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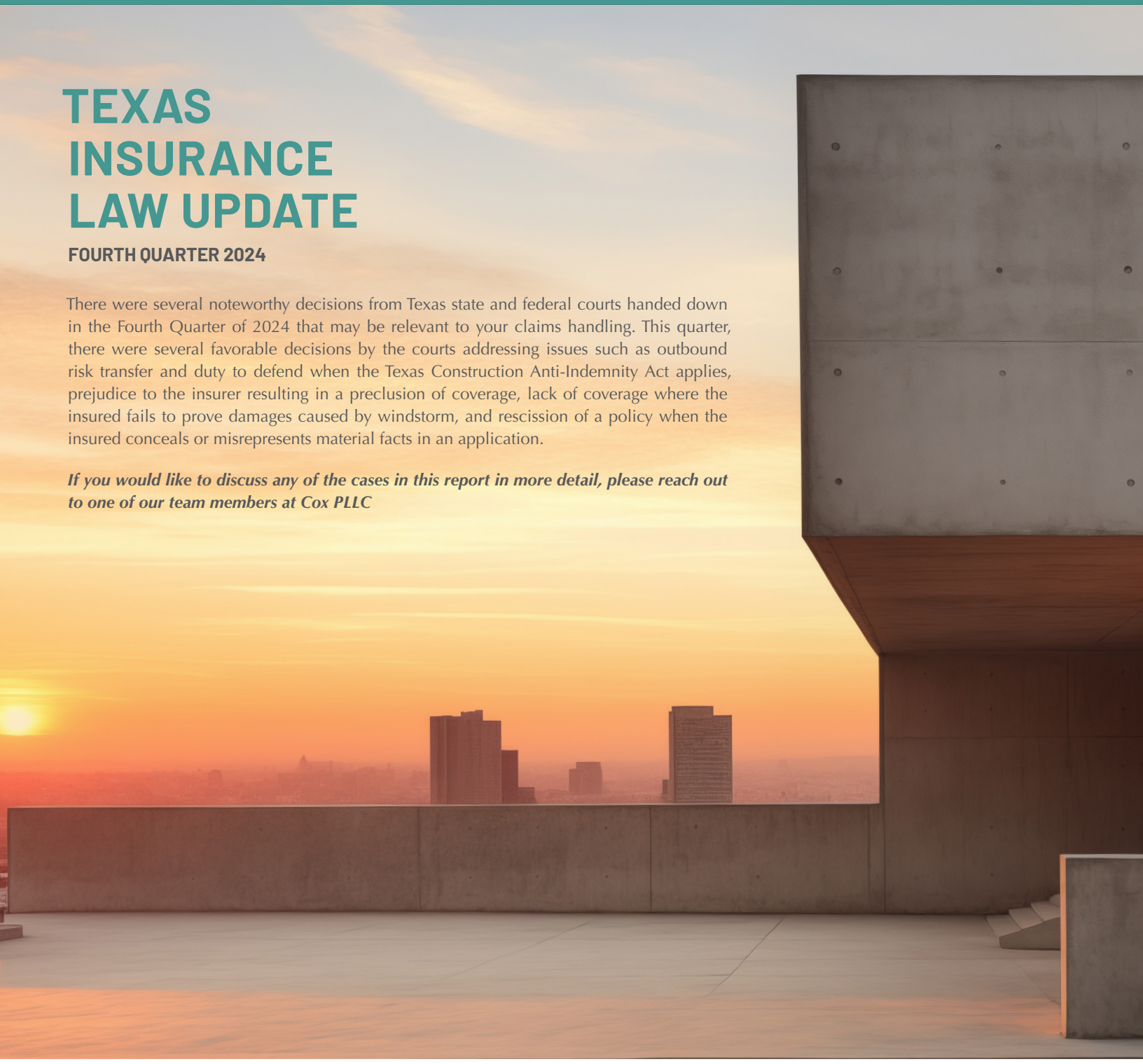
OUR INSURANCE COVERAGE TEAM UPDATES OUR CLIENTS ABOUT TEXAS INSURANCE LAWS AND NOTEWORTHY DECISIONS FROM TEXAS STATE AND FEDERAL COURTS.



TEXAS INSURANCE LAW UPDATE

FOURTH QUARTER 2024

There were several noteworthy decisions from Texas state and federal courts handed down in the Fourth Quarter of 2024 that may be relevant to your claims handling. This quarter, there were several favorable decisions by the courts addressing issues such as outbound risk transfer and duty to defend when the Texas Construction Anti-Indemnity Act applies, prejudice to the insurer resulting in a preclusion of coverage, lack of coverage where the insured fails to prove damages caused by windstorm, and rescission of a policy when the insured conceals or misrepresents material facts in an application.

If you would like to discuss any of the cases in this report in more detail, please reach out to one of our team members at Cox PLLC

COMMERCIAL GENERAL LIABILITY/ EXCESS/UMBRELLA

TEXAS SUPREME COURT CLARIFIES RULES OF CONSTRUCTION WHEN ANALYZING FOLLOW FORM EXCESS INSURANCE POLICIES.

In *Ohio Cas. Ins. Co. v. Patterson-UTI Energy, Inc., Patterson-UTI Management Services, LLC, Patterson-UTI Drilling Company, LLC, and Marsh USA, Inc.*, __ S.W.3d __, 2024 Tex. LEXIS 1123 * (Tex. December 20, 2024), the Texas Supreme Court analyzed whether, or under what circumstances, a follow form excess policy provides coverage for attorneys' fees incurred by the named insured where the underlying policies define "damages" to include attorneys' fees and the appropriate methodology for analyzing follow form excess insurance policies. In *Patterson*, Patterson is a supplier of oil and gas equipment, including drilling rigs, to well operators and exploratory companies in Texas. In order to protect itself, as best as possible, Patterson purchases a substantial "tower" of liability insurance.

For the 2017 – 2018 policy period, Patterson obtained a primary policy, an umbrella policy, and multiple layers of follow form excess coverage. At issue in *Patterson* was the umbrella policy issued by Liberty Mutual Insurance – Europe ("Liberty Mutual") and a follow form excess policy issued by Ohio Casualty Insurance Company ("Ohio Casualty"). After a tragic oil well incident, Patterson was involved in several lawsuits which Patterson settled after extensive litigation.

All of the underlying policies, including the Liberty Mutual umbrella policy had exhausted their limits in the payment of the settlements and in reimbursing Patterson its attorneys' fees. When it came time for Ohio Casualty to pay, it agreed to pay for the settlement amounts, but refused to reimburse Patterson for the remaining attorneys' fees. Patterson sued Ohio Casualty and the matter eventually made its way to the Texas Supreme Court.

