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Don't Mess with Texas: Unique Coverage, Liability and Venue Issues in the Lone Star State

Liability issues for Texas construction defect claims

a. Anti-indemnity statute for construction contracts

Application to indemnification and additional insured issues

Anti-indemnity laws have been adopted in some form by statute or via case law in the majority of states across the country in an effort to narrow the obligation of a downstream contractor to the upstream contractor in a construction contract. Texas has joined this trend by adopting Insurance Code Chapter 151 (aka the Texas Anti-Indemnity Statute), which applies to all commercial construction contracts entered into as of January 1, 2012. Chapter 151 makes any provision in a commercial construction contract, or in an agreement collateral to or affecting a commercial construction contract, void and unenforceable as against public policy to the extent that it requires an indemnitor (downstream) to indemnify, hold harmless, or defend a party, including a third party, against a claim caused by the negligence or fault of the indemnitee (upstream), its agent, employee or any third party under the control/supervision of the indemnitee. The impact of this provision is that, for commercial construction contracts, only limited form indemnity provisions are allowed.

In Texas, a limited form indemnity provision obligates a downstream contractor to indemnify the upstream contractor only to the extent of the downstream contractor's own negligence or fault. Moreover, the language of Chapter 151 expressly states that this provision may not be waived by either party.

In addition to Chapter 151 limiting the scope of an indemnification provision in commercial construction contracts, this statute also extends to similarly limit the scope of any additional insured endorsement that the downstream is required to obtain. Specifically, the statute mandates that any provision in a construction contract that requires the purchase of additional insured coverage, or any coverage endorsement, or provision within an insurance policy providing additional insured coverage, is void and unenforceable to the extent that it requires or provides coverage which is prohibited under Chapter 151. Accordingly, in order to comply with Chapter 151, an additional insured endorsement for property damage is limited to that arising from that downstream contractor's own negligence or fault.

Exceptions for certain construction projects

While the definition of a "construction contract" is broad under Chapter 151, including design, construction, alteration, renovation, remodeling, repair or the furnishing of material or equipment, currently, Texas has not applied the anti-indemnity statute to municipal construction projects nor residential construction contracts (single family home, townhouse, duplex, or land development related to residential projects). Moreover, the anti-indemnity statute has limited application to controlled insurance programs, only requiring that a controlled insurance program that provides general liability insurance coverage must provide completed operations coverage for a period of not less than three years.

Exception for bodily injury or death to employees of an indemnitor

The Texas anti-indemnity statute does not apply to claims for bodily injuries or death to employees of an indemnitor. This exception allows for continued contractual risk transfer by way of an over action claim to the downstream contractor or employer of the injured party, even if the upstream contractor's sole negligence is involved. This often leads to the drafting of separate indemnity provisions within a construction contract, in order to address the broader scope of indemnification allowed under the law for bodily injury claims versus property damage.

Trigger of the anti-indemnity statute

The inception of the application of the anti-indemnity statute is triggered if the primary/original commercial contract was executed on or after January 1, 2012, and is not dictated by the date of the subcontract or related agreement execution.

Contrast of the fair notice requirements

Under the fair notice requirement, a party is required to obtain indemnification for its own negligence in advance. Fair notice has two components: express negligence and conspicuousness test. Whether these components are satisfied is a determination for the court. For contracts which do not fall under the Texas anti-indemnity statute, indemnification agreements are still evaluated and assessed as to enforceability in line with the fair notice requirements.

