The Weekly Update of Texas Insurance News
TEXAS INSURANCE LAW NEWSBRIEF
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TEXAS SUPREME COURT REVISITS THREE PRIOR OPINIONS TO DECIDE ISSUES ARISING FROM A COVERAGE DISPUTE BETWEEN TWO INSURERS AND HOME BUILDER

Last Friday the Texas Supreme Court revisited its decisions in *Lamar Homes*, *Don's Building Supply*, and *GuideOne Elite* to reach a decision related to a coverage dispute arising from five underlying homeowners' suits which allege water damage because of defective construction. In *Pine Oak Builders, Inc. v. Great Am. Lloyds Ins. Co.*, 2009 WL 353526 (Tex. February 13, 2009), two insurers, Great American and Mid-Continent Casualty Co., issued CGL policies covering time periods during a residential construction project involving Pine Oak. Five homeowners sued Pine Oak alleging their homes suffered water damage because of defective construction. The insurers denied Pine Oak's request for a defense in the homeowner suits, prompting suit. Both carriers sought a declaratory judgment that they had no obligation to defend or indemnify Pine Oak and the trial court granted summary judgment for the insurers on all issues.

The appellate court affirmed summary judgment for Mid-Continent because of an EIFS exclusion in its policies, and Pine Oak did not appeal this ruling. However, the appellate court concluded Great American had a duty to defend four homeowner suits and further held Pine Oak could not recover statutory damages under the Prompt Payment of Claims statute for Great American's failure to defend the suits. The Texas Supreme Court granted the parties' cross-petitions for review.

***Lamar Homes*:** The relevant policy language in the Great American policies was identical to the policy language construed in the *Lamar Homes, Inc. v. Mid-Continent Casualty Co.* decision. Therefore, a claim for faulty workmanship against a homebuilder was a claim for property damage caused by an occurrence under a CGL policy. Once again, applying *Lamar Homes*, the Texas Supreme Court held the Prompt Payment of Claims statute (Tex. Ins. Code 542) does apply to a situation where an insurer breaches its duty to defend under a liability policy.

Editor's note: The high court's treatment of the Prompt Payment penalty provision continues to provide an interesting analysis in light of the court's proper ruling in *Evanston Ins. Co. v. Atofina Petrochemicals, Inc.*, 256 S.W.3d 660 (Tex. June 13, 2008)(*See* *MDJW Newsbrief* June 16, 2008), where it ruled the penalty provision does not apply to indemnity benefits under a liability policy. It still leaves claims for previously tendered defense benefits subject to the 18% statutory penalty pursuant to its decision in *Lamar Homes*, despite the obvious inconsistency between the two decisions. A majority of the Texas Supreme Court apparently doesn't have any problems with applying the 18% statutory penalty to *defense benefits* under a liability policy when coverage is later determined to exist, but it does have problems applying the same penalty provision to the same claim under the same policy as it relates to *indemnity*

benefits. The decision in *Atofina Petrochemicals* is simply a good illustration of why the 21.55 holding in *Lamar Homes* was terribly wrong. In the prior decision from the high court, they reversed and rendered. The new *Atofina Petrochemicals* opinion reversed and *remanded* back to the trial court to decide the question of attorney fees and interest.

Don's Building Supply: On the question whether Great American's policies were triggered under the facts alleged in the underlying suits, the court of appeal followed the "exposure rule" for determining whether a property damage claim is covered under an occurrence-based CGL policy. Great American urged the Supreme Court to adopt the "manifestation rule" for deciding whether a property-damage claim was covered. Both of these approached were rejected in *Don's Building Supply, Inc. v. OneBeacon Ins. Co*., another case involving insurance coverage of EIFS claims. In that case, the Supreme Court instead adopted the actual-injury rule, under which property damage occurs during the policy period if "actual physical damage to the property occurred" during the policy period. So, here, property damage occurred under the Great American policies "when a home that is the subject of an underlying suit suffered wood or rot or other physical damage."

***GuideOne Elite*:** The final issue was whether evidence extrinsic to the eight corners of the policy and the underlying lawsuit may be used to establish the insurer's duty to defend. Coverage here depended in part on whether the alleged defective work was performed by Pine Oak or a subcontractor. Four of the five underlying suits alleged damages from work performed by a subcontractor. Pine Oak submitted evidence that the defective work alleged in the last case was performed by subcontractors; And based on the extrinsic evidence Pine Oak argued Great American had a duty to defend.

The extrinsic fact Pine Oak sought to introduce contradicted the facts alleged in the last suit. After a brief review of the *GuideOne Elite v. Fielder Road Baptist* Church decision compared to the actual policy language, the high court concluded Great American's duty to defend was not triggered by the last lawsuit. To hold otherwise would "conflate the insurer's defense and indemnity duties."

FIFTH CIRCUIT INTERPRETS CONTRACT AND HOLDS INSURANCE CLAUSE LANGUAGE UNAMBIGUOUS

Last Thursday the Fifth Circuit held a contractual insurance provision was unambiguous and required the carrier ("Gray") to pay for expenses incurred in litigation involving personal injuries. In *The Lubrizol Corp. v. The Gray Ins. Co*., 2009 WL 348820 (5th Cir. February 12, 2009), Lubrizol sued Gray to pay for expenses associated with litigation against Lubrizol arising from injuries suffered by a contractor's employees while repairing a storage tank. Lubrizol contracted with Pat Tank, Inc. ("Pat Tank") for Pat Tank's services in repairing a storage tank. To fulfill its obligations under the contract, Pat Tank purchased a CGL policy from Gray. The district court ordered Gray to pay Lubrizol's legal expenses and Gray appealed.

The relevant language of the insurance clause states:

INSURANCE. [Pat Tank] shall maintain insurance policies . . . in amounts of at least $1,000,000 . . . for each of the following insurance coverages . . .:

a) Worker's Compensation (statutory)
b) Employer's Liability
c) Comprehensive General Liability . . .
d) Automobile Liability

e) Include Lubrizol as additional insured on c) and d) above

. . .

[Pat Tank], . . . to the extent necessary to provide coverage under [its] insurance for the liabilities assumed by [it] under the indemnity provisions of this Agreement, shall designate Lubrizol as an additional insured on Comprehensive Contractor's General Liability Insurance . . . .

Under Lubrizol's reading, line (e) stands alone and obligates Pat Tank to acquire at least $1 million of CGL insurance and add Lubrizol as an additional insured. The last paragraph dealt with Pat Tank's indemnity obligations under the contract. Under Gray's reading, line (e) still obligated Pat Tank to acquire at least $1 million of CGL insurance, but the final paragraph clarifies Lubrizol need only be added as an additional insured for indemnity purposes. After reviewing the district court's conclusion, the Fifth Circuit agreed the contract was unambiguous, but for different reasons. The court then addressed Gray's reliance on a two-factor test for interpreting "additional insured" provisions. Finding the two-factor test no longer viable, the court instead indicated a direct statement that the owner should be an additional insured under the contractor's insurance policy was precisely what the contract provided.