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Insurance Law

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INSURANCE LAW

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I. INTRODUCTION

Despite the global COVID-19 pandemic and the closure of many businesses, schools, places of worship, and other establishments, Texas federal and state courts were busy in 2020. They issued significant opinions in several different areas of insurance law during the Survey period. These include:

- Three decisions by the U.S. District Court for the Western District of Texas finding no insurance coverage for COVID-19 business interruption claims because the COVID-19 virus: (1) did not cause direct physical loss or damage as required by the policies; (2) was excluded from coverage by Virus Exclusions; and (3) was not covered under a Civil Authority provision in the policy.

- The first decision by the Texas Supreme Court recognizing an exception to the well-established rule that extrinsic evidence cannot be used to determine an insurer's duty to defend—the collusive fraud exception.
- A decision from the U.S. District Court for the Western District of Texas holding that Texas public policy precluded an insurer from indemnifying an insured's employee for punitive damages awarded because the employee was driving while intoxicated when he injured another motorist.
- A decision by the U.S. Court of Appeals for the Fifth Circuit that an insured does not need to prove an insurer acted wrongfully or in bad faith to recover under the Texas Prompt Payment of Claims Act.

Despite these decisions, it remains to be seen whether other federal and state courts will find that COVID-19 business interruption claims are not covered. Moreover, the Texas Supreme Court continues to decline the opportunity to decide the validity of broader exceptions to the extrinsic evidence rule, such as the *Northfield* exception, despite the inconsistent approach of Texas federal courts and state appellate courts with respect to such exceptions.¹

II. COVID-19

In 2020, the world faced an unprecedented pandemic of the novel, highly infectious coronavirus, COVID-19. The pandemic generated great uncertainty in many aspects of modern life, including whether claims for COVID-19 injuries and damages are covered by insurance. Fortunately, recent decisions of the U.S. District Court for the Western District of Texas provide some clarity as to coverage for COVID-19 claims. As a result of orders closing non-essential businesses, lawsuits by insureds seeking coverage for COVID-19 claims tend to raise four principal issues: (1) whether COVID-19 losses are “direct, physical loss”; (2) whether a policy's “Virus Exclusion” applies to COVID-19; (3) whether a policy's “Civil Authority” provision applies to COVID-19 claims; and (4) the requirements for obtaining extra-contractual damages in COVID-19 claims.

These recent COVID-19 decisions emphasize a close review of the policy language and application of the basic rules of contract interpretation.² The “paramount rule is that courts enforce unambiguous policies as written” such that the district court must “honor plain language, reviewing policies as drafted, not revising them as desired.”³ The factual back-

1. *See Northfield Ins. Co. v. Loving Home Care, Inc.*, 363 F.3d 523, 531 (5th Cir. 2004).

2. *See, e.g., Diesel Barbershop, LLC v. State Farm Lloyds*, 479 F. Supp. 3d 353, 358 (W.D. Tex. Aug. 13, 2020) (“Insurance policies are contracts and are governed by the principles of interpretation applicable to contracts.”).

3. *Id.* (quoting *Pan Am Equities, Inc. v. Lexington Ins. Co.*, 959 F.3d 671, 674 (5th Cir. 2020)).

grounds of the decisions analyzing COVID-19-related insurance claims have been relatively similar—the insured’s claim for business interruption coverage is denied because the insurer believes that COVID-19 and its consequences are an excluded cause of loss.

A. THE IMPACT OF GOVERNMENT-MANDATED CLOSURE ORDERS
DUE TO COVID-19 DOES NOT CONSTITUTE A “DIRECT
PHYSICAL LOSS” UNDER AN INSURANCE POLICY IF
THE LOSS IS MERELY ECONOMIC AS
OPPOSED TO A DISTINCT, DEMONSTRABLE, PHYSICAL ALTERATION OF
THE PROPERTY

The U.S. District Court for the Western District of Texas, in *Diesel Barbershop, LLC v. State Farm Lloyds*, granted the insurer’s motion to dismiss after finding that the insured did not sustain a “direct physical loss.”⁴ The policies’ “Covered Causes of Loss” section stated that State Farm would “insure for *accidental direct physical loss* to Covered Property” unless the loss is excluded or limited under the policy.⁵ The district court held that a loss must be a “distinct, demonstrable, physical alteration of the property” to constitute direct physical loss.⁶ Whereas odor and the release of asbestos are found to constitute a “physical” loss because they make a business uninhabitable, the same cannot be said for COVID-19.⁷ COVID-19 is distinguishable because it does not have a physical presence at the property, nor does it make a business uninhabitable. Rather, the consequences of the government-mandated closure orders are the cause of an insured’s damages, not the virus itself. Because the virus merely causes a detrimental economic impact unaccompanied by a distinct, demonstrable, physical alteration of the property, courts find that the insureds failed to plead a direct physical loss as required by the policy for COVID-19 related damages.⁸

4. *Id.* at 362.

5. *Id.* at 356 (emphasis added); *see also* *Vizza Wash, LP v. Nationwide Mut. Ins. Co.*, No. 5:20-CV-461-DAE, 2020 WL 6578417, at *6 n.7 (W.D. Tex. Oct. 26, 2020) (“Covered Cause of Loss” was defined as a “direct physical loss” unless the loss is otherwise excluded or limited under the policy.).

6. *Diesel Barbershop*, 479 F. Supp. 3d at 360; *see also* *Hartford Ins. Co. of Midwest v. Miss. Valley Gas Co.*, 181 F. App’x 465, 470 (5th Cir. 2006) (“The requirement that the loss be ‘physical’ . . . is widely held to exclude alleged losses that are intangible or incorporeal and, thereby, to preclude any claim against the property insurer when the insured merely suffers a detrimental economic impact unaccompanied by a distinct, demonstrable, physical alteration of the property.”).

7. *Diesel Barbershop*, 479 F. Supp. 3d at 360.

8. *Id.*; *see also* *Vizza Wash*, 2020 WL 6578417, at *6 n.7 (Plaintiff did not allege any physical alteration or damage to its own property or the adjacent properties, and thus, plaintiff’s contract claim might also be subject to dismissal on this basis. However, the court did not decide this issue because the Virus Exclusion barred coverage.).

B. THE “VIRUS EXCLUSION” IN A POLICY WILL LIKELY BAR
RECOVERY FOR LOSS OF BUSINESS INCOME DUE TO THE
EFFECTS OF COVID-19

Even assuming an insured’s complaint adequately alleges a direct, physical injury, an insured’s breach of contract claim for COVID-19 related damages will likely still fail if the policy contains a “Virus Exclusion” that is plainly applicable to the insurance claim.⁹ In *Vizza Wash, LP v. Nationwide Mutual Insurance Co.*, the U.S. District Court for the Western District of Texas held that the policy language excluding any “loss or damage caused *directly or indirectly* by . . . any virus” unambiguously excluded the insured’s claimed damages.¹⁰ The plaintiff’s allegations were clear: its business income losses stemmed—at least indirectly—from the COVID-19 pandemic.¹¹

Similarly, the district court in *Diesel Barbershop* held that the Virus Exclusion barred coverage for business interruption losses because the closure orders were only issued due to the rapid spread of the COVID-19 virus throughout the community.¹² The anti-concurrent causation clause in the Virus Exclusion expressly stated that a loss is excluded regardless of “whether other causes acted concurrently or in any sequence within the excluded event to produce the loss.”¹³ Therefore, even if the district court found that there was a direct, physical loss, the Virus Exclusion applied and barred the insured’s claims because a covered cause of loss (i.e., physical damage to property) would have combined with an excluded cause of loss (i.e., a virus capable of causing physical distress, illness, or disease) and the enforcement of related orders, which would cause the policies’ ACC clauses to exclude coverage for the insured’s losses.¹⁴

In *Independence Barbershop v. Twin City Fire Insurance Co.*, the Virus Endorsement contained essentially the same language as in *Diesel Barbershop* and *Vizza Wash*.¹⁵ However, there was one difference that led to a different result: the Virus Endorsement contained an additional provision, Section B.1.f. This provision specifically included coverage for viruses for up to thirty days for business interruption if “loss or damage to property caused by . . . virus” leads to suspension of operations and if “Time Element Coverage applies.”¹⁶ The court found that the insured pled a plausible claim for relief under this section because “[t]he text of the insurance policy does not limit Section B.1.f. to certain contributing

9. See *Vizza Wash*, 2020 WL 6578417, at *6.

10. *Id.* at *6 (emphasis added).

