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SUPREME COURT OF TEXAS NARROWLY INTERPRETS UMBRELLA POLICY "NOT FOR BROADER COVERAGE" CLAUSE

The Supreme Court of Texas closed out the work week of April 14, 2023, by siding with Exxon to require an umbrella insurance provider to reimburse Exxon for payments made to a burn victim. In *Exxonmobile Corporation v. National Fire Union Insurance Company of Pittsburgh*, 2023 WL 2939596, Exxon hired Savage Refinery Services to work at its refinery in Baytown, Texas. Exxon and Savage had a Services Agreement in which Savage agreed to obtain general liability insurance and to name Exxon as an additional insured. Savage obtained primary and umbrella insurance policies from National Fire, among other policies. The primary policy covered any person or organization that Savage was contractually obligated to provide insurance—as the Services Agreement did. The umbrella policy covered any additional insured under the primary policy, but "not for broader coverage" than the primary policy.

Two Savage employees were involved in an accident at the refinery and were severely burned. They settled with Exxon for over twenty-four million dollars. National Fire (and another insurer, Starr) denied umbrella policy coverage. National Fire argued that the "not for broader coverage" clause of the umbrella policy meant that Exxon was limited to the Service Agreement's payout limits. The trial court sided with Exxon; the First district Court of Appeals in Houston sided with National Fire; and in the final say, the Texas Supreme court sided with Exxon.

The Court began by noting that insurance contracts may incorporate extrinsic documents in limited circumstances: only if the policy explicitly requires viewing extrinsic documents, and only to the extent absolutely necessary and no further. In this case, the Court said that the umbrella policy explicitly incorporated the Services Agreement, but only for the purpose of determining who was an insured. While the umbrella policy excluded "broader coverage" than what was in the primary policy, the Court interpreted "broader coverage" not to refer to limits and instead to losses that the primary policy would not reach. The Court reversed in Exxon's favor and remanded the case.

FEDERAL COURT DISMISSES HAIL CLAIMS AS TIME-BARRED

Last Monday, the United States District Court for the Western District dismissed an insured's claims for property damage as time-barred. In *Sutton Place 1 Townhomes v. AmGuard Insurance Company*, Sutton Place claimed it suffered hail damage in 2019 and that AmGuard breached the insurance policy, among other things, in its January 29, 2020, claim decision. Plaintiff timely filed suit on November 2, 2021, but did not serve AmGuard for another six months – three months after the statute of limitations expired. AmGuard removed to federal court and asserted that the lawsuit was time-barred in a motion to dismiss under Rule 12(b)(6), arguing that Plaintiff did not meet Texas' due diligence requirement in bringing suit. The district court analyzed the applicable policy language setting forth the contractual limitations period, holding that the two-year contractual period applied to the claims at issue.

Sitting in diversity, the district court then analyzed Texas' due diligence requirement, noting that Texas courts perform a burden-shifting analysis in which the Plaintiff may explain its delay to show due diligence. Here, the Plaintiff did not offer any explanation. The district court then analyzed whether AmGuard's motion was appropriate as a 12(b)(6) motion or whether it should be converted to a summary judgment motion, finding that it was not required to convert to a 12(b)(6) motion. Additionally, the district court considered whether AmGuard's 12(b)(6) motion should be considered as a 12(b)(4) or (5) motion, adopting the majority position that the defense is one that should be considered under 12(b)(6). Finally, the Court considered whether Plaintiff's presuit notice letter under 542A excused its failure to timely file and serve its petition on AmGuard, holding that it did not.

Editor's Note: Martin, Disiere, Jefferson & Wisdom, LLP had the privilege of representing AmGuard in this matter.

NO BUSINESS INTERRUPTION PROCEEDS FOR THIS BANKRUPTCY

Also this past week, in *In re: New York Inn Inc. v. Associated Industries Insurance*, 2023 WL 2938371, the United States Bankruptcy Court for the Northern District of Texas evaluated whether an additional insured to a general liability policy had standing to file a lawsuit for a denial of a business interruption claim. The Court determined it did not.

Here, Viva Inn owned a hotel property in Arlington, Texas. The hotel property was also listed as the principal place of business for New York Inn. Viva Inn obtained property, business interruption, and commercial liability insurance from Associate Industries Insurance. Then, Viva Inn's principal requested through an insurance agent that Associate Industries add New York Inn as an additional insured on the policy. In response, Associated Industries added New York Inn as an additional insured on the general commercial policy only. In the February 2021 ice storm, the hotel suffered catastrophic water damage that required it to shut down

entirely. New York Inn declared bankruptcy and pursued a business interruption claim from Associate Industries that it denied. New York Inn filed suit for the business interruption proceeds, and Associate Industries sought a dismissal, arguing that New York Inn was not an additional insured for the business interruption policy.

