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***GILBERT, LENNAR AND EWING OUTSIDE OF  
THE CONSTRUCTION CONTEXT***

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Over the past few years, the Texas Supreme Court has immersed itself in insurance coverage questions arising from construction defect litigation. Front and center in this effort are a trilogy of cases beginning with *Gilbert Texas Construction, L.P. v. Underwriters at Lloyd's London*, 327 S.W.3d 118 (Tex. 2010) and then more recently *Lennar Corp. v. Markel Am. Ins. Co.*, 413 S.W.3d 750 (Tex. 2013) and *Ewing Construction Co. v. Amerisure Ins. Co.*, 420 S.W.3d 30 (Tex. 2014). While all of these opinions arose from construction defect situations, as a practical matter this caselaw impacts much more than the construction defect coverage questions addressed by the courts. This paper and presentation will address some of the implications of these opinions outside of the construction defect arena.

**I. *Gilbert Texas Construction, L.P. v. Underwriters at Lloyd's London*, 327 S.W.3d 118 (Tex. 2010)**

Most insurance practitioners and insurance specialists view the Texas Supreme Court's opinion in *Gilbert* as a unique decision resulting from an unusual fact situation to negate coverage to a contractor based its policy's contractual liability exclusion because the contractor's contractual risk was actually greater than its liability in the absence of the contract under the common law. Still, it has been cited almost 300 times in published opinions all over the United States, including many cases other than those analyzing construction defect coverage questions.

In a nutshell, *Gilbert* involved a suit by a general contractor (Gilbert Texas) against one of its excess insurers (Underwriters at Lloyd's) over coverage for a settlement it entered into with a property owner that suffered water damage in connection with Gilbert Texas' construction of a light rail line in downtown Dallas. In the underlying liability litigation, the trial court granted a partial summary judgment for Gilbert Texas on the plaintiff's tort and statutory claims because of the governmental immunity enjoyed by Gilbert Texas due to the fact that the construction project at issue was for the Dallas Area Rapid Transit Authority (DART). This ruling left only the plaintiff's breach of contract claims (asserted as a third-party beneficiary) to proceed to trial. The breach of contract claims, however, were not for Gilbert Texas' indemnity obligations to DART or some other party. Rather, they were based on a provision of the DART-Gilbert Texas contract requiring Gilbert Texas to protect its work site and surrounding property. *Id.* at 121-22. Accordingly the surrounding property owner sought breach of contract damages against Gilbert Texas

Many practitioners and commentators believe that the unique facts of *Gilbert* render it uneventful for most construction defect situations. This notion is substantiated by the Texas Supreme Court's limitation of the impact of *Gilbert* in *Ewing Construction Co. v. Amerisure Ins. Co.*, 420 S.W.3d 30 (Tex. 2014). While that perception may be true, the estoppel and prejudice analysis in *Gilbert* are important in all types of insurance claims and policies. For example in *Gilbert*, the Texas Supreme Court reaffirmed its

analysis in *Ulico Cas. Co. v. Allied Pilots Ass'n*, 262 S.W.3d 773, 787 (Tex. 2008) that coverage does not necessarily exist "simply because the insurer assumes control of the lawsuit defense," however, "if the insurer's actions prejudice the insured, the lack of coverage does not preclude the insured from asserting an estoppel theory to recover for any damages it sustains because of the insurer's actions."

Notwithstanding this rule, the Texas Supreme Court rejected Gilbert Texas' estoppel argument based on the apparent direction by Underwriters at Lloyd's for Gilbert Texas to move for summary judgment on the potentially covered tort and statutory claims, leaving only the non-covered breach of contract claim left in the lawsuit. In fact, Gilbert argued that if it did not assert its governmental immunity defense (which eliminated the plaintiff's tort and statutory claims), that Underwriters at Lloyd's would have denied coverage for lack of cooperation.

The Texas Supreme Court noted that Underwriters at Lloyd's issued excess policies and that Gilbert Texas' primary insurer assumed its defense. *Gilbert Texas*, 327 S.W.3d at 122. While the court of appeals specifically concluded that Underwriters at Lloyd's did not assume control of the defense of Gilbert Texas, the Texas Supreme Court held that "[w]e need not address whether Underwriters assumed control of the defense, however, because we conclude that even if Gilbert was deprived of the opportunity to make an informed decision as it claims, it was not prejudiced by the deprivation because in the final analysis, Gilbert did not have coverage for the contract claim." *Id.* at 137.

It should be noted that the Texas Supreme Court expressed no opinion on whether Gilbert Texas would have breached the policy's cooperation clause if Gilbert Texas refused to assert its governmental immunity defense. *Id.* at 138. Also, *Gilbert* involved coverage for a settlement and it did not analyze the duty to defend. There is no indication that Gilbert Texas' primary insurer ever withdrew its defense. Thus, the propriety of an insurer providing a defense to an insured and then taking steps to force the insured to obtain dismissals of covered claims to support a withdrawal of a defense was not decided by *Gilbert*.

## II. *Lennar Corp. v. Markel Am. Ins. Co.*, 413 S.W.3d 750 (Tex. 2013)

In its decision of last summer in *Lennar Corp. v. Markel*, the Texas Supreme Court tackled a pesky construction defect coverage case involving a homebuilder's remediation of 800 homes it built with faulty exterior insulation and finish systems. While the Texas Supreme Court's holding that the insurance policy at issue covered the remediation project was indeed noteworthy, also important were the Texas Supreme Court's holdings that: 1) the lack of prejudice suffered by the insurer as found by the jury precluded the insurer from denying coverage based on the homebuilder's voluntary payments to fund the remediation project without the insurer's consent; and 2) the trigger mechanism under Texas law for determining coverage between multiple consecutive policies for long tail claims is the "All Sums" approach as articulated in *Keene Corp. v. Insurance Co. of N. Am.*, 667 F.2d 1034, 1049-50 (D.C. Cir. 1981).

