Martin, Disiere, Jefferson & Wisdom

The Weekly Update of Texas Insurance News

TEXAS INSURANCE LAW NEWSBRIEF

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FEDERAL COURT RULES INSURED TAKE NOTHING ON PROPERTY CLAIMS AGAINST INSURER FOR AMOUNT IN EXCESS OF ACV PAYMENT

Recently in *Central Mut. Ins. Co. v. White Stone Prop., Ltd.*, A-12-CA-275-SS, 2014 WL 1092121 (W.D. Tex. Mar. 19, 2014), a Federal District Court Judge ruled that the insured take nothing after a bench trial on coverage issues. The Court found the insurer complied with all its obligations under the Policy and was not liable to the insured for further payment regarding previously withheld depreciation.

Insured White Stone Properties ("WSP") reported a claim to Insurer Central Mutual Insurance Company ("CMI") concerning hail damage to the roof of WSP's building from a hailstorm that occurred on in May 2009. CMI hired adjuster Lon Smith to inspect the property and prepare a roof replacement cost estimate. However, CMI made payments to WSP based on the actual cash value as the Policy states that CMI will not pay on a replacement cost basis *until the damaged property is actually repaired or replaced*. The actual cash value payments made by CMI totaled $1.4 million of which $1.2 million was allocated to the roof.

After receiving the actual cash value payments, WSP contracted with Innotech Construction to perform the replacement of the hail damage to the property. The contract between Innotech and WSP was for "Insurance Proceeds Received Only." Innotech placed its contract price with WSP at approximately $2.5 million. After the work was completed, WSP went back to CMI in order to recover the withheld depreciation. When CMI sought documentation from WSP regarding the cost to replace damaged property, CMI discovered that the construction work was actually performed by CEI Roofing Texas, which eventually led to its decision to refuse to provide WSP with the withheld depreciation.

Evidence presented at trial showed that the replacement work performed by CEI on the roof totaled approximately $817,000 and that amount was paid to CEI by Innotech. At trial, no party could explain Innotech's work, expenses or efforts on the project and there was no reasonable justification for why Innotech could be making a claim for over $2,000,000 to re-roof the Property. The Court went further to state the evidence in the record supported the finding there was little-to-nothing legitimate about Innotech's role as a general contractor on the Project.

CMI filed the lawsuit seeking a declaratory judgment that it has no further liability to WSP above the actual cash value previously paid. WSP counterclaimed against CMI for breach of contract and extra-contractual claims arguing it was owed $2.5 million because that was the amount of the Innotech contract. The Court found this position taken by WSP was without merit because the only amounts actually spent that were necessary to replace the roofs were the payments made to CEI. The Court noted that even if Innotech's alleged overhead and profit were added to the CEI contract amount, the total cost would not exceed the $1.2 million actual cash value payment. Therefore, the Court found WSP failed to show CMI breached the insurance contract.

The Court further found CMI was not liable for any extra-contractual claims because WSP failed to show it was entitled to the withheld depreciation and CMI was correct in not paying that sum. It was held both CMI and WSP had satisfied their obligations under their insurance contract, and neither party had anymore obligations concerning the insurance claim.

[**Editor's Note**: although the facts in this claim are unusual, the holding is very helpful for carriers defending property claims in Texas. Insureds and their lawyers *always* make replacement cost damages claims and their coverage and bad faith claims *always* attack the carrier for not paying their RC claim. The ACV calculation and payments, however, are almost always ignored. Because most RC policies require the property to be actually repaired or replaced before *any* RC benefits are owed, more carriers and their counsel should make this argument when sued.]

BEAUMONT COURT OF APPEALS DENIES MANDAMUS BY CARRIER ON AN ORDER COMPELLING COUNSEL TO PRODUCE HIS DEFENSE FILE IN SUBSEQUENT LITIGATION

The Beaumont Court of Appeals in *In re Mid Century Ins. Co. of Texas*, Cause No. 09-14-00068-CV, 2014 WL 989726 (Mar. 13, 2014) denied mandamus relief sought by Mid Century arising out of a discovery order where the trial court compelled defense counsel (for the driver of a vehicle insured by Mid Century) to produce his complete defense file from the underlying tort litigation to the representatives of the driver's estate in subsequent separate litigation between Mid Century and assignees of the insureds' claims against Mid Century.