The issue presented to the Court was whether a follow form excess policy applies on the same basis and in the same manner as the underlying policy. In the appeal, Patterson argued that because the underlying policy treated attorneys' fees as "damages" and, being a follow form policy, the Ohio Casualty excess policy should be read to do the same. The Texas Supreme Court disagreed and looked to the specific policy language in the excess policy. Notably, the Court posited that the lower courts reached an erroneous result because it started first by analyzing the primary policy before looking at the terms of the excess policy. In this regard, the court looked to the Ohio Casualty excess policy's insuring agreement which provided that:

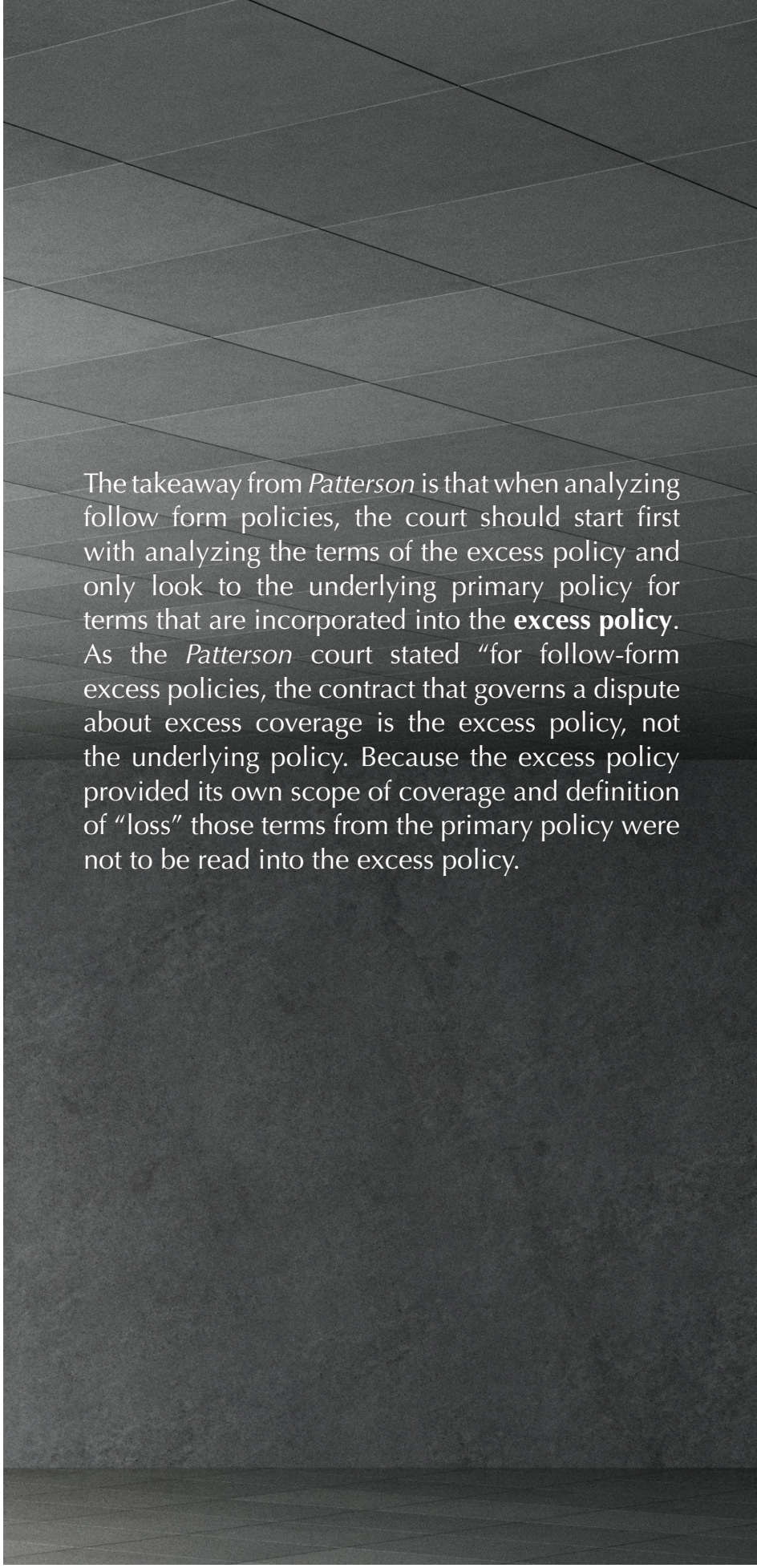
> We will pay on behalf of [Patterson] the amount of "loss" covered by this insurance in excess of the "Underlying Limits of Insurance[.]"… Except for the terms, conditions, definitions and exclusions of this policy, the coverage provided by this policy will follow the [underlying policy].

"Loss" was defined to mean "those sums actually paid in the **settlement or satisfaction of a claim** which [Patterson is] legally obligated to pay as damages after making proper deductions for all recoveries and salvage (emphasis added). The underlying Liberty Mutual umbrella policy did not include a similar definition for "loss" or for "damages" – rather, it stated it would pay the "ultimate net loss" which referred to damages. "Ultimate net loss" was defined to include:

> The amount [Patterson] is obligated to pay, by judgement or settlement, as damages resulting from an "Occurrence" to which this Policy applies, including the service of suit, institution of arbitration proceedings and all 'Defence Expenses' in respect of such "Occurrence."

The term "defence expenses" was further defined to specifically include defense costs incurred by Patterson. The Texas Supreme Court agreed that the Liberty Mutual umbrella policy unquestionably covered attorneys' fees for purposes of indemnity coverage, but that the Ohio Casualty excess policy did not despite being a follow form excess policy:

> Rather than covering "ultimate net loss" as defined by the underlying policy (or even, as with many follow-form policies, simply agreeing to the same coverage terms as the underlying policy), the excess policy instead specifies that it covers "loss," a term for which it provides its own definition. That definition refers to "damages" – a term that, without more, does not include defense expenses. And even if the excess policy's use of the term "damages" included defense expenses, Ohio Casualty would still have no duty to indemnify Patterson for those expenses here. That is because the excess policy covers only "those sums actually paid in the settlement or satisfaction of a claim which [Patterson is] legally obligated to pay as damages."
>
> In other words, the excess policy confines its coverage to sums paid to an adverse party, like the personal-injury claimants who sued Patterson after the drilling-rig incident (emphasis in original).



The takeaway from *Patterson* is that when analyzing follow form policies, the court should start first with analyzing the terms of the excess policy and only look to the underlying primary policy for terms that are incorporated into the **excess policy**. As the *Patterson* court stated "for follow-form excess policies, the contract that governs a dispute about excess coverage is the excess policy, not the underlying policy. Because the excess policy provided its own scope of coverage and definition of "loss" those terms from the primary policy were not to be read into the excess policy.

