

THOUGHT LEADERSHIP

News

## FEDERAL COURT APPLIES CGL “BREACH OF CONTRACT EXCLUSION” FINDS NO DUTY TO DEFEND OR INDEMNIFY

Newsbrief

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Last Tuesday, a federal district court in Houston interpreted a “Breach of Contract Exclusion” added by endorsement to a CGL policy and found that the insurer had no duty to defend or indemnify the insured in a lawsuit brought against them by a general contractor. In *Mt. Hawley Insurance Company v. Huser Construction Company, Inc.*, 2019 WL 1255756 (S.D. Tex. March 19, 2019), the insured was sued by the general contractor alleging breach of contract and negligence after finding multiple deficiencies in workmanship and materials used in the project, primarily concerning work performed by the insured’s HVAC subcontractor. The insurer denied coverage and filed this declaratory judgment action asserting it had no duty to defend or indemnify the insured in the underlying action.

Both parties filed motions for summary judgment and the court applied Texas law noting the limited exception for determining both the duty to defend and indemnify when “the same reasons that negate the duty to defend likewise negate any possibility [that] the insurer will ever have a duty to indemnify.” *Farmers Texas County Mutual Insurance Company v. Griffin*, 955 S.W.3d 81, 84 (Tex. 1997). The insurer asserted that the Breach of Contract Exclusion added by endorsement precluded any coverage for any claim or “suit” for “property damage” “arising directly or indirectly out of” breaches of contract or warranty. And the court noted Texas law gives “arising out of” exclusions, a much broader interpretation than more restrictive “caused by” exclusions. Applying the Breach of Contract Exclusion to the facts and allegations asserted in the underlying action, the court found that the “property damage” at issue, clearly arose “directly or indirectly” from the insured’s breach of contract with the general contractor.

The insured argued that a subcontractor exception to the “Your Work” exclusion served to bring the claims back within coverage. But the court noted that insurers were not prohibited adding an additional exclusion to eliminate coverage arising out of breach of contract. And the court rejected arguments that the Breach of Contract Exclusion rendered all coverage illusory, stating that “the exclusion requires a breach of contract, not merely the existence of a contract.” Further, the court stated that “[j]ust because the “Your Work” Exclusion preserves coverage for damage caused by subcontractors does not mean that other policy exclusions must do the same.” The court noted that it is well-settled that when found in conflict with other policy language an endorsement controls and the intent of the Breach of Contract Exclusion is clear: “to limit the coverage afforded” by the policy. Accordingly, the court found that the insurer had no duty to defend the lawsuit, and applying the same facts, also found the insurer had no duty to indemnify. Lastly, the court dismissed the insured’s extra-contractual claims against the insurer as having no

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independent basis or damages apart from the contractual claims under the policy.