Mid Century issued a policy that covered a vehicle driven by Robert Conrad in an accident that injured the Herberts. The Herberts offered to settle the case for policy limits but ultimately filed suit against Conrad. The Herberts suit against Conrad for personal injuries resulted in a judgment in excess of policy limits. The trial court in that personal injury case issued an order for the dependent administrator of Conrad's estate to turn over any assignable causes of action to the Herberts.

The active litigation concerning this matter includes Mid Century's declaratory judgment action consolidated with a *Stowers* claim asserted by the Herberts under the assignments of Conrad's claims against Mid Century. The Herberts obtained an assignment of the right to waive any attorney-client or work product privileges and then sought the attorney's defense file from the representation of Conrad. The trial court ordered that the file be turned over after an *in camera* review.

Mid Century contended that the file is not relevant to the second litigation and contains privileged communications between Mid Century and defense counsel because documents in the file explain the evaluation of the tort claim covered by the policy. The Herberts argued the privileges belong to the insured, Conrad, and were waived through Conrad's assignment of claims. Mid Century argued Conrad's waiver of privileges could not affect any privileges Mid Century possessed by virtue of the tripartite insurance relationship.

The Beaumont Court of Appeals found the trial court did not disregard established legal principles when it declined to recognize the insurance company's assertion of privilege in the face of the insured's assignment of the *Stowers* claim and the right to waive attorney-client and work product privileges.

[**Editor's note**: This case illustrates two important aspects of Texas insurance law: one, rejecting a policy limit demand in Texas is always a risky strategy and; two, Texas law on the existence of privilege protections arising out of the tripartite relationship are not as developed as they are in other states. As to the second point, the Texas Supreme Court has never addressed the attorney client and attorney work-product privilege protections, if any, which a liability insurer may claim arising out of the tripartite relationship. As such, the first point – the risk to a liability insurer following a policy limit demand – becomes even more risky when the carrier declines to pay a policy limit demand because of liability, damage or coverage concerns. Any time an insured is motivated to cut a side settlement deal with the plaintiff, the liability carrier should assume it will contain a waiver of any applicable attorney client or attorney work product privileges.]

SOUTHERN DISTRICT GRANTS INSURER'S SUMMARY JUDGMENT ON INSURED'S BREACH OF CONTRACT AND BAD FAITH CLAIMS

On March 13th, in *15625 Ft. Bend Ltd. d/b/a Mercedes-Benz of Sugarland v. Sentry Select Ins. Co.*, 2014 WL 1052608 (S.D. Tex. Mar. 13, 2014), a Federal District Court Judge dismissed all causes of action asserted by the insured, Mercedes-Benz, against the insurer, Sentry Select Insurance Company ("Sentry"). Mercedes-Benz brought claims against Sentry for bad faith, breach of contract, and violations of the Texas Insurance Code/DTPA.

Mercedes-Benz sought to recover payment under an Error and Omissions Liability Policy and Commercial Excess/Umbrella Policy issued by Sentry to Mercedes-Benz, for thirty-eight vehicles sold to, but not paid for by, vehicle wholesaler Tag Teams, Inc. and its president, Timmy Tieu. The title clerk at Mercedes-Benz, Sue Baze released the titles to the vehicles to Tieu before the payments for them were received and someone else at Mercedes-Benz released the vehicles to Tieu, who subsequently did not pay for them.

When Mercedes-Benz discovered the loss, it made a claim to Sentry, which paid Mercedes-Benz the $100,000 limit of the "false pretense coverage" of the policy. Sentry then paid another $100,000 in entering into a settlement with Mercedes-Benz by which all of its claims against Sentry were released, except for two exceptions. The relevant exception was "any claim for coverage Mercedes-Benz may have for any claim Mercedes-Benz may have against Baze under the Error and Omission coverage and excess/umbrella policy, and any claim for breach of duty of good faith dealing or Insurance Code claims relating to such." Mercedes-Benz also sued Tieu and a few other parties (not Baze) and obtained a judgment against Tieu after he defaulted.

