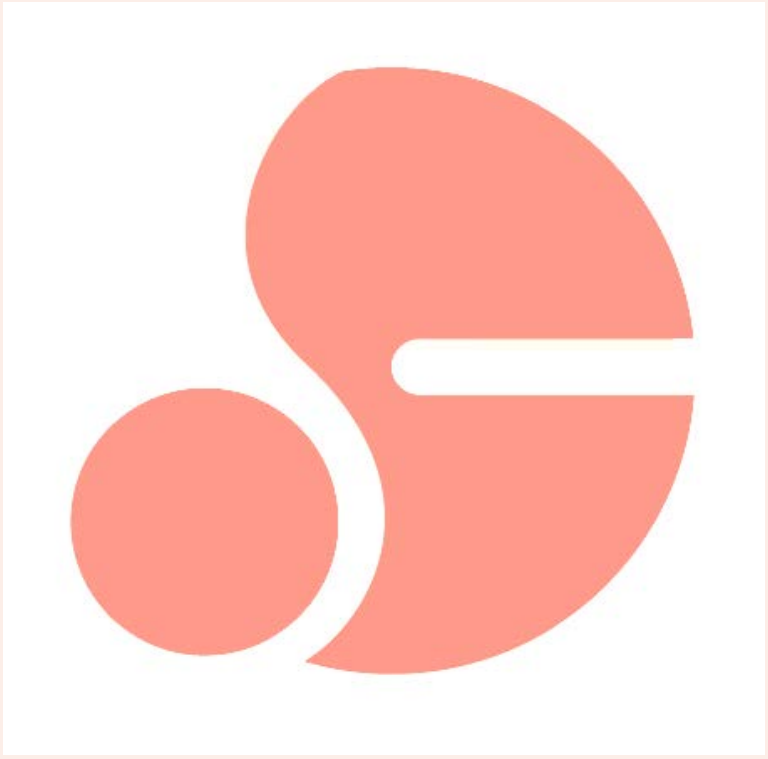
"IT'S YOUR PROBLEM, NOT MINE": Effective Risk Transfer from Contract Negotiations to Post-Loss Pursuit of Carriers

Presented by:

Blake S. Evans
Stephen Burnett
Schubert & Evans, P.C.



City of Dallas

June 26, 2014

City of Dallas

Primary Risk Transfer Mechanisms

- Indemnity from Vendor
  - Direct claim for coverage/defense against vendor under contract
  - Claim for coverage/defense under vendor's insurance policy
  - Direct defense from vendor's carrier

- Additional Insured status on vendor's insurance policy

Indemnity Provisions: Why are they important?

- An enforceable indemnity provision is the lynchpin to contractual liability coverage.
- "Legalese" and other (valid) complaints

> "**It is hard to imagine another set of legal terms with more soporific effect than indemnity, subrogation, contribution, co-obligation and joint tortfeasorship.** Perhaps because the words describe legal relationships between multiple parties, they are vaguely reminiscent of complex mathematical equations which, after all, also describe relationships, except in numbers rather than words – and for most of us, they are about as easy to understand. **Even lawyers find that words like 'indemnity' and 'subrogation' ring of obscure Martian dialect."**

Herrick Corp. v. Canadian Ins. Co. of California, 29 Cal.App.4th 753, 34 Cal.Rptr.844 (4th Dist. 1994).

Additional Insured v. Indemnitee

ADDITIONAL INSURED	INDEMNITEE
Must comply with policy conditions just like any insured (*i.e.,* notice, request for defense, etc.)	Not bound by policy conditions; not an insured
Insurer owes duties to AI just like any other insured; rights depend on the policy	Insurer owes no direct duty to them as it would an insured; rights depend on the contract with the insured
May be entitled to direct defense as an AI	Limited to recovering defense costs as part of overall indemnity claim v. insured Exceptions: - ISO GL forms – supplemental payment - Practical considerations
Standing to sue the carrier	No standing to sue carrier directly

Indemnity Provisions 101

- Enforceability varies dramatically from state to state
  - Which law applies?
    - Choice of law provision
    - Other factors (location of parties, where was contract negotiated/signed, place of performance)

- Generally, agreements are categorized by courts as one of three types:
  (1) broad form
  (2) intermediate form
  (3) limited form

- Many provisions are not easily categorized or mix elements of each "type"

Broad Form Indemnity Agreements

- Indemnitor indemnifies the indemnitee for
  (1) indemnitor's sole negligence;
  (2) indemnitee's sole negligence; and,
  (3) joint negligence of indemnitor and indemnitee
- Seeks to transfer *entire* risk of loss to indemnitor
- Numerous obstacles to enforcement
- Enforceability prohibited or severely restricted in many states

Intermediate Form Indemnity Agreements

- Indemnitor indemnifies the indemnitee, for:
  (1) indemnitor's sole negligence; and
  (2) joint negligence of indemnitor and indemnitee

- Indemnitor assumes all risk of loss except where indemnitee is solely at fault

- Source of numerous conflicts between indemnitor and indemnitee

- Frequently requires indemnitor to provide defense pending ultimate resolution

Limited Form (Comparative Fault) Indemnity Agreements

- Basically provides that each party will take care of their own negligence
- Will usually be enforced by courts
- May actually be less favorable than what jurisdiction provides

The Texas Two-Step

- Step 1:
  - Scope of the Agreement
  - Enforceability

- Step 2 (Pursuit of Coverage Under Indemnitor Policy – different from AI pursuit):
  - Does Coverage Exist?