11. *Id.* at *7.

12. *Diesel Barbershop*, 479 F. Supp. 3d at 361.

13. *Id.*

14. See *id.* at 362.

15. *Indep. Barbershop, LLC v. Twin City Fire Ins. Co.*, No. A-20-CV-00555-JRN, 2020 WL 6572428, at *2 n.2 (W.D. Tex. Nov. 4, 2020) (“the virus endorsement” excludes losses caused by virus “regardless of any other cause or event that contributes concurrently or in any sequence to the loss.”).

16. *Id.* at *4.

causes.”¹⁷ However, the U.S. District Court for the Western District of Texas also held that there was a valid exclusion clause incorporated in the Virus Endorsement that barred recovery under all other sections of the policy and thus partially granted the insurer’s motion to dismiss.¹⁸ This decision underscores the importance of closely reviewing Virus Exclusions because they may provide coverage for a limited period of time.

In *Diesel Barbershop*, even though the insureds alleged that the insurer denied the insureds’ claims without any investigation and without requesting any information or documentation, the district court still held that plaintiffs’ claims were not covered, or, even if covered, would be excluded from coverage under the policies, and thus granted the motion to dismiss.¹⁹ In *Jada Restaurant Group, LLC v. Acadia Insurance Co.*, the insured similarly alleged that the insurer and the adjuster made no requests for documentation or information and quickly denied the claim.²⁰ In reviewing the motion to remand, the U.S. District Court for the Western District of Texas conducted a 12(b)(6) motion to dismiss analysis to see if plaintiffs pled a reasonable basis to predict that they may recover against the in-state defendant adjuster.²¹ The district court found that the plaintiffs pled a viable claim against the in-state defendant adjuster by alleging that the adjuster erroneously denied coverage based on the policy’s virus exclusion, did not conduct a proper investigation, and misrepresented the scope of the policy to the plaintiffs.²² Thus, the district court remanded the case back to state court.²³

C. IN ORDER FOR A CIVIL AUTHORITY POLICY PROVISION TO BE
TRIGGERED, THERE MUST BE PHYSICAL DAMAGE TO
OTHER PREMISES NEAR THE INSURED’S PROPERTY

Diesel Barbershop is the only Texas federal decision pertaining to COVID-19 coverage to significantly address the Civil Authority provision.²⁴ *Diesel Barbershop* held that the provision was not triggered by COVID-19.²⁵ The U.S. District Court for the Western District of Texas explained that “civil authority coverage is intended to apply . . . where access to an insured’s property is prevented or prohibited by an order of civil authority issued as a direct result of *physical damage* to other premises in the proximity of the insured’s property.”²⁶ As previously discussed,

17. *Id.*

18. *Id.* The court also denied the insurer’s motion to dismiss the class action claims and stated it would determine the question of class certification at the appropriate time. *Id.* at *5.

19. *Diesel Barbershop*, 479 F. Supp. 3d at 357–62.

20. *Jada Rest. Grp., LLC v. Acadia Ins. Co.*, No. SA-20-CV-00807-XR, 2020 WL 5362071, at *1 (W.D. Tex. July 10, 2020).

21. *Id.* at *2.

22. *Id.* at *3–4.

23. *Id.* at *4.

24. *See Diesel Barbershop*, 479 F. Supp. 3d at 357.

25. *Id.* at 362.

26. *Id.* (emphasis added) (quoting *Dickie Brennan & Co. v. Lexington Ins. Co.*, 636 F.3d 683, 686–87 (5th Cir. 2011)).

the district court found no physical damage and the Virus Exclusion applied such that the insureds failed to allege a legally cognizable “Covered Cause of Loss.”²⁷

D. IF THERE IS NO COVERAGE FOR A COVID-19 CLAIM, AN
INSURED CAN ONLY RECOVER EXTRA-CONTRACTUAL
DAMAGES ARISING OUT OF THE CLAIM BY
DEMONSTRATING AN INDEPENDENT
INJURY

In *Vizza Wash*, the U.S. District Court for the Western District of Texas, relying on the Texas Supreme Court’s decisions in *Republic Insurance Co. v. Stoker* and *USAA Texas Lloyds Co. v. Menchaca*, found that when a policy expressly excludes coverage for COVID-19 related damages, the denial of the insurance claim may not serve as the basis for extra-contractual claims unless the plaintiff has alleged an injury independent of the policy claim.²⁸ The damages must be “truly independent” and not “stem” or “flow” from the denial of the insured’s claim.²⁹

In *Vizza Wash*, the district court held that the insured failed to plausibly allege any independent injury apart from the insurer’s alleged failure to pay benefits under the policy.³⁰ Nor did the insured attempt to specifically explain how its extra-contractual claims were independent of its contract claims.³¹ Therefore, the district court dismissed the insured’s extra-contractual statutory and bad faith claims.³² Notably, the district court also denied leave for the plaintiff to amend its complaint after two previous amendments because a third amendment would be futile, as the policy did not provide coverage for loss of business income caused by the COVID-19 virus.³³ *Diesel Barbershop* also found that the plaintiff’s extra-contractual claims for breach of the Texas Insurance Code and breach of the duty and good faith of fair dealing failed where there was no coverage provided under the policy.³⁴

27. *Id.*

28. *Vizza Wash, LP v. Nationwide Mut. Ins. Co.*, No. 5:20-CV-00680-OLG, 2020 WL 6578417, at *8 (W.D. Tex. Oct. 26, 2020) (“For an insured to recover on a bad-faith insurance claim when the insurer has properly denied coverage for the claim, the insured must demonstrate that the insurer has committed an injury independent of the policy claim. [citations omitted] Similarly, an insured cannot recover any damages based on an insurer’s statutory violation unless the insured establishes a right to receive benefits under the policy or an independent injury caused by the insurer’s conduct.”) (citing *Republic Ins. Co. v. Stoker*, 903 S.W.2d 338, 341 (Tex. 1995); *USAA Tex. Lloyds Co. v. Menchaca*, 545 S.W.3d 479, 500 (Tex. 2018)).

29. *Id.*

30. *Id.* at *9.

31. *Id.*

32. *Id.*

33. *Id.*

34. *Diesel Barbershop, LLC v. State Farm Lloyds*, 479 F. Supp. 3d 353, 362 (W.D. Tex. Aug. 13, 2020).

