunity. Gilbert assumed liability under the contract that it would not have had under the law. The exception, therefore, does not apply. The exclusion bars coverage.

Id. at 34–35.

The court of appeals rejected Gilbert's contention that the word "liability" should be construed to include both adjudicated and unadjudicated liability such that Gilbert's alleged tort liability—before being resolved by adjudication—would be compared to the liability assumed under the DART contract for purposes of determining the application of the exception. In particular, the court found that "[t]his comparison would render Gilbert's immunity from tort liability of no consequence to the determination of whether the exception applies because Gilbert's potential liability before the resolution of its immunity defense would be sufficient to trigger the exception." *Id.* at 35. This, the court found, means that allegations of liability rather than liability established through judgment or settlement would control an insurer's duty to indemnify under the exception in contravention of the longstanding rule that indemnification under an insurance contract does not accrue until the indemnitee's liability becomes fixed and certain. *Id.*

The appellate court also dismissed Gilbert's contention that applying the exclusion in the instant case creates an irreconcilable conflict between an insurer and its insured because the successful assertion of an affirmative defense to a tort claim causes the previously covered contract claim to be outside the scope of insurance coverage. *Id.* The court said that "such conflicts arise frequently in insurance cases, and it is common that insurance coverage depends upon the adjudicated basis for the insured's liability. .

. . Such a conflict cannot form the basis for coverage where coverage does not exist under the plain language of the policy." *Id.*

As an alternative argument, Gilbert asked the appellate court to preclude the Underwriters from denying coverage under the doctrines of waiver and estoppel. *Id.* While normally such doctrines cannot be used to create coverage, an exception exists when the insurer assumes the defense of its insured without a reservation of rights and with knowledge of facts indicating that no coverage exists. *Id.* at 35–36.[1] In particular, Gilbert asserted that the Underwriters assumed its defense by pressuring it to seek summary judgment on the immunity issues without notifying Gilbert of the coverage position the Underwriters would take if summary judgment were granted. In fact, Gilbert presented testimony that the Underwriters informed it that if it did not move forward on the summary judgment, the Underwriters would deny coverage under the cooperation clause of the insurance policy. *Id.* at 36. Nevertheless, the court disagreed, finding that the Underwriters' actions did not amount to an assumption of the defense of Gilbert, as Gilbert's primary insured assumed that defense and asserted the defense of governmental immunity without any consultation from the Underwriters. *Id.* Moreover, the court found that the Underwriters had the ability to "associate with" the defense without being found to have "assumed" the defense under the policy's cooperation clause. And, it said that Gilbert could have resisted the alleged pressure as to the summary judgment motion and fought the Underwriters on any denial of coverage under the cooperation clause, as that would not have affected Gilbert's defense in the underlying suit, which was being provided by its primary insurer. *Id.* Because the appellate court found that the Underwriters had not assumed responsibility for Gilbert's defense, the court found that the insurer had not waived its defenses and was not estopped from raising the defense of non-coverage. *Id.* at 37.

Accordingly, the court of appeals reversed the trial court's holdings, finding that RT Realty's claim for breach of contract against Gilbert fell within the "contractually assumed liability" exclusion. And, as such, the court of appeals determined that Underwriters was not obligated to indemnify Gilbert for the settlement monies it paid to RT Realty. *Id.*

C. Petition for Review to the Supreme Court of Texas

1. The "Contractually Assumed Liability" Exclusion is Inapplicable

Gilbert filed a petition for review with the Supreme Court of Texas on April 2, 2008. It raised three issues for the Court to address: (i) the appellate court erred in applying the "contractually assumed liability" exclusion to negate coverage; (ii) even if the appellate court correctly concluded that the exclusion applied, it erred when it failed to apply the express exception for liability the insured would have in the absence of the contract or agreement; and (iii) the appellate court erred

[1] Importantly, when the case was before the appellate court, Gilbert's waiver and estoppel argument was premised on what was then known as the "*Wilkinson* exception" to the general rule that waiver and estoppel cannot create coverage where none exists. The "*Wilkinson* exception," however, was abrogated by the Supreme Court of Texas' decision in *Ulico Casualty Co. v. Allied Pilots Association*, 262 S.W.3d 773 (Tex. 2008).

in concluding that Underwriters was not estopped from raising coverage defenses.[2]

Regarding the first issue, Gilbert argued that Underwriters misleadingly asserted, and the court of appeals mistakenly concluded, that the "contractually assumed liability" exclusion bars a breach of contract claim. In fact, Texas precedent makes clear that the "contractually assumed liability" exclusion is *not* a breach of contract exclusion. Rather, by its plain language, the exclusion addresses situations when an insured assumes the liability of another for claims by a third party. The Fifth Circuit, in interpreting identical policy language, stated:

> This exclusion operates to deny coverage when the insured assumes responsibility for the conduct of a third party. As GEI is not being sued as the contractual indemnitor of a third party's conduct, but rather for its own conduct, the exclusion is inapplicable. Moreover, even if the contractual liability exclusion were somehow applicable to situations in which the insured is being sued for its own conduct, the exclusion would not apply here. It is true, as Maryland notes, that under the subcontract between GEI and T&S, GEI agreed to indemnify T&S and hold it harmless for claims arising both from conduct of specified third parties and from its own conduct.
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> This indemnity provision is not, however, the only source of GEI's duty to T&S. Even absent a contractual indemnity provision, GEI would be liable to T&S—under generally applicable contract law—for damage caused by GEI's negligent failure to perform its contractual duties according to the specifications of the subcontract.
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> When, as here, liability could be imposed pursuant to either a contractual indemnity provision or a generally applicable legal principle, the contractual liability exclusion will not bar coverage.

Federated Mut. Ins. Co. v. Grapevine Excavation, Inc., 197 F.3d 720, 726–27 (5th Cir. 1999). The Fifth Circuit's logic has been followed consistently by other courts within Texas. *See E&R Rubalcava Constr., Inc. v. Burlington Ins. Co.*, 147 F. Supp. 2d 523, 528 (N.D. Tex. 2000) (holding that the "contractually assumed liability" exclusion does not apply even though the claimant sued the insured for breach of contract because the liability was based on the insured's own conduct); *Home Owners Mgmt. Enters., Inc. v. Mid-Continent Cas. Co.*, 2005 WL 2452859 (N.D. Tex. Oct. 3, 2005) (noting that the "contractually assumed liability" exclusion only applies when the insured assumes responsibility for the conduct of another as opposed to when the insured is liable in contract for its own conduct), *aff'd* 294 F. App'x 814 (5th Cir. Aug. 26, 2008);[3] *Ins. Co. of N. Am. v.*

[2] In the interest of full disclosure, the author represents Gilbert in its appeal to the Supreme Court. So, if the remainder of this discussion sounds argumentative, it probably is.

[3] In its opinion, the Fifth Circuit found that even if the contractual assumed liability exclusion applied—which it said was "not without doubt given our and other courts' construction of it and similar exclusions"—an exception to the exclusion applied. *See Home Owners Mgmt. Enters., Inc. v. Mid-Continent Cas. Co.*, 294 F. App'x 814, 820 (5th Cir. Aug. 26, 2009).

McCarthy Bros. Co., 123 F. Supp. 2d 373, 377 (S.D. Tex. 2000) (holding that "assumption of liability" exclusion did not preclude coverage for insured builder's agreement through settlement to repair damage caused by its faulty construction because insured accepted liability for its own conduct—not liability of another); *Lennar Corp. v. Great Am. Ins. Co.*, 200 S.W.3d 651, 693 (Tex. App.—Houston [14th Dist.] 2006, pet. denied) ("Exclusion B(2) precludes coverage when the insured contractually assumes liability for the conduct of a third party such as through an indemnity or hold harmless agreement.").