Insurance industry's response to the anti-indemnity statute

In an attempt to respond to the complexities of the varying state anti-indemnity laws, ISO issued a new additional insured endorsement form in April of 2013. Form CG 20 38 04 13 (ongoing operations) and CG 20 37 04 13 (completed operations). These endorsements were seen by many as an attempt to avoid the necessity of "state specific" additional insured endorsements in order to comply with respective anti-indemnity laws. ISO's 2013 form reveals an increasing focus on aligning scope of coverage with contract terms requiring additional insured coverage. The attempted impact of the new 2013 form is to (1) restrict coverage to the extent permitted by law; and (2) restrict coverage scope to that which is required by contract. This form makes it even more imperative that additional insured requirements be clearly delineated in the contract.

b. Venue issues

School district cases in South Texas

There has been a trend of increased construction defect litigation involving school districts, especially in South Texas and along the Rio Grande Valley. Many of these cases involve complex factors, including political motivations, small counties with tightly networked communities, elected school board members, and jury pools being drawn from communities in which taxpayers' money is directed into the school districts resulting in jurors feeling they have a personal (and even financial) stake in the outcome of the litigation. Managing the legal issues, while realistically evaluating these challenging environments is important in order to help to properly evaluate the risk and exposure of the claim.

Juridical hellholes

The American Tort Reform Foundation (ATRF) has published its list of "Judicial Hellholes" every year since 2002. The list of Judicial Hellholes frequently includes entire states. For example, in its most recent 2016-2017 rendition, the ATRF included the states of California, New Jersey, and Louisiana. While Texas has never been included on this list as a "state," many venues within the State of Texas have made frequent appearances on this list from year to year in varying forms. Hidalgo County, Texas made no. 9 on the 2016-2017 list.

Areas located along the Texas Gulf Coast and East Texas are known to be the most plaintiff-friendly, while the great majority of Texas counties, and the largest cities in Texas (Houston, San Antonio, Austin, Dallas, Fort Worth, and El Paso), are not included on the list of "judicial concerns". However, while this may be a consideration when assessing potential exposure/risk, fewer and fewer Texas venues have been identified as a judicial hellhole and those that have are more limited as to types of litigation, including hail claims and patent litigation. While Hidalgo County was no. 9 on the most recent ATRF list, the judicial concern is identified as the abusive number of lawsuits accusing insurers of not paying for storm damage. The Northern District of Texas made the "watch list" for 2016-2017, in connection with the largest False Claims Act judgment in history. Strategically managing a case that is venued in one of these plaintiff-friendly locations can help to limit the potential exposure of a party.

Joint and several liability where an insured is found more than 50% at fault

Texas enacted a modified joint and several liability under Chapter 33 of the Civil Practice & Remedies Code. Defendants are responsible for their share of the plaintiff's damages, unless or except a defendant may be jointly and severally liable if the defendant's responsibility is in excess of 50%. However, where the tortious acts of two or more wrongdoers join to produce an indivisible injury, Texas courts have found that joint and several liability could be applied to those parties.

<u>Coverage issues for Texas construction defect claims</u>

a. Additional insured coverage

Application of Gilbane to the duty to defend (narrow construction)

With respect to additional insured endorsements that provide coverage for liability "caused, in whole or in part," by the named insured's work or operations, the U.S. Fifth Circuit Court of Appeals found that

the insurer had no duty to defend the additional insured where the allegations did not specifically allege that the named insured or anyone acting on its behalf caused or contributed to the cause of the accident. *Gilbane Bldg. Co. v. Admiral Ins. Co.*, 664 F.3d 589 (5th Cir. 2011). This decision was based on a strict application of the eight corners rule. The court stated that it may not infer additional facts that are not in the pleadings and Admiral was not required to defend the additional insured if the petition did not affirmatively allege facts that would trigger the duty under the policy. Thus, the court found that a defense was owed to the additional insured only if the pleadings alleged that the named insured, or someone acting on its behalf, proximately caused the alleged injuries.