With respect to the Texas Supreme Court's ruling on when a showing of prejudice is required to support a coverage denial, *Lennar Corp. v. Markel* is important for all types of insurance claims. Here, the insurer argued that it was prejudiced as a matter of law because it was "not asked to adjust [the] claim, provide a defense, or be involved in negotiating [the] settlement[s], but [was] simply told that it [had] to pay for a voluntary payment." *Lennar Corp. v. Markel*, 413 S.W.3d at 755-56. Instead, the Texas Supreme Court agreed with the homebuilder that the issue of prejudice, i.e., whether "insured's unilateral settlement was a material breach of the policy--that is, that it significantly impaired the insurer's position ... is a question of fact, not of law." *Id.* at 756.

Interestingly, the consent to settlement requirement was located not only in the policy's Conditions, but also in the policy's Insuring Agreement. Thus, the insurer argued that even if it was not prejudiced as a matter of law for purposes of the insured's breach of the consent to settle condition, the fact that this requirement also existed in the Loss Establishment Provision in the Insuring Agreement excused the insurer from having to show prejudice. The Texas Supreme Court essentially found this to be a distinction without a difference. Here the Texas Supreme Court held that the purpose of the consent to settle condition and the Loss Establishment Provision were "exactly the same," i.e., "precluding liability for the insured's voluntary payments without the insurer's consent." *Id.* Accordingly, *Lennar Corp. v. Markel* can be read to expand the prejudice requirement to the entire insurance contract; not just the conditions.

Another important aspect of *Lennar Corp. v. Markel* outside of the construction context is the Texas Supreme Court's decision that Texas is an All Sums jurisdiction for the purpose of triggering policies for claims encompassing multiple policies. On this issue, the Texas Supreme Court rejected the Pro-Rata approach to allocate coverage amongst multiple insurers in long tail claims and instead it reaffirmed its language approving the *Keene Corp. v. Insurance Co. of N. Am.*, 667 F. 2d 1034, 1049-50 (D.C. Cir. 1981) All-Sums approach allowing the policyholder to pick its coverage period offering the most insurance. *Id.* at 758-59.

Interestingly notwithstanding the importance of the issue, the Texas Supreme Court did not conduct an in-depth analysis of the trigger issue. Rather, it adopted dicta in a 20 year old opinion that cited to *Keene* with approval in ruling that a tort claimant could not stack multiple policies over successive years in order to increase the limits for making a settlement demand within limits and invoke an insurer's duty to settle within limits--a/k/a the "Stowers" doctrine. *Id.* (citing and quoting *American Physicians Insurance Exchange v. Garcia*, 876 S.W. 2d 842, 855 (Tex. 1994)). Accordingly under Texas law as announced by *Lennar Corp. v. Markel*, an insured can take the position that it is singling out the policy year with the most coverage and then it can force the insurers on that year to cover a long tail claim.

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

The holding in *Gilbert* led to the appellate odyssey in *Ewing Construction Co., Inc. v. Amerisure Ins. Co.*, 420 S.W.3d 30 (Tex. 2014). *Ewing* began as a federal district

court summary judgment in favor of the insurer in a coverage suit analyzing a garden variety construction defect situation on the basis that in as much as the insured's liability was totally contractually based, the contractual liability exclusion precluded coverage in its entirety. That result was initially affirmed by the Fifth Circuit in a 2-1 decision. While the initial Fifth Circuit decision was on rehearing, the Fifth Circuit certified two questions to the Texas Supreme Court pertaining to the scope of the contractual liability exclusion and the exception to the exclusion when the insured likewise faces legal exposure to the claimant in the absence of the contract.

Upon acceptance of the certified questions, the Texas Supreme Court had to decide the law of Texas with respect to the contractual liability exclusion; i.e., whether Texas would adopt an expansive or a restrictive interpretation of the exclusion. In this regard, the Texas Supreme Court held that a general contractor who enters into a contract in which it agrees to perform its construction work in a good and workmanlike manner, without more, does not "assume liability" for damages arising out of the contractor's defective work so as to trigger the contractual liability exclusion. In light of that holding, the Texas Supreme Court did not have to analyze the exception to the exclusion for liability the insured would otherwise have in the absence of the contract. In essence, the Texas Supreme Court rejected the reasoning of the Texas federal courts and adopted a restrictive application of the contractual liability exclusion.

In the context of construction defect coverage litigation, *Ewing* may be the most important of the trilogy of cases. After all, if Texas adopted an expansive interpretation of the contractual liability exclusion, the most basic construction defect situations would be excluded from coverage under a standard commercial liability policy. The significance of *Ewing* outside of the construction context, however, is probably the most limited of the three opinions. There is no question that non-construction contracts can include terms where an insured party might assume liability greater than the liability imposed on the insured under the common law. Also, it is possible for these contracts to transfer risk in bodily injury situations. The important take away from *Ewing* outside of the construction context is that Texas has aligned itself with the jurisdictions taking a limited view of the contractual liability exclusion. *Id.* at 37.

Another important feature of *Ewing* is that it is a case reaching the Texas Supreme Court through certified questions from the federal Fifth Circuit Court of Appeals. State and Federal Courts analyzing Texas insurance and bad faith law have handed down inconsistent opinions on issues including the contractual liability exclusion and more recently, statutory bad faith damages. Meanwhile, the Texas Supreme Court has accepted and is accepting numerous insurance cases with certified questions from the Fifth Circuit and quite often, it has reversed the federal court holdings. Since so many insurance cases are filed or removed to federal court, the existence of inconsistent rules on similar issues in the parallel state and federal court universes can have outcome determinative consequences.