Scope of Indemnity Agreements

- Is the claim within the scope of the Agreement?
  - Does the provision apply to the nature of the claim (*i.e.,* property damage, bodily injury, etc.)?
  - Who is the injured party (third-party stranger, employee of one of the parties, etc.) and does the indemnity include that category of persons?
  - What is the causal connection required between the indemnity right/obligation and work being performed by the contracting parties (*i.e.,* "caused by" or "resulting from" or "arising out of," etc.) and is that connection satisfied?
  - Does the indemnity provision build a fault-based question into the required analysis by, for example, only applying to cases of concurrent negligence and not applying to the indemnitee's sole negligence?

Issues in Analyzing Enforceability

- What degree of fault can be transferred?
- Can sole negligence be transferred?
- Special concerns regarding “construction” contracts
  - Anti-indemnity statutes / the Subcontractors’ Relentless Effort

Tex. Ins. Code 151.001

(Effective 1/1/12)

- Voids provisions in construction contracts requiring indemnity or additional insured status to party for its fault, negligence, or statutory/contractual breach.

- Effect:
  - Void broad form and intermediate indemnification provisions.
  - Companion additional insured requirements also void.
  - Exceptions:
    - Claims made by indemnitor's own employees or subcontractor below it against other party (maintain indemnity on "third party-over suits")
    - Residential construction (single family homes, townhomes, duplexes)
    - Multi-family residences / apartment and condominium complexes?
    - * * * **"PUBLIC WORKS PROJECTS OF MUNICIPALITIES"**

Enforceability Under Texas Law:

"We don't like liars, cheaters, and tricksters"

- "Fair Notice" Doctrine
  - (1) "Express Negligence" Rule
  - (2) "Conspicuousness" Requirement

- Caveat: Doctrine does not apply if indemnitor had "actual knowledge".

"Express Negligence" Rule

- Party seeking indemnity for its own negligence must state it specifically within the contract.
  - *Ethyl Corp. v. Daniel Construction*, 725 S.W.2d 705 (Tex. 1987);
  - *Dresser Industries, Inc. v. Page Petroleum, Inc.*, 53 S.W.2d 505 (Tex. 1993).

- Does not require use of the term "negligence".
  - *Banzhat v. ADT Sec. Sys. Southwest, Inc.*, 28 S.W.3d 180 (Tex.App. – Eastland 2000, pet. denied)

- **Correct inquiry:** whether parties made clear in agreement intent of the indemnitor to indemnify the indemnitee for its own acts of negligence.

"Express Negligence" Rule *(cont'd)*

- Example No. 1:
  - "Contractor shall indemnify and hold Owner harmless against any loss or damage to persons or property as a result of operations growing out of the performance of this contract and caused by the negligence or carelessness of Contractor, Contractor's employees, Subcontractors, and agents or licensees."
  - **NOT ENFORCEABLE**—*Ethyl Corp. v. Daniel Construction*, 725 S.W.2d 705 (Tex. 1987)

"Express Negligence" Rule *(cont'd)*

- Example No. 2:

"To the fullest extent permitted by law, Subcontractor shall indemnify, hold harmless, and defend Contractor ... from and against all claims, damages, losses, and expenses ... arising out of or resulting from the performance of Subcontractor's Work … provided that any such claim is caused in whole or in part by any negligent act or omissions of Subcontractor or anyone directly or indirectly employed by it or anyone for whose acts it may be liable regardless of whether it is caused in part by a party indemnified hereunder."

- **NOT ENFORCEABLE**—*Lee Lewis Construction, Inc. v. Harrison,* 64 S.W.3d 1 (Tex. App.—Amarillo 1999).

- Can't "dance around it" – must affirmatively, expressly mention indemnitee's negligence.

"Express Negligence" Rule *(cont'd)*

- Example No. 3:

"Application of indemnities. Except as otherwise provided in this contract, any indemnification and defense obligation in this contract applies regardless of

(1) the cause of or reason for any covered loss or liability;
(2) the sole, joint or concurrent negligence or other fault, whether active or passive, of the indemnified party; and
(3) whether the loss or liability results from actions of [Conoco], its agents or employees."

- **ENFORCEABLE—***Ayers Welding Co. v. Conoco, Inc.,* 243 S.W.3d 177 (Tex. App.—Houston [14th Dist.] 2007).

"Express Negligence" Rule *(cont'd)*

- Example No. 4:

"Operator agrees to ... indemnify, and save Contractor harmless from and against all claims ... without limit and without regard to the cause or causes thereof or the negligence of any party or parties ..."

  - **ENFORCEABLE**—*Maxus Exploration Co. v. Moran Bros., Inc.*, 817 S.W.2d 50, 57 (Tex.1991)

"Express Negligence" Rule *(cont'd)*

A.