III. THE DUTY TO DEFEND

A. WHETHER EXTRINSIC EVIDENCE CAN BE CONSIDERED IN DETERMINING THE DUTY TO DEFEND

In order to determine whether a liability insurer has a duty to defend its insured against an underlying lawsuit, Texas state and federal courts apply the “eight-corners rule.”³⁵ Under this well-established rule, the duty to defend is determined by considering only the claims alleged in the “four-corners” of the underlying lawsuit’s petition or complaint and the coverage provided within the “four-corners” of the insurance policy.³⁶ Until 2020, the Texas Supreme Court had never expressly recognized any exception to the eight-corners rule that would allow consideration of “extrinsic evidence,” i.e., evidence outside of the pleading and the policy.³⁷ However, numerous intermediate Texas appellate and Texas federal courts employ exceptions to allow extrinsic evidence, particularly where the evidence pertains to a pure coverage question.³⁸ The courts have been inconsistent, though, regarding whether to recognize these exceptions and how to apply them.³⁹

As discussed in the 2020 *SMU Annual Texas Survey*, in March 2020, the Texas Supreme Court in *Richards v. State Farm Lloyds*, on a certified question from the U.S. Court of Appeals for the Fifth Circuit, refused to find that the eight-corners rule is inapplicable where the policy does not include a “groundless-claims clause.”⁴⁰ The supreme court declined to broadly address the eight-corners rule and any exceptions and instead addressed only the narrow certified question.⁴¹ The supreme court held that the “‘policy-language exception’ to the eight-corners rule articulated by the federal district court . . . is not a permissible exception under Texas law.”⁴² The supreme court specifically noted that it was expressing no opinion on the exception allowing for extrinsic evidence on coverage issues that do not overlap with the merits of the underlying suit, and that it was reserving comment on whether other policy language or other factual scenarios may justify the use of extrinsic evidence, as “[t]he varied circumstances under which such arguments for the consideration of evidence may arise are beyond imagination.”⁴³

35. *State Farm Lloyds v. Richards*, 784 Fed. App’x 247, 250 (5th Cir. 2019).

36. *State Farm Lloyds v. Richards*, 966 F.3d 389, 392 (5th Cir. 2020).

37. *Loya Ins. Co. v. Avalos*, 610 S.W.3d 878, 881 (Tex. 2020).

38. *See Atain Specialty Ins. Co. v. Galvestonian Condo. Ass’n*, No. 3:16-CV-00329, 2020 U.S. Dist. LEXIS 59784, at *16 n.9 (S.D. Tex. Apr. 6, 2020); *Richards*, 784 Fed. App’x at 251–52.

39. *See Richards v. State Farm Lloyds*, 597 S.W.3d 492, 496–97 (Tex. 2020); *Atain Specialty Ins.*, 2020 U.S. Dist. LEXIS, at *16–17 (both citing state appellate cases that differ on whether to follow the 5th Circuit’s *Northfield* exception to the eight-corners rule).

40. *See J. Price Collins, Janet Tolbert, & Ashley Gilmore, Insurance Law*, 6 SMU ANN. TEX. SURV. 167, 171–72 (2020); *Richards*, 597 S.W.3d at 493.

41. *Richards*, 597 S.W.3d at 497.

42. *Id.* at 500.

43. *Id.*

In May 2020, just two months after *Richards*, the Texas Supreme Court, in *Loya Insurance Co. v. Avalos*, recognized for the first time an exception to the eight-corners rule.⁴⁴ The supreme court held that, in determining whether an insurer has a duty to defend, a court may consider extrinsic evidence that an insured and a third party suing the insured colluded to make false factual representations in order to secure a defense and coverage that would otherwise not exist.⁴⁵

Karla Flores Guevara (Guevara) was insured under an auto policy issued by Loya Insurance Company (Loya).⁴⁶ The policy explicitly excluded Guevara's husband, Rodolfo Flores (Flores), as an excluded driver.⁴⁷ While operating Guevara's automobile, Flores struck an automobile occupied by Osbaldo Hurtado Avalos and Antonio Hurtado (the Hurtados).⁴⁸ Although Flores was the driver at fault, Guevara, Flores, and the Hurtados reported to the police and Loya that Guevara was driving the vehicle that collided with the Hurtados.⁴⁹

The Hurtados sued Guevara, alleging that her negligence caused the accident.⁵⁰ Loya appointed defense counsel to defend Guevara.⁵¹ During discovery, Guevara told her attorney that Flores was actually driving the vehicle at the time of the accident.⁵² Loya responded by denying coverage and withdrawing a defense from Guevara.⁵³ A judgment was ultimately rendered against Guevara.⁵⁴ The Hurtados, as assignees of Guevara, then filed suit against Loya and alleged that Loya breached its duty to defend Guevara.⁵⁵ Loya counterclaimed for breach of contract, fraud, and a declaration that it had no duty to defend Guevara because Flores was an excluded driver.⁵⁶ Loya moved for summary judgment and provided as support Guevara's deposition testimony in the coverage lawsuit against Loya in which Guevara admitted that Flores was driving the car at the time of the accident.⁵⁷ The trial court granted Loya's motion for summary judgment.⁵⁸

On appeal to the Fourth San Antonio Court of Appeals, the Hurtados contended that summary judgment was improper because the trial court failed to evaluate Loya's duty to defend pursuant to the eight-corners

44. See *Loya Ins. Co. v. Avalos*, 610 S.W.3d. 878, 879 (Tex. 2020).

45. *Id.* at 884.

46. *Id.* at 880.

47. *Id.*

48. *Id.*

49. *Id.*

50. *Id.*

51. *Id.*

52. *Id.*

53. *Id.*

54. *Id.*

55. *Id.*

56. *Id.*

57. *Id.*

58. *Id.*

rule.⁵⁹ The appellate court agreed and reversed the trial court.⁶⁰

The Texas Supreme Court noted that it had applied the eight-corners rule numerous times since 1965.⁶¹ Although the supreme court had not recognized any exceptions to the rule, it had indicated twice before that collusive fraud by the insured might be the basis for an exception.⁶² The supreme court observed that there was conclusive, undisputed evidence that Flores, an excluded driver, and not Guevara, was driving the car.⁶³ It was also undisputed that the Hurtados agreed with Guevara and Flores to make false statements regarding who was driving in order to ensure that there would be coverage and the insurer would have a duty to defend.⁶⁴

The supreme court found that, in light of the contractual basis for the eight-corners rule, the rule did not preclude courts from considering such extrinsic evidence in determining whether there is a duty to defend.⁶⁵ The insurer did not agree to, and the insured did not pay for, a duty to defend the insured against fraudulent allegations that the insured had a role in creating.⁶⁶ “Thus, an insurer owes no duty to defend when there is conclusive evidence that groundless, false, or fraudulent claims against the insured have been manipulated by the insured’s own hands in order to secure a defense and coverage where they would not otherwise exist.”⁶⁷ Accordingly, the supreme court held that “[i]n determining an insurer’s duty to defend, a court may consider extrinsic evidence regarding whether the insured and a third party suing the insured colluded to make false representations of fact in that suit for the purpose of securing a defense and coverage where they would not otherwise exist.”⁶⁸ Because the trial court correctly determined that the extrinsic evidence conclusively proved collusive fraud, the supreme court reversed the court of appeals and reinstated the trial court’s summary judgment in favor of the insurer.⁶⁹

The Texas Supreme Court’s refusal in *Richards* to recognize broader exceptions to the eight-corners rule, despite many Texas appellate courts and federal courts applying exceptions (such as the *Northfield* exception), will continue to create uncertainty in determining whether a duty to defend is owed in the face of extrinsic evidence demonstrating that a claim is ultimately not covered.⁷⁰ However, *Loya* reflects for the first time the supreme court’s willingness to allow the use of extrinsic evidence to de-

59. *Id.*

60. *Id.*

61. *Id.* at 881.

62. *Id.*

63. *Id.* at 882.

64. *Id.*

65. *Id.*

66. *Id.*

67. *Id.*

68. *Id.* at 884.

69. *Id.*

70. See generally *Northfield Ins. Co. v. Loving Home Care*, 363 F.3d 523 (5th Cir. 2004).

termine the duty to defend, albeit under very narrow circumstances. It remains to be seen whether *Loya* is an anomaly or a precursor to further, and perhaps incremental, relaxation of the eight-corners rule by the supreme court. Significantly, the supreme court has not rejected the *Northfield* exception. Therefore, at least in federal courts, parties may still rely on extrinsic evidence when the elements of *Northfield* are satisfied.