The vast majority of courts outside of Texas also agree with this view. The most notable example is from the Wisconsin Supreme Court. *See Am. Family Mut. Ins. Co. v. Am. Girl, Inc.*, 673 N.W.2d 65 (Wis. 2004). In *American Family Mutual*, the Wisconsin Supreme Court reversed an appellate court that—like the court of appeals here—had applied the identical "contractually assumed liability" exclusion to a breach of contract claim against an insured:

> The term "assumption" must be interpreted to add something to the phrase "assumption of liability in a contract or agreement." Reading the phrase to apply to all liability sounding in contract renders the term "assumption" superfluous. We conclude that the contractually-assumed liability exclusion applies where the insured has contractually assumed the liability of a third party, as in an indemnification or hold harmless agreement; it does not operate to exclude coverage for any and all liabilities to which the insured is exposed under the terms of the contracts it makes generally.
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> Limiting the exclusion to indemnification and hold-harmless agreements furthers the goal of protecting the insurer from exposure to risks whose scope and nature it cannot control or even reasonably foresee. The relevant distinction "is between incurring liability as a result of breach of contract and specifically contracting to assume liability for another's negligence."

Id. at 81 (internal citations omitted). Other cases are in accord with this view as well. *See, e.g.*, *ACUITY v. Burd & Smith Constr., Inc.*, 722 N.W.2d 33, 40 (N.D. 2006); *Marlin v. Wetzel County Bd. of Educ.*, 569 S.E.2d 462, 469 (W. Va. 2002); *Gibbs M. Smith, Inc. v. U.S. Fid. & Guar. Co.*, 949 P.2d 337, 342 (Utah 1997); *Olympic, Inc. v. Providence Washington Ins. Co.*, 648 P.2d 1008, 1011 (Alaska 1982); *Broadmoor Anderson v. Nat'l Union Fire Ins. Co.*, 912 So.2d 400, 406–07 (La. Ct. App. 2005). Simply put, and as recognized by all of these courts and others, the liability of another must be assumed in order for the exclusion to apply in the first instance. Otherwise, the phrase "assumption of liability" in the exclusion has no meaning.

Leading commentators also are in accord with this view. As an example, one well-known commentator specifically states: "The CGL coverage for a policyholder's liability assumed by contract 'refers to liability incurred when one promises to indemnify or hold harmless another, and does not refer to liability that results from breach of contract.'" 2 JEFFREY W. STEMPEL, STEMPEL ON INSURANCE CONTRACTS § 14.14 (3d ed. 2005 & Supp. 2008) (internal citations omitted). *See also* 2 ALAN D. WINDT, INSURANCE CLAIMS & DISPUTES § 11.7 (5th ed. 2007 & Supp. 2008) ("The foregoing policy provision

refers to certain indemnity and hold harmless agreements. And it refers to an underlying tort liability that was assumed, not to an underlying contractual liability."); SCOTT C. TURNER, INSURANCE COVERAGE OF CONSTRUCTION DISPUTES § 10:1 (2d ed. 1999 & Supp. 2007) ("While the term 'contractual liability' coverage is well established in the jargon of those dealing with CGL coverage, one must approach this subject with the knowledge that this term is highly deceptive and has led to many misunderstandings . . . . In any event, the term 'contractual liability' does not include the insured's liability in contract other than its contractual 'assumption' of *another's* liability.") (emphasis added); BARRY R. OSTRAGER & THOMAS R. NEWMAN, HANDBOOK ON INSURANCE COVERAGE DISPUTES § 7.05 (14 ed. 2007 & Supp. 2008) ("Thus, courts have consistently interpreted the phrase 'liability assumed by the insured under any contract' to apply only to indemnification and hold-harmless agreements, whereby the insured agrees to 'assume the tort liability of another.' This phrase does not refer to the insured's breaches of its own contracts."). *See generally* LEE R. RUSS & THOMAS F. SEGALLA, COUCH ON INSURANCE § 129.31 (3d ed. 1995 & Supp. 2007); Rowland H. LONG, THE LAW OF LIABILITY INSURANCE § 10.05[2], 10-56, 10-57 (2002); 21 ERIC MILLS HOLMES, APPLEMAN ON INSURANCE § 132.3, at 36–37 (2d ed. 2002). And, in the most recent update of the Bruner & O'Connor treatise, the authors specifically point to the *Gilbert* case as an example of a misapplication of the "contractually assumed liability" exclusion. 4 PHILIP L. BRUNER & PATRICK J. O'CONNOR, JR., BRUNER & O'CONNOR ON CONSTRUCTION LAW § 11:52 (2009) (discussing the appellate court's erroneous application of the exclusion).

No dispute exists that Gilbert was sued directly for its own purported breach of contract. In fact, in the opening paragraph of the opinion, the court of appeals states that "[t]he controlling issue we decide is whether there is coverage under the policies for damage allegedly caused by the insured's breach of a contractual duty." *Gilbert*, 245 S.W.3d at 31. While the issue was framed correctly, the court of appeals mistakenly equates damage to a third party for which a contract breach is claimed with a claim based on the contractual assumption of the liability of a third party. *See Musgrove v. Southland Corp.*, 898 F.2d. 1041, 1044 (5th Cir. 1990) ("The assumption by contract of the liability of another is distinct conceptually from the breach of one's contract with another. Liability on the part of the insured for the former is triggered by contractual performance; for the latter liability is triggered by contractual breach.") (citations omitted). It is only a contractual *assumption* of the liability of another to a third party that falls within the scope of the exclusion. Had Gilbert assumed DART's liability to RT Realty and had Gilbert been sued based on its assumption of DART's liability, then perhaps the "contractually assumed liability" exclusion would have applied. But those were not the facts presented to the appellate court. Gilbert *did not* assume DART's liability, and Gilbert was not sued for any assumption of DART's liability to RT Realty. Rather, it is undisputed that RT Realty sued Gilbert directly for Gilbert's own purported breach of contract.

Aside from simply misapplying the exclusion, the court of appeals opinion that a breach of contract claim falls within the "contractually assumed liability" exclusion effectively eviscerates the Supreme Court's opinion in *Lamar Homes*. Notably, the Court went to great lengths in concluding that "the

CGL policy makes no distinction between tort and contract damages." *Lamar Homes*, 242 S.W.3d at 13. The Supreme Court's opinion in *Lamar Homes*, as well as the numerous cases that came before and were pending with it, would have been completely unnecessary if the CGL policy already excluded breach of contract claims.

And, in fact, certain CGL carriers have added specific "breach of contract" exclusions to their policies. *See B. Hall Contracting, Inc. v. Evanston Ins. Co.*, 447 F. Supp. 2d 634, 643 (N.D. Tex. 2006), *rev'd on other grounds by,* 2008 WL 942937 (5th Cir. 2008) (applying an express "breach of contract" exclusion); *Essex Ins. Co. v. Patrick*, 2006 WL 3779812 (W.D. Tex. Oct. 16, 2006) (same). *See also Carolina Cas. Ins. Co. v. Sowell*, 603 F. Supp. 2d 914 (N.D. Tex. 2009) (addressing the application of an exclusion precluding coverage for claims "based upon, arising out of, directly or indirectly resulting from or in consequence of, or in any way involving any oral or written contract or agreement"). Certainly, such exclusions would be wholly unnecessary if the "contractually assumed liability" exclusion already excluded breach of contract claims. Moreover, one only needs to look at Coverage B of the standard ISO policy to see that it contains *both* a "contractually assumed liability" exclusion and a "breach of contract" exclusion. Again, and in violation of well-settled contract interpretation rules, the breach of contract exclusion would be mere surplusage if the "contractually assumed liability" exclusion already excluded breach of contract claims.

2. In Any Event, the Exception to the Exclusion Is Applicable

The court of appeals correctly recognized that the "contractually assumed liability" exclusion contains an exception for "liability that would exist in the absence of the contract or agreement." *See Gilbert*, 245 S.W.3d at 34. The court of appeals, however, after mistakenly concluding that the exclusion applies in the first place, held that the exception did not apply because Gilbert's liability to RT Realty did not exist other than by its contract. *See id*. The court of appeals was wrong.

