The Weekly Update of Texas Insurance News
TEXAS INSURANCE LAW NEWSBRIEF
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FIFTH CIRCUIT CERTIFIES ADDITIONAL INSURED'S LATE NOTICE ISSUES TO TEXAS SUPREME COURT

Last Friday, the Fifth Circuit Court of Appeals certified three questions to the Texas Supreme Court dealing with an additional insured's duties to comply with the ISO standard Notice Clause and whether a carrier has any duty to notify an additional insured that it may qualify as an additional insured under the policy. In *Crocker v. National Union Fire Insurance Company of Pittsburgh, P.A.*, 2006 WL 2789842 (Sept. 29, 2006), Crocker, a third-party judgment creditor, sought recovery from National Union on the basis of a default judgment that Crocker obtained against National Union's insured, Morris. Crocker had sued Morris and Morris' employer for injuries she had received when she was struck by a swinging door allegedly pushed by Morris acting in the course and scope of his employment. Morris initially refused service or process but was eventually served in September, 2002. Because he was an employee of the named insured acting in the course and scope of his employment at the time of the underlying accident, Morris was an additional insured under the terms of ten National Union policy. National Union provided a defense to the named insured, but did not provide a defense to Morris, apparently because Morris failed to forward the suit papers to National Union or otherwise inform it of the suit against him and did not request it to provide him a defense.

Morris never answered Crocker's suit and Crocker moved for a default judgment. Crocker then sued National Union as a third-party judgment creditor. On appeal, the parties did not dispute:

- Crocker's original claims against both the named insured and Morris were covered by National Union's policy;
- National Union knew that Morris was a named defendant in the lawsuit.
- National Union knew or should have known that Morris had been served in the lawsuit.
- Morris was not aware of the terms and conditions of the National Union policy.
- Morris did not know that he was an additional insured under the policy and did not forward the suit papers to National Union or otherwise inform National Union that he had been sued and did not request a defense from National Union.
- National Union did not inform Morris that he was an additional insured and did not offer to defend Morris against Crocker's claims.

National Union argued that Morris' failure to comply with the policy's Notice Clause and the ensuing default judgment relieved National Union of any contractual obligation to defend or indemnify Morris. Crocker argued that National Union was not prejudiced by Morris' failure to forward the suit papers because National Union was aware of the lawsuit against both its named insured and its additional insured, Morris, and National Union was on notice that Morris had been served. Thus, according to Crocker, because National Union breached its duty to defend Morris as a matter of law, National Union was liable to Crocker for the full amount of the default judgment.

The Fifth Circuit began its analysis by reviewing the Texas Supreme Court's holdings in *Weaver v. Hartford Accident & Indemnity Company*, 570 S.W.2d 367 (Tex. 1978) wherein the Texas Supreme Court stated that the most basic purpose of the notice requirement is to advise the insurer that an insured has been served with process and that the insurer is expected to timely file an answer. The Court stated:

> Under the facts of this case, Hartford would have been gratuitously subjecting itself to liability if it had entered an appearance for Busch, who had failed to comply with the policy conditions, who had stated he was not a permissive user, and who had never been served with process, in a suit which sought damages in excess of the policy limits. Therefore, we hold that Hartford had no duty to voluntarily undertake a defense for Busch.

Continuing, the Fifth Circuit noted that the issue of whether the insurer had a duty to inform the ignorant additional insured was apparently argued in *Weaver*. Further, the *Weaver* majority did not directly address the dissenters' opinions regarding the additional insured's apparent ignorance of the policy's terms combined with the carrier's knowledge of the suit.