IV. U.S. DISTRICT COURT FOR THE NORTHERN DISTRICT
OF TEXAS HOLDS THAT CLAIM AGAINST
MANUFACTURER FOR FAILURE TO
HONOR ROOF WARRANTY
ALLEGED “OCCURRENCE” UNDER ROOF
MANUFACTURER’S COMMERCIAL GENERAL LIABILITY
POLICIES BUT WAS EXCLUDED UNDER “YOUR WORK” AND
“YOUR PRODUCT” EXCLUSIONS

In *Siplast, Inc. v. Employers Mutual Casualty Co.*, the U.S. District Court for the Northern District of Texas held that a claim brought against a roof manufacturer for failing to honor its roof warranty alleged an “occurrence” under the manufacturer’s Commercial General Liability (CGL) policies, but the claim was excluded from coverage by the “Your Work” and “Your Product” exclusions in the policies.⁷¹

Siplast, Inc. (Siplast) was a developer and manufacturer of waterproofing and roofing systems.⁷² The defendant, Employers Mutual Casualty Company (EMCC), insured Siplast under CGL policies issued annually from 2012 to 2017 (Policies).⁷³

In October 2018, Cardinal Spellman High School, the Archdiocese of New York, and the Catholic High School Association (collectively the Archdiocese) filed a lawsuit against Vema Enterprises (Vema) and Siplast in New York state court (Underlying Suit).⁷⁴ According to the Complaint in the Underlying Suit (Underlying Complaint), in 2011, Vema and the Archdiocese entered into an agreement under which Vema would provide and install a new roof at the Cardinal Spellman High School (High School).⁷⁵ The roof membrane that Vema installed was manufactured by Siplast. Siplast provided a Roof/Membrane System Guarantee (Siplast Guarantee) that warranted that the roof membrane and system (Roof) would remain watertight for twenty years or Siplast would repair the Roof at Siplast’s expense.

According to the Underlying Complaint, in November 2016, High School employees noticed water damage to ceiling tiles throughout the High School after a rainstorm.⁷⁶ Siplast referred the Archdiocese to a

71. *Siplast, Inc. v. Emps. Mut. Cas. Co.*, No. 3:19-CV-1320-E, 2020 WL 5747869, at *6 (N.D. Tex. Sept. 25, 2020).

72. *Id.* at *1.

73. *Id.*

74. *Id.*

75. *Id.* at *3.

76. *Id.*

designated roofing contractor to fix the leaks and damage. Notwithstanding the contractor's repair work, there continued to be additional water leaks and damage at the High School. At a meeting with Archdiocese officials, Siplast admitted the Roof had problems that required correction.⁷⁷ At a subsequent meeting with Vema and the Archdiocese, Vema advised that any damage or leaks were solely Siplast's responsibility under the Siplast Guarantee.⁷⁸

The Underlying Complaint alleged that, in May 2017, Siplast advised the Archdiocese that it would hire a contractor to repair the leaks.⁷⁹ Siplast subsequently told the Archdiocese that Siplast's earlier attempts to repair were temporary and that Siplast would not make any permanent improvements to the Roof under the Siplast Guarantee.⁸⁰ The Archdiocese's consultant found that there were problems with the materials and workmanship in the Roof and the Roof had to be replaced.⁸¹ The Archdiocese in the Underlying Suit (Underlying Plaintiffs) asserted a breach of guarantee claim against Siplast.⁸²

EMCC denied defense and indemnity to Siplast for the Underlying Suit.⁸³ In response, Siplast filed a suit (Coverage Suit) against EMCC for declaratory relief, breach of contract, and violations of the Texas Insurance Code.⁸⁴ EMCC filed a counterclaim seeking a declaratory judgment that EMCC was not required to defend or indemnify Siplast from the Underlying Suit.⁸⁵

Both parties filed motions for summary judgment in the Coverage Suit.⁸⁶ In its motion for summary judgment, EMCC contended that Siplast failed to meet its burden to prove that relief sought by the Underlying Plaintiff was for an "occurrence" as the Policies defined that term.⁸⁷ The Policies defined "occurrence" in relevant part as an "accident."⁸⁸ "Accident" is interpreted by Texas courts to mean losses caused by negligence.⁸⁹ EMCC claimed that the Underlying Lawsuit alleged that Siplast breached the Siplast Guarantee, but that Siplast's breach was intentional—not negligent.⁹⁰ EMCC argued alternatively that the Your Work and Your Property exclusions, which excluded coverage for "property damage" to Siplast's work or product, excluded coverage.⁹¹ In its motion for partial summary judgment, Siplast asserted that the Archdiocese's

77. *Id.*

78. *Id.*

79. *Id.*

80. *Id.*

81. *Id.*

82. *Id.* at *4.

83. *Id.*

84. *Id.* at *1

85. *Id.* at *2.

86. *Id.*

87. *Id.* at *4.

88. *Id.*

89. *Id.*

90. *Id.*

91. *Id.* at *5.

claims were predicated on an occurrence because there were allegations of damage due to faulty products and work.⁹² There was no allegation that Siplast intended or expected damage.⁹³

The district court concluded that the property damage alleged in the Underlying Suit was caused by defects in the Roof's workmanship and materials.⁹⁴ The Underlying Complaint did not allege that Siplast intended or expected the Roof to fail.⁹⁵ The Archdiocese's legal theory for breach of the Siplast Guarantee was irrelevant.⁹⁶ Therefore, the court held that the Underlying Complaint alleged that an accident or "occurrence" caused "property damage" alleged by the Archdiocese.⁹⁷

With respect to the Your Work and Your Property Exclusions in the Policies, EMCC argued that the Archdiocese only sought the cost to replace the Roof, not damages resulting from the Roof.⁹⁸ Siplast countered that the Underlying Complaint alleged property damage to the High School's interior, such as ceiling tiles that were damaged by water.⁹⁹ The district court found that the Archdiocese did not assert any claim for damage to the High School caused by the Roof other than damage to the Roof itself.¹⁰⁰ The Archdiocese's sole claim against Siplast was for Siplast's refusal to honor the Siplast Guarantee and replace the Roof.¹⁰¹ As a result of refusal, the Archdiocese would be forced to spend approximately \$5 million to replace the Roof.¹⁰² The Your Work Exclusion excluded coverage for the cost to repair Siplast's work.¹⁰³ Accordingly, because the Archdiocese was seeking damages from Siplast that were excluded by the Your Work and Your Product Exclusions, the Court found that EMCC had no duty to defend Siplast.¹⁰⁴ Because EMCC had no duty to defend Siplast, EMCC thus had no duty to indemnify Siplast from the Underlying Suit.¹⁰⁵

Siplast underscores the need for insurers and their counsel to closely examine the allegations of the underlying lawsuit before making a determination as to the insurer's defense and indemnity obligations. Like the policies in *Siplast*, many modern CGL policies state that "[t]his insurance applies . . . only if: [t]he 'bodily injury' or 'property damage' is caused by an 'occurrence.'"¹⁰⁶ These policies do not explicitly state that an insured's conduct must be an "accident" or "occurrence." Thus, when a petition or

92. *Id.* at *4.

93. *Id.*

94. *Id.* at *5.

95. *Id.*

96. *Id.*

97. *Id.*

98. *Id.* at *6.

99. *Id.*

100. *Id.*

101. *Id.*

102. *Id.*

103. *Id.*

104. *Id.*

105. *Id.* at *7.