More specifically, the court of appeals failed to recognize *why* Gilbert was cloaked with governmental immunity protection in the first place—its contract with DART. Consequently, it is clear that but for Gilbert's contract with DART, Gilbert would have had common law tort liability to RT Realty for the damages allegedly caused by Gilbert to the neighboring property owned by RT Realty. Thus, Gilbert's liability to RT Realty is one Gilbert "would have in the absence of a contract or agreement." Therefore, assuming the exclusion even applies, the exception to the "contractually assumed liability" exclusion negates the application of the exclusion to the instant set of facts.

3. Waiver and Estoppel in Light of *Ulico*

As previously mentioned above, Gilbert also argued in the appellate court that Underwriters waived or should be estopped from raising its defense of no coverage under what used to be known as the "*Wilkinson* exception." *See Gilbert*, 245 S.W.3d at 35–36 (discussing *Farmers Tex. County Mut. Ins. Co. v. Wilkinson*, 601 S.W.2d 520, 521–22 (Tex. Civ. App.—Austin 1980, writ ref'd n.r.e.)). The crux of Gilbert's alternative argument was that Underwriters had assumed control of Gilbert's defense in the Underlying Lawsuit by threatening to pull coverage via the cooperation clause unless Gilbert filed a motion for summary judgment on the sovereign immunity ground. It is important to note, however, that Underwriters *had not*

reserved rights based on the "contractually assumed liability" exclusion and the underlying carrier had defended without any reservation of rights. *Id.* at 36.

While the petition for review was pending before the Supreme Court, the Court decided *Ulico Cas. Co. v. Allied Pilots Association*, 262 S.W.3d 773 (Tex. 2008), in which the Court held that an insured's coverage could not be expanded by waiver and estoppel. Accordingly, in its brief on the merits Gilbert modified its argument to fit within the rubric of *Ulico*, contending that Underwriters assumed or asserted control over its defense in a manner that prejudiced Gilbert and that Underwriters did so without providing a reservation of rights identifying the "contractually assumed liability" exclusion on which it ultimately relied on to deny coverage. The estoppel argument is an alternative argument that only will come into play if the Court rules that Underwriters' interpretation of the "contractually assumed liability" exclusion is correct.

Commentary:

Confusion arising from the applicability of the "contractually assumed liability" exclusion is nothing new to insurance coverage law. The Supreme Court of Texas, however, now has an opportunity to clarify the application of the exclusion, much as the Fifth Circuit did in *Grapevine Excavation*. Quite simply, as recognized by a majority of courts and commentators, the exclusion is not a "breach of contract" exclusion. Rather, it applies only when the insured contractually assumes the liability of a third party.[4] In reaching its holding, the court of appeals necessarily suggests that coverage is dependent on the viability of a tort claim against Gilbert. In stark contrast, the Supreme Court of Texas has held that liability defenses do not equate with coverage defenses. *See Lamar Homes*, 242 S.W.3d at 13 (rejecting the economic loss doctrine as a defense to coverage). Likewise, in *Lamar Homes*, the Court re-emphasized the long-standing principle that the label attached to a cause of action does not determine insurance coverage. *See id*. Given that precedent, the court of appeals decision has the effect of impermissibly barring coverage, for example, in every instance in which the economic loss rule prevents contracting parties from suing one another in tort. Not only does such a result find no support in the actual policy language, but also it defeats a main function of CGL coverage for contractors (i.e., to cover "property damage" to a third party caused by the work of an insured or its subcontractors).

Oral argument was held before the Court on October 6, 2009.

III. *Trinity Universal Insurance Co. v. Employers Mutual Casualty Co.*, 586 F. Supp. 2d 718 (S.D. Tex. 2008), rev'd 2010 WL 6903 (5th Cir. Jan. 4, 2010)

The Supreme Court of Texas' decision in *Mid-Continent Insurance Co. v. Liberty Mutual Insurance Co.*, 236 S.W.3d 765 (Tex. 2007) ("*Mid-Continent*"), is, at least in this author's view, the "anti-settlement" case in that it has had a chilling effect on settlements in situations involving multiple insurers that owe settlement duties to an insured. In particular, in *Mid-Continent*, the

[4] And, even then, the "contractually assumed liability" exclusion does not apply to certain contractual assumptions as defined by the term "insured contract" within the CGL policy. By way of example, the exclusion does not apply if the insured "assumes the tort liability of another."

Court held that no right of contribution and no right of subrogation existed between co-insurers. In 2008, the broad language used by the Supreme Court in *Mid-Continent* was seized on by the Southern District of Texas to extend its holding to the duty to defend. *See*, *Trinity Universal Ins. Co. v. Employers Mut. Cas. Co.*, 586 F. Supp. 2d 718 (S.D. Tex. 2008) ("*Trinity I*"). The Fifth Circuit Court of Appeals, though, recently pulled back the reins on that extension, reversing the Southern District of Texas' decision. *See Trinity Universal Ins. Co. v. Employers Mut. Cas. Co.*, 2010 WL 6903 (5th Cir. Jan. 4, 2010) ("*Trinity II*"). The Supreme Court's opinion in *Mid-Continent* as well as the Fifth Circuit's opinion in *Trinity* will have a significant impact on how insurance coverage obligations are allocated among co-insurers.

A. *Trinity I*

1. The Background Facts

Lacy Masonry, Inc. ("Lacy Masonry") was the named insured under four CGL policies issued by Plaintiffs Trinity Universal Insurance Company, Utica National Insurance, and National American Insurance Company (collectively, the "Plaintiffs"), and Defendant Employers Mutual Casualty Company ("EMC"). Together the insurers provided insurance to Lacy Masonry from March 25, 2000 to May 14, 2004 and May 16, 2004 to May 16, 2005. Each policy contained identical "other insurance" clauses, providing that when more than one policy is applicable the insurers contribute on a "pro rata" basis. *Trinity I*, 586 F. Supp. 2d at 720.

On November 1, 2005, Lacy Masonry (along with others) was sued in Texas state court by McKenna Memorial Hospital ("McKenna") for damages caused by extensive water infiltration issues, arising out of the construction and improvement of a building. In particular, Lacy Masonry was alleged to have performed "all masonry work" on the project and other façade items. A co-defendant in that lawsuit allegedly installed an EIFS system on the project. *Id.* at 720–21.

On or before February 2, 2006, Lacy Masonry notified the Plaintiffs and EMC of the underlying lawsuit. Each of the Plaintiffs agreed to defend Lacy Masonry subject to a reservation of rights, but EMC claimed that it had no such duty, refusing to contribute any portion of the defense costs. Instead, those costs were borne entirely by the Plaintiffs. As a result, the Plaintiffs asserted claims against EMC for breach of contract, contribution, and attorneys' fees, as well as sought a declaration that EMC had a duty to defend Lacy Masonry against McKenna. The parties cross-moved for summary judgment as to whether the allegations in McKenna's suit were potentially covered by EMC's policy so as to trigger its duty to defend Lacy Masonry, and whether Texas law allows a co-insurer to recover a share of defense costs from another insurer when their policies contain identical "other insurance" clauses. *Id.* at 721.

2. The Duty to Defend Exists

Before reaching a discussion as to the application of *Mid-Continent* to the facts before it, the Southern District of Texas first had to assess whether EMC's duty to defend its insured even was triggered by the allegations in McKenna's pleadings against Lacy Masonry. For two reasons, EMC claimed that no such duty existed: (1) the "designated work" exclusion barred coverage for any claims arising out of a project on which EIFS is applied; and (2) the fortuity doctrine barred coverage for the claims. The court addressed each in turn.

