Martin, Disiere, Jefferson & Wisdom

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TEXAS INSURANCE LAW NEWSBRIEF

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FARMERS WINS SMOKE & SOOT BAD FAITH CASE IN HARRIS COUNTY

Farmers recently won a bad faith jury trial in Houston in a homeowners' property damage case arising out of extensive smoke and soot damage to their residence. In *Khushru Dastoor vs. Texas Farmers Ins. Co and Gregory Owen*, No. 2013-69578, in the 80th District Court of Harris County, the insured submitted a claim for pervasive smoke and soot damage to the walls of his residence. Farmers denied the claim because a covered cause of loss could not be determined. The insured couldn't identify a fire, electrical damage, lightening, or any other covered cause of loss. Under the policy, smoke and soot damage had to be "sudden and accidental" to be covered. Farmers investigation determined the insured's constant burning of an oil lamp in his fire place for religious purposes was the cause of the loss and denied the claim as not being sudden and accidental. Dastoor hired counsel and sued both Farmers and the adjuster who handled the claim for breach of contract, bad faith, Insurance Code violations and fraud.

Plaintiff's counsel, Robert Collins of Houston, argued the insured didn't have to prove the cause of the smoke and soot damage. He argued the insured only had to prove the loss was sudden and accidental to him. Plaintiff called several expert witnesses who are well known in Texas property cases including CIH Marion Armstrong (Armstrong Forensic Lab in Dallas), Public Adjuster Randell Smith, PA and estimator Stephen Hadhazi, and engineer Claudia Autry. Farmers relied on CIA Michael Possen from Exponent in Oakland, California and estimator Randall Taylor from West Fire Construction in Houston. Prior to submitting the case to the jury, the trial court granted Farmers' Motion for Directed Verdict dismissing the claims against the adjuster and also dismissing the fraud claim against Farmers. Following a jury trial which lasted over parts of two weeks, the jury determined Farmers didn't breach the contract, didn't commit bad faith and didn't violate the Texas Insurance Code.

Editor's Note: MDJW Partners Chris Martin and Leslie Tan tried this bad faith case for Farmers and thanks the Farmers team for the opportunity to win the case and also congratulates everyone on the team who contributed to the development of the case and the trial court win.

HOUSTON FEDERAL COURT FINDS HOMEOWNER MISLED STATE FARM BY SUING INCORRECT ENTITY & RULES STATE FARM SHOULD NOT HAVE TO DEFEND SAME LAWSUIT IN SECOND TRIAL

In another victory against unscrupulous forum shopping by plaintiff's attorneys, a Houston federal court recently granted a summary judgment in favor of State Farm in *Vada De Jongh v. State Farm Lloyds, Inc.*, No. H-14-2305 (S.D. Tex. Aug. 17, 2015). The case arose out a homeowner's claim for damage from an April 2012 hailstorm in Alvin, Texas. After the State Farm adjuster found that covered loss was below the deductible, State Farm denied the claim and closed its file. When De Jongh asked State Farm to reopen the file to reinspect the property, another adjuster inspected the property and again found the loss was below the deductible. De Jongh sued State Farm Lloyds Inc. and the original adjuster. State Farm timely removed the case arguing De Jongh had misidentified State Farm as State Farm Lloyds *Inc.*, a Texas entity that was not involved in the claim. The court eventually entered a take-nothing judgment in favor of State Farm and the adjuster.

On appeal, the Fifth Circuit vacated the trial court's judgment because it found that State Farm Lloyds, Inc., rather than State Farm, was the intended defendant. Because both De Jongh and State Farm Lloyds, Inc. were Texas residents, the trial court lacked diversity jurisdiction. After remand, *despite arguing to the Fifth Circuit that she had meant to sue State Farm Lloyds, Inc.*, De Jongh amended her complaint to name only State Farm as a defendant. State Farm *again* removed the action to federal court based on diversity jurisdiction.

Once back in federal court, State Farm moved for summary judgment on the basis that De Jongh failed to sue State Farm within the 2-year limitations period. Judge Lynn Hughes took De Jongh at her word to the Fifth Circuit where her lawyers said she meant to sue State Farm Lloyd's, Inc. and the Court found she misled State Farm by taking it to trial even though she possessed sufficient knowledge that "Inc." was not her intended defendant. Noting that allowing the case to proceed would require State Farm to defend against the exact same claims in a second trial, the Court held limitations would not relate back to the original filing date and granted summary judgment for State Farm.