- The ENGINEER agrees to defend, indemnify and hold CITY . . . harmless against any and all claims, lawsuits , judgments, costs and expenses for personal injury (including death), property damage or other harm . . . suffered by any person . . . that may arise out of or be occasioned by ENGINEER'S breach of any of the terms or provisions of this Contract, or by any negligent act or omission of ENGINEER . . . in the performance of this Contract; …

B.

- except that the indemnity provided for in this Paragraph shall not apply to any liability resulting from the sole negligence or fault of CITY…

C.

- and in the event of joint and concurrent negligence of both ENGINEER and CITY, responsibility and indemnity . . . shall be apportioned in accordance with the laws of the State of Texas, without, however, waiving any governmental immunity…

A: Violates "express negligence" test-unenforceable

B and C:

- Intent to include joint negligence?
- Do **B** and **C** "save" joint negligence indemnity?
  - Answer: Probably not.
    - Negative inference does not satisfy "express negligence" test.
- Fix?

"25. **PATENT AND COPYRIGHT INDEMNITY**

A. Engineer agrees to completely defend and indemnify City . . . against a claim that any of the designs, plans or specifications prepared by Engineer . . . pursuant to this Contract infringe a U.S. Patent or copyright directly, indirectly or contributorily, regardless of whether or not City is proven to have actively induced or contributed to the infringement."

- **ENFORCEABLE**
- Spells out other material terms: control of defense, City monitoring, other rights

“Conspicuousness” Requirement

- Must attract the attention of a reasonable person.
  - *Ling & Co. v. Trinity Sav. & Loan Ass’n*, 482 S.W.2d 841 (Tex. 1972)

- Separate provision, bold, capitalization, contrasting font/color.

Examples

Asset Purchase Agreement

* * *

(e) *Payments.* Payments of all amounts owing by an Indemnifying Party pursuant to this Article X relating to a Third Party Claim shall be made within 30 days after the latest of (i) the settlement of such Third Party Claim, (ii) the expiration of the period for appeal of a final adjudication of such Third Party Claim or (iii) the expiration of the period for appeal of a final adjudication of the Indemnifying Party's liability to the Indemnified Party under this Agreement. Payments of all amounts owing by an Indemnifying Party pursuant to Section 10.04(d) shall be made within 30 days after the later of (i) the expiration of the 60-day Indemnity Notice period or (ii) the expiration of the period for appeal of a final adjudication of the Indemnifying Party's liability to the Indemnified Party under this Agreement.

(f) *Escrow Deliveries.* For so long as the Escrow Agreement is in effect and for so long as Shares are held by the Escrow Agent, the rights of the Purchaser Indemnitees to indemnification pursuant to this Article X shall be satisfied with the Shares deposited with the Escrow Agent under the Escrow Agreement, valuing such Shares as set forth therein. If and to the extent that any indemnifiable Claim exceeds the value of the Shares so disposed or if the Escrow Agreement is no longer in effect, the Sellers and the Holders, subject to Sections 10.08 and 10.10, shall pay such Claim, jointly and severally. In no event, however, shall defense costs of the Sellers and the Holders as Indemnifying Parties be paid from the Shares so deposited.

Section 10.05 NEGLIGENCE. THE INDEMNIFICATION PROVIDED IN THIS AGREEMENT SHALL BE APPLICABLE WHETHER OR NOT THE SOLE, CONCURRENT, CONTRIBUTORY OR COMPARATIVE NEGLIGENCE OR THE SOLE OR CONCURRENT STRICT LIABILITY OF THE PERSON ENTITLED TO INDEMNIFICATION HEREUNDER IS ALLEGED OR PROVEN.