With regard to the "designated work" exclusion, the court noted that the endorsement specifically excluded coverage for "[a]ny work or operations with respect to any exterior component, fixture or feature of any structure i[f] an 'exterior insulation and finish system' is used on any part of that structure.'" *Id.* at 723. On the other hand, the allegations stated that Lacy Masonry performed "all masonry work" on the project and that water infiltration existed, in part, because of improperly installed masonry. As noted, allegations also existed that EIFS had been applied by a different subcontractor. EMC claimed that such allegations made "clear that the only thing Lacy Masonry is being sued for involves exterior components of a structure that incorporate[s] EIFS." *Id.* The court, however, disagreed. It found that the petition did not allege that "masonry work was performed exclusively on the *exterior* of the building or that there was no masonry work done in the *interior* of the building." *Id.* at 724–25. Because Texas law requires that such allegations be construed in favor of the insured, the court held that EMC was not excused from its defense duty by the "designated work" exclusion. *Id.*

Turning to the "fortuity doctrine," the court recognized that EMC relied entirely on extrinsic evidence to support its claim that Lacy Masonry was aware of the McKenna loss before its policy incepted on May 16, 2004. *Id.* The court addressed Texas law on the use of extrinsic evidence as to the duty to defend and found that even if the Supreme Court of Texas were to acknowledge an exception to the strict "eight corners" rule, the evidence relied upon by EMC was inadmissible. In particular, the court said that the evidence proffered by EMC "does not fit within this presumed narrow exception to the eight-corners rule." *Id.* at 726 For instance, some of the evidence was developed during litigation of the underlying lawsuit and other evidence overlapped—at least in part—with the merits of McKenna's claims against Lacy Masonry. *Id.* at 726–27. Accordingly, the court found that EMC could not escape its duty to defend its insured. *Id.* at 728.

Or could it . . .

3. Taking *Mid-Continent* Another Step Too Far

After finding that EMC had wrongfully denied a defense to its insured and had breached its contract in doing so, the court in *Trinity I* addressed whether the Plaintiffs could recover any of the defense costs that they had incurred in fully defending the parties' mutual insured. On that issue, EMC argued that the Supreme Court of Texas' decision in *Mid-Continent* precluded the Plaintiffs' recovery from EMC for those costs. Addressing that contention, the Southern District of Texas discussed the intricacies of the *Mid-Continent* decision.

First, in *Mid-Continent*, the Court adhered to its longstanding opinion in *Traders & Gen. Ins. Co. v. Hicks Rubber Co.*, 169 S.W.2d 142 (Tex. 1943), and ruled that when two co-insurers have identical "pro rata" or "other insurance" clauses, a contribution claim asserted by one against the other to recoup defense costs was precluded. Second, the Court had found that when an insurer pays more than its pro-rata share under an "other insurance" clause, its payment is voluntary, also barring it from recovering via a claim for contribution. Third, in addressing Liberty Mutual's subrogation claims, the Court held that an insurer steps into the shoes of its insured in such cases, and that because such an insured—which has been fully indemnified—cannot sue another insurer for subrogation, neither can one co-insurer that seeks to recover from

another co-insurer. *Trinity I*, 586 F. Supp. 2d at 729.

Applying that case to the facts before it, the Southern District of Texas extended the *Mid-Continent* decision beyond the duty to indemnify context in which it was rendered and incorporated the same logic to the duty to defend. As for contribution, the court held that the *Hicks Rubber* decision, as analyzed and reaffirmed in *Mid-Continent*, "applies squarely to Plaintiffs' claim for contribution." *Id.* at 729. More specifically, the court found that the insurers' policies all contained "other insurance" clauses identical to those addressed in *Mid-Continent*. Because such clauses render the contractual obligations of the Plaintiffs and EMC to their mutual insured "several and independent of each other, not joint . . . Plaintiffs cannot establish the common obligation element of their contribution claim." *Id.* at 730.

In attempting to distinguish themselves from the *Mid-Continent* decision, Plaintiffs argued that their duty to their insured included the provision of a "complete defense"—not a pro-rata one. In other words, the Plaintiffs contended that they did not "voluntarily" pay anything over their pro-rata share of expenses. According to the Plaintiffs, "the 'other insurance' language typically found in insurance policies—because it specifically references only 'loss,' *i.e.*, indemnity—does not apply to the duty to defend." *Id.* The court disagreed, finding that the critical portion of the Supreme Court's decision addressed the impact of "other insurance" clauses on the "commonality of obligation" between co-insurers. In particular, the court noted:

> *Mid-Continent* categorically bars direct contribution claims between coinsurers whose policies contain "other insurance" clauses by construing their contractual obligations as "several and independent of each other." [citation omitted] The independence of these contractual obligations affects not only the duty to indemnify, as discussed in *Mid-Continent*, *but necessarily applies with equal force to the duty to defend.*

Id. Accordingly, the insurers turned their otherwise shared contractual obligations into independent duties enforceable—if at all—by Lacy Masonry. *Id.*

Finally, the court addressed the Plaintiffs assertion of a subrogation action for breach of contract as a means to recover from EMC its pro-rata share for the cost of defense. Because Lacy Masonry had been fully compensated, though, the court found that *Mid-Continent* precluded any claim for subrogation. *Id.* at 730–31. The court also rejected the Plaintiffs' argument that EMC's improper denial of a defense for Lacy Masonry meant that Lacy Masonry could have brought a declaratory judgment action on its own to enforce its contractual rights. Such a declaration was not at issue (and besides, the court already had determined that a duty to defend existed). *Id.* Rather, it is the Plaintiffs' subrogation claim for breach of contract and damages equal to EMC's share of the defense costs that *Mid-Continent* prohibits. This is because the Plaintiffs stand in no better position than Lacy Masonry vis-à-vis EMC.

In light of the foregoing, the *Trinity I* court ruled that EMC owed Lacy Masonry a defense. Nevertheless, it also ruled that any previously paid defense costs were non-recoverable because the Plaintiffs had no right to any claims for contribution or subrogation—even at the duty to defend stage—in adherence to *Mid-Continent. Id.* at 731.

4. Commentary on *Trinity I*

The *Mid-Continent* decision—which already was a bad decision from a settlement perspective—was made worse by its extension to the duty to defend. After the decision in *Trinity I*, a co-insurer that denied a duty to defend had no real incentive to undertake its insured's defense if another insurer had done so. Following *Mid-Continent*, the reasoning appears to be that no claim existed so long as the insured had been fully compensated. The problem with that rationale is that, by enabling unreasonable co-insurers to skirt their duties, the court created a disincentive for insurers to act reasonably. The decision in *Trinity I* garnered a considerable amount of attention in the form of amicus briefs from both policyholders and insurers. The amicus briefs, in fact, were consistent in requesting that the Fifth Circuit reverse the district court's opinion. And, recently, the Fifth Circuit Court of Appeals listened to the calls for reversal.

B. *Trinity II*

On January 4, 2010, the Fifth Circuit Court of Appeals handed down its long-awaited opinion regarding the *Trinity I* appeal. *Trinity II*, 2010 WL 6903. The court recognized that the matter before it was one of first impression. In particular, the court noted that the task before it was to "decide whether the holding in *Mid-Continent* extends to an insurer's duty to defend its insured." *Id.* at *1. If not, the court was faced with the issue of "whether insurance companies that pay defense costs may recoup a portion of those costs from a co-insurer that fails to defend a common insured." *Id.*

1. EMC's Duty to Defend

At the outset, the Fifth Circuit agreed with the district court that EMC was under an obligation to defend Lacy Masonry in the suit filed against it by McKenna. *Id.* at *2. In doing so, the court rejected EMC's claim that the Designated Work exclusion in its policy negated the duty to defend. *Id.* The court explained Texas law on the duty to defend standard, noting that it was restricted by Texas' "eight corners" rule. *Id.* at *3. Thus, the court only could compare the allegations in McKenna's Fourth Amended Petition to Lacy Masonry's EMC policy to determine whether a potential for coverage existed. *Id.*

Addressing the terms of the insurance policy, the court recognized that it was a standard CGL policy that provided coverage for "property damage" caused by an "occurrence." *Id.* at *4. After quoting the policy's language defining "property damage" and the "products/completed operations hazard," the court turned its attention to the Designated Work exclusion. *Id.* Quoting the district court, the Fifth Circuit said that the exclusion:

> excludes coverage for injuries to or loss of use of tangible property on premises not owned or rented by the insured, Lacy Masonry, if those injuries arise out of either its construction, installation, application, or other service of an EIFS, and also excludes coverage for any work or operations performed by Lacy Masonry on any exterior components or features of a structure if EIFS is used on that structure or any part of the structure.