Editor's Note: State Farm's defense in the first trial, the appeal, and the second round of litigation was handled by MDJW attorneys Chris Martin, Levon Hovnatanian, Marilyn Cayce, and Raymond Kutch. We congratulate the State Farm team for its win.

DALLAS COURT OF APPEALS HOLDS INSURER WAIVED APPRAISAL CLAUSE & MANDAMUS RELIEF DENIED

Recently the Dallas Court of Appeals denied mandamus relief to an insurer seeking to compel appraisal holding the insurer had waived its right to appraisal by engaging in extended litigation and mediation before invoking the appraisal clause. In *In re GuideOne Nat'l Ins. Co*., No. 05-15-00981-CV, 2015 WL 5050233 (Tex. App. —Dallas Aug. 27, 2015), the insurer denied the claim in July 2014 and the insured sued in September 2014. The court ordered the parties to mediation and the mediation was conducted in April 2015. The insurer moved to compel appraisal one week after the failed mediation. The Court of Appeals held there was some evidence the parties had been at an impasse since the denial of the claim nine months earlier and, as such, the trial court did not abuse its discretion by ruling the insurer waived its right to appraisal.

HOUSTON FEDERAL COURT HOLDS EXCESS CARRIER MUST INDEMNIFY ITS ADDITIONAL INSURED

Houston Federal District Court Judge Kenneth Hoyt recently held a commercial liability carrier was required to defend and indemnify its additional insured under circumstances in which its named insured was not held liable for the loss. In *L-Con, Inc. v. CRC Ins. Servs., Inc.*, No. 4:13-CV-1526, 2015 WL 5021985 (S.D. Tex. Aug. 24, 2015), L-Con and Oiltanking entered into a Master Service Agreement (MSA) which included certain welding services by L-Con. The MSA required L-Con to name Oiltanking as an additional insured on its policies and obtain at least $1 million in primary coverage and $3 million in excess coverage. It also required that L-Con's insurance be primary to Oiltanking's own coverage. L-Con obtained $2 million primary coverage from American Contractors (ACIG) and $17 million in excess coverage from Interstate. Meanwhile, Oiltanking had a package policy provided by Lloyd's of London which included $5 million in primary coverage and $46 million in excess coverage.

An explosion during a welding project caused a death and severe injuries to several L-Con employees. The claimants sued only Oiltanking and not L-Con, presumably because L-Con was protected from suit by the worker's comp bar. ACIG agreed to defend Oiltanking as an additional insured, and the claimants obtained a $21 million judgment against Oiltanking. Presented with the excess judgment, Interstate refused to defend or indemnify Oiltanking, asserting three main arguments:

1. Oiltanking was not an additional insured under its policy because Oiltanking had been found solely negligent for the claimants' damages, and thus the loss did not "arise out of" L-Con's work for Oiltanking as required by the additional insured endorsement.

2. L-Con's employees were insureds by definition under the terms of L-Con's policies, and therefore this suit by one insured against an additional insured violated the Cross Suits exclusion.

3. The Interstate policy, by its Other Insurance clause, was excess to all other coverage available to Oiltanking and therefore Oiltanking's own carrier must exhaust its $5 million primary coverage before Interstate's coverage is triggered, and the two excess carriers must share the loss on a *pro rata* basis.

On cross motions for summary judgment, the court rejected the first two arguments. First, the court noted that the "arising out of" standard in the additional insured endorsement is a broad "but-for" causal connection and *does <u>not</u> require a finding of actual liability on the part of the named insured.* The court also noted in this regard that L-Con had never been sued or designated as a responsible third party and thus the jury had no opportunity to assign any liability to L-Con, implying the court did not intend to let a strategic decision by the claimants stymie the parties' contractual intentions. Looking to the terms of the MSA as authorized by the policy itself and *In re Deepwater Horizon*, the court concluded there was "no doubt" that the loss arose out of L-Con's welding work for Oiltanking and thus Oiltanking was entitled to additional insured status.