In this suit, Mercedes-Benz essentially claimed coverage for the stolen vehicles. Mercedez Benz argued Baze was an insured under the policy's "Separation of Insured" provision, making Baze a separate insured; therefore allowing Mercedes-Benz to bring a claim directly against Sentry under the Error and Omissions coverage. In summary, the Court rejected Mercedes-Benz's arguments and agreed with Sentry that Mercedes-Benz clearly sought recovery for its own loss, i.e. a first party loss for vehicles sold and transferred by it for which it never received payment. Thus, there is no coverage under the Error and Omissions coverage because that coverage

is third party liability coverage. Further the Court agreed with Sentry that because Mercedes-Benz had not obtained a judgment against Baze, it had no standing to sue Sentry directly under the Error and Omissions coverage.

EASTERN DISTRICT OF TEXAS FINDS INSURER ACTED REASONABLY IN ITS DECISION TO DENY DEATH BENEFITS BASED ON ITS DETERMINATION THAT THE DECEDENT DIED FROM A PRE-EXISTING HEART CONDITION

In *Daly v. Standard Ins. Co.*, 2:11-CV-001-JRG-RSP, 2014 WL 111688a6 (E.D. Tex. Mar. 18, 2014), the Marshall Division of the U.S. District Court for the Eastern of District of Texas adopted a magistrate's recommendation to deny plaintiff's life insurance benefits on a group life insurance policy issued by Standard Insurance Company on the life of plaintiff's late husband. The claim was covered by ERISA since the policy was part of the employee benefit plan of Southwest Airlines for whom plaintiff's late husband was a pilot at the time of his death.

The sole issue the Court decided was whether accidental death benefits are unavailable because a policy excludes such benefits where the death is "caused or contributed to by…sickness…existing at the time of the accident [or] hearth attack or stroke." The insurer argued that plaintiff's husband had heart/chest problems before he had a syncopal episode (fainting) which resulted in a fatal injury to his head. On the other hand, the carrier contended the medical records showed her husband's heart problem was the result of the fall, rather than the cause of it.

The Court considered a substantial amount of medical evidence to determine the cause of her late husband's fall. Before her husband passed away, plaintiff called Mother Frances Hospital and reported that her husband showed signs of an upper respiratory type infection, was having mild chest pain, and was becoming diaphoretic, cold, and clammy. She also told the triage staff he was 61 years old and had no chronic medical issues. She spoke with several doctors about her husband's symptoms, including a cardiologist who noted that Ms. Daly described her husband as "coming down with a cold" and noting he experienced chest pressure and pain which radiated to his right arm. Another consultation report noted plaintiff's husband was suffering from pneumonia.

After her phone calls with the consulting doctors, plaintiff decided to take him to the emergency room. She drove up to the emergency room entrance where her husband got out of the car and walked into the emergency room while she found a parking spot. While her husband was waiting at the receptionist's desk, he fainted and fell to the floor, severely hitting his head.

The Court found the triage notes from plaintiff's consultation with several doctors before bringing her husband to the emergency room most persuasive. The Court noted that the deceased complaints to his wife about chest pressure were due to his cold or pneumonia. Further, the fact that the attending physician, who had no relationship with the insurer, concluded that her husband's fainting episode was "probably secondary to a cardiac event," makes it impossible for the Court to conclude the insurer was unreasonable in finding that a pre-existing heart condition "caused or contributed to" Plaintiff's husband's death. As such, the Court dismissed Plaintiff's claims with prejudice.

MDJW First Friday Webinar - Insurance Fraud

Kenni Lucas - presenter

Our next First Friday will be held on April 4, 2014 at noon **Central** Time. Kenni Lucas, a partner in the Houston office will present "Insurance Fraud." This presentation is designed to provide an overview of the crime of insurance fraud, recognized fraud indicators, claims handling and coverage issues, and civil remedies for insurance companies.

Ms. Lucas has 25 years of experience in the Texas insurance industry. She has worked in both property and casualty underwriting, agency claims management, and as a licensed property and casualty insurance adjuster for a major insurance carrier. Ms. Lucas' law practice involves the defense of lawsuits involving coverage, extra-contractual liability and policy interpretation issues in both commercial and personal lines policy litigation, as well as assisting with special investigation for insurers' claims investigations.

We have applied to the Texas Department of Insurance for one hour of Texas CE credit. Insurance professionals accredited by the Texas Department of Insurance should have their license number available during the training in order to request credit for the course.

Register for this webinar at: https://student.gototraining.com/r/3919514119227592704. After registering you will receive a confirmation email containing information about joining the training. We have a limit of 200 participants for the webinar.

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