Id. at *4 (quoting *Trinity I*, 586 F. Supp. 2d at 723).

Looking to the allegations in the underlying petition against Lacy Masonry, the Fifth Circuit agreed with the district court that they potentially fell within the scope of the EMC policy's coverage. *Id.* at *5. In particular, the allegations were clear that Lacy Masonry was responsible for all masonry work on the project and that improperly installed masonry led to water infiltration. *Id.* More importantly, the petition specifically identified "'water infiltration at the *interior* and exterior building envelope," which would likely include portions of the building other than its exterior. *Id.* (quoting the Fourth Amended Petition against Lacy Masonry). Thus, according to the court, "the potential [for coverage] clearly exists." *Id.* In other words, "[b]ecause the allegations do not clearly and unambiguously fall outside the scope of the EMC policy's coverage, the district court properly found that EMC had a duty to defend Lacy Masonry." *Id.*

2. *Mid-Continent* and the Duty to Defend

The Fifth Circuit then addressed the Supreme Court of Texas' holding in *Mid-Continent* and its application to the facts before it. *Id.* at *5–*6. The court noted that the district court had correctly explained most of the *Mid-Continent* decision, but, with respect to the denial of Liberty Mutual's contribution claim in *Mid-Continent*, the district court mischaracterized the Court's holding. *Id.* at *6. More specifically, in *Mid-Continent*, the Court addressed only "the question of whether one co-insurer has a right of contribution or subrogation against a non-paying co-insurer to recover money paid to *indemnify* a common insured for a loss. *Mid-Continent* left open the separate question of whether a co-insurer that pays more than its share of *defense costs* may recover such costs from a co-insurer who violates its duty to defend a common insured." *Id.*

In fact, Texas courts routinely have recognized that the duty to defend and the duty to indemnify are distinct and separate duties. *Id.* And, in addition, the EMC policy is clear that its "other insurance" provision applies only to "loss" and provides that where co-primary insurance policies exist, EMC will share the cost of loss suffered by Lacy Masonry. *Id.* With respect to the duty to defend Lacy Masonry, however, the policy does not include a similar proration of costs incurred. *Id.* The Fifth Circuit found this fact to be dispositive of the issue before it. *Id.* at *7. In order to establish a claim for contribution, an insurer needed to prove that the insurers had a common obligation but the "other insurance" clause renders the duty to indemnify "several and independent," making establishment of that requirement impossible. *Id.* (citing *Mid-Continent*, 236 S.W.3d at 772).

The duty to defend under the EMC policy is not affected by the "other insurance" clause and, in fact, the policy provides that EMC "will have the right and duty to defend the insured against any 'suit' seeking" covered damages. *Id.* And, while EMC's obligation with respect to the duty to indemnify might be a one-fifth obligation (at least as between the other insurers), each carrier owed a complete defense to Lacy Masonry. That is, "[t]he duty to defend creates 'a debt which is equally and concurrently due by' all of its insurers." *Id.* (citing *Mid-Continent*, 236 S.W.3d at 772). Importantly, the Fifth Circuit noted, the conclusion that the debt is equal and concurrent is supported by Texas case law requiring an insurer to provide a complete defense even if only a single claim in a lawsuit potentially falls within coverage. *Id.* (citations omitted). Accordingly, contrary to the findings of the district court, the insurers in *Trinity II* established the "common obligation" requirement necessary for a contribution

claim. *Id.* And, because EMC admitted that it did not contribute to Lacy Masonry's defense, the other insurers also were able to satisfy the second requirement for a contribution claim—"that the insurer seeking contribution has made a compulsory payment or other discharge of more than its fair share of the common obligation or burden." *Id.* (quoting *Mid-Continent*, 236 S.W.3d at 772). Having found that the other insurers' contribution claim was valid, the court reversed and remanded the case to the district court for a determination of the amount of defense costs to which those insurers were entitled. *Id.* The court did not address the subrogation issue raised by the parties because its finding on the contribution claim rendered it unnecessary. *Id.* at *8.

3. Commentary on *Trinity II*

The Fifth Circuit Court of Appeals' decision in *Trinity II* reversed what could have been a potentially disastrous decision regarding co-insurers' obligations to defend their mutual insureds. While the headache of *Mid-Continent* remains, at least recalcitrant insurers will not be able to hang their hat on *Trinity I* in order to avoid participating in their insured's defense altogether. And, in fact, that such insurers cannot shirk their duty to defend under *Mid-Continent* may actually help minimize the effect *Mid-Continent* has on settlement. In particular, because all the carriers that owe an obligation to defend will be under pressure to participate in an insured's defense, they likewise will have an incentive to participate in settlement as well.

Another important aspect of *Trinity* is the Fifth Circuit's recognition that its conclusion is supported by "the uniform holdings of Texas courts that even a single claim in a lawsuit potentially falls within an insurance policy's coverage, the insurer has a duty to provide a *complete* defense." *Trinity II*, 2010 WL 6903. Further, in making this recognition, the Fifth Circuit specifically noted that Texas law does not support a pro-rata defense. Accordingly, even if multiple insurers owe a defense, each insurer owes the insured a *complete* defense and its up to the insurers to figure out a pro-rata application among themselves. Despite the fact that this has been the law for some time, it is quite commonplace for insurers to send letters stating that they will agree to "participate" in the defense of the insured or that they will agree to "fund their part" of a defense obligation.

IV. Other Cases of Note

The following provides a brief synopsis of other important Texas insurance law decisions issued during the last twelve months (in reverse chronological order). Each synopsis addresses the key holdings made by the respective courts but the authors recommend that practitioners thoroughly review each decision in order to fully understand the context in which the decisions were issued.

A. Insurance Coverage for a Successor Entity: *VRV Development, L.P. v. Mid-Continent Casualty Co.*, 2010 WL 375499 (N.D. Tex. Feb. 3, 2010)

The Northern District of Texas found that an insurance policy issued to VRV, Inc. did not provide coverage to its successor—VRV Development, L.P.—or the successor's general partner or sole limited partner. The insured did not notify its insurer of the company's conversion into a limited partnership and coverage was not requested for the new entity after the conversion. The pleadings against the new entity did not mention the old corporation and, therefore, Mid-Continent did not have a duty to defend. In fact, the policy even stated that

"[n]o person or organization is an insured with respect to the conduct of any current or past partnership, joint venture or limited liability company that is not shown as a Named Insured in the Declarations."

Interestingly, despite being able to determine that no coverage existed through review of the eight corners of the insurance policy and pleadings, the court went a step further and reviewed extrinsic evidence under a "coverage only" exception to the "eight corners" rule. The court claimed that such an exception was applied by the Fifth Circuit in *Ooida Risk Retention Group, Inc. v. Williams*, 579 F.3d 469, 475–76 (5th Cir. 2009), and that the exception equally was applicable in the instant case. Using the exception and looking at the corporation's conversion, the court determined that: "Allowing Plaintiffs to substitute a new party to an insurance contract, without Mid-Continent's knowledge or approval, and without giving Mid-Continent the opportunity to evaluate the entity or person it is purportedly insuring, materially rewrites the insurance contract in a way that would seem to contravene existing authority." *VRV Dev., L.P.*, 2010 WL 375499 at *4 (citations omitted).

B. Classification Limitation and Duty to Defend: *Essex Ins. Co. v. Hines*, 2010 WL 10941 (5th Cir. Jan. 4, 2010)

In January, the Fifth Circuit Court of Appeals addressed the "seemingly simple task" of determining whether an insured had a duty to defend its insured and, in doing so, reminded insurers: "When in doubt, defend." The policy at issue, which was issued to a woman who bought a house, renovated it and resold it to a couple, included a "Classification Limitation Endorsement." The policy included a classification for "DWELLING-SINGLE FAMILY-LESSOR'S RISK ONLY," so when the new owners sued for faulty construction, Essex denied coverage—even though another endorsement specifically stated that the policy covered a renovation project. The court disagreed with Essex's claim that the policy did not cover construction work, saying: "Suffice to say, that if a 'Commercial General Liability Coverage' policy taken out by a contractor is not generally intended to cover 'construction,' it might surprise the Texas Supreme Court; it seems to treat this conclusion as axiom." *Hines*, 2010 WL 10941 at *2 (citations omitted).