106. *Id.* at *4.

complaint alleges that an insured has committed intentional conduct, insurers and their counsel must carefully consider whether the insured's intentional conduct is alleged to be the true cause of the property damage before denying defense and indemnity based on no occurrence. Additionally, the mere allegation in the petition or complaint of property damage to property other than the insured's work or product does not mean the Your Work and Your Product exclusions are inapplicable. If the plaintiff is not seeking damages from the insured for property damage to property other than the insured's work or product, the Your Work and Your Product exclusions may still apply, precluding the insurer from having a duty to defend and indemnify.

V. U.S. COURT OF APPEALS FOR THE FIFTH CIRCUIT
HOLDS THAT “PROPERTY DAMAGE” OCCURED
WHEN CONTRACTOR DAMAGED
ELECTRICAL WIRING, NOT WHEN
HOME WAS LATER DAMAGED BY FIRE

In *Gonzalez v. Mid-Continent Casualty Co.*, the U.S. Court of Appeals for the Fifth Circuit held that, under a CGL policy, where a fire damaged a home after the policy period—but the fire was allegedly caused by a contractor who damaged the home's electrical wiring during the policy period—the “property damage” occurred during the policy period.¹⁰⁷

In the summer of 2013, Gilbert Gonzalez (Gonzalez) was hired by Norman Hamilton (Hamilton) to install new siding on Hamilton's home.¹⁰⁸ Mid-Continent Casualty Company (Mid-Continent) issued a CGL policy to Gonzalez, which was in effect from July 2012 to June 2013 and renewed until June of 2014 (collectively, the Policy).¹⁰⁹ A fire damaged Hamilton's home in December 2016.¹¹⁰ Hamilton and his insurer filed suit in Texas state court against Gonzalez (Underlying Suit), alleging that Gonzalez caused the fire by negligently hammering nails through the electrical wiring in the home during installation of the siding.¹¹¹

Mid-Continent refused to defend or indemnify Gonzalez, so Gonzalez sued Mid-Continent in Texas state court (Coverage Suit).¹¹² After removing the Coverage Suit to federal court, Mid-Continent filed a motion for summary judgment.¹¹³ Mid-Continent's motion was denied and the federal court entered partial final judgment in favor of Gonzalez, holding that Mid-Continent had a duty to defend him.

Gonzalez's Policy stated in relevant part that “[t]his insurance applies to . . . ‘property damage’ only if . . . [the] ‘property damage’ is caused by an ‘occurrence’ . . . [and the] ‘property damage’ occurs during the policy

107. *Gonzalez v. Mid-Continent Cas. Co.*, 969 F.3d 554, 554 (5th Cir. 2020).

108. *Id.* at 556.

109. *Id.*

110. *Id.*

111. *Id.*

112. *Id.*

113. *Id.* at 557–58.

period.”¹¹⁴ The term “occurrence” was defined in relevant part as “an accident,” and “property damage” was defined in relevant part as “[p]hysical injury to tangible property, including all resulting loss of use of that property. All such loss of use shall be deemed to occur at the time of the physical injury that caused it.”¹¹⁵

The Fifth Circuit found the petition in the Underlying Suit alleged an accident, and thus an “occurrence,” and also alleged “property damage.”¹¹⁶ The court then considered whether the property damage occurred during the policy period.¹¹⁷ It was undisputed that all of Gonzalez’s actions, including his hammering of the nails, took place during the policy period. Thus, the damage to the home’s electrical wiring occurred during the policy period. Moreover, the Underlying Petition alleged that the fire at the Home in 2016 related back to Gonzalez’s 2013 siding installation.¹¹⁸ Thus, the fire damage in 2016 was deemed to occur when Gonzalez damaged the electrical wires in 2013.¹¹⁹ Because the requirements of “occurrence,” “property damage,” and “property damage” that occurs during the policy period were met, the Fifth Circuit found that Mid-Continent had a duty to defend.¹²⁰

Mid-Continent also asserted that the Damage to Property Exclusions in the Policy, (j)(5) and (j)(6), excluded coverage.¹²¹ However, the Fifth Circuit noted that these exclusions only pertained to the particular part of the property on which the insured’s work was performed.¹²² Because Gonzalez was not hired to perform, and did not perform, work on the electrical wiring, exclusions (j)(5) and (j)(6) were inapplicable.¹²³ Accordingly, the Fifth Circuit affirmed the district court’s partial final judgment in Gonzalez’s favor on the duty to defend.¹²⁴

It is important to note that the Fifth Circuit did not find that it was the date of the accident (i.e., “occurrence”) that triggers coverage under the Policy. Rather, the court found that, in this particular instance, property damage occurred simultaneously with the insured’s accidental conduct because the insured’s conduct instantly damaged the wiring.¹²⁵ Because this property damage occurred during the policy period, coverage was triggered.¹²⁶

114. *Id.*

115. *Id.* at 558.

116. *Id.*

117. *Id.*

118. *Id.*

119. *Id.*

120. *Id.*

121. *Id.* at 560.

122. *Id.* at 561.

123. *Id.*

124. *Id.* at 562.

125. *See id.* at 560.

126. *See id.*

VI. U.S. DISTRICT COURT FOR THE WESTERN DISTRICT OF TEXAS HOLDS THAT, UNDER TEXAS PUBLIC POLICY, INSURER HAS NO OBLIGATION TO INDEMNIFY INSURED'S EMPLOYEE FOR PUNITIVE DAMAGES RESULTING FROM EMPLOYEE'S GROSS NEGLIGENCE

In *Frederking v. Cincinnati Insurance Co.*, the U.S. District Court for the Western District of Texas, San Antonio Division, held that Texas public policy barred an insurer from having an obligation to indemnify an employee of its insured for punitive damages awarded because of the employee's gross negligence in causing an automobile accident while intoxicated.¹²⁷

Richard Frederking (Frederking) sustained serious personal injuries after a vehicle driven by Carlos Sanchez (Sanchez) collided with Frederking's vehicle (Accident).¹²⁸ Sanchez pled guilty to driving while intoxicated (DWI) and admitted he caused the Accident.¹²⁹ Sanchez was operating a vehicle owned by his employer, Advantage Plumbing Services (Advantage), at the time of the Accident. Advantage had assigned the vehicle to Sanchez for work. Despite the suspension of his driver's license, Sanchez told Advantage that he had a valid license. Sanchez had four prior DWI convictions.¹³⁰ Cincinnati had issued an insurance policy to Advantage (Policy).¹³¹

Frederking sued Sanchez and Advantage in Texas state court (Underlying Suit), asserting claims of negligence and gross negligence against Sanchez, and negligent entrustment and respondeat superior against Advantage.¹³² In the Underlying Suit, Cincinnati defended Sanchez and Advantage.¹³³ Sanchez was found negligent and grossly negligent by the jury. Advantage was found liable for negligent entrustment. The jury awarded compensatory damages to Frederking against Sanchez and Advantage. The jury awarded \$207,550.00 to Frederking for punitive damages against Sanchez.¹³⁴ Cincinnati satisfied the compensatory damages award but refused to pay the punitive damages award. Frederking then sued Cincinnati in the U.S. District Court for the Western District of Texas, San Antonio Division, as a third-party beneficiary to the Policy.¹³⁵ Frederking sued Cincinnati for breach of contract and a declaration that Cincinnati had to pay the award of punitive damages.

Cincinnati moved for summary judgment, in part, on the ground that Texas public policy barred an obligation by Cincinnati to indemnify

127. *Frederking v. Cincinnati Ins. Co.*, 447 F. Supp. 3d 577, 582 (W.D. Tex. 2020).

128. *Id.* at 578.