In a construction defect case, does this mean that there is no duty to defend a general contractor as an additional insured if the plaintiff sues only the general contractor? That may depend on whether the plaintiff also alleged that subcontractors were at fault and identified the subcontractors. In *D.R. Horton-Texas, Ltd. v. Markel Int'l Ins. Co.*, 300 S.W.3d 773 (Tex. App.- Houston [14th Dist.] 2006), *rev'd on other grounds*, 300 S.W.3d 740 (Tex. 2009), the additional insured endorsement in the Markel policy limited coverage to those claims arising out of work the named insured performed for D.R. Horton. The plaintiffs' petition did not list the named insured as a defendant, did not make any reference to the named insured, and did not allege that any person or entity other than D.R. Horton was liable. The court stated that "[g]iven their most liberal interpretation in favor of coverage, the factual allegations in the *Holmes* petition cannot be interpreted as stating a claim for damages arising from Ramirez's work." *Id*. at 779-80. The court refused to consider extrinsic evidence which showed that the plaintiffs' damages arose out of the named insured's work, and concluded that Markel had no duty to defend D.R. Horton. *Id*. at 781. This decision was challenged in the Texas Supreme Court and D.R. Horton argued that extrinsic evidence "relating to coverage-only facts" must be considered. *D.R. Horton- Texas, Ltd. v. Markel Int'l Ins. Co.*, 300 S.W.3d 740 (Tex. 2009). The Court found that D.R. Horton waived the argument and refused to address the issue. *Id*. at 743. Although *D.R. Horton* stands for the proposition that the plaintiff must allege that subcontractors were at fault to trigger additional insured coverage, what happens if the plaintiff alleges that subcontractors were at fault but failed to identify the subcontractors by name? It is not clear whether a Texas court will allow extrinsic evidence for this mere identification issue.

Application of Gilbane to the duty to indemnify (broad construction)

In *Gilbane*, the U.S. District Court for the Southern District of Texas found that Admiral had a duty to indemnify the additional insured. So, unlike many states, it is important to keep in mind that an insurer in Texas may still have a duty to indemnify even if there is no duty to defend. In *Gilbane*, the court determined that a jury would have found the claimant or his employer 1% or more responsible for causing the accident and/or injuries at issue. *Gilbane Bldg. Co. v. Empire Steel Erectors, L.P.*, 2010 WL 4791493, *4 (S.D. Tex. Nov. 16, 2010). Accordingly, the court found that the Admiral policy owed indemnity for the entire amount of the settlement the additional insured reached with the claimant. This issue was not directly addressed on appeal.

Pursuant to *Gilbane*, additional insured endorsements that provide coverage for liability "caused, in whole or in part," by the named insured's work or operations may provide coverage for all of an additional insured's liability even if the named insured is only 1% at fault. Nevertheless, the anti-indemnity statute would limit additional insured coverage if it is applicable in your particular case.

Additional insured endorsements which limit coverage to vicarious liability

Similar to *Gilbane*, in 2008 the Texas Supreme Court rejected the insurer's argument that an additional insured endorsement precluded coverage for an additional insured's own negligence, stating that "had the parties intended to insure ATOFINA for vicarious liability only, language clearly embodying that intention was available." *Evanston Ins. Co. v. ATOFINA Petrochemicals, Inc.*, 256 S.W.3d 660, 666 (Tex. 2008). In support, the Court stated: "[The insurer] easily could have limited coverage by including in the endorsement terms such as 'vicarious liability' or 'negligence of the named insured'." *Id.* at n. 20 (citing *Mid-Continent Cas. Co. v. Chevron Pipe Line Co.*, 205 F.3d 222, 228-29 (5th Cir. 2000)).

In contrast, since *ATOFINA* was decided, Texas courts have limited additional insured coverage to just vicarious liability where the additional insured language in the policies stated:

- No obligation for defense or indemnity under the policy is provided to any Additional Insured for "claims" or "suits" directly or indirectly "arising from" the status, actions or inaction, including (without limitation) for vicarious, derivative or strict liability of said Additional Insured, its agents, consultants, servants, contractors or subcontractors (other than the Named Insured), except for the actions or inactions of the Named Insured. *Cont'l Cas. Co. v. Am. Safety Cas. Ins. Co.*, 365 S.W.3d 165, 170 (Tex. App.- Houston [14th Dist.] 2012).
- The party is an additional insured "but only with respect to liabilities arising out of their operations performed by or for the named insured, but excluding any negligent acts committed by such additional insured." *Burlington N. and Santa Fe Ry. Co. v. Nat'l Union Fire Ins. Co.*, 394 S.W.3d 228, 234 (Tex. App.- El Paso 2012).
- The party is an additional insured "but only with respect to their legal liability for acts or omissions of the named insured." *Shell Chem. v. Discover Prop. & Cas. Ins. Co.*, 2010 WL 1338068, *2 (S.D. Tex. March 29, 2010).

