THOUGHT LEADERSHIP

News

TEXAS SUPREME COURT CONSTRUES COMMERCIAL SCHEDULED-VALUE POLICY IN FAVOR OF INSURED

Newsbrief
15 OCT 2015

The Supreme Court of Texas recently denied rehearing on an important opinion construing a large commercial policy insuring multiple apartment complexes in favor of the insured and imposing a $4 million judgment on the carrier in connection with losses incurred to numerous apartment complexes during Hurricane Rita in 2005. We previously reported on *RSUI Indem. Co. v. The Lynd Co.*, 466 S.W.3d 113 (Tex. 2015) on April 2, 2012 and January 17, 2013 as it made its way through the appellate courts. The Supreme Court of Texas has now denied rehearing on its opinion originally issued on May 8, 2015, finalizing its holding in favor of the insured.

The policy involved was part of a tower of insurance covering over 100 apartment complexes in several states. RSUI provided excess coverage from $20 million to $480 million. Fifteen of the insured's apartment complexes were damaged in Hurricane Rita, and the parties agreed the total adjusted amount of loss for all fifteen properties was approximately $24.5 million. The primary carrier paid its $20 million policy limit, and Lynd demanded the remaining $4.5 million from RSUI.

The RSUI policy included a "Scheduled Limit of Liability" endorsement which allowed RSUI to select the "least" from among three valuation alternatives:

> 1. In the event of loss hereunder, liability of the Company shall be limited to the least of the following in any one "occurrence":
>
> > a. The actual adjusted amount of the loss, less applicable deductibles and primary and underlying excess limits;
> >
> > b. 115% of the individually stated value for each scheduled item of property insured at the location which had the loss as shown on the latest Statement of Values on file with this Company, less applicable deductibles and primary and underlying excess limits. If no value is shown for a scheduled item then there is no coverage for that item; or
> >
> > c. The Limit of Liability as shown on the Declarations page of this policy or as endorsed to this policy.

TEXAS SUPREME COURT CONSTRUES COMMERCIAL SCHEDULED-VALUE POLICY IN FAVOR OF INSURED

The crux of the dispute between the parties was whether RSUI was entitled to choose the least of the three options for each damaged location, or whether it was required to choose one of the three methods and apply that method to all locations affected by a single occurrence. At thirteen of the damaged properties, the actual adjusted loss was the lowest of the three values. But the remaining two properties had incurred actual adjusted losses several million dollars in excess of the stated value reported by the insured.

In a detailed opinion, the Supreme Court carefully examined the policy and struggled to resolve apparently circular and interlocking definitions of "loss" and "occurrence."

> **LOSS:** "a *loss* or series of *losses* arising out of one *event* or *occurrence*."
> **OCCURRENCE:** "any one *loss* ... or series of *losses* ... arising from one *event*."
> **EVENT:** "all *losses*" in a 72–hour period.

The court ultimately concluded that because both "loss" and "occurrence" could refer to either "a loss" or a "series of losses," both parties' urged constructions were reasonable, and thus the policy was, by definition, ambiguous. Applying the time-honored "*contra proferentum*" rule of contract and policy construction, under which all ambiguities are construed against the drafter, the court declared Lynd's approach the winner, requiring RSUI to pay the remaining $4 million, rather than the $750,000 it had paid after applying the endorsement on a location-by-location basis.

In a stinging Scalia-esque dissent authored by Chief Justice Hecht, three justices characterized the majority's painstaking grammatical parsing approach as "excruciatingly detailed," "absorb[ed] with minutiae," "twisted," "strange," "unrealistic," "baffling," "nonsensical," "untroubled by realities and consequences," "glaringl[ly] peculiar," "textual flyspecking," and, ultimately, "simply wrong." The dissent accused the majority of creating windfalls to insureds by converting 2 + 2 into 5 anytime more than one insured location sustains a loss.

Arguably, the dissent makes a quite cogent point regarding fortuitous recoveries by insureds. The majority's ruling, which forces the insurer to apply a single method of loss calculation across multiple insured locations, allows Lynd, and potentially other insureds, to receive a windfall: it will either recover the full scheduled value on some locations when the actual loss was less than that amount, or it will recover payments for actual losses which it never scheduled and for which it paid no premium.

The dissent is difficult to ignore, given the fact that most insurers who issue policies with this endorsement probably thought they knew precisely what it meant, until the Supreme Court declared it ambiguous. The majority suggested this be solved by insurers at an underwriting level, but given the majority's "textual flyspecking" approach, in which it pulled sources of ambiguity from multiple parts of the policy, it may be difficult to create a simple fix. We recommend any commercial insurer who issues scheduled-value policies containing this endorsement examine the opinion carefully and consider its options. One possibility may be a separate co-insurance provision for any individual location at which the actual loss exceeds the stated value by more than 15%. The majority opinion hints at another solution, by noting that RSUI and the amici supporting it threatened that such a ruling may cause commercial insurers to simply stop writing scheduled-value policies for multiple locations in Texas, instead requiring insureds to obtain an individual policy for each location, which would cause those insureds to lose the ability to obtain insurance at the discounts that scheduled-value policies offer.