129. *Id.*

130. *Id.*

131. *Id.*

132. *Id.*

133. *Id.*

134. *Id.*

135. *Id.*

Sanchez for the punitive damages award.¹³⁶ According to Cincinnati, Texas public policy made Sanchez solely responsible for the punitive burdens of his gross negligence.¹³⁷ Thus, the punitive damages were not insurable under the Policy.¹³⁸ Frederking responded that excusing Cincinnati from its contractual obligations that were freely negotiated would violate Texas public policy.¹³⁹

In *Fairfield Co. v. Stephens Martin Paving, L.P.*, the Texas Supreme Court previously provided guidance on insurability of punitive damages.¹⁴⁰ *Fairfield* established a two-step test to determine whether punitive damages were insurable: (1) determine whether the policy's plain language covers punitive damages, and (2) if so, decide whether Texas public policy permits coverage under the circumstances of the underlying lawsuit.¹⁴¹ Absent legislative decision, the interests in enforcing an agreement must be weighed against the public policy interest in not enforcing the agreement.¹⁴² In assessing the public policy interest, the courts should consider the purpose of punitive damages to punish the wrongdoer and deter such conduct by others.¹⁴³

The district court in *Frederking* observed that the U.S. Court of Appeals for the Fifth Circuit's decision in *Minter v. Great American Insurance Co.*¹⁴⁴ addressed whether Texas public policy precluded an employer's insurance policy from covering punitive damages awarded for the gross negligence of an employee whose intoxicated driving caused injury.¹⁴⁵ While *Minter* is an unpublished opinion and not binding on the district court, it is instructive and persuasive in how to apply *Fairfield* to the facts of this case.¹⁴⁶ As in *Minter*, Sanchez pled guilty to DWI in connection with the Accident, admitted he was responsible for causing injuries, and was a repeat DWI offender.¹⁴⁷ The jury found the punitive damages were justified solely against Sanchez, not Advantage, because of Sanchez's extreme and avoidable conduct.¹⁴⁸ Allowing Advantage's Policy to cover the punitive damages would not further the punitive or deterrent purposes of punitive damages under Texas law because the burden would fall entirely on the insurer and the insured, not the tortfeasor.¹⁴⁹ It would frustrate the significant public policy of deterring and punishing

136. *Id.* at 579.

137. *Id.*

138. *Id.*

139. *Id.* at 579–80.

140. *See generally* *Fairfield Co. v. Stephens Martin Paving, L.P.*, 246 S.W.3d 653 (Tex. 2008).

141. *Frederking*, 447 F. Supp. 3d at 580 (citing *Fairfield*, 246 S.W.3d. at 655).

142. *Id.* at 581.

143. *Id.*

144. 394 F. App'x 47, 50 (5th Cir. 2010).

145. *Frederking*, 447 F. Supp. 3d at 582.

146. *Id.*

147. *Id.* at 582–83.

148. *Id.* at 583.

149. *Id.*

drivers who choose to drive while intoxicated and injure others.¹⁵⁰ Moreover, Advantage, not Sanchez, negotiated the policy and paid the premiums.¹⁵¹ To punish and deter Sanchez's grossly negligent conduct, Sanchez, not Cincinnati, must be held responsible for the punitive damages.¹⁵²

Therefore, the district court held that Texas public policy prohibited Cincinnati from having to indemnify Sanchez for the punitive damages awarded because of Sanchez's gross negligence.¹⁵³ Accordingly, the district court granted Cincinnati's motion for summary judgment and dismissed Frederking's claims with prejudice.¹⁵⁴

Frederking represents a significant application of the *Fairfield* test for determining the insurability of punitive damages where there is gross negligence. However, it remains to be seen whether Texas courts will rely on *Frederking* to find that punitive damages in gross negligence cases not involving intoxicated driving are not insurable. Arguably, any punitive damages awarded for grossly negligent or reckless conduct for which there is a strong public interest to punish and deter should not be insurable.

VII. U.S. DISTRICT COURT FOR THE WESTERN DISTRICT
OF TEXAS DISMISSES INSURED'S BREACH OF
CONTRACT ACTION AGAINST
UNDERINSURED MOTORIST
INSURER BECAUSE NO LIABILITY JUDGMENT WAS
OBTAINED, BUT PERMITS INSURED TO PROCEED WITH
DECLARATORY JUDGMENT ACTION AGAINST
UNDERINSURED MOTORIST INSURER

In *Ibarra v. Allstate Fire & Casualty Insurance Co.*, the U.S. District Court for the Western District of Texas dismissed an insured's claim against his underinsured motorist (UIM) insurer for breach of contract for the insurer's failure to pay UIM benefits, because the insured had not obtained a judgment that the responsible driver was liable and that the insured was entitled to damages.¹⁵⁵ However, the district court allowed the insured to proceed to litigate the tortfeasor's liability and damages through a declaratory judgment action against the insurer.¹⁵⁶

Ibarra filed suit in the district court against his UIM Insurer, Allstate Fire and Casualty Insurance Company (Allstate).¹⁵⁷ Ibarra alleged that an underinsured driver, Joel Saucedo (Saucedo), negligently caused seri-

150. *Id.*

151. *Id.*

152. *Id.*

153. *Id.*

154. *Id.*

155. *Ibarra v. Allstate Fire & Cas. Ins. Co.*, No. SA:20-CV-00280-JKP, 2020 WL 3259806, at *3 (W.D. Tex. June 16, 2020).

156. *Id.* at *1, *3.

157. *Id.* at *1.

ous bodily injury to Ibarra during an automobile accident. However, Allstate rejected Ibarra's UIM claim. After Allstate filed a 12(b)(6) motion to dismiss all of Ibarra's claims, Ibarra filed an amended complaint. The amended complaint set forth a breach of contract claim for Allstate's alleged failure to pay UIM benefits and, alternatively, sought a declaratory judgment under the Federal Declaratory Judgment Act as to the amount of UIM benefits Ibarra was entitled to obtain.¹⁵⁸

Relying on the Texas Supreme Court's decision in *Brainard v. Trinity Universal Insurance Co.*,¹⁵⁹ Allstate argued that it was not contractually obligated to pay Ibarra UIM benefits until Ibarra obtained a judgment establishing Saucedo's underinsured status and liability.¹⁶⁰ Because there was no such judgment, Ibarra's breach of contract claim had to be dismissed for failure to state a claim.¹⁶¹ However, Allstate acknowledged that Ibarra's alternative demand for relief under the Federal Declaratory Judgment act was proper.¹⁶² Ibarra argued that the Sixth Texarkana Court of Appeal's decision in *In re Koehn*¹⁶³ permitted Ibarra to pursue a breach of contract claim.¹⁶⁴

The U.S. District Court for the Western District of Texas found that, under *Brainard*, the UIM insurer had no contractual obligation to pay UIM benefits until the insured obtained a judgment establishing the alleged tortfeasor's underinsured status and liability.¹⁶⁵ This judgment could be obtained against the tortfeasor in a coverage suit against the UIM insurer.¹⁶⁶ However, under established case law from the Texas federal district courts, if Ibarra opted to proceed directly against Allstate, he could obtain a judgment as to the tortfeasor's liability and Ibarra's damages through a declaratory judgment action, but could not obtain a judgment on a breach of contract claim.¹⁶⁷ Until Ibarra obtained a judgment establishing Saucedo's liability and that Ibarra was entitled to damages, and Allstate denied payment of UIM benefits after such judgment was rendered, Allstate did not breach the UIM insurance contract.¹⁶⁸

Therefore, the district court held Ibarra's breach of contract claim against Allstate for failure to pay UIM benefits was premature and not ripe for adjudication.¹⁶⁹ The district court thus had no subject matter jurisdiction over the unripe breach of contract claim.¹⁷⁰ Accordingly, the district court dismissed the breach of contract claim without prejudice for

158. *Id.*

159. 216 S.W.3d 809, 818 (Tex. 2006).