Examples

"Boilerplate" Subcontractor Agreement

* * *

11. CONTRACTOR'S INDEMNITY AND WAIVER. TO THE FULLEST EXTENT PERMITTED BY LAW, CONTRACTOR HEREBY AGREES TO PROTECT, DEFEND, INDEMNIFY, AND HOLD OWNER, ITS PARENT CORPORATION, SUBSIDIARIES AND AFFILIATES, AND ANY OF THEIR RESPECTIVE OFFICERS, DIRECTORS, PARTNERS, EMPLOYEES, AGENTS AND INSURERS, (HEREIN COLLECTIVELY REFERRED TO AS THE "INDEMNITEE"), FREE AND HARMLESS FROM AND AGAINST ANY AND ALL CLAIMS, DEMANDS, CAUSES OF ACTIONS, SUITS, OR OTHER LITIGATION OF EVERY KIND AND CHARACTER (INCLUDING ALL COSTS THEREOF AND ATTORNEYS' FEES), WHETHER ASSERTED BY THE HOMEOWNER, CONTRACTOR, OR ANY THIRD PARTY (INCLUDING, BUT NOT LIMITED TO, PERSONNEL FURNISHED BY CONTRACTOR, ITS SUPPLIERS AND PERMITTED SUBCONTRACTORS OF ANY TIER), ON ACCOUNT OF BODILY OR PERSONAL INJURY, DEATH, OR DAMAGE TO OR LOSS OF PROPERTY(INCLUDING THE LOSS OF USE THEREOF), (HEREIN COLLECTIVELY REFERRED TO AS "LOSS"), IN ANY WAY OCCURRING, INCIDENT TO, ARISING OUT OF, OR IN CONNECTION WITH: (I) A BREACH OF THE WARRANTIES, REPRESENTATIONS, OBLIGATIONS, AND COVENANTS PROVIDED HEREIN BY CONTRACTOR; (II) THE WORK PERFORMED OR TO BE PERFORMED BY CONTRACTOR OR CONTRACTOR'S PERSONNEL, AGENTS, SUPPLIERS, OR PERMITTED SUBCONTRACTORS; OR (III) ANY NEGLIGENT ACTION AND/OR OMISSION OF THE INDEMNITEE RELATED IN ANY WAY TO THE WORK, EVEN WHEN THE LOSS IS CAUSED BY THE FAULT OR NEGLIGENCE OF THE INDEMNITEE. ANY PAYMENTS BY CONTRACTOR UNDER THIS PARAGRAPH ON BEHALF OF THE INDEMNITEE SHALL BE IN ADDITION TO ANY AND ALL OTHER LEGAL REMEDIES AVAILABLE TO THE INDEMNITEE AND SHALL NOT BE CONSIDERED THE INDEMNITEE'S EXCLUSIVE REMEDY. CONTRACTOR AND CONTRACTOR'S EMPLOYEES, PERSONNEL, AGENTS, AND PERMITTED SUBCONTRACTORS SHALL BE SOLELY RESPONSIBLE FOR THEIR RESPECTIVE TOOLS AND EQUIPMENT, AND HEREBY WAIVE ANY RIGHT OF RECOVERY AGAINST THE INDEMNITEE WITH RESPECT TO ANY LOSS INVOLVING SUCH TOOLS OR EQUIPMENT IN ANY WAY OCCURRING, INCIDENT TO, ARISING OUT OF, OR IN CONNECTION WITH, THE WORK TO BE PERFORMED HEREUNDER.

12. Representations and Warranties. Contractor represents and warrants to Owner that: (i) the person executing this Agreement on behalf of Contractor is duly authorized and has full power to execute and deliver this Agreement, (ii) all corporate, partnership, or other action requisite for the due execution of this Agreement has been duly and effectively taken or shall be taken prior to the execution and delivery of this Agreement, (iii) this Agreement is or will be (when executed) valid and binding obligations of Contractor, enforceable in accordance with its terms , (iv) this Agreement and Contractor's performance thereof, does not and will not violate any provisions of Contractor's constituent or organizational documents, or any contract, agreement, or governmental requirement to which Contractor is subject, and the same do not require the consent or approval of any governmental authority, (v) Contractor has, and each Contractor's employees, agents or permitted subcontractors shall have, the requisite skills, expertise, experience, licenses, and knowledge to perform the Work, (vii) Contractor is in compliance with all governmental requirements to which it is subject, and (viii) Contractor has the financial ability and resources to perform the Work and all other obligations, duties, and covenants of Contractor under this Agreement.

13. **Insurance.** Contractor agrees to carry: (a) Broad Form Commercial General Liability Insurance on an Occurrence Form, naming the Indemnitee as an additional insured with completed operations coverage and containing a per occurrence limit of no less than One Million Dollars ($1,000,000.00), and an aggregate limit of no less than One Million Dollars ($1,000,000.00) protecting against bodily injury, broad form property damage, and personal injury claims arising from the exposures of: (i) premises-operations; (ii) products and completed operations including materials designed, furnished, and/or modified in any way by Contractor; (iii) independent subcontractors; (iv) contractual liability risk covering the indemnity obligations set forth in this Agreement; and (v) property damage resulting from explosion, collapse, or underground (x, c, u) exposures; (b) Worker's Compensation Insurance that provides statutory benefits and coverage such that Owner will have no liability to Contractor's personnel, employees or agents; and (c) Professional Liability Insurance for Architects, Engineers, Surveyors, and other Professional Service Organizations, that provides a per claim limit of no less than One Million Dollars ($1,000,000.00) and an aggregate of no less than One Million Dollars ($1,000,000.00) protecting against faulty design and faulty professional judgement. Owner and Contractor (collectively, the Parties) intend and agree that the coverage obtained by Contractor naming Owner as an additional insured as set forth herein shall apply on a primary basis with any insurance of Owner being excess coverage. Such coverages will be carried continuously during the term of this Agreement with insurance companies acceptable to Owner in its sole and absolute discretion. Such insurance shall provide for a waiver of subrogation.

INITIALS: Owner: _____ Contractor: _____

Maximizing Enforceability

- Coordination/communication between risk management and legal on drafting/review of contracts.
- Avoid “boilerplate” provisions where possible
- Separate indemnity provisions for different types of activities
- Document specific contracting intent
- Be particularly cautious with “construction”/design contracts
- Establish who controls defense/settlement of claim
- Place indemnity provisions and insurance provisions in separate parts of contract

Step 2: If seeking coverage under indemnitor's policy, enforceability isn't the end of the story

- Does Coverage Exist?
  - Insuring Agreement
  - Exclusions

"And, for what we don't cover, there's insurance insurance."