FEDERAL COURT DETERMINES NO DUTY TO DEFEND WHEN TCAIA APPLIES WHEN PLEADING ALLEGES INDEPENDENT AND VICARIOUS LIABILITY OF THE ADDITIONAL INSURED.

In *Allied World Assurance Co. U.S., Inc. v. Acadia Ins. Co.*, the United States District Court for the Eastern District of Texas – Sherman Division addressed whether the Texas Construction Anti-Indemnity Act ("TCAIA") applied to invalidate the contractual risk transfer provisions in two subcontractor agreements and additional insured provisions in a policy in relation to property damage claims involving the construction of a reservoir. In 2018, construction of the Lower Bois D'Arc Creek Reservoir Dam and Intake Project ("the Project") began in Fannin County, Texas. The North Texas Municipal Water District ("NTMWD") was the owner of the Project.

NTMWD contracted in April 2015 with Archer Western ("Archer") to act as the "Construction Manager" for the Project (referred to as the "Prime Contact"). Archer subcontracted with Philips and Jordan ("P&J") to construct the dam, intake tower, service spillway and clear the area adjacent to the site for the reservoir (the "Archer–P&J contract"). In March 2018, Archer entered into a subcontract with Hammett Excavation, Inc. ("Hammett") for Hammett to excavate and clear the reservoir and dam footprint—thereby creating the lakebed (the "Hammett–Archer subcontract"). P&J subcontracted to Hammett the clearing work it had agreed to perform in the Archer–P&J contract and for Hammett to provide erosion control services during the construction Project.

The Hammett–Archer subcontract and the P&J–Hammett subcontract required Hammett to name Archer and the Water District as additional insureds on a primary and noncontributory basis on Hammett's general liability insurance, and included a contractual indemnity provision in favor of Archer, NTMWD, and any other subcontractor of Archer—i.e., P&J. Similarly, the P&J–Hammett subcontract obligated Hammett to name P&J, Archer, and NTMWD as additional insureds with such coverage applying on a primary and non-contributory basis.

On November 22, 2019, Loyd D. Johnson Family Limited Partnership No. 1 and LDJ Operations, LLC (together, the "Underlying Plaintiffs") filed suit against P&J, Archer, NTMWD, and Hammett, alleging property damages in connection with the Project (the "Johnson Family Action"). The Underlying Plaintiffs owned LoJo Ranch, which is located a few miles northeast and downstream from the Project and in the fall of 2018, heavy rain caused a portion of the LoJo Ranch to flood. The gravamen of the Johnson Family Action was that P&J, NTMWD, Archer, and Hammett failed to properly control floodwaters in connection with the Project which caused damage to the LoJo Ranch. Allied World Assurance Co., U.S., Inc. ("Allied") defended P&J, Archer, and NTMWD in the Johnson Family Action.

Archer, NTMWD, and P&J requested Hammett, and its liability insurer, Acadia Insurance Company ("Acadia"), provide them with a defense based on the additional insured requirements and indemnity provisions in the Hammett–Archer subcontract and P&J–Hammett subcontract, which Acadia denied. Allied continued to defend Archer, NTMWD, and P&J. On October 8, 2021, the Johnson Family Action settled for $850,000.00, with Allied paying $629,000 as part of the settlement, including $254,500.00 for NTMWD, $254,500.00 for Archer, and $120,000.00 for P&J.

On July 17, 2023, Allied filed a Complaint against Acadia seeking a declaratory judgment that it was entitled to contractual subrogation from Acadia for the costs paid by Allied in defending P&J, Archer, and NTMWD in the Johnson Family Action. In addressing cross motions for summary judgment, the District Court initially determined that Archer, NTMWD, and P&J qualified as additional insureds under the Acadia policy in that the Johnson Family Action alleged that the property damage was purportedly caused at least in part by Hammett's performance of its "ongoing operations." The District Court next turned to whether the Texas Construction Anti-Indemnity Act (referred to in this opinion as to "TCAIA") applied.

Allied took the position that the TCAIA did not apply because "the Johnson Family Action sought to hold the Water District, Archer, and [P&J] liable for the acts or omissions of Hammett[.]" In support of its position, Allied pointed to the fact the indemnity provisions at issue did "not require indemnification for the negligence or fault of NTMWD or Archer," but instead applied to:

> any act, omission, fault or negligence whether active or passive of [Hammett], or anyone acting under its direction, control, or behalf or for which it is legally responsible, in connection with or incident to [Hammett's] Work or arising out of any failure of [Hammett] to perform any of the terms and conditions of this Subcontract.

However, Acadia correctly pointed out that the indemnity provision also included the following language:

> [Hammett's] obligation to indemnify, defend and hold harmless an Indemnified Party shall apply regardless of any allegations of active and/or passive negligent acts or omissions of an Indemnified Party.

The District Court found that the language plainly was meant to require Acadia, as Hammett's insurer, to defend P&J, Archer, and NTMWD against their own negligence. Therefore, because the indemnity provision required Acadia to defend P&J, Archer, and NTMWD against their own negligence, the District Court held that the provisions in the Archer–Hammett subcontract naming P&J, Archer, and NTMWD as additional insureds was void. Next Allied claimed that the provisions in the P&J–Hammett subcontract were enforceable because, although the indemnification provision applied "whether or not caused in part by the active or passive negligence or other fault of a party indemnified hereunder," it also stated that "this paragraph is not intended to require the indemnification of any party against the party's sole negligence."

Acadia countered that that language left open the possibility of joint or concurrent negligence which is contrary to the TCAIA and noted the additional insured endorsement provided coverage for property damage "caused, in whole or in part" which had been found to cover situations involving the joint or concurrent liability of the named insured and the additional insured. The District Court agreed with Acadia, noting that this language still leaves open the possibility that Acadia, as Hammett's insurer, would be required to defend P&J, Archer, or NTMWD for their percentage of fault in causing the resulting damage because "[i]f coverage exists for any portion of a suit, the insurer must defend the insured in the entire suit."

Allied further argued that the "[Johnson Family Action] is replete with allegations that [Archer] and [P&J] were liable due to the conduct of their 'agents,' namely [Hammett]…For example, it is alleged that [Archer], P&J, or their 'agents performed the construction.' " The assertion by Allied was that the inclusion of claims based on possible vicarious liability fell within an exception to the TCAIA and obligated Acadia to defend Archer, P&J, and NTMWD against the entire suit.