Having found that construction work was covered by the policy, the court addressed the exclusions raised by Essex. The court disagreed that the "expected or intended" work exclusion applied because the allegations against the insured involved only claims of negligence, which do not involve an expected or intended act. And, the exclusion for "property damage to . . . that particular part of any property that must be restored, repaired or replaced because 'your work' was incorrectly performed on it" also did not apply because "that particular part" limits the scope of the exclusion. In particular, the allegations against the insured included claims that her work damaged portions of the house that she did not replace or renovate. Accordingly, Essex had a duty to defend its insured.

C. Additional Insured Coverage: *Brown & Brown of Texas, Inc. v. Omni Metals, Inc.*, 2009 WL 4856782 (Tex. App.—Houston [1st Dist.] Dec. 17, 2009, no pet.)

In a lengthy decision, the 1st Court of Appeals in Houston held that, among other things, an additional insured can rely on the statements of an insured's agent and the terms of a certificate of insurance in order to pursue a claim against the agent and the

insurer because of a failure to provide accurate information about coverage. Omni Metals had its metals stored and processed by Port Metals Processing and, as a condition of their arrangement, required Port Metals to obtain general liability insurance naming Omni as an additional insured. When a fire broke out and damaged some of Omni's products, a dispute arose about the loss. Ultimately, Omni sued Port Metals' agent and insurer. The court rejected the claim that Omni should not be able to rely on the certificate or the agent's statements because Omni is a third party to the insurance contract. Instead, the court allowed Omni to support its causes of action by focusing on the insurance agent's failure to inform its insured—Port Metals—that its policy had changed over time and an exclusion now existed that did not originally exist. Justice Sam Nuchia issued a dissent, claiming that an additional insured should not be able to rely on anything outside the insurance policy to support a cause of action against an insurance company or an agent.

Notably, at least on its face, this appears to be a clear detour from prior Texas case law that emphasizes that certificates of insurance cannot be relied on by third parties. The court, however, distinguished recent case law on that issue, noting that those cases involve situations where the complaining party claims to be an additional insured under an insurance policy. *Brown & Brown*, 2009 WL 4856782 at *23–*25 (discussing *TIG Ins. Co. v. Sedgwick James*, 184 F. Supp. 2d 591 (S.D. Tex. 2001) ("*Via Net I*"); *Via Net v. TIG Ins. Co.*, 211 S.W.3d 310 (Tex. 2006) ("*Via Net II*")). In such situations, the purported additional insured is held to the same burden as the named insured in reading the policy to understand its coverage rights. *Id.* at *25. In contrast, the complaining party in *Brown & Brown* was a customer of the insured and the court found that, under those facts, the customer should be able to rely on the representations of the insured's insurance agent regarding the extent of coverage available for the business dealings between the customer and the insured. As such, that customer, according to the Houston Court of Appeals, does not have a duty of due diligence to seek out and review the third party's insurance policy to verify its terms in order to maintain a suit for misrepresentation and deceptive trade practices against the third party's insurance agent and the agent's principal—the insurer.

D. Additional Insured Coverage: *Burlington Northern & Santa Fe Railway Co. v. National Union Fire Insurance Co.*, 2009 WL 4653406 (Tex. App.—El Paso Dec. 9, 2009, pet. filed)

In *Burlington North*, the additional insured endorsement at issue provided blanket additional insured coverage where required by written contract. The coverage was limited, however, to "liabilities arising out of [the additional insured's] operations performed by or for the named insured, but excluding any negligent acts committed by such additional insured." *Burlington Northern*, 2009 WL 4653406 at *3. The insurer argued that because allegations existed that the railroad was at fault (at least partly) for the collision that occurred additional insured coverage did not exist. That is, the additional insured coverage only could be triggered by allegations involving the sole negligence of the named insured. Following *Evanston Insurance Co. v. ATOFINA Petrochemicals, Inc.*, 256 S.W.3d 660, 665–66 (Tex. 2008), the El Paso Court of Appeals disagreed with the insurer, ruling that the railroad was entitled to a defense and the insurer could not escape its duty to defend the entire lawsuit against the additional insured.

E. Waiver and Estoppel: *Pierre v. Potomac Insurance Co. of Illinois*, 2009 WL 3444790 (5th Cir. Oct. 26, 2009)

Although addressed in the context of a property insurance claim, the 5th Circuit reiterated that Texas law does not allow an insured to avoid the operation of an exclusion under the doctrines of waiver and estoppel. Accordingly, although the insurer did not raise a fungus exclusion as a defense to coverage until three years after the lawsuit was filed, the insurer still was entitled to summary judgment on its application because "although waiver and estoppel may operation to avoid a forfeiture of [an insurance] policy," the doctrines may not operate to "create a new and different contract with respect to risks covered by the policy." *Pierre v. Potomac Ins. Co. of Ill.*, 583 F. Supp. 2d 806, 810 (N.D. Tex. 2008), *aff'd* 2009 WL 3444790 (5th Cir. Oct. 26, 2009).

F. Conflicts of Law: *Trammell Crow Residential Co. v. Virginia Surety Co., Inc.*, 2009 WL 3353035 (N.D. Tex. Oct. 16, 2009)

In this case, Trammell Crow filed suit against its insurer, Virginia Surety, alleging that the insurer mishandled its defense in a Colorado construction defect case. Virginia Surety counterclaimed, alleging that Trammell Crow was obligated to participate in the defense of the Colorado lawsuit because it had fulfilled its deductible obligations under policies with Old Republic and American Protection Insurance Co. ("APIC"). Virginia Surety also alleged claims for contribution and subrogation against Old Republic and APIC.

Before the court in October 2009 was Virginia Surety's Motion for Choice of Law. The court found that a conflict existed between Colorado and Texas law on several issues: (1) "Under Colorado law, an insured does not appear to have the right to pick an insurer to provide a defense from several that have time on a risk, whereas Texas law allows an insured to make such a choice"; (2) "Colorado law specifically recognizes the right of an insurer to seek contribution from non-participating insurers, while under Texas law there is generally no right to contribution between co-insurers and no right to contractual or equitable subrogation once an insured is made whole"; and (3) "Colorado and Texas law differ in some respects regarding the standards for establishing bad faith in an insurance context."

Faced with those differences in substantive law, the Court evaluated the application of Article 21.42 of the Texas Insurance Code, which requires application of Texas law to an insurance matter if the proceeds are payable to a Texas citizen, the policy is issued by a company doing business in Texas and the policy is issued in the course of that company's Texas business. Evaluating those requirements, the court determined that Article 21.42 applied to the contractual claims involved in the lawsuit. In particular, the court found that, despite Virginia Surety's claims, Trammell Crow had adequately proven its status as a citizen or inhabitant of Texas. Moreover, Trammell Crow's claims would be first-party claims under Texas law, making them payable to Trammell Crow in Texas. Further, the Colorado claimants already had been paid and had no further monetary interest in the case. Finally, the policies at issue all were issued by companies doing business in Texas and in the course of their Texas business.

Turning to the statutory claims in the lawsuit, through its analysis of the factors under Restatement (Second) of Conflict of

Laws § 145, the court held that they weighed in favor of applying Texas law. The court found that the policy was purchased in Texas by a Texas company from an insurance company doing business in Texas. Accordingly, the effect of any bad faith denial of coverage would have occurred in Texas. Those factors outweighed the fact that the conduct that caused any such bad faith took place in Illinois, Virginia Surety's home, where the handling of the claim occurred.