General Liability - Additional Insured Endorsements

- Those individuals or entities who generally are not automatically included as Insured under the liability policy of others, but for whom the Named Insured provides a certain degree of protection under its liability policies. An endorsement is typically required to effect additional insured status for these parties.

- The Named Insured's impetus for providing additional insured status to others may be a desire to protect the other party because of a close relationship with that party (e.g., employees) or to comply with a contractual agreement requiring it to do so (e.g., customers or owners of property leased by the named insured).

General Liability - Additional Insured Endorsements *(cont'd)*

- The State of Texas has approved numerous ISO Additional Insured Endorsements for attachment to General Liability Policies. Pertinent endorsements include:
  - Additional Insured – Elective or Appointive Executive Officers of Public Corporations (CG 20 25)
  - Additional Insured – Managers or Lessors of Premises (CG 20 11)
  - ***Additional Insured – State or Governmental Agency or Subdivision or Political Subdivision – Permits or Authorizations (CG 20 12) (04/13)
  - ***Additional Insured - State or Governmental Agency or Subdivision or Political Subdivision – Permits or Authorizations Relating to Premises (CG 20 13) (04/13)
  - ***Additional Insured – Owners, Lessees or Contractors – Scheduled Person or Organization (CG 20 10) (04/13)
  - Additional Insured – Owners, Lessees or Contractors – Completed Operations (CG 20 37)
  - ***Additional Insured – Designated Person or Organization (CG 20 26) (04/13)

***New multistate ISO forms

- Replace Texas-specific equivalent
  - Coverage limited: (1) to extent permitted by law; (2) coverage limited to lesser of contract or limits

Coverage for Additional Insureds

Types of Additional Insured Endorsements

- Limited to claims arising out of the A/I's "ongoing operations for the named insured" ;
- A/I specifically required to be named v. blanket "as required" by contract.
- Excluding any bodily injury sustained by any employee of the named or additional insured as well as employees of any contractors or subs;
- Coverage limited to the A/I's acts/omissions in the general supervision of the named insured's operations.
- Coverage limited to concurrent negligence.
- **Actual coverage may be different than what was represented on the Certificate of Insurance**.

Additional Insureds - Advantages

- Creates a direct contractual relationship with insurer and policy rights for A/I.
- Provides coverage independent of indemnity rights.
- Insurer owes equal duty of good faith to both named insured and A/I.

Additional Insureds - Disadvantages

- Potential dilution of policy limits.
  - Per occurrence
  - Aggregate
- Potential adverse impact on loss experience.
- “Other insurance” issues between the A/I coverage and the indemnitee’s own coverage.
- Notice of cancellation issues.
- Scope of coverage limitations.

Additional Insureds - Strategies

- Identify/review A/I endorsement being used.
  - City Requirement: Name the City as A/I on all applicable policies.
    - Only on COI / not policy
    - Consider identifying particular form sought.
- Require certain exclusions be eliminated.
- Have COI and policy specifically state "primary, non-contributory."
  - City Requirement: primary only.
- Synchronize your own coverage/retentions with A/I coverage.

Application of Policy Exclusions to A/I's

- Unless the wording of the exclusion uses the term "you" or "your" to require a causal connection between the excluded conduct and the named insured or its products, work, etc., then exclusions must be applied to each insured, including A/Is.
  - This is especially true if the exclusion speaks in terms of some excluded category of conduct of "any insured".

- Exclusions j5, j6, l and m in CGL refer to "your work", "your product" and "work on your behalf" thereby only applying to the **named insured's** work/product.

Exclusions in CGL typically applicable to A/I's, as well:

- Intentional injury;
- Contractual liability;
- Liquor liability;
- Worker's compensation obligations;
- Employer's liability;
- Pollution;
- Auto/watercraft;
- Mobile equipment;
- Care, custody or control.

Certificates of Insurance

- "Evidence" of Coverage?
  - Not the best evidence of coverage.
    - May not evidence all of the coverage intended to be transferred.
    - Conflicts between COI and policy.
      - *Policy governs*; COI *is not* an insurance policy and will not alter or amend its terms.
    - "Moment in time" document – coverage may not be available when needed.

Practical Pointers

- Secure a copy of the policy *if feasible*.
  - Alternatively, try to secure dec page and AI endorsement.
- Compare the contract requirements with the policy.
  - Types of coverage
  - Limits
  - Scope of the AI endorsement
- Review the policy / AI endorsement to ensure that likely claims scenarios may be covered.

Recent Change in ACORD Forms

- ACORD 25 (2014/01) – Certificate of Liability Insurance

- Background
  - DOI activity (South Dakota)
  - ACORD working groups

Notice of Cancellation Changes

Old Text	New Text
Should any of the above described policies be cancelled before the expiration date thereof, the issuing insurer will endeavor to mail ___ days written notice to the certificate holder named to the left, but failure to do so shall impose no obligation or liability of any kind upon the insurer, its agents or representatives.	Should any of the above described policies be cancelled before the expiration date thereof, notice will be delivered in accordance with the policy provisions.