After examining *Weaver*, the Fifth Circuit noted changes in Texas insurance law that led it to question whether *Weaver* constitutes controlling law. Specifically, the *Crocker* Court noted the post-*Weaver* advent of the TDI's Board Order imposing a prejudice element to a late notice defense. Also, the Fifth Circuit examined *Cruz*, 883 S.W.2d 164 (Tex. 1993), *Hernandez*, 875 S.W.2d 691 (Tex. 1994), *Risinger*, 960 S.W.2d 708 (Tex. App. – Tyler 1997, writ den'd), and *Struna*, 11 S.W.3d 355 (Tex. App. – Houston [1st Dist.] 2000, no pet.) and the recent concept that an insurer's actual knowledge of the filing of a lawsuit and actual knowledge of an insured's service, irrespective of the source of such notice (*i.e.*, from the third-party claimant) was sufficient to trigger an insurer's duty to defend. The Court, noting the difficulty in reconciling *Weaver* with the changes in Texas law, questioned whether an insurer had any right or duty to defend a covered suit against an additional insured with whom it has no direct relationship and who, knowing of the suit, has not expressly or impliedly requested a defense. If the insurer knows of the covered suit, what duty, if any, does the carrier have to notify an additional insured (who does not know of the coverage) of the applicable coverage? What duty, if any, does an additional insured who has been sued have in such a situation? Accordingly, the Fifth Circuit certified the following questions to the Texas Supreme Court:

1. Where an additional insured does not and cannot be presumed to know of coverage under an insurer's liability policy, does an insurer that has knowledge that a suit implicating policy coverage has been filed against its additional insured have a duty to inform the additional insured of the available coverage?
2. If the above question is answered in the affirmative, what is the extent or proper measure of the insurer's duty to inform the additional insured, and what is the extent or measure of any duty on the part of the additional insured to cooperate with the insurer up to the point he is informed of the policy provisions?
3. Does proof that an insurer's actual knowledge of service of process in a suit against its additional insured, when such knowledge is obtained in sufficient time to provide a defense for the insured, establish as a matter of law the absence of prejudice to the insurer from the additional insured s failure to comply with the notice of suit provisions of the policy.

The certified questions were submitted on September 29th. We shall continue to monitor and this significant coverage case.

MAY THE NATURE OF THE INSURED'S BUSINESS AS DESCRIBED ON THE POLICY'S DECLARATIONS BE CONSIDERED IN DETERMINING "INSURED" STATUS?

In the recent case of *Gemini Insurance Company v. S&J Diving, Inc.*, H-05-661 one of the Federal District Courts for the Southern District examined what evidence may be considered in determining an additional insured's standing to claim coverage under a policy. Issues arose over whether Gemini owed an individual and his various business interests defense and/or indemnification for a minor's abduction and assault. The policy in question identified the named insured as a corporate entity, S&J Diving, its executive officers and directors (to the extent of their duties as officers or directors) and S&J Diving's employees (to the extent they may be liable for acts within the scope of their employment).

On the declarations page of the policy, S&J Diving was described as a diving contractor/inspector, surveyor and repairer of docks & vessels. Further, in designating the policy terms, S&J Diving was classified, for purposes of the premium charged, as "Diving-Marine; Inspections and Appraisal Companies – Inspecting for Insurance or Valuation Purposes; Ship Repair or Conversion; and Carpentry NOC." Finally, there was a provision, designated as "common policy declarations,' which made it clear that the policy declarations, the property coverage, and the conditions and endorsements were to be considered together as the complete agreement of the parties.

Gemini insisted that it owed no duty to defend, much less indemnify, S&J Diving for any of the claims that arose out of the assault which occurred during a party sponsored by another of the individual's businesses wholly uninvolved with diving or marine survey or repairs. Further, Gemini argued that its duty to defend the individuals was limited to any liability that might arise from their actions as officers or directors of the corporate entity. The Court concurred, noting that the policy declarations and exclusions, when read together, reveal a clear intent by the parties to contract for liability insurance coverage for activities related only to marine survey operations. The court held: "It is equally clear that the plain language of the policy characterizes S&J as a diving company; S&J agreed that such a description of its business operations was accurate and complete; and, Gemini relied on those representations in setting the premiums and issuing the policy." The court continued: "In this case, a reasonable reading of the entire policy limits the coverage available to Defendants to the business purpose declared when the contract was negotiated….It is not reasonable to conclude that the policy covers any and all activity, not specifically excluded, when the insured negotiated as, and described itself to be, a marine operation."

Gemini also sought reimbursement for the funds it expended in the defense and settlement of the underlying action. Noting that the Texas Supreme Court is currently reviewing *Excess Underwriters at Lloyd's, London v. Frank's Casing Crew & Rental Tools, Inc.*, 2005 WL 1252321(May 27, 2005) on rehearing, the court reserved its decision until a future date, after the Supreme Court has issued its decision on rehearing in *Frank's Casing* and the parties have had the opportunity to submit briefing on this issue.