The District Court was not persuaded pointing to the fact the pleading clearly alleged that Archer, P&J, and NTMWD were at least in part independently liable for the property damage to the LoJo Ranch, citing to allegations of independent liability specific to Archer, P&J, and NTMWD. Allied also took the position that NTMWD was owed a defense based on the claim for vicarious liability against it. Allied further argued that because "the duty to defend is based on the allegations of the First Amended Petition, the allegations of vicarious liability therein are sufficient to create a duty to defend by Acadia." The court stated "regardless of whether the respondeat superior claims are tenable, the Underlying Plaintiffs alleged that the Water District 'is liable for the actions/omissions of its contracts, Archer Western, P&J, and/or Hammett, over whose tasks [the Water District] had the legal right and obligation to control through its contracts or otherwise.'" Thus, Allied again neglects to account for 'and/or' in the Petition which leaves open the possibility that the Water District may be vicariously liable for the conduct of Archer and P&J but not Hammett."

Allied also asserted that "[i]t was [Hammett's] clearance of the dam footprint and inadequate erosion control which allegedly led to materials from the Project being washed down to and deposited on the property of the Underlying Plaintiffs." Allied additionally argued that the "potential" that all damages resulting from the Project were caused by Hammett "[was] sufficient to take this matter outside the TCAIA and sufficient to create a duty to defend on the part of Acadia."

In rejecting the arguments of Allied, the District Court reasoned that:

> [T]he TCAIA does not require a determination of "who is truly at fault for the injuries complained of[,]" whether in whole or in part. *See Signature Indus. Servs., LLC v. Int'l Paper Co.*, 638 S.W.3d 179, 196 (Tex. 2022) (For purposes of the anti-indemnity statute, IP's alleged breach . . . was the cause of Ogden's claim, regardless of whether SIS's actions were also part of what truly brought about the injuries alleged by Ogden. The [TCAIA] does not require factual inquiry into the 'true' cause of the plaintiff's injuries."). "Instead, it asks only whether the 'claim' for which indemnity is sought was 'caused by' the fault…of the indemnitee." *Signature Indus. Servs.*, 638 S.W.3d at 196. Here, a review of the Petition makes clear that the Underlying Plaintiffs alleged that P&J, Archer, and the [NTMWD] were independently liable or liable in the alternative to Hammett. Accordingly, the TCAIA renders the provisions naming P&J, Archer, and the [NTMWD] as additional insureds void to the extent that they purport to require Acadia to defend them against their own negligence as alleged in the [Johnson Family Action].

In its last argument, Allied contended that, even if the TCAIA applied, the public works exception applied making the additional insured provisions valid and enforceable. In this regard, Allied specifically argued that NTMWD is a municipality because it has "municipality" in its name and because it is a "'legally incorporated or duly authorized association of inhabitants of limited area for local governmental or other public purpose,'" with Allied citing BLACK'S LAW DICTIONARY. Acadia countered that NTMWD does not qualify as a "municipality," pointing to a 2018 case in which NTMWD itself argued that it was not a "municipality." The District Court agreed with Acadia:

> As established above, the agreements at issue are construction contracts. Additionally, no party disputes that the Project belonged to the [NTMWD]. However, the [NTMWD] is not a municipality. See Municipality BLACK'S LAW DICTIONARY ("1. A city, town, or other local political entity with the powers of self-government; 2. The governing body of a municipal corporation; 3. The community under the jurisdiction of a city's or township's government."); *Wasson Ints., Ltd. v. City of Jacksonville*, 489 S.W.3d 427, 429-30 (Tex. 2016) (explaining that, in the sovereign immunity context, "[p]olitical subdivisions of the state—such as counties, municipalities, and school districts—share in the state's inherent immunity") (citation omitted); *N. Tex. Mun. Water Dist. v. Jinright,* 2018 Tex. App. LEXIS 9630 *3 (Tex. App. November 27, 2018) (explaining that the "governmental/proprietary dichotomy applies only to municipalities, whereas the [NTMWD] is a water conservation and reclamation district created under the authority of the Texas Constitution…and pursuant to a statute.") (citations and internal quotation marks omitted); *Bexar Metro. Water Dist. v. Educ. & Econ. Dev. Joint Venture*, 220 S.W.3d 25, 28 (Tex. App. 2006) ("[A]s a conservation district created pursuant to the provisions of article XVI, section 59 of the Texas Constitution, [Bexar Metropolitan Water District] is a political subdivision of this State and performs only governmental functions."). Because the [NTMWD] is not a municipality, the public works exception to the TAIA does not apply.

The District Court granted Acadia summary judgment and dismissed the suit with prejudice. Allied did not file an appeal with the Fifth Circuit Court of Appeals and it appears this opinion is to be published. Although this opinion is from a Texas federal court, it is likely persuasive authority for the proposition that when the TCAIA applies and the relevant pleading alleges the additional insured's independent negligence, the insured's carrier has no duty to defend the additional insured, even though the pleading may also include allegations of vicarious liability.

TEXAS SUPREME COURT REJECTS CLAIM FOR COMPUTER FRAUD COVERAGE IN FRAUD SCHEME

In *Westlake Chemical Corporation v. Berkley Regional Insurance Company*, the Supreme Court of Texas denied Westlake Chemical Corporation's attempt to recover over $16 million in losses under its insurance policies after falling victim to a fraudulent invoicing scheme. The Court affirmed that the policies' exclusions for dishonest acts by "authorized representatives" and the narrow interpretation of computer-fraud coverage barred recovery.

Westlake contracted with Tinkle Management Inc. ("TMI") to monitor inventory and supply packaging materials for its operations. TMI's owner, John Tinkle, exploited his authority to submit fraudulent invoices for supplies never provided. Westlake paid the invoices, incurring significant losses before uncovering the scheme. Tinkle was later convicted of fraud and money laundering. Westlake sought reimbursement under its policies with Berkley Regional Insurance Company and Zurich American Insurance Company, which covered losses caused by computer fraud but excluded dishonest acts by "authorized representatives."

The trial court granted summary judgment for the insurers, finding that Tinkle acted as Westlake's authorized representative and that his actions fell under the exclusion. The court of appeals upheld the decision, construing "authorized representative" broadly to include anyone authorized to act on Westlake's behalf. Westlake argued that the term required a direct legal agency relationship, which Tinkle did not have, as he lacked authority to represent Westlake in dealings with third parties.

Justice Boyd, concurring with the denial of rehearing, expressed skepticism about the lower courts' broad interpretation of "authorized representative," suggesting it might reasonably be limited to individuals with a direct, representative relationship akin to employees or agents. However, he agreed with the trial court that Westlake's losses did not fall within the policies' computer-fraud coverage.