G. Other Insurance Clauses: *Colony Insurance Co. v. Peachtree Construction, Ltd.*, 2009 WL 3334885 (N.D. Tex. Oct. 14, 2009)

The Northern District of Texas ruled that allegations against Peachtree Construction for its *sole* negligence were insufficient to trigger additional insured coverage under its subcontractor's (Cross Roads, L.P.) insurance policy. The additional insured provision at issue provided that Peachtree is an additional insured only with respect to liability arising out of Cross Roads' ongoing operations performed for Peachtree. Accordingly, absent any allegations against Cross Roads, the subcontractor's carrier did not have a duty to defend or indemnify Peachtree. And, as such, the "other insurance" clause in Peachtree's CGL policy, which made its CGL insurance excess over any additional insured coverage, was not implicated and Colony was under no obligation to reimburse Travelers—Peachtree's primary carrier—for settlement funds that Travelers paid on Peachtree's behalf.

If the additional insured provision had been applicable, it appears the court was prepared to rule that Cross Roads' insurer was primary over Peachtree's insurer. In light of the recent pronouncement in *Trinity Universal* that "other insurance" clauses apply only to "indemnity" and not "defense," it is questionable whether that holding would have been correct. In particular, if "other insurance" clauses apply only to "indemnity," the "other insurance" provision in Peachtree's policy stating that it is excess over any other primary policy in which Peachtree is named as an additional insured may not apply when considering the duty to defend.

H. Exclusions J(5) and J(6): *Basic Energy Services, Inc. v. Liberty Mutual Insurance Co.*, 655 F. Supp. 2d 666 (W.D. Tex. 2009) (vacated due to settlement)

The Western District of Texas followed *Lamar Homes, Inc. v. Mid-Continent Casualty Co.*, 242 S.W.3d 1 (Tex. 2007), and held that an "occurrence" was alleged in an underlying lawsuit where a third party claimed that the insured dropped tubing into an oil well, damaging the oil well casing. And, having established that the insuring agreement was satisfied, the court addressed exclusions J(5) and J(6), reaffirming the Fifth Circuit's finding that the phrase "that particular part" limits those exclusions, barring coverage only for the specific portions of the well on which Basic Energy worked and not the entire well. Notably, in reaching its conclusions, the court held that Texas' "eight corners" rule applies to an insurer's obligation to reimburse defense costs even when there is no duty to defend contained within the policy. Judge Junell also ruled that the 18% penalty under the "prompt payment of claims" act applied to a contractual duty to advance defense costs even though the policy did not provide for a traditional duty to defend. In other words, although it is well-settled that the "prompt payment of claims" act does not apply to the duty to indemnify, the court held that it applied to the extent that the duty to

indemnify encompassed a duty to advance defense costs.

I. Trigger: *Wilshire Insurance Co. v. RJT Construction, Co., LLC*, 581 F.3d 222 (5th Cir. 2009)

The Fifth Circuit, following the Supreme Court of Texas' adoption of the "actual injury" trigger, held that an insurer owed a defense to its insured because the pleadings against the insured homebuilder alleged that property damage occurred during the policy period at issue. When determining whether an "occurrence" took place, as required by the policy, courts must look at when the property damage is alleged to have occurred and not when the damage was discovered. Accordingly, the court found that allegations that "cracks in the walls and ceilings" were "suddenly appearing in 2005" were sufficient to allege "property damage" during the 2005 policy period. The cracks were not warning signs of future damage, but were held to be the damage itself. *See Wilshire*, 581 F.3d at 225.

Having ruled that an "occurrence" took place during the applicable policy period, the court turned to the subsidence exclusion in the policy. The court disagreed with the district court's application of the exclusion, finding that the lower focused on the movement of the foundation as opposed to the movement of land. According to the Fifth Circuit, faulty work of the insured caused the foundation to be unable to withstand subsidence—it did not cause the land movement itself. Because the movement of land must "result [] from the [insured's] operations" in order for the exclusion to bar coverage, the court found that the exclusion was inapplicable. *Id.* at 226.

J. The "Highly Probable" Standard for an "Occurrence": *National Union Fire Insurance Co. v. Puget Plastics Corp.*, 649 F. Supp. 2d 613 (S.D. Tex. 2009) (reh'g pending)

On remand from a Fifth Circuit ruling affirming the district court's opinion on the parties' cross-motions for summary judgment, the Southern District of Texas issued a lengthy opinion in *Puget Plastics*, addressing the existence of an insurer's duty to indemnify its insureds. Two particular issues addressed by the court are worth highlighting.

First, in determining whether an "occurrence" existed, the court applied the Supreme Court of Texas' "highly probable" language from *Lamar Homes*, 242 S.W.3d at 8–9 (finding that, among other things, deliberate acts may constitute an accident unless the resulting damage was "highly probable" whether the insured was negligent or not). In doing so, the court found that the "highly probable" standard was an *objective* rather than a *subjective* standard. Accordingly, the court ultimately held that because "it was highly probable, and a reasonable molder would have known it was highly probable, that Puget's substandard processing and work conditions" would render Puget's plastic water chambers weak and likely to fail, Puget's actions did not constitute an "occurrence" under its CGL policy.

In this author's opinion, such a holding undercuts the *Lamar Homes* decision and jeopardizes the availability of CGL coverage in similar cases. In *Lamar Homes*, the Supreme Court of Texas specifically rejected foreseeability as a boundary line between accidental and non-accidental conduct. By applying a "highly probable" test, the district court essentially adopted a "highly foreseeable" test. This does not

appear to be what the Supreme Court intended in *Lamar Homes*.

Second, the court reaffirmed that CGL insurance provides coverage for consequential economic damages. Such coverage only exists, however, when those consequential damages result from *covered* property damage or bodily injury under the policy. This is the case because the policy clearly states that it pays for damages "because of" property damage covered by the policy.

As noted above, a motion for rehearing has been filed by Puget Plastics. The focus of the rehearing is on the court's application of the "highly probable" test.

K. Waiver of Subrogation: *Travelers Lloyds Insurance Co. v. Dyna Ten Corp.*, 2009 WL 2619232 (Tex. App.—Fort Worth Aug., 26, 2009)

The Fort Worth Court of Appeals held that even though an owner and a contractor agreed to waive all rights against each other—and, thus, that the owner's insurer also waived such rights—the owner (and its insurer) did not waive such rights against the subcontractor, whose faulty plumbing work damaged multiple floors and systems in a condominium skyscraper. The provision in the owner's contract with the contractor clearly stated that the waiver was only as to claims against each other and said nothing of the owner waiving any such rights in favor of subcontractors on the project. More specifically, the waiver provision provided: "Owner and Contractor waive all rights *against each other*, if any, for damages caused by fire or other causes of loss to the extent of actual recovery of any insurance proceeds under any property insurance applicable to the Project except such rights as they have to proceeds of such insurance held by Owner in good faith. . . ." Further, the provision required that subcontractors obtain similar written waivers *in favor of the Owner* but it did not obligate the owner to provide a mutual waiver.

The waiver of subrogation provision in the contractor's insurance policy also did not apply because the policy paid out under the property coverage form and not the CGL coverage form. The CGL form contained a blanket waiver of subrogation endorsement that did not apply to the property coverage form. That endorsement waived the insurer's subrogation rights where required of the insured by written contract but only for claims paid for the insured that the insured is legally obligated to pay as damages to a third party. Because the insurance paid was for first-party property coverage, the waiver of subrogation provision was inapplicable on its face.

L. Contractually Assumed Liability Exclusion: *Century Surety Co. v. Hardscape Constr. Specialties, Inc.*, 578 F.3d 262 (5th Cir. 2009)

In August 2009, the Fifth Circuit Court of Appeals followed the Supreme Court of Texas' decision in *Lamar Homes, Inc. v. Mid-Continent Casualty Co.*, 242 S.W.3d 1 (Tex. 2007), finding that allegations of allegedly defective construction of a pool was an "occurrence" within the meaning of a CGL policy. In addition, the court addressed the "contractually assumed liability" exclusion and found that the claims asserted did not trigger the "insured contract" exception to the exclusion. In particular, the court found that all the allegations gave rise to contract claims only—not tort liability as required to trigger the "insured contract" exception—because the damages occurred only to property that was the subject matter of the parties' contract (i.e., the pool). Thus, although an "occurrence" existed, no coverage existed

because of application of the contractually assumed liability exclusion.