Notice of Cancellation Changes

- Reason:
  - Policy provisions on cancellation govern
  - Different states have different notice periods

    Texas Cancellation Endorsement – (IL 02750907, ISO 2006)
    - Notice to First Named Insured within 10 days
    - Condo Association: 30 days to First Named Insured
      30 days to Unit Owners with COIs

- Problems:
  - COI holder has no rights to receive notice.
  - Brokers cannot issue older forms (ACORD doesn't support)
  - Brokers cannot amend new COI to provide notice.

Texas COI Statute

(TEX.INS.CODE §1811.001 [Effective 1/1/12])

- Purpose - "Bogus" COI's.
- Applies to all property/casualty insurance
- Applies only to operations/risks in Texas.
- Prohibited Acts
  - Insurance/Agent can't issue COI that alters, amends or extends coverage.
  - COI can't convey contractual rights to a holder (information only).
- Insurers/Agents can only issue:
  - (A) compliant COI's (§1811.101) or
  - (B) standard form pre-approved by TDI.
    - ***ACORD 25 (2014/01)
    - AAIS
    - ISO

- A person may not alter/amend TDI – approved form unless change is also approved.
- A person may not require issuance of COI that contains false/misleading information about the policy.
- A person may not require an agent/insurer to issue in addition to/in lieu of COI "documents inconsistent" with statute.
  - Policy?
  - Endorsements?
- Approved form constitutes confirmation only that policy was issued and/or coverage was bound.
- * * * COI cannot reference contract or insurance requirement unless reference is contained in insurance policy.
  - "As required by written contract" COI's

- Notice:
  - A person may receive notice of cancellation, non-renewal material change only if:
    - (A) named insured
    - (B) policy, endorsement or law/rule requires notice be given
      - Texas Cancellation Endorsement – Condo owners.
- Impact:
  - Agents/Insurers move exclusively to standardized COI's.
  - May be more difficult for policyholders to obtain copies of policies and endorsements.
  - Reduction in "bogus" COI's
    - $1,000/willful violation penalty

City of Dallas COI Requirements

✓ a) Name the City of Dallas and its officers, employees, and elected representatives as additional insureds to all applicable coverages.

✓ b) Waive subrogation against the City of Dallas, its officers and employees, for bodily injury (including death), property damage or any other loss to all applicable coverages.

✓ *(if negotiated)* c) Provide thirty (30) days prior written notice in the event of material change to [the City]

✗ d) Ensure that all certificates of insurance identity the service or product being provided.

✓ e) Ensure that all certificates of insurance name the City of Dallas as the Certificate Holder.

Practical Pointers

- Seek policy amendment to specifically provide notice.
- Include requirement in contracts that named insured must forward notices immediately/10 days/30 days.
  - City requirement:
    - 30 day prior written notice of cancellation or non-renewal
- Develop procedures to closely track cancellation, expiration and renewal.
- Issues:
  - Long-term contracts with “old” notice provisions?

Tendering the Underlying Lawsuit

- Cast as wide a net as possible and keep casting it.
  - Tender lawsuit to contractor/vendor for indemnity; and
  - Tender lawsuit to insurers for additional insured coverage.
    - Tender to carriers for all applicable subcontractors/vendors; and
    - Tender to carriers for all applicable policy periods.

"8 Corners" Rule

- **The "Complaint Allegation" / "8 Corners" Rule**
  - Compare the words of the insurance policy to the allegations in the plaintiff's complaint, without regard to the truth or falsity of the allegations to determine if any claim is potentially covered. *National Union Fire Ins. Co. v. Merchants Fast Motor Lines, Inc.,* 939 S.W.2d 139, 141 (Tex. 1997); *see also Zurich American Ins. Co. v. Nokia Inc.*, 268 S.W.3d 487, 491 (Tex. 2008).

"8 Corners" Rule *(cont'd)*

- The Subset Rules
  - When allegations are silent or ambiguous on some coverage-critical fact, courts apply one of two somewhat contradictory subset rules.

"8 Corners" Rule *(cont'd)*

- **Subset Rule No. 1:**
  - "Courts must resolve all doubts regarding the duty to defend in favor of the duty." *Heyden Newport Chem. Corp. v. Southern Gen. Ins. Co*., 387 S.W.2d 22, 26 (Tex. 1965).
- Is a one-way street benefiting the insured.

"8 Corners" Rule *(cont'd)*

- Example:
  - Alleging bodily injury and property damage occurring in the "past" triggered policies over a five-year period. *Great Am. Lloyds Ins. Co. v. Audubon Ins. Co.*, 2012 WL 3156571 (Tex. App.—Dallas, Aug. 6, 2012).

"8 Corners" Rule

- **Subset Rule No. 2:**

  - "We will not read facts into the petition, nor will we look outside of the petition, or imagine factual scenarios which might trigger coverage." *Merchants Fast Motor Lines*, 939 S.W.2d at 142.

  - Is a two-way street that can be invoked by the insurer or insured.

"8 Corners" Rule

- Example:
  - Petition that alleged date when damage was discovered but did not allege date when damage occurred did not trigger a duty-to-defend under the “8 Corners” rule. *Amerisure Mut. Ins. Co. v. Travelers Lloyds,* 2010 WL 1068087 (S.D. Tex. March 22, 2010).