In evaluating and ultimately granting the dismissal request, the Court pointed out that separate insurance coverages are each distinct contracts. So, when evaluating the business interruption contract within its four corners, there was no indication that it listed New York Inn as an additional insured. Further, in considering whether New York Inn was a third-party beneficiary, that could only be implied and enforced if both contracting parties intended to add New York Inn as third-party beneficiary, and there was no documented intent that Associate Industries meant to do so. For similar reasons, the Court found a lack of standing in New York Inn's Deceptive Trade Practices (not the "consumer" that purchased insurance), Reformation of the contract (not the immediate party to the contract), Breach of Good Faith and Fair Dealing (no legal relationship to the insurer), and declaratory judgment actions (no standing). Associate Industries therefore was not required to add business interruption proceeds to New York Inn's bankruptcy estate.

CORPUS CHRISTI COURT REVERSES SUMMARY JUDGMENT FOR INSURER - DELIVERY OF ENDORSEMENT TO RETAIL AGENT MAY NOT BE EFFECTIVE

The Corpus Christi appellate court recently examined the effect of a policy endorsement that was not delivered to the insured before the loss and addressed the question of which party an insurance intermediary actually represents. In *Wendlandt v. Certain Underwriters At Lloyd's, London*, No. 13-21-00323-CV, 2023 WL 2711104, (Tex. App.—Corpus Christi–Edinburg Mar. 30, 2023, no pet. h.) (slip op.) a property policy included a Named Storm exclusion endorsement, but the endorsement was mistakenly not added to the policy at the time of initial delivery to the insured. It was added to the policy, and the change endorsement was delivered to the broker, who in turn delivered it to the retail insurance agent who sold the policy to the insured. It was undisputed that the retail agent never provided it to the insured or informed the insured of it.

The property was damaged in Hurricane Harvey, and the insurer denied the claim, relying on the Named Storm exclusion, resulting in this suit. The crucial point of law at issue both in the trial court and on appeal was that an endorsement added to the policy after its initial issuance only becomes effective upon *delivery* to the insured. Thus, the key question here was whether the endorsement had been properly delivered.

The insurer argued that by delivering the change endorsement to the retail agent, who was the legal representative of the insured, it had achieved delivery of the endorsement to the insured so that it became enforceable. The trial court agreed and granted summary judgment for the insurer, but the court of appeals, applying the summary judgment standard which requires all evidence to be construed in the light most favorable to the non-movant, was not convinced. The insurer's summary judgment win was reversed, requiring the insurer to continue litigating a change endorsement which might not be effective even though the final delivery from retail agent to policyholder was out of its hands.

Editor's Note: Although the opinion does not discuss it, it is likely this policy was a surplus lines policy, which requires two layers of insurance intermediaries to be involved in its sale – a retail agent who typically represents the insured, and a specially licensed surplus lines broker who typically represents the insurer. Under that general rule, one would expect delivery of an endorsement to the retail agent to be sufficient to enforce it. While there is case law in Texas setting out this legal agency relationship, there may be some circumstances in which specific acts can change the relationships. It is not clear whether one of those acts occurred here.

PAYMENT OF APPRAISAL AWARD AND INTEREST RESULTS IN SUMMARY JUDGMENT

In the latest salvo in the Texas appraisal wars, a federal judge in Sherman held that an insurer who pays an appraisal award of a weather claim and all interest which may be due under Texas Insurance Code Chapter 542A (a/k/a the Texas Prompt Payment of Claims Act) defeats any remaining claim for 542A interest and attorney fees as a matter of law.

Morakabian v. Allstate Vehicle And Property Ins. Co., No. 4:21-CV-100-SDJ, 2023 WL 2712481 (E.D. Tex. Mar. 30, 2023) (slip op.) involved a property claim for storm damage. After the parties disagreed on the value of the claim, the policyholder filed suit, and also demanded appraisal. When appraisal was complete, the insurer promptly paid the resulting award and an added amount of $4,699 which was intended to cover all Chapter 542A interest that could potentially be due. The payment did not include any amount of attorney fees.

The insurer moved for summary judgment on all claims, and the policyholder agreed to nonsuit all claims except the Chapter 542A claim. The policyholder did not argue that the $4,699 was insufficient to cover the statutory interest due, but instead argued more generally that the insurer could not nullify his right to litigate the 542A claim and recover attorney fees by pre-emptively paying the interest due.