Additional insured coverage limited to the amount of insurance required by contract

In 2015, the United States District Court for the Southern District of Texas held that the excess insurer was obligated to pay no more than the contracted for limits of additional insured coverage. *L-Con, Inc. v. CRC Ins. Services, Inc.*, 122 F. Supp. 3d 627, 638 (S.D. Tex. 2015), *as amended* (Aug. 24, 2015). In *L-Con*, the subcontractor agreed to name the facility owner/operator as an additional insured on its policies and agreed "to carry at least $1 million per occurrence of commercial general liability ("CGL") insurance for bodily injury… and $3 million in excess/umbrella coverage." The subcontractor actually obtained $2 million in primary coverage and $15 million in excess coverage. Subsequently, one of the subcontractor's employees was killed and several others were injured while working as the result of an explosion. A jury entered judgment in the amount of $21 million against the owner/operator. After finding that the owner/operator was an additional insured under the subcontractor's policies, the court addressed the issue of how much coverage the subcontractor's insurers were obligated to provide. In holding that the excess insurer was not obligated to pay more than $3 million, even though the excess policy exceeded the minimum excess coverage the subcontractor was obligated to obtain, the court observed that the excess policy specifically incorporated the subcontractor's contract with the owner/operator. The court noted that the excess policy provided that "an additional insured is limited to the lesser of '[t]he amount of coverage that the 'Named Insured' [subcontractor] has contractually agreed to provide to that Additional Insured' or the limits of insurance available under the [excess insurer] Policy." In holding that the excess insurer was obligated to pay no more than the contracted for $3 million, the court implied that the minimum required coverage, even though the subcontractor

actually obtained more, was the "lesser of" the amount contractually agreed to by the parties and the actual limits of insurance which exceeded the minimum requirements.

It is important to examine the policies carefully to determine whether the contract is incorporated into the policy and, if so, whether it limits the insurance available to the additional insured.

b. Eight corners conundrum and the duty to defend

The expanding exception for extrinsic evidence

Although the Texas Supreme Court has not explicitly recognized an exception to the "eight-corners" rule, the Fifth Circuit and Texas appellate courts generally allow consideration of extrinsic evidence under certain circumstances. In particular, where the insurer seeks to determine a fundamental coverage issue resolved by readily determined facts. One such example is from *ACE Am. Ins. Co. v. Freeport Welding & Fabricating, Inc.*, 699 F.3d 832, 840–41 (5th Cir. 2012). In the *Freeport Welding* case, the court began its analysis with a determination of whether Freeport qualified as an "additional insured" under a Named Insured's (Brand Energy's) insurance policy. In doing so, the Fifth Circuit reviewed a 2009 purchase agreement. The court specified that "If we determine that Freeport qualifies as an additional insured during the relevant time period, our analysis will then proceed to the eight-corners rule to decide if the facts alleged in the underlying state court proceedings were sufficient to trigger ACE's duty to defend Freeport as an additional insured under Brand Energy's insurance policy." This opinion demonstrates that the determination of additional insured status was made using extrinsic evidence.