160. *Ibarra*, 2020 WL 3259806, at *1.

161. *Id.*

162. *Id.*

163. 86 S.W.3d 363, 368 (Tex. App.—Texarkana 2002, no pet.).

164. *Ibarra*, 2020 WL 3259806, at *2.

165. *Id.*

166. *Id.*

167. *Id.* at *3.

168. *Id.*

169. *Id.*

170. *Id.*

lack of subject matter jurisdiction.¹⁷¹ However, the district court held that Ibarra's suit against Allstate would proceed as to the request for declaratory relief under the Federal Declaratory Judgment Act.¹⁷² Thus, while an insured may not successfully recover against an insurer on contractual and extra-contractual claims until there is a judgement establishing that the insured is entitled to recover damages from the UIM, the district court determined that the insured may establish its entitlement to damages from the UIM in a declaratory judgment action against the insured. If, after receiving such a declaratory judgment, the insurer refuses to pay UIM benefits owed, the insured may proceed at that time with breach of contract and extra-contractual claims.

VIII. EXTRA-CONTRACTUAL DAMAGES

A. U.S. COURT OF APPEALS FOR THE FIFTH CIRCUIT HOLDS THAT RECOVERY UNDER THE TEXAS PROMPT PAYMENT OF CLAIMS ACT ONLY REQUIRES LIABILITY UNDER THE POLICY AND FAILURE TO COMPLY WITH THE ACT'S DEADLINES

In *Agredano v. State Farm Lloyds*, the U.S. Court of Appeals for the Fifth Circuit held that insureds: (1) could recover 18% interest and attorney's fees under the Texas Prompt Payment of Claims Act (TPPCA) even without specifically citing to the TPPCA or its language, and (2) insureds did not need to prove the insurer acted wrongfully or in bad faith to recover under the TPPCA, but only needed to prove liability under the policy and violation of the TPPCA's deadlines.¹⁷³

State Farm Lloyds (State Farm), the homeowners' insurer of Jesus and Margaret Agredano (Agredanos), denied the Agredanos' claim for wind-storm damage to their home.¹⁷⁴ The Agredanos sued State Farm for breach of contract and extra-contractual causes of action.¹⁷⁵ The district court granted summary judgment in favor of State Farm on all claims except for the Agredanos' claim for breach of contract.¹⁷⁶ Ultimately, the district court held that the failure of the Agredanos to specifically plead relief under the TPPCA precluded their recovery of the requested 18% statutory interest and attorney's fees and entered judgment only for the breach of contract damages found by the jury, along with the regular pre-judgment and post-judgment interest.¹⁷⁷ The Agredanos appealed.¹⁷⁸

On appeal, State Farm argued that because the Agredanos did not cite the TPPCA or quote the statute's language, they did not plead a claim for

171. *Id.*

172. *Id.*

173. *Agredano v. State Farm Lloyds*, 975 F.3d 504, 504–07 (5th Cir. 2020).

174. *Id.* at 504–05.

175. *Id.* at 505.

176. *Id.*

177. *Id.*

178. *Id.*

TPPCA interest.¹⁷⁹ The Fifth Circuit observed that the Agredanos pled that they were entitled to an “18% [p]enalty [i]nterest pursuant to Ch. 542 of the Texas Insurance Code” and “[a]ttorney’s fees.”¹⁸⁰ While the pleading could have been more explicit, the Fifth Circuit stated that the *Twombly/Iqbal* “plausibility” standard does not generally require magic words or detailed facts.¹⁸¹ The court determined that the statutory interest claim was not improperly pled because the claim was not speculative.¹⁸² Further, State Farm was clearly aware of the Agredanos’ claims because it did not file a Rule 12(e) motion for a more definite statement arguing that it did not understand the pleadings, the TPPCA was noted in the Agredanos’ discovery responses, and State Farm argued in its own summary judgment motion that the Agredanos asserted causes of action based on Chapter 542 of the Texas Insurance Code.¹⁸³

The Fifth Circuit then considered the question addressed in its prior unpublished and non-precedential opinion, *Chavez v. State Farm Lloyds*:¹⁸⁴ whether violation of the bad faith provisions of the Texas Insurance Code is a prerequisite to recovery under the TPPCA.¹⁸⁵ While the *Chavez* court held that, upon dismissal of bad faith insurance code claims, recovery under § 542.060 of the Texas Insurance Code becomes impossible, the Fifth Circuit stated that this holding was contrary to subsequent Texas Supreme Court cases and was no longer good law.¹⁸⁶ In *Barbara Technologies Corp. v. State Farm Lloyds*, the Texas Supreme Court held that “[n]othing in the TPPCA would excuse an insurer from liability for TPPCA damages if it was liable under the terms of the policy but delayed payment beyond the applicable statutory deadline.”¹⁸⁷ The supreme court found that “[t]o prevail under a claim for TPPCA damages under § 542.060, the insured must establish: (1) the insurer’s liability under the insurance policy, and (2) that the insurer has failed to comply with one or more sections of the TPPCA in processing or paying the claim.”¹⁸⁸

The Fifth Circuit observed that the Texas Supreme Court treats the TPPCA as a strict liability provision.¹⁸⁹ Thus, a plaintiff does not need to prove that the insurer acted wrongfully or in bad faith.¹⁹⁰ Rather, the statute only requires two things: (1) liability under the policy, and (2) a

179. *Id.*

180. *Id.* at 506.

181. *Id.*; see also *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009); *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007).

182. *Agredano*, 975 F.3d at 506.

183. *Id.*

184. 746 F. App’x 337, 343 (5th Cir. 2018).

185. *Agredano*, 975 F.3d at 506.

186. *Id.* at 507.

187. *Id.* (quoting *Barbara Techs. Corp. v. State Farm Lloyds*, 589 S.W.3d 806, 819 (Tex. 2019)).

188. *Id.* (quoting *Barbara Techs.*, 589 S.W.3d at 813).

189. *Id.*

190. *Id.*

failure to comply with the timing requirements set forth in the TPPCA.¹⁹¹ Because the Agredanos were successful on their breach of contract claim, and the district court erred in holding that *Chavez* barred the Agredanos' claims for 18% penalty interest and attorney's fees under the TPPCA, the Fifth Circuit reversed and remanded.¹⁹²

IX. APPRAISAL

A. THE U.S. DISTRICT COURT FOR THE NORTHERN DISTRICT OF TEXAS VOIDS AN APPRAISAL AWARD AND STRIKES THE APPOINTED UMPIRE BECAUSE OF THE INSURED'S FAILURE TO SATISFY THE SWORN PROOF OF LOSS CONDITION PRECEDENT

In *GuideOne Mutual Insurance Co. v. First Baptist Church of Brownfield*, First Baptist Church of Brownfield (First Baptist) submitted a claim for hailstorm damage to its property.¹⁹³ After its investigation, First Baptist's insurer, GuideOne Mutual Insurance Company (GuideOne) paid the insured \$38,000.00.¹⁹⁴ Disputing the value of the loss, the insured invoked the appraisal clause in the policy issued by GuideOne (Policy). GuideOne informed First Baptist that this was premature, and GuideOne made its first request for a sworn proof of loss. First Baptist requested that a state court appoint an umpire. After the court appointed an umpire, GuideOne hired its own appraiser. First Baptist never sent GuideOne a sworn proof of loss. The appraisers' evaluations were over \$1 million apart; the umpire then issued an award of \$918,085.38.¹⁹⁵ The umpire and First Baptist's appraiser signed the award, but GuideOne's appraiser did not.¹⁹⁶

GuideOne moved for summary judgment in the U.S. District Court for the Northern District of Texas seeking a declaratory judgment: (1) finding the appraisal award was not made in substantial compliance with the policy and/or was not made with proper authority; (2) striking the appointed umpire; and (3) setting aside the appraisal award as void.¹⁹⁷ The district court ultimately granted the motion for summary judgment because the appraisal award was made without authority and not in substantial compliance with the Policy, and GuideOne did not waive any condition precedent.¹⁹⁸

Texas courts often recognize three situations where a binding appraisal may be disregarded: "(1) when the award was made without authority;

191. *Id.*

192. *Id.*

193. *GuideOne Mut. Ins. Co. v. First Baptist Church of Brownfield*, No. 5:19-CV-086-H, 2020 WL 6268477, at *1 (N.D. Tex. Oct. 20, 2020).