The court carefully parsed the wording of Chapter 542A, examined several other recent opinions on the matter, and openly disagreed with the 2020 opinion out of Houston, *Martinez v. Allstate Vehicle & Property Insurance Co.*, No. 4:19-CV-2975, 2020 WL 6887753 (S.D. Tex. Nov. 20, 2020). The court reasoned that because the claim had been entirely satisfied by payment of the appraisal award, the amount of the remaining claim was $0 and therefore could not support an award of attorney fees. The court relied on *Ortiz v. State Farm Lloyds*, 589 S.W.3d 127, 134 (Tex. 2019) for this conclusion.

Editor's Note: Texas Insurance Code Chapter 542A is an extension of Chapter 542 that specifically applies to weather claims. Because Chapter 542 and 542A provide for awards of attorney fees as well as statutory interest on claims not paid in compliance with their terms, they have become ground zero for an ongoing legal battle over the potentially large attorney fee claims being asserted by policyholder attorneys in conjunction with appraisals. An increasing number of court opinions have weighed in on this issue, and a split is developing both between the interpretation of 542 and 542A, which contain slightly different provisions, and between courts. We will continue to watch this developing issue.

FEDERAL COURT UPHOLDS JUDGMENT AGAINST INSURER AFTER ISSUING DEATH PENALTY SANCTIONS AGAINST INSURER'S ATTORNEY

Recently, a federal court in McAllen denied an insurer's motion to vacate the court's prior issuance of death penalty sanctions for conduct by the insurer's attorney during litigation. *Sylvia Perez v. Meridian Security Ins. Co.*, Civil Action No. 7:21-cv-00487, 2023 WL 2433978 (W.D. Tex.—McAllen March 9, 2023). Upon doing so, the court held that the insurer's attorney's conduct during litigation was attributable to the insurer.

During litigation, the insurer's attorney did not properly respond to the Plaintiff's discovery requests, file responsive pleadings, or comply with the court's orders. As a result, the court struck the insurer's answer and set a hearing to assess damages. At that hearing, the court issued a final judgment against the insurer, and the insurer filed a motion asking the court to vacate its judgment and reinstate its answer.

The insurer stated it had been in contact with its attorney during pre-suit investigations, settlement negotiations, and a pre-suit mediation, and after the Plaintiff filed suit, it communicated with its attorney about handling the litigation moving forward. The insurer was not aware of the discovery dispute that its attorney experienced with Plaintiff, and when the insurer's representative requested an update from the attorney, the attorney pushed the phone call out for a few months. During this phone call, the attorney did not mention that the court had granted the Plaintiff's motion to compel discovery and motion for sanctions striking the insurer's answer. In a subsequent correspondence, the insurer's attorney requested authorization from the insurer to travel for a hearing, but he did not inform the insurer what the hearing was about, and the insurer's representative did not ask about the reason for the hearing. The hearing was to assess damages against the insurer, now that the court had struck its answer. It was not until after the final judgment against the insurer was issued that it found out about it.

In striking the insurer's answer, the court stated that, in civil cases, clients are bound by the conduct of their attorneys, and it maintained that its holding was not erroneous or just, especially where the party is familiar with litigation, the discovery process, and the need to ensure effective representation of its own interests, such as with an insurance company.

The insurer argued that its attorney's conduct constituted gross negligence, which several federal appellate courts have held may be an extraordinary circumstance warranting relief from a default judgment against a party. The court disagreed, stating that the insurer was also negligent due to its failure to manage the litigation process through its attorney properly. As the court emphasized, "when a litigation adjuster allows outside counsel to ignore him for months at a time, he does so at his own risk." Because the Court did not find that it made a clear error or manifest injustice in striking the insurer's answer, it denied the insurer's motion to vacate the judgment and reinstate the insurer's answer.

U.S. DISTRICT COURT GRANTS SUMMARY JUDGMENT BASED ON POLICY'S COSMETIC-DAMAGE EXCLUSION

On March 13, 2023, the United States District Court for the Northern District of Texas granted summary judgment in favor of Allstate based on the policy's cosmetic-damage exclusion. In *Amphay v. Allstate Vehicle and Property Ins. Co.*, No 2:21-CV-219-Z-BR, 2023 WL 2491285 (N.D. Texas—Amarillo, March 13, 2023, mem. op.), Amphay made a claim for damage to his metal roof sustained in a hailstorm. Allstate denied Amphay's claim on the ground that the damage to the metal roof was cosmetic damage and not covered by Amphay's homeowner's policy, which excluded coverage for "cosmetic damage caused by hail to the surface of a metal roof, including but not limited to, indentations, dents, distortions, scratches, or makes, that change the appearance of the surface of a metal roof." The exclusion did not apply to "sudden and accidental direct physical damage to the surface of a metal roof caused by hail that results in water leaking through the surface of a metal roof." Amphay filed suit and Allstate sought summary judgment, which the court granted.