Additionally, the Texas Supreme Court allowed the use of extrinsic evidence in *In re Deepwater Horizon*, 470 S.W.3d 452 (Tex. 2015), *reh'g withdrawn*, (May 29, 2015). There, the supreme court in a duty to indemnify context explained that the scope of coverage is "determined from the language employed in the insurance policy, and if the policy directs us elsewhere, we will refer to an incorporated document to the extent required by the policy." The Court stated: "[W]e have long held insurance policies can incorporate limitations on coverage encompassed in extrinsic documents by reference to those documents. We do not require 'magic' words to incorporate a restriction from another contract as part of the policy." (internal citations and quotations omitted). Other Texas state and federal courts have applied *Deepwater Horizon* in the duty to defend context. *See ACE Amr. Ins. Co. v. Freeport Welding & Fabricating, Inc.*, 699 F.3d 832, 840-43 (5th Cir. 2012) (because separate contract did not impose obligation to procure additional insured coverage, insurer had no duty to defend purported additional insured); *Miramar Petroleum, Inc. v. First Liberty Ins. Corp.*, 2015 WL 7301096, at *3 (S.D. Tex. Nov. 18, 2015) (scope of indemnity obligation in separate contract determined duty to defend under policy); *Ill. Union Ins. Co. v. Sabre Holdings Corp.*, 2015 WL 3917981, at *4 (Tex. App.—Fort Worth June 25, 2015), *reh'g overruled*, (Aug. 6, 2015), *review dismissed*, (Jan. 15, 2016) (documents referred to in policy to be construed must be considered in ascertaining duty to defend).

A duty to defend when the Petition is silent on dates

Insurance carriers often struggle with whether they owe a defense when no date of injury (Texas applies an injury-in-fact trigger) is stated in the petition or complaint. In *Pine Oak Builders v. Great American Lloyds*, 292 S.W.3d 48 (Tex. App. Hous. – 14th Dist. 2006), the court noted that the petition did not allege exactly when the EIFS at issue failed or when any of the alleged defects caused damages. The court stated, "We will not read facts into a petition to create a duty to defend." It started with the

premise that if the petition itself does not contain sufficient facts to establish that the policy has been triggered, there is no duty to defend. It then noted that although the plaintiffs' petitions did not allege a specific date on which damage occurred, it could be "readily ascertained" from the petition that the alleged damage occurred in 1996 (the year of construction) or later. Accordingly, the court held that the petition stated a cause of action potentially within the coverage of each of the policies that covered a time period from 1996 or later.

Application of the Prompt Payment of Claims Act to defense costs

Texas Insurance Code Chapter 542 a/k/a the Texas Prompt Payment Act sets forth deadlines by which an insurance company must respond to a claim. A "claim" is defined as "a first party claim made by an insured or a policyholder under an insurance policy or contract or by a beneficiary named in the policy or contract that must be paid by the insurer directly to the insured or beneficiary." 542.051. Chapter 542 is premised on the presumption that insurance companies have the right to dispute claims; however, they must do so promptly. *Dunn v. Southern Farm Bureau Casualty Ins. Co.*, 991 S.W.2d 467, 471 (Tex.App.—Tyler 1999, pet. denied. The Texas Supreme Court, in construing Chapter 542 liberally, held it applied to a wrongful refusal to defend. *Lamar Homes v. Mid-Continent Casualty Company*, 242 S.W.3d 1, 19-20 (Tex. 2007). Note that the Act mandates that (1) if a claim is made pursuant to an insurance policy, (2) the insurer is liable under the policy, and (3) the insurer is not in compliance with the requirements of section 542.056, the insurer shall be liable to pay the claimant or beneficiary, in addition to the amount of the claim, 18% per annum of the amount of the claim as damages, together with reasonable attorney's fees.

c. An insured's entitlement to independent counsel

In Texas, if a conflict of interest actually exists between the insurer and the insured, the insured has the privilege of rejecting the representation offered by the insurer and hiring counsel of its own choosing to be paid for by the insurer. An insurer's issuance of a reservation of rights can create a potential conflict of interest, but it does not by itself create such a conflict. "Instead, the test to apply is whether 'the facts to be adjudicated in the [underlying] lawsuit are the same facts upon which coverage depends.'" *Graper v. Mid-Continent Cas. Co.*, 756 F.3d 388, 392 (5th Cir. 2014) (citing *N. Cnty. Mut. Ins. Co. v. Davalos*, 140 S.W.3d 685, 689 (Tex. 2004)). Moreover, a conflict of interest does not arise just because facts that could be *developed* in the underlying litigation are the same facts upon which coverage depends.