The Court found that while Tinkle used email to submit fraudulent invoices, the losses did not "result directly" from computer use, as required by the policy. Instead, the use of a computer was incidental to the fraud, and the outcome would have been the same if invoices were submitted by other means. Citing the Fifth Circuit's interpretation in *Apache Corp. v. Great American Insurance Co.*, the court concluded that applying the computer-fraud provision to any scheme involving email would transform it into general fraud coverage.

This decision underscores the narrow scope of computer-fraud coverage in Texas and the importance of policyholders understanding the breadth of exclusions related to dishonest acts. The Court's analysis also highlights potential ambiguities in terms like "authorized representative," emphasizing the need for precise policy language to avoid disputes.

FEDERAL COURT RULES THAT ABATEMENT AND NEW TRIAL APPROPRIATE, AND POSSIBLY REQUIRED, IN UI/UIM CASES

Elham v. State Farm Mut. Auto. Ins. Co., involved a UIM/UM coverage dispute between State Farm and its insured and arises from an uninsured/underinsured motorist coverage dispute. In this case, the insured sued State Farm asserting claims for breach of contract and also asserted several extracontractual claims. State Farm removed the case to federal court and filed a motion requesting abatement and a separate trial for the extracontractual claims. The United States Court for the Southern District of Texas, Houston Division, concluded that State Farm's motions should be granted.

The insured attempted to argue that federal courts are not required to follow the state court approach to UM/UIM cases, which consistently grant abatements and separate trials in UM/UIM extra-contractual cases such as this. The federal district court agreed and concluded that Plaintiff's extracontractual claims in this UM/UIM case should be tried separately and abated until coverage is finally determined. Specifically, the Court reasoned that UM/UIM disputes warrant separate trials because UI/UIM contracts are unique, in that the benefits are conditioned upon the insured's legal entitlement to receive damages from a third party, and as such, an insurer's obligation to pay benefits does not arise until liability and damages are determined. Additionally, in the UIM context, extra contractual claims have the additional hurdle in that the insured must first establish that the policy requires payment on the claim. Because of this, Texas courts have routinely concluded that separate trials for and abatement of extra-contractual claims are not only proper but are required in UIM cases. The Court concluded that the lack of separate trials could prejudice the insurer, such as when the insurer has made a settlement offer that was rejected. The Court also concluded that abatement would help to avoid wasting resources.

U.S. DISTRICT COURT DISMISSES LAWSUIT AGAINST THE INSURER BECAUSE THE INSURED OFFERED NO EVIDENCE TO SUPPORT CLAIM FOR UNINSURED MOTORIST BENEFITS.

In *Mann v. Amica Mut. Ins. Co.*, Plaintiff Manuela Moro was traveling in a vehicle when an uninsured motorist collided with her vehicle. Moro claimed she sustained personal injuries and brought a declaratory judgment action against her insurer, Amica Mutual Insurance Company ("Amica"), seeking a judicial declaration that she was entitled to recover uninsured motorist benefits under her policy. In response, Amica filed a motion for summary judgment, arguing that declaratory relief was inappropriate because Moro's treating doctor testified that "it was fair to say, based on the information [known], [that he/she] just [didn't] know whether the degenerative changes or the disc prolapse or herniation were degenerative or acute or caused by the accident." As such, Amica argued that Moro could not establish that she was entitled to damages from the uninsured motorist as a result of the motor vehicle accident. The Court agreed and granted summary judgment.

The Court began its analysis by noting that "a UM/UIM insurer's contractual obligation to pay benefits does not arise until liability and damages are determined. Neither requesting UM/UIM benefits nor filing suit against the insurer triggers a contractual duty to pay." The Court acknowledged the testimony of Moro's treating doctor and reasoned that Moro offered no evidence indicating that the accident caused her any injury.

> "Because Moro has failed to carry her burden of establishing that the accident at issue resulted in any damages, she cannot show that she is entitled to policy benefits."

HOMEOWNERS AND COMMERCIAL PROPERTY

TYLER COURT OF APPEALS FINDS INSURER PREJUDICED BY INSURED'S FAILURE TO COMPLY WITH POLICY CONDITIONS

In *Cade v. State Farm Lloyds*, State Farm concluded a fallen tree had damaged only a portion of the insureds' home following a windstorm in April 2019 and issued payment pursuant to the insureds' homeowners policy for the repairs the insurer deemed were caused by the tree and the windstorm. About eighteen months after the storm, the insureds brought up for the first time damage to personal property, asserted the home was a total loss, and that State Farm's payment of approximately $30,000 was inadequate. Five days after selling the house, the insureds filed suit against State Farm asserting claims for breach of contract and violations of the Texas Insurance Code and Deceptive Trade Practices Act.

State Farm filed separate motions for summary judgment on the personal property and the real property claims alleging 1) further damage to the home was not caused by the windstorm, 2) there was no personal property of value in the home, and 3) the insureds failed to comply with conditions precedent of the policy. The insureds argued State Farm failed to prove prejudice. The trial court granted both of State Farm's motions without specifying its grounds for doing so and the insureds appealed.

State Farm's adjuster inspected the property in May 2019 and concluded that the home had been abandoned for many years, was deteriorating and in poor condition, and that there was no personal property of any significant value in the home. A second adjuster inspected the home along with a roofer in April 2020 and noted damage to the rear elevation and north side of the home that was not caused by the April 2019 storm and observed a lot of pre-existing damage attributed to neglect, lack of maintenance, and long-term settlement among others. In March 2021, an engineer retained by State Farm and another roofer inspected the home. The engineer concluded the damage to the home from the tree that fell in the April 2019 storm was limited to the front wall of the residence and the front roof slope; however, there was severe deterioration and rot throughout the home from deferred maintenance and neglect. The roofer concluded the home was beyond repair before the tree fell on it and had not been habitable by humans for some time. Both noted long term animal infestation and other damage. During his deposition, Mr. Cade admitted he had not lived at the home since 2008 and that he had no personal knowledge of the condition of the home prior to the April 2019 storm. While he testified that his wife spent time living between the home and a neighboring property, there had been no water service at the home for seven years or more. Further, the policy precluded coverage for damages due to deterioration, neglect, deferred maintenance, or animal damage. Based on the evidence, the court concluded the insureds failed to show the home was a total loss as a result of the April 2019 storm and that damages beyond the $30,791.02 State Farm paid for the tree damage were not caused by the storm but rather from neglect and deferred maintenance. Accordingly, the Court affirmed the summary judgment for the claim related to the dwelling.

