Martin, Disiere, Jefferson & Wisdom

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TEXAS INSURANCE LAW NEWSBRIEF

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FIFTH CIRCUIT CERTIFIES EXTRINSIC EVIDENCE QUESTION TO SUPREME COURT OF TEXAS

Since the Supreme Court of Texas issued its 2006 opinion in *GuideOne Elite Ins. Co. v. Fielder Road Baptist Church*, 197 S.W.3d 305 (Tex. 2006), in which the court coyly hinted that an exception to the eight-corners rule might exist in certain circumstances, but declined to openly endorse its existence, the question of considering extrinsic evidence in duty-to-defend cases has remained in a state of flux and uncertainty. Some courts have applied the exception as though approved by the supreme court, while others have been more cautious, leading to significant inconsistencies. Last week, the Fifth Circuit took definitive steps to end the suspense by certifying a direct question to the supreme court on the issue, and just days later, the supreme court accepted the certified question.

In *State Farm Lloyds v. Richards*, No. 18-10721, 2019 WL 4267354 (5th Cir. Sept. 9, 2019), certified question accepted (Sept. 13, 2019), a child died in an all-terrain vehicle accident while in the care of his grandparents, and the parents sued the grandparents. State Farm sought a declaratory judgment that it had no duty to defend, relying on two pieces of extrinsic evidence to show that (a) the accident occurred away from the insured premises and was thus excluded by the policy's motor vehicle exclusion, and (b) the child qualified as a resident of the grandparents' household and the claim was thus excluded by the policy's insured vs. insured exclusion. The parents had filed a bare-bones petition which made no allegations as to either of these fact issues, so the evidence did not contradict the allegations.

The Fifth Circuit asked,

Is the policy-language exception to the eight-corners rule articulated in *B. Hall Contracting Inc. v. Evanston Ins. Co.*, 447 F. Supp. 2d 634 (N.D. Tex. 2006), a permissible exception [to the eight-corners rule] under Texas law?

The court noted that this particular policy confined the duty to defend to claims or suits "to which this coverage applies," and did not use broader traditional language requiring the insurer to defend even if the claims are "groundless, false, or fraudulent." At least one district court had previously held that under language similar to this policy, the eight-corners rule does not apply at all, and all relevant evidence may be freely considered. That was the *B. Hall* case mentioned in the court's certified question.

Editor's Note: The supreme court was quick to accept the certified question, and we will monitor this case for further developments which we hope will significantly clarify the state of Texas law on the existence of an extrinsic-evidence exception to the eight-corners rule and its limits.

"INSURER PAID TOO MUCH," ALLEGES INSURED; FIFTH CIRCUIT DISAGREES

In two related cases, the Fifth Circuit last week affirmed a summary judgment in favor of a church's property insurer and dismissal of all claims against the adjusting company who handled the church's claim. In *Univ. Baptist Church of Fort Worth v. Lexington Ins. Co.*, No. 18-11415, 2019 WL 4281938 (5th Cir. Sept. 10, 2019) and *Univ. Baptist Church of Fort Worth v. York Risk Services Group, Inc.*, No. 18-10713, 2019 WL 4281934 (5th Cir. Sept. 10, 2019), the church sued its property insurer and the insurer's outside adjusting company, alleging its claim for storm damages was mishandled.

The insurer paid its policy limit of $250,000 for required code compliance work, and the church bore additional non-covered costs of about $600,000. Rather than a more typical allegation that the insurer's estimate was too low and the claim was underpaid, the church alleged that the defendants should have held the repair contractor to his initial, lower bid (which all parties admit they knew was far too low) rather than asking him to correct his bid. The church believed the insurer should have forced the contractor to take a bath to the tune of $575,000, to save the church from having to pay the portion of the claim exceeding its policy limit.

On appeal, the Fifth Circuit affirmed the district court's rulings in favor of the insurer and adjuster, holding it was neither common-law bad faith nor a violation of the Insurance Code or the DTPA to pay the claim based on the contractor's higher, corrected bid, rather than the initial, clearly incorrect bid.