d. Tender and allocation issues

Application of other insurance provisions for consecutive policies

In Texas, "other insurance" clauses in insurance policies apply only when the coverages at issue are concurrent. Generally, for multiple insurance policies to provide concurrent coverage, the policies must cover the same risk. Recent cases in Texas have held that, for concurrent coverage to exist for purposes of the other insurance provision, the policies must apply for the same policy period. In *LSG Tech., Inc. v. U.S. Fire Ins. Co.*, 2010 WL 5646054 (E.D. Tex. Sept. 2, 2010), the court refused to apply "other insurance" provisions in consecutive policies, relying on the following statement from a leading treatise:

> "Other insurance" refers only to two or more concurrent policies, which insure the same risk and the same interest, for the benefit of the same person, during the same period. However, "other insurance" clauses are not intended to allocate liability among successive insurers

> because they do not insure the same risk and would unjustly make consecutive insurers liable for damages occurring outside their policy periods.

Similarly, the Texas Court of Appeals stated that, "[b]ecause the policies are for *different* policy periods, by necessity the policies do not cover the same injury or damage and there is no 'other valid and collective insurance [that] is available to the insured for a loss we cover....'" *Great Am. Lloyds Ins. Co. v. Audubon Ins. Co.*, 377 S.W.3d 802, 811 (Tex. App.—Dallas 2012), opinion withdrawn and superseded by 2013 WL 85240 (Jan. 8, 2013). Thus, it appears that the recent trend is for courts to find concurrent coverage existing only in overlapping policies.

A targeted tender and "all sums" allocation

The all sums allocation method allows an insured to target the policy, or policies, that will best cover its claim. This method of allocation is based on the Insuring Agreement provision which states that "[w]e will pay *all sums* that the insured becomes legally obligated to pay as damages…" With this language, an insurer becomes jointly and severally liable with other triggered insurers.

In the construction defect arena, the Supreme Court of Texas applied the all sums allocation method in *Lennar Corp. v. Markel Am. Ins. Co.*, 413 S.W.3d 750 (Tex. 2013). In that case, Lennar underwent a program of replacing EIFS on hundreds of homes with conventional stucco when it was discovered that EIFS trapped water inside causing damage to the home. Lennar notified its insurers that it would seek indemnification for the remediation costs, but all refused to participate. Come trial, only Markel was left which had issued Lennar a $25 million umbrella policy effective from June 1, 1999 to October 19, 2000. "A fair inference from the record" was that most of the damage to the homes began before or during Markel's policy period and continued after. As such, Markel argued that only the costs for remediating the damage in existence during the policy period were covered. In response, Lennar argued that it would be practically impossible to prove the specific amount of damage to each house during the policy period and, further, that the policy did not require it. The Court agreed stating:

> Coverage under Markel's policy is limited to property damage that occurs during the policy period but expressly includes damage from a continuous exposure to the same harmful conditions. For damage that occurs during the policy period, coverage extends to the "total amount" of loss suffered as a result, not just the loss incurred during the policy period. No question remains that all 465 houses at issue suffered property damage during the policy period, which began before or during the policy period and continued until it was repaired, all because of water trapped in home walls by EIFS applied to wood-frame construction. Thus, the policy covered Lennar's total remediation costs.

The Court also rejected Markel's argument that it should be responsible along with Lennar's other insurers only for its pro rata share of the total remediation costs finding, instead, that it was up to the insurers who share responsibility for a loss to allocate it among themselves according to their subrogation rights.