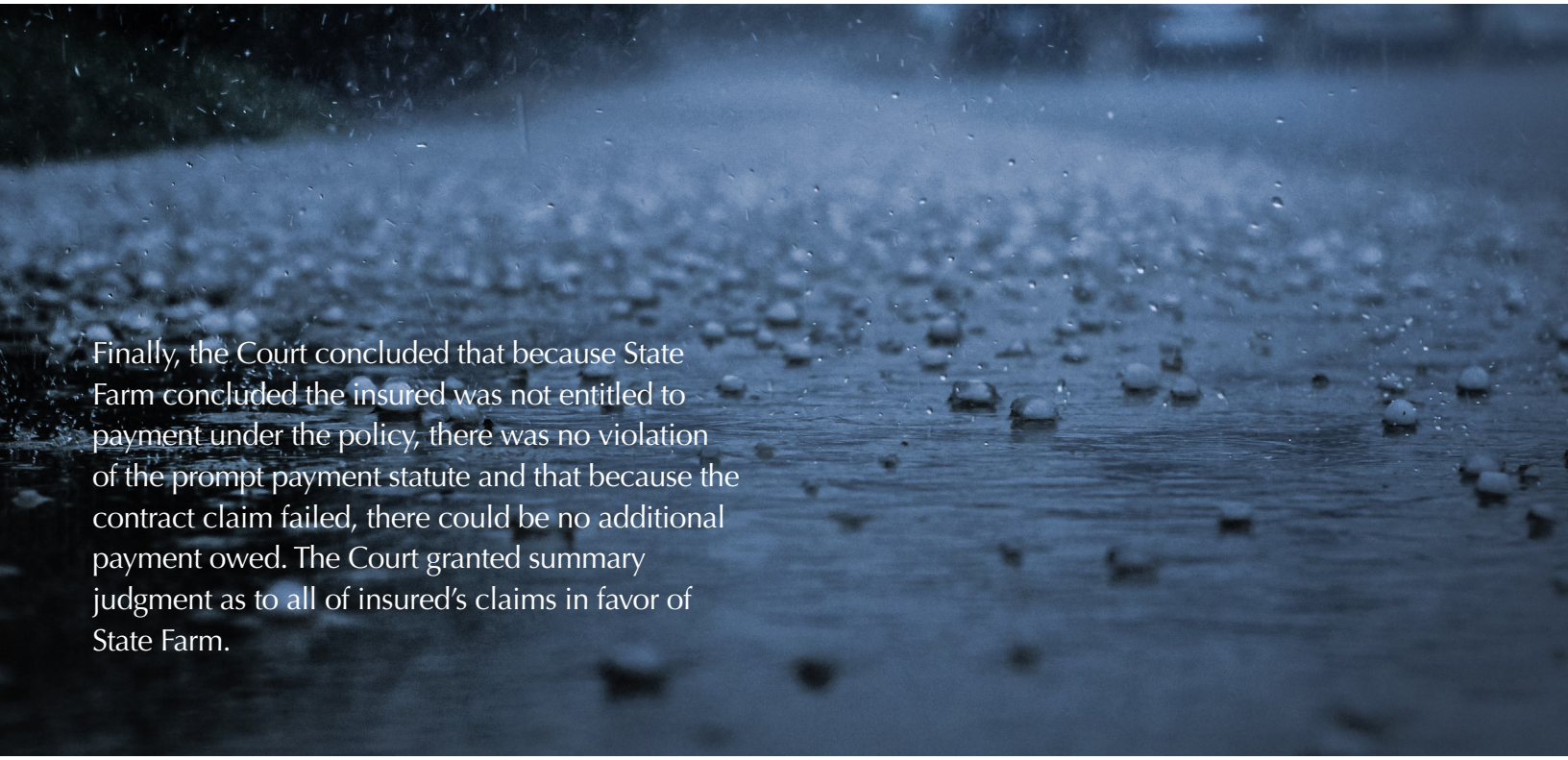
As to the insureds' personal property claim, State Farm argued it was not required to cover the insured's personal property claim because the insured's failed to comply with the policy's terms and conditions specifically by failing to 1) give immediate notice; 2) protect the property from further damage; 3) prepare a detailed inventory with bills, receipts or other documents to substantiate the amount of loss; 4) comply with requests for documentation; and 5) submit a signed and sworn proof of loss with 91 days of the loss. There was no dispute the insured failed to comply with the policy conditions inasmuch as he did not notify State Farm of the personal property claim until September 2020, could not support any of the claimed values, and admitted he did not remove contents from the home for years to protect the contents from further damage. However, the parties disputed whether State Farm was required to show prejudice by the insured's failure to comply. Acknowledging the notice-prejudice rule set forth in *PAJ, Inc. v. Hanover Ins. Co.*, 243 S.W.3d 630, 636-37 (Tex. 2008), wherein the Texas Supreme Court held that an insurer cannot deny coverage solely based on untimely notice unless the insurer was prejudiced by the late notice, the Cade court noted it was less clear whether the rule applies to other policy provisions. The Court reviewed how Texas courts and federal courts had applied the rule in different scenarios.

Without deciding whether State Farm was required to show prejudice, the Court concluded State Farm had in fact demonstrated prejudice because State Farm was unable to investigate the claim or the personal property. Thus, the Court affirmed summary judgment regarding the personal property claim.

TEXAS WESTERN DISTRICT COURT GRANTS SUMMARY JUDGMENT IN FAVOR OF THE INSURER WHERE THE INSURED COULD NOT SEGREGATE BETWEEN COVERED AND UNCOVERED DAMAGES

In *Espinoza v. State Farm Lloyds*, the insured filed a claim on April 30, 2022 for damages allegedly sustained to his home during a purported severe hail and windstorm almost a year earlier on May 28, 2021, seeking coverage under his homeowners policy for damage to the roof and exterior gutters and downspouts. State Farm inspected the property on May 4, 2022, and found no hail damage to the roof, one wind damaged shingle, and normal deterioration and granule loss for the age of the shingles. State Farm also observed hail damage to the gutters on the back elevation of the home but based on the buildup of dirt and soot, it was claimed the damage had been there for some time and did not correlate to the May 28, 2021 date of loss. Accordingly, State Farm estimated $580.25 for the damaged shingle, which was less than the insured's $3,650.00 deductible, and no damages for the gutter system. Accordingly, State Farm issued no payment and sent a letter to the insured explaining its decision on May 4, 2022. On January 21, 2023, State Farm received a letter from the insured's public adjuster estimating the storm damage at $51,400.76, which State Farm concluded was not actual damage and/or not covered damage. On March 14, 2023, State Farm received a letter from the insured's counsel asserting the storm damage was $62,642.32; however, there was no supporting documentation provided to support the alleged amount of damages. Accordingly, State Farm refused to revise its $580.25 damage estimate.