194. *Id.*

195. *Id.*

196. *Id.*

197. *Id.* at *2.

198. *Id.* The court also found that the Declaratory Judgment Act was satisfied because the dispute was a judicially remediable right and not merely academic or moot. *Id.*

(2) when the award was the result of fraud, accident, or mistake; or (3) when the award was not made in substantial compliance with the terms of the contract.”¹⁹⁹ The first and third situation existed in *GuideOne*, and the court analyzed these two issues.²⁰⁰

The district court found that the first situation existed because First Baptist did not properly invoke the appraisal process by filing a sworn proof of loss, which was a condition precedent under the insurance contract.²⁰¹ A condition precedent is generally defined as “an event that must happen or be performed before a right can accrue to enforce an obligation.”²⁰² Under the Texas Supreme Court’s holding in *Paj, Inc. v. Hanover Insurance Co.*, an “insured’s failure to timely notify its insurer of a claim or suit does not defeat coverage if the insurer was not prejudiced by the delay.”²⁰³ The so-called notice-prejudice rule has been interpreted differently by Texas appellate and federal district courts, and the district court analyzed whether it applied to the case at bar.²⁰⁴ The district court reconciled the competing holdings and found they supported a finding that a sworn proof of loss is a condition precedent to invoking appraisals.²⁰⁵ Although the Policy’s language requiring a sworn proof of loss was not included in the appraisal clause, the district court read all of the parts of the Policy together to find that, taken as a whole, it is clear the proof of loss was a condition precedent.²⁰⁶ The district court reasoned that *Paj*’s notice-prejudice rule applies when the sworn proof of loss’s purpose is merely to serve as a *notice* of disagreement, but not when, as in the present case, the sworn proof of loss was intended to *quantify* the parties’ disagreement.²⁰⁷

Moreover, the district court found that the notice-prejudice rule was intended to avoid complete forfeiture of coverage as the result of an insured’s failure to provide timely notice of the loss to the insurer.²⁰⁸ Here, there was no potential forfeiture of coverage and GuideOne never challenged First Baptist’s coverage.²⁰⁹ Instead, GuideOne sought compliance with their agreement even after the loss was paid.²¹⁰ Consequently, the district court held that GuideOne did not need to demonstrate prejudice from First Baptist’s failure to provide a sworn proof of loss under the Policy.²¹¹

Next, the district court found that the appraisal award was not made in

199. *Id.* at *3.

200. *Id.*

201. *Id.*

202. *Id.* (quoting *Solar Applications Eng’g v. T.A. Operating Corp.*, 327 S.W.3d 104, 108 (Tex. 2010)).

203. *Id.* (quoting *Paj, Inc. v. Hanover Ins. Co.*, 243 S.W.3d 630, 636–37 (Tex. 2008)).

204. *Id.* at *4–8.

205. *Id.* at *6–7.

206. *Id.* at *6.

207. *Id.* at *7.

208. *Id.*

209. *Id.*

210. *Id.*

211. *Id.*

substantial compliance with the Policy's terms.²¹² First Baptist argued it satisfied the proof of loss provision by providing the same information through its appraisal; however, it failed to identify when that information was provided or argue whether it was timely.²¹³ While a proof of loss only requires substantial compliance, to be effective, it must occur within the time period allowed for furnishing the formal proof of loss.²¹⁴ The district court found that the request for a sworn proof of loss was made on February 21, 2018, and the appraisal was not compiled until June 28, 2018—127 days after the first request.²¹⁵ At a minimum, even if the appraisal contained the right information, it was sixty-seven days late, and the district court found that First Baptist did not substantially comply with the proof of loss provision.²¹⁶

Moreover, the district court found that First Baptist did not properly invoke the appraisal process because it sought appointment of an umpire prior to submitting a proof of loss.²¹⁷ Reading the Policy as a whole, the district court found that the proof of loss was necessary in the event of a loss, regardless of whether the parties sought to invoke appraisal because it provided substantive information that would allow the parties to determine whether appraisal was appropriate.²¹⁸ Therefore, without satisfying this condition precedent, First Baptist could not invoke the appraisal process under the terms of the agreement.²¹⁹ Because First Baptist did not comply with the proof of loss provision or generally cooperate with GuideOne, who did not hide the provision, the appointment of the umpire and the subsequent award were premature.²²⁰

Because “[t]he failure to perform a condition precedent may be waived by the failure to insist on performance,” the court then analyzed whether GuideOne waived the requirement of a sworn proof of loss.²²¹ While a policy's non-waiver clause is binding and enforceable and may be “some evidence of non-waiver,” it is not a complete bar to finding that a particular provision was indeed waived.²²² Here, the Policy at issue contained a non-waiver clause, which, under Texas law, created the presumption that GuideOne did not intend to relinquish its rights.²²³ First Baptist attempted to argue that GuideOne waived any condition precedent to the

212. *Id.* While normally this is an issue for the trier of fact because all material facts were undisputed, the court was able to determine that First Baptist did not substantially satisfy the proof of loss provision through substantial compliance. *Id.*

213. *Id.* at *8.

214. *Id.*

215. *Id.*

216. *Id.*

217. *Id.*

218. *Id.*

219. *Id.*

220. *Id.*

221. *Id.* (quoting *Farmer v. Holley*, 237 S.W.3d 758, 760 (Tex. App.—Waco 2007, pet. denied)).

222. *Id.* at *9 (quoting *Conn Credit I, L.P. v. TF LoanCo III, L.L.C.*, 903 F.3d 493, 503 (5th Cir. 2018); *Bott v. J.F. Shea Co.*, 388 F.3d 530, 533 (5th Cir. 2004)).

223. *Id.*

appraisal clause by selecting its appraiser and participating in the appraisal process.²²⁴ However, the district court rejected this argument, finding that First Baptist's brief failed to raise any legal arguments on the issue of waiver and thus failed to overcome the presumption created by the non-waiver provision.²²⁵ In addition, the district court noted that GuideOne insisted that a sworn proof of loss be provided on four separate occasions, suggesting that this would be enough to show that waiver did not occur.²²⁶

Thus, because the condition precedent was not fulfilled and GuideOne did not waive compliance, the district court held that the appraisal award was not entered with the appropriate authority and was not in substantial compliance with the Policy's terms.²²⁷ Therefore, GuideOne was entitled to judgment as a matter of law on its declaratory judgment action.²²⁸ Accordingly, the district court granted *GuideOne's* Motion for Summary Judgment, declared that the appraisal award was void, and struck the appointed umpire.²²⁹

Under *GuideOne*, where the insured has not submitted a proof of loss, an insurer would appear to have the option to prevent the appraisal from proceeding, or as happened in *GuideOne*, allow the appraisal to go forward and subsequently challenge an unfavorable appraisal award. However, one reason for the district court's decision was that GuideOne asked the insured four times to provide a proof of loss and the insured did not cooperate. Thus, insurers would be well-advised to make repeated demands for a proof of loss from their insureds.

224. *Id.*

225. *Id.*

226. *Id.*

227. *Id.*

228. *Id.* at *10.

229. *Id.*