A targeted tender where the policy provides coverage for "those sums"

A so-called targeted tender and the all sums method of allocation should not be applicable where the Insuring Agreement states that the insurer will pay "*those sums* that the insured becomes legally obligated to pay as damages…" So, a triggered policy with this Insuring Agreement should have no

obligation to pay repair costs for more than the property damage which occurred during its policy period. This policy language stays true to the intent of the CGL policy which is to only cover property damage which occurs during its policy period. In this situation, damages should be allocated among consecutively triggered policies and no insurer should be liable for property damage which occurred outside its policy period. Obviously, the difficulty lies in determining precisely when property damage occurred and determining what portion of the repair costs are for that particular property damage.

e. Contribution between insurers

The Mid-Continent rule for contribution claims

Contribution claims against co-insurers are difficult if made post-settlement in light of the Texas Supreme Court's decision in *Mid-Continent Ins. Co. v. Liberty Mutual Ins. Co*., 346 S.W.3d 765 (Tex. 2007). Liberty insured Kinsel, the general contractor on a highway project for the State of Texas. Crabtree, one of Kinsel's subcontractors was responsible for the signs and dividers on the project. Liberty issued a $1 million primary policy and a Liberty affiliate issued a $10 million excess policy to Kinsel. Mid-Continent insured Crabtree under a nearly identical $1 million policy under which Kinsel was an additional insured. Thus, Kinsel had insurance under both primary policies and each policy had identical "other insurance" clauses providing equal or pro rata sharing and each contained a voluntary payment clause, a subrogation clause and a version of the standard "no action" clause.
During construction of the highway, a driver crossed over the center barrier into oncoming traffic and hit another car head-on. The Boutin family was in the second car, suffered substantial injuries, and sued Kinsel (among others). Liberty Mutual and Mid-Continent both accepted Kinsel's defense. At mediation, Liberty Mutual agreed to settle with the Boutins for $1.5 million and demanded that Mid-Continent contribute half, but Mid-Continent only paid $150,000. Liberty paid $1.35 million, $350,000 over its primary policy limits, and retained the right to seek recovery from Mid-Continent for Mid-Continent's pro rata share. Additionally, Mid-Continent settled the claims against Crabtree for $300,000, leaving $550,000 in outstanding limits. The district court awarded Liberty Mutual the remaining $550,000 limit of Mid-Continent's $1 million policy. On appeal, the Fifth Circuit certified questions to the Texas Supreme Court, the first of which was:

> Two insurers, providing the same insured applicable insurance liability coverage under policies with $1 million limits and standard provisions (one insurer also providing the insured coverage under a $10 million excess policy), cooperatively assume defense of the suit against their common insured, admitting coverage. The insurer also issuing the excess policy procures an offer to settle for the reasonable amount of $1.5 million and demands that the other insurer contribute its proportionate part of that settlement, but the other insurer, unreasonably valuing the case [Kinsel's liability] at no more than $300,000, contributes only $150,000, although it could contribute as much as $700,000 without exceeding its remaining available policy limits. As a result, the case settles (without an actual trial) for $1.5 million funded $1.35 by the insurer which also issued the excess policy and $150,000 by the other insurer.
>
> In that situation is any actionable duty owed (directly or by subrogation to the insured's rights) to the insurer paying the $1.35 million by the underpaying insurer to reimburse the former respecting its payment of more than its proportionate part of the settlement?

Liberty Mutual Ins. Co. v. Mid-Continent Ins. Co., 405 F.3d 296, 310 (5th Cir. 2005).

In responding to the Fifth Circuit's certified questions, the Texas Supreme Court concluded that there was no right of reimbursement. The court determined that Liberty Mutual was actually seeking a right of contribution from Mid-Continent. Under Texas law, a right of contribution exists when two or more insurers bind themselves to pay an entire loss, but one pays the whole loss. *General Ins. v. Hicks Rubber*, 169 S.W.2d 142 (Tex. 1943). The insurer paying the whole loss is entitled to a right of contribution in the amount of the ratable proportion of the amount paid. The right of contribution requires that several insurers share a common obligation or burden and that the insurer seeking contribution has made a compulsory payment of more than its fair share of that common burden. Importantly, when "other insurance" and "pro rata" clauses exist, however, then the direct claims for contribution between co-insurers disappears because the "pro rata" clause makes the contracts several and independent from each other. In other words, there is no common obligation because each co-insurer contractually agrees with the insured to pay its pro rata share of the loss, but does not contractually agree to pay another co-insured's pro rata share. Since the Liberty Mutual and Mid-Continent policies contained pro rata other insurance clauses, the two insurers agreed with their common insured, Kinsel, to pay a proportionate share of the insured's loss up to $1 million. But the co-insurers did not create a similar contract between themselves.