PRIMARY INSURER HELD TO HAVE BREACHED STOWERS DUTY TO EXCESS CARRIER IN CYCLIST DEATH CASE

Last week, a bench trial of a Stowers case between a primary and excess insurer resulted in a ruling requiring the primary carrier to pay the excess carrier the difference between the primary carrier's limit and the much larger post-judgment settlement the excess carrier was required to pay.

Am. Guar. & Liability Ins. Co. v. Ace Am. Ins. Co., No. 4:18-CV-382, 2019 WL 4316531, (S.D. Tex. Sept. 11, 2019) (slip op.) involved an underlying suit in which a cyclist was killed in Cypress, Texas when he collided with the back of a stopped truck. The defendant, a landscaping company, had liability policies with three different carriers - $2 million primary, $10 million excess, and $40 million high excess. The underlying suit went through two unsuccessful mediations, and on three different occasions – before trial, during trial, and during jury deliberations – the plaintiffs made Stowers demands to fully settle the case for the primary carrier's $2 million limit. The primary carrier rejected all three demands, and the jury returned a verdict of nearly $40 million, resulting in a judgment of approximately $27 million. This Stowers suit between the primary and excess carriers followed.

After a bench trial, the district court held the primary carrier was unreasonable in refusing Stowers demands for its $2 million limit, and owed the excess carrier the difference between the $2 million primary limit and the $9 million post-judgment settlement negotiated by the first excess carrier. The court held the primary carrier's initial evaluation, which was significantly below defense counsel's evaluation and apparently consisted of multiplying its policy limit by defense counsel's projected risk of a plaintiff verdict, was unreasonable on its face. The Stowers duty requires the carrier to consider the insured's total risk of exposure and not merely its own policy limit. Nevertheless, the primary carrier's rejection of the pre-trial Stowers demand was reasonable at that time in light of numerous factors favoring the defense. But several unfavorable rulings during trial should have alerted the primary carrier to the increased risk of excess exposure to its insured, and its rejection of the second and third Stowers demands was unreasonable, particularly in light of defense counsel's prior settlement evaluation of up to $2 million.

HOUSTON COURT OF APPEALS REJECTS EFFORTS TO "GAME" THE APPRAISAL PROCESS, UPHOLDS ATTORNEY SANCTIONS

Last week, a Houston court of appeals upheld sanctions against a policyholder attorney after an appraisal process went off the rails. In *Etienne v. State Farm Lloyds*, No. 14-18-00665-CV, 2019 WL 4266104 (Tex. App.—Houston [14th Dist.] Sept. 10, 2019, no pet. h.) (slip op.), the policyholder invoked appraisal of a claim under her homeowners policy. After State Farm agreed to the appraisal and both sides appointed their appraisers, Etienne filed suit against State Farm, accusing State Farm of refusing to participate in the appraisal. State Farm answered the lawsuit, filed a motion to appoint an umpire, and set a hearing on the motion.

Twelve hours before the hearing, Etienne non-suited her case, and her counsel did not appear for the hearing. (Meanwhile, outside the context of the original lawsuit and unbeknownst to State Farm, Etienne filed a separate application for appointment of an umpire.) At the hearing, which was already on the court's docket, the court appointed an umpire. The next day, the court signed the nonsuit and dismissed the lawsuit.

Etienne sought to vacate the court's order appointing the umpire, arguing the court lost jurisdiction the moment she filed her nonsuit and could not appoint an umpire. In response, State Farm sought and won sanctions against Etienne's counsel for signing and filing a pleading which falsely alleged State Farm had refused to participate in appraisal, in violation of Texas Rule of Civil Procedure 13. Etienne appealed both the umpire appointment and the sanctions order.

On appeal, the court pointed out that as a procedural matter, a nonsuit does not immediately deprive the court of jurisdiction if another party has sought affirmative relief. Additionally, the court retained plenary power for 30 days after its own dismissal order, and had the power to hear and rule on State Farm's motion to appoint an umpire the morning after Etienne filed her nonsuit. The court summarily rejected Etienne's appeal of the sanctions order because she had not been personally sanctioned – only her attorney, Eric Dick, had.