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CAR BUYER HAD "INSURABLE INTEREST" IN VEHICLE SHE NEVER TOOK POSSESSION OF—FIFTH CIRCUIT UPHOLDS COVERAGE DENIAL BASED ON "STEP DOWN" PROVISION OF AUTO LIABILITY POLICY

Recently, the Fifth Circuit Court of Appeals upheld a declaratory judgment in the district court that Sentry Select Insurance Company ("Sentry") did not owe a duty to defend or indemnify a claimant who Sentry argued was not an "insured" under its policy and, in any event, was already covered under an automobile liability policy pursuant to the "step down" provision of the policy. *Sentry Select Ins. Co. v. Home State Cty Mut. Ins. Co. v. Ortiz*, No 21-40371, 2022 WL 2800809 (5th Cir. July 18, 2022) arose out of a coverage dispute between Sentry and Home State County Mutual Insurance Company ("Home State").

Zusuky Ortiz ("Ortiz") entered a contract to buy a Kia from Knapp Honda ("Knapp"). Amongst other things, the contract required Ortiz to provide proof of insurance coverage for the Kia, assume any responsibly for damage to the vehicle resulting from the use, maintenance or operation of the vehicle, and to hold Knapp free from any loss, claim, or liability resulting from any damage to the vehicle or form the vehicle's use, maintenance or operation"; however, the Kia was undergoing repairs, so Knapp, which was insured by Sentry, lent Ortiz a Hyundai to drive until the Kia was ready. Ortiz paid her initial premium for the policy issued by Home State covering the Kia, and the same day, returned to Knapp and provided proof of insurance. She then left the dealership in the loaner Hyundai.

Ortiz's policy obligated Home stay to pay damages for bodily injury or property damage for which any covered person became legally responsible due to an auto accident, and a "covered person" included Ortiz and "any person using [Ortiz's] covered auto." A "covered auto" included the Kia and "any auto [Ortiz did] not own while used as a *temporary substitute* for the [Kia] which is out of normal use because of its repair, servicing, breakdown, loss, or destruction."

The next day, Ortiz's brother, Juan Antonio Ortiz Ramirez ("Ramirez"), was involved in a one car auto accident in the Hyundai, with Ortiz and their other brother as passengers. Ortiz and her other brother subsequently sued Knapp and Ramirez in state district court for personal injuries. Sentry, Knapp's insurer, provided Ramirez a defense under a reservation of rights. The primary auto liability section of the Sentry policy included a "step down" provision that limited Sentry's coverage to "the amount needed to comply with [Texas's] minimum limits after . . . other insurance is exhausted." So Sentry then filed suit in federal district court seeking a declaratory judgment that it had no duty to defend or indemnify Ramirez in the underlying state lawsuit, alleging that Ramirez was not an "insured" under the policy and that, even if he was, the policy's "step down" provision precluded coverage because Ramirez was already insured by Ortiz's Home State policy up to the minimum limits required by Texas law. Ramirez filed a counterclaim against Sentry seeking the opposite.

In its motion for summary judgment, Sentry asserted that Ramirez was covered under the Home State policy because the Hyundai was a "temporary substitute" for Ortiz's Kia and the Kia was out of normal use due to breakdown, repair, servicing, etc. In response, the other parties argued that Ortiz failed to obtain an "insurable interest" in the Kia because she never took possession of it and did not complete the purchase process, so the Hyundai could not have served as a "temporary substitute."

The district court found Ortiz's assumption of liability for the Kia's "use, maintenance or operation" of the Kia sufficient to establish an "insurable interest" in it, which kept Ramirez's use of the Hyundai within coverage. As such, the trial court held that Ramirez was covered under the Home State policy, and the "step down" provision of the Sentry policy relieved Sentry of any duty to defend or indemnify Ramirez in the state court action.

The only issue the Ramirez brought up on appeal was the trial court's finding that Ortiz obtained an "insurable interest" in the Kia. In upholding the district court's decision, the Fifth Circuit emphasized that, unless the policy specifically provides otherwise, actual ownership is not necessary to establish an insurable interest in the subject vehicle under Texas law. Instead, the only interest necessary is that the insured may incur liability because of the operation, maintenance, or use of the automobile, which Ortiz had in this case based on the sales contract with Knapp. In turn, the Fifth Circuit held the Hyundai was a "covered auto," Ramirez was a "covered person," and the "step down" provision of Sentry's policy precluded coverage as between Sentry and Ramirez—thereby affirming the district court.

AUSTIN FEDERAL COURT CONSIDERS EXTRINSIC EVIDENCE - GRANTS SUMMARY JUDGMENT IN COVERAGE DISPUTE ARISING FROM COLLAPSED CONDOMINIUM BALCONY

A federal district court in Austin recently granted a summary judgment filed by Western World Insurance Company ("Western") and dismissed the declaratory judgment action filed by Plaintiff, Xavier Benites ("Benites"). *Benites v. Western World Ins. Co.*, 1:21-CV-1093-RP, 2022 WL 2820669 (W.D. Tex.—Austin July 18, 2022).

Benites owned a condominium unit in the BeachGate Condominiums ("BeachGate Condos") that he rented out to visitors, and BeachGate Owners Association, Inc. ("BOA") was the homeowners association for BeachGate Condos. A group of people rented a condo unit at BeachGate Condos and were assigned Benites' unit. On one evening, the group was congregating on the upstairs outdoor balcony attached to the unit when it collapsed, injuring those on it. The group then sued BOA and Benites in state district court for personal injuries. Western provided a defense to BOA in the state court action under a reservation of rights. Benites sought a defense from Western as an "additional insured," arguing that the balcony attached to his unit was a "General Common Element" of the property for which BOA was responsible. Western contended that the balcony was reserved for Benites' "exclusive use or occupancy," which precluded Benites from being considered an "additional insured" under its policy. As such, Western denied Benites' claim.

Benites then filed a third-party claim against Western in the state court action, and Western successfully severed and removed the third-party claim to federal court based on diversity jurisdiction. Once in federal court, both Benites and Western filed motions for summary judgment on the coverage issue, which rested on whether Benites was an "additional insured" under Western's policy.

Although the district court noted that the "eight-corners" rule applied to determine whether an insurer owed a duty to defend an insured, and that the duty to indemnify is only determined when a plaintiff ultimately prevails on claims covered by the policy, the court concluded that the allegations in the state court petition did not conclusively show whether coverage existed in this case. As such, and under the facts alleged in the state court action, the court could consider extrinsic evidence, such as the BeachGate Condo Declarations and Bylaws. Because the Declarations and Bylaws did not state that the balconies of individual condo units are included as "General Common Elements" and the Uniform Condominium Act and case law considered balconies to be "limited common elements allocated exclusively to [the] unit" and not "general common elements," the district court concluded Benites' private balcony was reserved for his "exclusive use or occupancy," and he was therefore not an "additional insured" under the Western policy and not entitled to coverage.