The U.S. District Court began its analysis by noting that the plain grammatical meaning of the cosmetic exclusion was that cosmetic damage to Amphay's roof caused by hail was not covered unless it resulted in water leaking through the surface. Both of Allstate's experts confirmed that the damage to the metal roof was cosmetic and did not allow water to enter through the roof. The court, relying on *Tri Invs., Inc. v. United Fire & Cas. Co.*, No. 5:18-CV-116, 2019 WL 13114345, at *7 (S.D. Tex. Nov. 15, 2019) (excluding expert testimony as unreliable and unhelpful to a trier of fact because the expert provided no timeline or rate for the corrosion and whether it would ultimately result in failure of the roof at any particular indentation), concluded that Amphay's expert's contention that the roof could leak sometime in the future was speculation and insufficient to create a fact issue.

The U.S. District Court also dismissed Amphay's bad-faith claim, which was based on the contention that the adjuster never went into the primary bedroom to view the damage. However, the inspection occurred in October 2020, the first year of COVID, and Amphay was sick and secluded in the master bedroom. The adjuster advised Amphay's spouse that he could not inspect the master bedroom because of Amphay's condition. The court concluded that it could not attribute the adjuster's caution as bad faith on the part of Allstate. Further, the initial assessments were confirmed by the experts. Thus, there was no evidence of any "unfair or deceptive acts" committed by Allstate.

U.S. DISTRICT COURT GRANTS MOTION TO COMPEL APPRAISAL DESPITE INSURER'S POSITION THAT THE DAMAGE WAS NOT A COVERED LOSS

On March 16, 2023, the United States District Court for the Southern District of Texas granted the insured's motion to compel appraisal notwithstanding the insurer's position that the damage was not a covered loss. In *Chen v. Amguard Ins. Co.*, No 4:22-CV-3673, 2023 WL 2541704 (S.D. Texas—Houston, March 16, 2023, mem. op.), Chen made a claim for roof damage under his insurance policy with AmGuard. After an investigation, AmGuard denied the claim, asserting that the damage was excluded under the policy because it resulted from wear, tear, and deterioration. Consequently, Chen's counsel sent a letter to AmGuard demanding appraisal, which AmGuard rejected on the ground that the issue was a coverage issue and not a price/scope issue. The operative provision in the policy provided: "If you and we fail to agree on the amount of loss, either may demand appraisal of the loss." Chen subsequently sued AmGuard asserting contractual and extra-contractual claims.

The U.S. District Court began its analysis by noting that the language of the appraisal clause made the parties' disagreement "on the amount of loss" a condition precedent that required Chen to show that the parties failed to agree on the amount of loss before appraisal was warranted. The Court concluded that "AmGuard's attempt to avoid appraisal by focusing on the cause of the asserted loss [did] not comport with the Texas Supreme Court's decision" in *State Farm Lloyds v. Johnson*, 290 S.W.3d 886, 893 (Tex. 2009), wherein the Supreme Court concluded that the appraisal process "necessarily includes some causation element, because setting the 'amount of loss' requires appraisers to decide between damages for which coverage is claimed from damages caused by everything else." "This is true when—as here—the causation question involves separating loss due to a covered event from a property's pre-existing condition. And even when an insurer denies coverage, appraisers can still set the amount of loss in case the insurer turns out to be wrong. Moreover, nothing indicate[d] that coverage [was] so unlikely here that appraisal will never be needed. AmGuard therefore cannot avoid appraisal at this point merely because there might be a causation question that exceeds the scope of appraisal. Appraisal is warranted to determine the amount of loss, even if the ultimate causation and coverage determinations are reserved to the Court post-appraisal."

In sum, the Court concluded that the parties "[had], in fact, disagreed about the 'amount of loss,' notwithstanding AmGuard's position that the damage to Chen's property stem[med] from a non-covered cause." Thus, "because the condition precedent to invoking appraisal had been satisfied, the Court grant[ed] Chen's motion to compel appraisal."