The insured subsequently filed suit against State Farm and alleged the May 28, 2021 storm damaged his home's roof, vents, flashings, windows and window screens, fascia, gutters and downspouts, and the HVAC system. Plaintiff brought claims against State Farm for breach of contract, violations of the Texas Insurance Code regarding unfair settlement practices and prompt payment, and Texas Deceptive Trade Practices Act violations. In its motion for summary judgment, State Farm argued the insured did not segregate the damage State Farm attributed to the May 28, 2021 storm (a single damaged roof shingle) from other damages as required by the concurrent cause doctrine. The court reviewed State Farm's summary judgment evidence (wherein State Farm's initial inspection report and experts' reports concluded the damage to the roof was likely normal wear and tear and/or damage from other storms according to weather data and reports) and found that the storm on May 28, 2021 could not have caused all of the alleged damage, if any. The burden then shifted to the insured to present evidence to show the existence of a genuine fact issue. The Court noted the insured's expert found no storm event on May 28, 2021; rather, he noted a significant hailstorm on May 30, 2021 and that one of his weather sources on wind speeds indicated the storm may have been from March 30, 2021. The Court noted the insured never made an effort to amend the alleged date of loss, acknowledge the inconsistency, nor provide evidence showing his damages were traceable to the May 28, 2021 storm he alleged caused the damage. The Court found that Plaintiff failed to identify evidence a jury could use to segregate the existing damages from the May 28, 2021 alleged storm damage. Therefore, the Court granted summary judgment for State Farm on the insured's breach of contract claim. The Court further concluded that the insured's extra contractual claims failed because his breach of contract claim failed.



Finally, the Court concluded that because State Farm concluded the insured was not entitled to payment under the policy, there was no violation of the prompt payment statute and that because the contract claim failed, there could be no additional payment owed. The Court granted summary judgment as to all of insured's claims in favor of State Farm.

FIFTH CIRCUIT FINDS COVERAGE BARRED UNDER HOMEOWNERS POLICY WHERE THE INSURED WAS NOT RESIDING AT THE PROPERTY ON THE POLICY INCEPTION DATE

In *Hunt v. Meridian Security Insurance Company*, in an unpublished opinion, the Fifth Circuit found coverage was barred under the insured's homeowners policy based on the policy's requirement that the insured reside at the property on the inception date of the policy and the insured did not begin to reside at the property until over a year after the policy's inception date.

The insured purchased the property at issue on June 16, 2020, and obtained the homeowners insurance policy on June 27, 2020, with an effective date of June 16, 2020. In February 2021, the insured filed a claim for water damage from pipes that burst during a winter freeze for which the insurer paid $67,319.78 on March 30, 2021. Several months later, the insured contacted the insurer claiming her losses were then hundreds of thousands of dollars. During its continued investigation, the insurer requested the insured participate in an examination under oath where the insured testified she did not start living in the property until around July 2021 and not full-time until November 2021. The insured subsequently sued the insurer during its continued investigation. Based on the evidence, the district court held that because the insured did not reside at the property on the inception date as required by the plain language of the policy, there was no coverage for the loss and granted summary judgment in favor of the insurer.

On appeal, the insured did not dispute that the plain language barred coverage; rather, she argued that the court's interpretation of the policy led to a result that was "unreasonable, inequitable, and oppressive." The Fifth Circuit disagreed and noted that the caselaw is clear that the policy was correctly interpreted by the district court.

The Fifth Circuit cited its decision in *GeoVera Specialty Ins. Co. v. Joachin*, 964 F.3d 390, 393 (5th Cir. 2020) (applying Louisiana law), where it interpreted a similar policy and concluded the policy language was "clear and explicit" and that there was no coverage where the insured did not reside on the premises at policy inception. Noting that in GeoVera the insured never resided on the property, and that while the Fifth Circuit expressed concerns in situations, like in the matter before it, where the insured did eventually move into the property, it still concluded the restriction regarding residing at the property at policy inception did not "rise to the level of absurdity."

. . . Rather, the specific reside-at-inception requirement like the one in Askew Hunt's policy "makes perfect sense for a homeowner who purchases it while already living in the home." "Just as a policy requiring ownership would not become absurd if a renter mistakenly purchased it, the reside-at-inception policy is not absurd because the insureds who had yet to move in [mistakenly] purchased it." Further, this result is not oppressive or unreasonable because Askew Hunt is not without a remedy—she may still be entitled to recover damages from the agent who procured the wrong policy on her behalf.

Noting the insured failed to provide an alternative reading of the policy language and based on binding precedent, the Court concluded the district court's finding was not absurd or unreasonable. Finding the insurer could not be responsible for coverage it did not agree to provide, the Fifth Circuit affirmed summary judgment in favor of the insurer.

MOTOR CARRIER

CALIFORNIA FEDERAL DISTRICT COURT UPHOLDS RECISSION OF MOTOR CARRIER POLICY DUE TO MISREPRESENTATION OF INDIVIDUALS OPERATING VEHICLES ON POLICY APPLICATION.

In the case of *Williamsburg Nat'l Ins. Co. v. 7Az Transp., LLC*, Williamsburg National Insurance Company ("Williamsburg") issued a commercial auto policy to 7Az Transport, LLC and Angel H. Zatarain dba AZ Trucking ("7Az"). The Williamsburg policy only insured two heavy trucks, which the insured used for hauling rocks and other similar materials. On October 18, 2022, Williamsburg issued the policy to 7Az based on the representation in the policy application that 7Az only operated two heavy trucks and these trucks were only operated by Angel H. Zatarain and Jose Cervantes Velasco. Two months after issuing the policy, Williamsburg conducted an inspection of 7Az's business, and Zatarain again reiterated that the second driver was Jose Cervantes Velasco.

Approximately six months after issuing the policy, both trucks were involved in the same accident. Zatarain was operating the front vehicle, however, the second vehicle was operated by Jesus Loya Rodriguez. It was after this accident that Williamsburg first learned that the second insured vehicle was being regularly operated by Loya, not Cervantes Velasco. Plaintiff also learned that Loya was driving a commercial vehicle while he was prohibited from performing safety sensitive functions due to a prior felony involving a motor vehicle pursuant to 49 C.F.R. § 382.501. Williamsburg 's investigation also revealed that Loya's driver's license had been revoked from June 26, 2018 to September 21, 2020.

Zatarain testified in his Examination Under Oath ("EUO") that the second driver listed on the insurance application, Jose Cervantes Velasco, did not drive any insured vehicle at the time the policy application was submitted in late September 2022, or any time during the year 2022. In fact, Cervantes had not driven for him for about three and a half or four years. Zatarain further testified that Loya was an employee of his business and had been driving one of the trucks as his employee four or five times a week for at least six months before the accident. Additionally, he also testified that Loya's name should have been on the policy application as his second driver. Zatarain further admitted that the information on the policy application submitted in October 2022, and at the inspection of his vehicles in December 2022, was incorrect.