Exceptions to the "8 Corners" Rule

- Exceptions to the "8 Corners" Rule – When is Extrinsic Evidence Admissible?

Exceptions to the "8 Corners" Rule *(cont'd)*

- Texas Supreme Court in *GuideOne Elite Ins. Co. v. Fielder Rd. Baptist Church*, 197 S.W.3d 305 (Tex. 2006)
  - Expressly did not decide if there was an exception.
  - Dicta: favorably cited federal court's prediction that if there is any exception, (1) it is limited to situations where the evidence goes solely to a fundamental coverage issue and (2) does not overlap the liability merits or contradict the allegations. *GuideOne*, 197 S.W.3d at 308-09.
  - Rejected extrinsic evidence if it would engage the truth or falsity of any of the allegations. *Id.* at 309, 310.

Exceptions to the "8 Corners" Rule *(cont'd)*

- Stanger to a Contract
  - Court permitted insurer to introduce extrinsic evidence to show that the party that was sued (Weingarten Management) was not the entity (Weingarten Investors) that was a party to the contract requiring additional insured coverage. *Weingarten Realty Management v. Liberty Mut. Ins. Co*., 343 S.W.3d 859 (Tex. App.—Houston [14th Dist.] 2011, pet. denied).

The Duty to Defend as Applied to an Additional Insured

- Often complicated by A/I endorsements that condition A/I status on certain conditions being met. What if the suit allegations are silent on such things?
  - Does the claim arise out of the named insured's work for the additional insured at all?
  - What if the suit does not mention the named insured's work at all but it is undisputed that the claim against the additional insured is related thereto?

The Duty to Defend as Applied to an Additional Insured *(cont'd)*

- If Petition does not allege that the defendant's defective work was performed by a subcontractor, courts will not read facts into the petition or permit extrinsic evidence. *See Pine Oak Builders Inc. v. Great Am. Lloyds Ins. Co.*, 279 S.W.3d 650 (Tex. 2009); *see also Gilbane v. Admiral Ins. Co.*, 664 F.3d 589 (5th Cir. 2011); *Indian Harbor Ins. Co. v. KB Lone Star, Inc.*, 2012 WL 3866858 (S.D. Tex. Sept. 5, 2012).

Duty to Defend As Applied To An Additional Insured *(cont'd)*

- On the other hand, allegation that work was done by defendant and "its builders" without specifically naming the insured subcontractor triggered A/I coverage under the subcontractor's policy. *Global Sun Pools, Inc. v. Burlington Ins. Co.*, 2004 WL 878283, *2 (Tex.App.—Dallas 2004, no pet.).

Duty to Defend As Applied To An Additional Insured *(cont'd)*

- Example:
  - *Gordon et al. v. City of Dallas, et al.*
    - ALLEGATIONS:
      - "…the Atkins Defendants entered into a contract with the City of Dallas to perform pipeline capital improvements and/or construction…"
      - "Defendants, acting by and through their agents, servants, and employees, were each negligent…"

Reservation of Rights Letter

- Reserve rights to later deny coverage for settlement or judgment.

- Letter may say carrier is reserving rights to withdraw defense but carriers rarely do so, unless:
  - An amended pleading or summary judgment dismisses the only covered claims; or
  - The carrier first obtains a declaratory judgment finding it owes no duty to defend.

Reservation of Rights Letter *(cont'd)*

- A reservation of rights letter typically does not preserve a carrier's ability to seek reimbursement for previously paid defense or indemnity costs.

- *But see Gordon, et al. v. City of Dallas, et al.*:
  - Insurer wrote: "…the Company reserves all rights available to it under the law, *if any*, to seek recoupment of any defense costs expended on City's behalf…" (Emphasis in original.)

Reservation of Rights Letter *(cont'd)*

- Once a carrier pays defense or indemnity costs, it cannot get them back, unless:
  - The policy provides for reimbursement of non-covered costs; or
  - The carrier and insured reach a bilateral agreement. *Excess Underwriters at Lloyd's, London v. Frank's Casing Crew & Rental Tools, Inc.*, 246 S.W.3d 42 (Tex. 2008).

Insurer's Right to Independent Counsel

- Defense leads to tripartite relationship between insurer, insureds, and defense counsel. This tripartite relationship can lead to problematic scenarios.

- Insured can sometimes select its own counsel who will then be paid by the insurer.

Insurer's Right to Independent Counsel *(cont'd)*

- A right to independent counsel does not arise every time a reservation of rights letter is issued.

- Every "disagreement about how the defense should be conducted cannot amount to a conflict of interest," or the insured "could control the defense by merely disagreeing with the insurer's proposed actions." *Northern County Mut. Ins. Co. v. Davalos*, 140 S.W.3d 685, 690 (Tex. 2004).

Insurer's Right to Independent Counsel *(cont'd)*

- "When the facts to be *adjudicated* in the liability lawsuit are the same facts upon which coverage depends," a reservation of rights creates a "conflict of interest [that] will prevent the insurer from conducting the defense." *Northern Cnty. Mut. Ins. Co. v.* Davalos, 140 S.W.3d 685, 689 (Tex.2004) (emphasis added).