Second, the court rejected the Cross Suits exclusion, observing that in this case L-Con's primary policy, which controlled the terms of the Interstate policy, allowed L-Con to choose to designate its employees as insureds. L-Con denied ever exercising this option and Interstate could not present any evidence that L-Con had done so. Therefore, the employees were not insureds and their suit against Oiltanking did not violate the Cross Suits exclusion. (The court's analysis did not give any hints as to what it might have done if the employees had been defined insureds.)

As to Interstate's third argument, the court concluded the competing Other Insurance clauses in the Interstate policy and Oiltanking's policy were mutually repugnant under the standard set out by *Hardware Dealers Mut. Fire Ins. Co. v. Farmers Ins. Exch.*, 444 S.W.2d 583 (Tex. 1969), and thus both must be ignored. As a result, the court concluded Interstate and Oiltanking's primary layer must share the loss on a *pro rata* basis, and Oiltanking's excess layer would be triggered when its primary layer is exhausted. Although this outcome implies L-Con may have violated its contractual obligation to obtain primary and non-contributing coverage in favor of Oiltanking, it appears the parties did not raise this issue in the context of these summary judgment motions. The court also held that in

light of Interstate's policy terms which reduced the limits of its additional insured coverage to the minimum required by written contract, Interstate was only required to provide the $3 million of excess coverage required by the MSA and not its full $17 million.

Editor's note: We expect all aspects of this ruling will likely be appealed to the Fifth Circuit.

HOUSTON FEDERAL COURT ORDERS INSURER TO PAY $4 MILLION IN ATTORNEY FEES TO ITS INSURED

In what is surely not the last phase of a highly contentious three-year coverage battle between OneBeacon Insurance Company and its insured, Houston Federal District Court Judge Gray Miller recently awarded $4 million in attorney fees on a $30 million judgment previously rendered against OneBeacon in March of this year. The judgment was the result of a jury trial conducted in October 2014 after which the jury found OneBeacon breached its contract, violated its common-law and statutory duties under *Stowers*, violated the Texas Insurance Code, and committed a knowing violation of the Insurance Code.

In *OneBeacon Ins. Co. v. T. Wade Welch & Associates*, No. CIV.A. H-11-3061, 2015 WL 5021954 (S.D. Tex. Aug. 24, 2015), the Welch law firm, who represented itself through much of the coverage suit but hired outside counsel prior to trial, sought $9.3 million in attorney fees on a 36% contingent fee basis, or alternatively based on the Lodestar method authorized by Texas law, with a multiplier applied due to the complexity of the case. OneBeacon argued Welch should not be allowed to recover a contingent fee for representing itself but the fees should instead be awarded based on the Lodestar method with no enhanced multiplier. It also argued the lodestar amount should be reduced because Welch improperly billed some of its time and because outside counsel duplicated much of Welch's own work.

After a thorough review and consideration of controlling Texas law pertaining to attorney fee awards, including *El Apple I, Ltd. v. Olivas*, 370 S.W.3d 757 (Tex. 2012) and *Arthur Andersen & Co. v. Perry Equip. Corp.*, 945 S.W.2d 812 (Tex. 1997), the Court refused to award fees based on a straight contingency amount but instead applied the Lodestar method. After considering the *Arthur Andersen* factors which determine the reasonableness of a fee, the court applied a multiplier of 3.0 to the fees of outside counsel to account for the risk of taking on a difficult case on a contingent fee basis, but did not apply a similar multiplier to Welch's costs incurred in its own defense. The court also applied several reductions based on OneBeacon's complaints regarding the attorneys' billing methods, most notably applying a global reduction of Welch's fee by 5% because it concluded Welch had unduly inflated certain aspects of its billing.

Editor's Note: Although this ruling does not break any new legal ground on attorney fees, the court's thorough and detailed opinion serves as a good primer for calculating and litigating attorney fee awards under Texas law and is a reminder of the many complexities that can arise in the context of attorney fee awards.

DALLAS FEDERAL COURT REMANDS CASE & FINDS INDEPENDENT ADJUSTER PROPERLY JOINED

Federal District Court Judge Joe Fish of the Northern District of Texas recently held that a homeowner properly stated a claim against an independent adjuster in *Glidwell v. Safeco Ins. Co. of Indiana*, No. 3:15-CV-1099-G, 2015 WL 4868483 (N.D. Tex. Aug. 13, 2015). The case arose out of a claim for hail damage to Glidwell's home in Kaufman County, Texas. After Glidwell made an insurance claim, Safeco assigned independent adjuster Chad Davis to investigate the claim. Unsatisfied with Safeco's claims decision, Glidwell sued both Safeco and Davis in state district court. Safeco removed the case to federal court arguing Glidwell improperly joined Davis to defeat diversity jurisdiction.