> Williamsburg's underwriting guidelines do not allow it to insure drivers who have had felony motor vehicle violations within five (5) years of policy issuance, or who have had their license revoked or suspended within three years of policy issuance.

Loya therefore did not qualify as an insured driver under Williamsburg's underwriting guidelines. If 7Az had notified Williamsburg that the second driver was actually Loya, Williamsburg would either have declined to issue the Policy at all or would have issued the Policy to exclude Loya as a driver of the insured vehicles. Accordingly, Williamsburg notified 7Az that the policy was being rescinded and issued a refund check.

Shortly after issuing the refund, Williamsburg initiated a declaratory action seeking confirmation that the recission of the policy was appropriate. In response to the declaratory action, 7Az asserted counterclaims for breach of contract and bad faith. Ultimately, Williamsburg filed a motion for summary judgment seeking a declaration that the recission was proper and as a result the court should dismiss 7Az's breach of contract and bad faith claims.

Pursuant to California Insurance Code sections 330-361, an insurer may rescind a policy of insurance if the insured concealed or misrepresented a material fact in the policy application. The Court noted that the evidence shows that Zatarain misrepresented a material fact on the application, that is, that Loya would be driving his commercial vehicle instead of Jose Cervantes. This information was material because Williamsburg would not have issued the Policy if it had known Loya would be driving one of the insured vehicles. The Court further noted that under California law, the intent to deceive is not required when a material misrepresentation is on the application, as opposed to a post-policy misrepresentation. Accordingly, The Court held that Williamsburg was entitled to rescind the policy even if Zatarain's failure to disclose was a mistake, inadvertent or negligent. Furthermore, the Court also held that rescission extinguishes the Policy, rendering it void as if it never existed. Therefore, Williamsburg did not have any contractual obligations to 7Az. Thus, 7Az's breach of contract and bad faith claims were also dismissed.

> This case demonstrates that recission is a powerful tool that can be utilized if it is determined that the insured misrepresented material facts that if properly disclosed would have resulted in an insurer declining to issue a policy.

However, when considering recission as a possible defense, it is important to not only consider if the underwriting guidelines sufficiently establish that a misrepresentation constitutes a material misrepresentation, but also an insured must consider when the material representation occurred and if the governing law will require the insurer to establish the insured's intent to deceive in order to successfully assert a recission defense. Accordingly, while recission is a powerful coverage defense, the bar to establish a proper recission is typically set very high given the potentially catastrophic damage that results to an insured. Therefore, we recommend retaining counsel to vet a potential recession defense before starting the process of rescinding a policy.

OTHER CASES OF GENERAL CONCERN

TEXAS FEDERAL COURT ENFORCES INSURED V. INSURED EXCLUSION TO DENY COVERAGE

In *Kennedy v. United States Liability Insurance Co.*, the United States District Court for the Southern District of Texas addressed the applicability of the "Insured v. Insured" exclusion in a Directors and Officers (D&O) liability insurance policy. The case involved a dispute over whether United States Liability Insurance Company (USLIC) was obligated to defend and indemnify former executives of the National Diversity Council (NDC) in a lawsuit brought against them by NDC. The former executives, including R. Dennis Kennedy, sought coverage for claims of breach of fiduciary duty, conspiracy, and unauthorized computer access, alleging that these claims arose from their wrongful acts during their tenure at NDC.

USLIC denied coverage, asserting that the policy's "Insured v. Insured" exclusion precluded defense and indemnity because the lawsuit was initiated by NDC, a named insured, against its former executives, who were also insureds under the policy. The Court agreed with USLIC, finding that the exclusion was unambiguous and clearly barred coverage for claims brought by one insured against another. The former executives argued that exceptions to the exclusion should apply, including one for claims involving former executives. However, the Court concluded that the exception was explicitly limited to claims unrelated to wrongful acts committed during their tenure, which did not apply here.

Further, the Court rejected the executives' claims of bad faith and violations of the Texas Insurance Code. It emphasized that Texas law does not recognize a duty of good faith and fair dealing in the context of third-party liability claims. The Court also found that USLIC's denial of coverage was reasonable and based on clear policy terms, shielding the insurer from liability under the Bona Fide Dispute Doctrine. Additionally, the Court dismissed allegations of misrepresentation, citing the absence of evidence showing false statements by USLIC regarding coverage.

Ultimately, the Court granted USLIC's motion for summary judgment, reiterating that the eight-corners rule governs the determination of an insurer's duty to defend under Texas law. This decision underscores that the "Insured v. Insured" exclusion can serve as a powerful defense for insurers when claims arise between parties covered under the same policy.

1. No. 4:23-CV-00655-ALM-AGD, 2024 U.S. Dist. LEXIS 183831 (E.D. Tex. September 9, 2024), *adopted and judgment entered* at 2024 U.S. Dist. LEXIS 182692 (E.D. Tex. October 7, 2024).
2. No. 23-0789, 68 Tex. Sup. Ct. J. 85, 2024 Tex. LEXIS 1035 (Nov. 15, 2024).
3. No. 4:24-cv-02235, 2024 U.S. Dist. LEXIS 167049 (S.D. Tex. 2024).
4. No. 4:23-cv-01148, 2024 U.S. Dist. LEXIS 201881 (S.D. Texas [Houston Division], Nov. 6, 2024, mem. op.).
5. No. 12-23-00285-CV, 2024 Tex. App. LEXIS 7051 (Tex. App.—Tyler Sep. 30, 2024, pet. filed).
6. No. 1:23-CV-751-DII, 2024 U.S. Dist. LEXIS 166363 (W.D. Tex. 2024).
7. No. 24-10110, 2024 U.S. App. LEXIS 29164 (5th Cir. 2024).
8. *Id.* at *4 – 5 (citations omitted).
9. No. 5:23-CV-01893-SSS-DTBx, 2024 U.S. Dist. LEXIS 184861 (C.D. Cal. Oct. 8, 2024).
10. No. 4:24-CV-02139, 2024 U.S. Dist. LEXIS 215852 (S.D. Tex. 2024).

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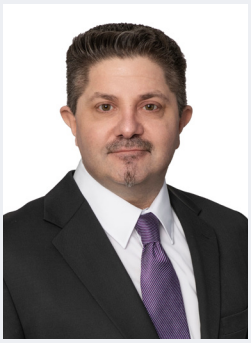

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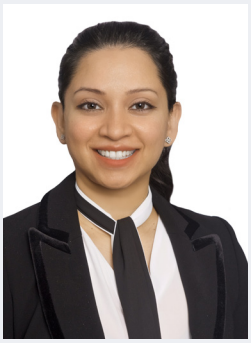

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