With regard to subrogation, Liberty Mutual asserted that it had such a right under its policy's subrogation clause. This subrogation right stems from the contractual and common law duties Mid-Continent owed Kinsel and is referred to as contractual subrogation. The court found however, that because Kinsel had been fully indemnified for its $1.5 million loss, it had no right to enforce Mid-Continent's duty to pay its pro rata share of the loss. The Court held "that a fully indemnified insured has no right to recover an additional pro rata portion settlement from an insurer regardless of that insurer's contribution to the settlement." Because the insured had no right to enforce, the co-insurer had nothing to assert against another co-insurer in subrogation.

> *Exceptions to the rule when not co-primary, pro rata, coverage has been denied, and/or not concurrent coverage*

In subsequent cases, the Fifth Circuit has restricted the scope of *Mid–Continent* to apply only to the specific facts of that case. *See Colony Ins. Co. v. Peachtree Construction Co.,* 647 F.3d 248, 256–58 (5th Cir. 2011) (noting the court's view that a broad reading of *Mid–Continent* was at odds with foundational principles of Texas insurance law, as well as in conflict with later decisions of the Texas Supreme Court). In *Trinity Universal Insurance Co. v. Employers Mutual Casualty Co.,* the Fifth Circuit made it clear that *Mid–Continent* does not address the recovery of defense costs from a co-insurer who violates its duty to defend a common insured. 592 F.3d 687 (5th Cir. 2010).

Furthermore, in *Amerisure Insurance Co. v. Navigators Insurance Co.,* the Fifth Circuit rejected an overly broad view of *Mid–Continent's* subrogation exclusion and held that *Mid–Continent* does not bar contractual subrogation simply because the insured has been fully indemnified. 611 F.3d 299, 305–07 (5th Cir. 2010); *see also Maryland Cas. Co. v. Acceptance Indem. Ins. Co.,* 639 F.3d 701 (5th Cir. 2011). The Fifth Circuit also held in *Amerisure* that *Mid–Continent* does not apply to bar contractual subrogation where an insurer has denied coverage. *Amerisure Ins. Co.,* 611 F.3d at 307; *see also Millis Devel. & Constr., Inc. v. America First Lloyd's Ins. Co.,* 809 F.Supp.2d 616, 635-36 (S.D. Tex. 2011) (holding that *Mid-Continent* bar to subrogation does not apply to preclude defending insurer from seeking

reimbursement for defense and indemnity costs paid over its pro rata share from non-defending insurer).

In the context of equitable (as opposed to contractual) subrogation, "[f]or an insurer to be entitled to equitable contribution from other insurers, the policies in question must insure the same party, the same interest, and the same risk." *Mt. Hawley Ins. Co. v. Lexington Ins. Co.*, 110 Fed.Appx. 371, 376 (5th Cir. 2004) (internal quotation marks and citations omitted); 15 Couch on Ins. § 218:3. "Accordingly, where insurers cover separate and distinct risks there can be no contribution among them." 15 Couch on Ins. § 218:3. Consecutive insurance policies provide distinct and independent contracts between the respective insurance companies and the insurers do not share an obligation to the insured. *Bain Enterprises LLC v. Mountain States Mut. Cas. Co.,* --F.Supp.3d--, No. EP-14-CV-472-PRM, 2016 WL 8138807, *20 (W.D. Tex. August 1, 2016). An insurer who pays more than its obligation "does so voluntarily" and "without a legal obligation to do so, thus precluding the insurer from recovering the excess it paid from other insurers. *Bain, supra* quoting *Mid-Continent,* 236 S.W.3d at 772.

Therefore, carriers must be cognizant of the *Mid-Continent* decision and consider it carefully before making any settlement or payment decisions where other insurance carriers are involved in the claim.