On Glidwell's motion to remand, the Court first applied the Texas state pleading standards rather than the stricter federal standards to determine whether Glidwell had sufficiently stated a claim against the adjuster. To defeat remand, a defendant must show that that the plaintiff could not reasonably recover against the improperly joined defendant under state law. Texas law recognizes that individual adjusters could be liable for improper claims handling under the Texas Insurance Code. The Court found that Glidwell had pleaded a potentially valid claim against Davis under the Insurance Code. Specifically, Glidwell alleged that Davis "conduct[ed] a substandard investigation, fail[ed] to include in his report all of the damages noted during his inspection, undervalue[ed] the damages he observed during the inspection, and perform[e]d an outcome-oriented investigation, all of which led to the underpayment of Glidwell's claim and an inequitable evaluation of Glidwell's losses."

Editor's Note: Judge Fish's ruling follows a recent trend among Texas federal district courts that have similarly granted a remand after finding potential liability against one or more adjusters. Although this ruling and others involve variations of the same boilerplate allegations contained in many first-party bad faith homeowner lawsuits, federal courts appear to be increasingly willing to find these allegations sufficient to send cases back to state court.

DALLAS FEDERAL COURT KEEPS CASE & DENIES REMAND BASED ON INADEQUATE PLEADINGS

In *Mainali Corp. v. Covington Specialty Ins. Co.*, 3:15-CV-1087-D, 2015 WL 5098047, at *1 (N.D. Tex. Aug. 31, 2015), Federal District Court Judge Sid Fitzwater of the Northern District of Texas denied an insured plaintiff's Motion to Remand and determined Plaintiff improperly joined the adjuster of Covington Specialty Insurance Company in an attempt to defeat diversity jurisdiction.

The case involved a fire that damaged the insured's property, a Chevron station and convenience store. Plaintiff alleged Covington insured the property and the policy covered fire damage and business interruption losses. The insured alleged the field adjuster failed to conduct a reasonable investigation, improperly denied coverage for damage to the property and business losses, underestimated the damage, improperly reduced the amount payable to the insured under the policy, relied on the field adjuster's inadequate investigation and conclusions regarding the damage, and only paid a portion of the amount due on the claim. Consequently, the insured was unable to reopen the Chevron station/ convenience store and suffered additional damage in lost business income. Plaintiff alleged breach of contract, Texas Insurance Code and DTPA causes against Covington, and Texas Insurance Code and DTPA causes of action against the field adjuster.

Covington removed the case on the basis of diversity citizenship, contending Plaintiff improperly joined the field adjuster. Plaintiff moved to remand shortly thereafter.

Covington argued the field adjuster had been improperly joined because Plaintiff had not alleged a reasonable basis for the court to predict that it could recover against the adjuster. Covington argued every cause of action alleged in the petition lumped together the allegedly wrongful conduct of the adjuster with that of Covington, without distinguishing the adjuster's conduct. It argued the allegations against the adjuster were too conclusory and vague to demonstrate a plausible right to relief.

The Court determined the allegations against the adjuster for violations of Chapter 541 of the Texas Insurance Code were not actionable because the alleged misrepresentations relate only to the adjuster's investigation and the scope of the damage, and they did not relate to the coverage provided under the terms of the policy. Importantly, the Court held the individual adjuster could not be liable under Tex. Ins. Code Ann. §§ 541.060(a) (1), 541.060(a)(2), 541.060(a)(3), and 541.060(a)(7) as a matter of law because an adjuster does not have the ability to affirm or deny coverage of a claim to a policyholder, nor does the adjuster have settlement authority on behalf of an insurer. The Court further reiterated that an individual adjuster cannot be liable under Chapter 542 of the Texas Insurance Code because that chapter applies only to insurers.

The Court further held there was no reasonable basis to predict that Plaintiff could recover against the adjuster for common law fraud. As such, Judge Fitzwater dismissed the adjuster from the lawsuit and denied Plaintiff's motion to remand.