On first blush, the *Century Surety* decision seems to support the argument that a breach of contract claim is excluded by the "contractually assumed liability" exclusion. Upon closer examination, however, it is clear that the case does not stand for that proposition. Rather, the parties stipulated that the exclusion applied and the entire issue on appeal was whether an *exception* for assuming the *tort* liability of another applied to the facts of the case. *See Century Surety*, 578 F.3d at 266 n.2. Moreover, in *Century Surety*, a general contractor was attempting to recover under a subcontractor's policy for the subcontractor's assumption of the general contractor's liability to the owner. Accordingly, the court properly focused on whether an exception to the exclusion applied. As further evidence that the court's opinion does not stand for the proposition that breaches of contract are excluded by the "contractually assumed liability" exclusion, the Fifth Circuit did not overrule—let alone address—any of the cases that address the scope of the exclusion itself, including its decision in *Federated Mut. Ins. Co. v. Grapevine Excavation, Inc.*, 197 F.3d 720 (5th Cir. 1999).

The Fifth Circuit's decision in *Century Surety* also is distinguishable from the *Gilbert Texas Construction* case discussed earlier in this paper. In that case, Gilbert was being sued solely for the alleged breach of its contract and not for liability it assumed to a third party in a contract.

M. Classification Limitation: *Essex Insurance Co. v. Davis*, 2009 WL 2424088 (N.D. Tex. Aug. 7, 2009)

In this case, an insurer refused to extend coverage to its insured for claims arising out of the roof it applied to a synagogue. The insurer argued that the claims were precluded because the policy contained a Classification Limitation Endorsement that limited coverage to that which was specified in the policy's declaration—i.e., "residential roofing." Finding the term "residential" to be undefined in the policy, the court noted that "residence" has been commonly understood as "the place where one actually lives as distinguished from one's domicile or a place of temporary sojourn." In contrast, a "synagogue" is a "house of worship and communal center of a Jewish congregation." And, although the insured alleged that he could show the policies were purchased for the job at the synagogue, he never produced competent evidence of such. Accordingly, the court found that the work on the synagogue was outside the scope of the policy, which limited coverage to residential roofing work.

N. Workers' Compensation: *BJB Construction, LLC v. Atlantic Casualty Insurance Co.*, 338 F. App'x 382 (5th Cir. July 13, 2009)

The Fifth Circuit Court of Appeals held that Texas Mutual Insurance Company, which issued a workers' compensation policy to a subcontractor on a construction project, did not owe that subcontractor a defense or indemnity arising out of claims by a non-employee who alleged that the subcontractor's negligence contributed to his injuries. The court reasoned that the subcontractor's workers' compensation carrier agreed to provide insurance for the subcontractor's employees—not commercial general liability coverage. Because the injured party's allegations focused on the control of the workplace environment and not on any employer-employee relationship with the subcontractor, the pleadings did not allege a claim within the coverage provide by Texas Mutual.

O. Additional Insured Requirements: *Aubris Resources, LP v. St. Paul Fire and Marine Ins. Co.*, 566 F.3d 483 (5th Cir. 2009)

In April 2009, the Fifth Circuit Court of Appeals found that, in accordance with *Evanston Insurance Co. v. ATOFINA Petrochemicals, Inc.*, 256 S.W.3d 660, 665–66 (Tex. 2008), an additional insured provision in a contract is to be read separately from the indemnity provision. The court construed an additional insured requirement that specified that it did not extend "to any obligations for which UNITED [an oil field owner] has specifically agreed to indemnify Contractor." *Aubris Resources*, 566 F.3d at 487. The insurer argued that such language referred specifically to the contract's general indemnity agreement in which United agreed to indemnify J&R Valley—which serviced United's oil fields—for United's sole negligence. The court disagreed, finding that the indemnity provision did not limit the additional insured requirement in the contract despite the inclusion of seemingly limiting language. In particular, the court read the additional insured provision to exclude additional insured coverage only in instances where a specific indemnity agreement relating to the litigation at issue existed. The indemnity agreement in the service contract did not apply to limit additional insured coverage.

P. Additional Insured Requirements: *Bituminous Cas. Corp. v. McCarthy Building Cos., Inc.*, 2009 WL 962536 (Tex. App.—San Antonio, Apr. 8, 2009, no pet.)

Also in April 2009, the San Antonio Court of Appeals emphasized the importance of clear contract language when requiring additional insured status. In particular, the court found that the parties' contract required that a subcontractor obtain both automobile liability coverage and a general liability insurance policy. But, the same agreement did not require additional insured coverage under the automobile liability policy—only under the CGL policy. Accordingly, the McCarthy Building Companies did not qualify as an additional insured and Bituminous, the automobile liability insurance carrier, did not have a duty to defend McCarthy.

Q. Workers' Compensation Insurance and the Exclusive Remedy Defense: *Entergy Gulf States, Inc. v. Summers*, 282 S.W.3d 433 (Tex. 2009), *HCBeck, Ltd. v. Rice*, 284 S.W.3d 349 (Tex. 2009), and *Lazo v. Exxon Mobil Corp.*, 2009 WL 1311801 (Tex. App.—Houston [14th Dist.] May 7, 2009, no pet.)

On April 3, 2009, the Supreme Court of Texas issued two opinions addressing workers' compensation benefits and the applicability of the exclusive remedy defense. In both cases at issue was whether a party qualified as a "general contractor" and had "provided" workers' compensation coverage such that each was entitled to the benefit of the exclusive remedy provision. In *Entergy*, the premises owner's contract for construction was with one of its related corporations. The contract included a requirement that Entergy provide workers' compensation insurance to the contractor's employees. And, it was undisputed that the injured party sought and obtained workers' compensation benefits from Entergy's owner provided insurance program. Accordingly, the Court then addressed whether Entergy—as a premises owner—qualified as a "general contractor" under the terms of the workers' compensation statutes. The court found that Entergy qualified because it "undertook to procure the performance of work." As such, it was a

"general contractor" and also an "employer" and was entitled to the benefit of the "exclusive remedy" provision.

Similarly, in *HCBeck*, the Court addressed whether a general contractor "provided" workers' compensation coverage as required by the statutes. The Court found that it did because the general contractor's contract with the owner and its contracts with its subcontractors required the subcontractor to enroll in an owner controlled insurance program. Moreover, both contracts specified that the general contractor was responsible for procuring workers' compensation insurance in the event the owner terminated the OCIP. Rice, the injured party, argued that the subcontract between HCBeck and Haley Greer did not obligate HCBeck to obtain workers' compensation insurance in the event that the OCIP was terminated, claiming instead that the subcontract specifically required Haley Greer to obtain "alternate insurance." The Court disagreed, however, noting that the last sentence of the provision at issue specifically referred the parties to the prime contract HCBeck executed and which specifically required HCBeck to purchase such insurance at the owner's cost in the event the owner could not furnish the OCIP. Accordingly, HCBeck "provided" workers' compensation insurance and was entitled to the protections of the exclusive remedy provision. In sum, the Court held that the Texas workers' compensation insurance scheme, as enacted by the Legislature, was intended to make the exclusive remedy defense available to a general contractor who, by use of a written agreement with the owner an subcontractors, provides workers' compensation insurance coverage to its subcontractors and the subcontractors' employees.

Shortly after the *Entergy* and *HCBeck* opinions were issued, the Houston Court of Appeals followed suit. *See Lazo v. Exxon Mobil Corp.*, 2009 WL 1311801 (Tex. App.—Houston [14th Dist.] May 7, 2009, no pet.). In that case, the court found that Exxon Mobil was entitled to assert the exclusive remedy defense because it procured the work of its subcontractor and its employees, qualifying Exxon Mobil as a "general contractor" under the statutes. In turn, Exxon Mobil qualified as an "employer" and was able to assert the defense. In doing so, the court relied almost exclusively on the Supreme Court's decision in *Entergy*.