- The mere possibility that facts may be "*developed*" in the underlying lawsuit that could affect coverage does not create a right to independent counsel. *Downhole Navigator, L.L.C. v. Nautilus Ins. Co.,* 686 F.3d 325, 330 (5th Cir. 2012).

Insurer's Right to Independent Counsel *(cont'd)*

- Examples of potentially disqualifying conflicts that MIGHT, depending on the facts involved, entitle an insured to independent counsel:
  - Insured sued for fraud and policy includes a fraud exclusion;
  - Insured sued for an intentional tort and policy excludes coverage for intentional torts;
  - There is a question as to whether a defendant was acting in course and scope of employment or in some other capacity upon which his insured status depends, and that issue will be litigated and decided in the underlying case as well;
  - There are contested statute of limitations or discovery rule/fraudulent concealment issues in the underlying suit and there is a coverage dispute concerning the applicable policy period.

Insurer's Right to Independent Counsel *(cont'd)*

- Even if insured is not entitled to independent counsel, it is still the client in the tripartite relationship. The defense counsel owes unqualified loyalty to insured and must represent insured's interests. *State Farm Mut. Auto Ins. Co. v. Traver*, 980 S.W.2d 625 (Tex.1998).
- *Except on Coverage Matters*
- Insured will need to retain its own counsel to handle any coverage disputes.

Coverage for an Indemnitee

- COVERAGE IMPLICATIONS FOR CITY'S INDEMNITY CLAIM AGAINST AN INSURED INDEMNITOR
  - Does the carrier owe coverage *to the indemnitor* for the City's claim?
    - If yes, then City's defense costs in the underlying lawsuit will constitute a component of its damages in its indemnity claim and the carrier will ultimately owe coverage for those damages.
  - Does the carrier owe a defense directly to the City?
    - Only in VERY limited circumstances.

Coverage for an Indemnitee *(cont'd)*

- Does the carrier owe coverage to the indemnitor for the City's claim?
- Contractual Liability Exclusion:
  - This insurance does not apply to:

  "Bodily injury" or "property damage" for which the insured is obligated to pay damages by reason of the assumption of liability in a contract or agreement. This exclusion does not apply to liability for damages:

  (1) That the insured would have in the absence of the contract or agreement; or

  (2) Assumed in a contract or agreement that is an "insured contract," provided the "bodily injury" or "property damage" occurs subsequent to the execution of the contract or agreement…"

Coverage for an Indemnitee *(cont'd)*

- "Insured Contract" means:

* * * *

d. An obligation, as required by ordinance, to indemnify a municipality, except in connection with work for a municipality;

* * * *

f. That part of any other contract or agreement pertaining to your business (including an indemnification of municipality in connection with work performed for a municipality) under which you assume the tort liability of another party to pay for "bodily injury" or "property damage" to a third party or organization.

Coverage for an Indemnitee *(cont'd)*

- *Ewing Construction Co., Inc. v. Amerisure Ins. Co.*, 420 S.W.3d 30 (Tex. 2014)

- *Held:* "A general contractor who agrees to perform its construction work in a good and workmanlike manner, without more, does not enlarge its duty to exercise ordinary care in fulfilling its contract, thus it does not 'assume liability' for damages arising out of its defective work so as to trigger the Contractual Liability Exclusion."

Coverage for an Indemnitee *(cont'd)*

- In sum, the contractual liability exclusion will apply when the insured would not have been liable but for a contractual assumption of the liability. *Gilbert Tex. Construction, L.P. v. Underwriters at Lloyds London*, 327 S.W.3d 118 (Tex. 2008) (but for contractually agreeing to protect property near the worksite, DART's insured contractor was entitled to governmental immunity for negligently causing the plaintiff's property to flood).

Coverage for an Indemnitee *(cont'd)*

- Does the carrier owe a defense directly to the City?
  - Potentially yes under the policy's Supplementary Payments provision, under VERY limited circumstances.
  - The indemnitor's insurer may be obligated to defend the City directly, IF:
    - The indemnitor and the City are both defendants in the underlying lawsuit;
    - The underlying lawsuit falls within the scope of the indmnity agreement within an "insured contract" and is also covered by the policy;
    - No conflict exists between the indemnitor and the City and both agree that the insurer can defend them with the same attorney; and
    - The City agrees in writing to cooperate and assist in seeking coverage from other carriers.

Insurer's Duty to Indemnify

- Separate obligation from duty-to-defend based not on the pleadings, but on the actual facts adjudicated in the underlying lawsuit. *D.R. Horton-Tex., Ltd. v. Markel Internat'l Ins. Co., Ltd*., 300 S.W.3d 740, 743-744 (Tex. 2009).

- Often discussed as being more narrow than the duty to defend.

Insurer's Duty to Indemnify *(cont'd)*

- Be careful that a carrier or court does not take this idea too far. There can be a duty to indemnify even if there is no duty to defend. *D.R. Horton,* 300 S.W.3d at 745.

SCHUBERT | EVANS

ATTORNEYS AND COUNSELORS

Blake S. Evans
Stephen Burnett

Schubert & Evans, P.C.
900 Jackson Street, Suite 630
Dallas, Texas 75202

www.schubertevans.com