BASICS OF INSURANCE COVERAGE ALL ATTORNEYS SHOULD KNOW

Prepared by
THOMISEE & THOMISEE, P.C.
806 Austin St.
Richmond, TX 77469
Tel. 281-341-5722
www.thomiseelaw.com

I. TYPICAL TYPES OF INSURANCE

Whether you are the plaintiff attorney or defense attorney, the claim you are dealing with will normally fall within the potential coverage of one of three types of insurance policies: 1) homeowners' insurance; 2) automobile insurance; and 3) commercial general liability insurance. This paper will discuss the types of claims and some of the issues which might arise under each type of insurance.

II. DUTY TO DEFEND

Before discussing the different types of insurance, it is important for each practitioner to understand the basic duties owed by the insurance carrier when a claim or suit is instituted against an insured.

Most liability policies, whether homeowners', auto, or general liability, contractually obligate the insurer to defend an insured only after a suit has been filed against him. Of course, this will be determined from the actual language in the policy.

A. The "Eight-Corners" Rule

In Texas, once suit is filed against the insured, whether the insurer owes a duty to defend is determined solely from comparing the terms of the insurance policy and the allegations in the petition. Generally, with limited exception, only these two documents should be utilized in determining whether there is a duty to defend. ***See Gilbert Tex. Construction, LP v. Underwriters at Lloyd's London*, 327 S.W.3d 118 (Tex. 2010); *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Merchants Fast Motor Lines, Inc.*, 939 S.W.2d 139 (Tex. 1997)**. This is known as the "eight-corners" rule.

The limited exception arises when it is not clear from the allegations whether the claim is covered. For example, suppose an insured is involved in an accident while in the course and scope of his sole proprietorship and suit is filed against him. The petition simply alleges negligence, and mentions nothing about the defendant insured being in course and scope since it is not relevant to the negligence cause of action against the driver. Suppose further that the auto liability policy covering the insured contains an exclusion which states that the coverage provided by the policy does not apply if the insured is in the course and scope of employment. If you compare only the allegations in the petition with the terms of the policy, a duty to defend would exist since there is nothing in the petition to trigger the exclusion in the policy. In this situation, however, the Texas appellate courts have held that extrinsic evidence may be considered to determine if a duty to defend under the policy exists. The courts hold that this exception applies only when the extrinsic evidence relates to a coverage issue only and does not relate in any way to the liability issues in the negligence suit. ***See Weingarten Realty Management Co. v. Liberty Mutual Fire Ins. Co.*, 343 S.W.3d 859 (Tex. App.–Houston [14th Dist.] 2011, pet. denied); *Gonzales v. American States Ins. Co. of Texas*, 628 S.W.2d 184 (Tex. App.–Corpus Christi 1982, no pet.); *State Farm Fire & Casualty Co. v. Wade*, 827 S.W.2d 448 (Tex. App.–Corpus Christi 1992, pet. denied); *see also GuideOne Elite Ins. Co. v.***

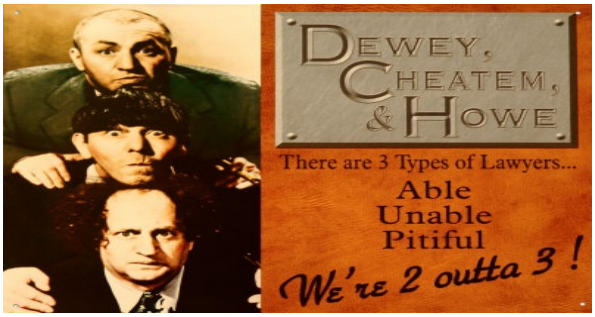
***Fielder Road Baptist Church*, 197 S.W.3d 305, 308 (Tex. 2006)**.

The duty to defend is determined by the court as a matter of law. Even if the allegations in the plaintiff's petition are false, fraudulent, or groundless, the insurer is obligated to defend if the allegations potentially come within the coverage of the insurance policy. ***Zurich American Ins. Co. v. Nokia, Inc.*, 268 S.W.3d 487 (Tex. 2008)**. If any part of the plaintiff's allegations potentially come within the coverage of the policy, the insurer has a duty to defend the insured as to all claims and causes of action even if some of the claims are otherwise not covered by the policy. ***Id.***

A separate and distinct duty of the insurer is the duty to indemnify. This is the duty to pay any judgment for covered causes of action asserted against the insured. Different from the duty to defend, the duty to indemnify is determined by the actual facts as found by the judge or jury. ***D. R. Horton-Texas, Ltd. v. Markel Int'l Insurance Co.*, 300 S.W.3d 740 (Tex. 2009); *Pine Oak Builders, Inc. v. Great American Lloyds Ins. Co.*, 279 S.W.3d 650 (Tex. 2009)**.

B. Reservation of Rights

In most liability insurance policies, the insurer, by contract, has the right to control the defense of the insured. Since the duty to indemnify is broader than the duty to defend, there may be situations where the pleadings trigger a duty to defend on the part of the insurer, but depending on the facts as determined by the jury or judge, there may be no duty to indemnify. When this occurs, the insurer will likely issue a reservation of right letter to the insured.



A reservation of rights letter simply notifies the insured that although a defense is being provided, the insurer is not waiving the right to contest coverage, and the insurer does not waive its coverage defenses. If an insurer provides a defense without issuing a reservation of rights letter, it could waive its right to contest its duty to indemnify should a judgment be entered against the insured.

If the determination of coverage under the policy involves the same facts as are being litigated in the liability suit, the insured has the right to retain his own counsel and look to the insurer for the payment of attorney's fees. ***See North County Mutual Ins. Co. v. Davalos*, 140 S.W.3d 685 (Tex. 2004)**.

C. Insured's Duty to Forward Suit Papers

An insurer's duty to defend is only triggered after suit is filed against the insured if the insured forwards the suit papers to her insurer **and** requests a defense be provided. If the insured is served with citation and does not contact her insurer, there is no duty to defend, and there will be no coverage if a default judgment is entered. ***National Union Fire Ins. Co. v. Crocker*, 246 S.W.3d 603 (Tex. 2008); *Jenkins v. State & County Mut. Fire Ins. Co.*, 287 S.W.3d 891 (Tex. App.–Fort Worth 2009, pet. denied)**. It should be noted that suit papers forwarded directly by the plaintiff

attorney to the defendant's insurer is not sufficient to trigger the insurer's duty to defend. ***Harwell v. State Farm Mut. Auto. Ins. Co.*, 896 S.W.2d 170 (Tex. 1995)**.

III. HOMEOWNERS' INSURANCE

A homeowners' policy provides two types of coverage: 1) property coverage; and 2) liability coverage.

With regard to liability coverage, a standard Texas homeowners' policy provides liability coverage for the insured in the event he is sued, subject to several exclusions, of course. Although most lay persons believe homeowners' liability coverage applies only when someone is hurt on the insured's property, this is not the case. As long as the claim is not otherwise excluded, a negligence claim against the insured will trigger the insurer's duty to defend. Typical exclusions to be aware is the exclusion which applies to a claim arising from the use of an auto, the exclusion which applies to a claim arising from the operation of a business, and the exclusion which applies if it is alleged the insured intended to inflict the injury.

A. Liability Coverage

In 1992, the author of this paper was involved in a case where the president of a fraternity was sued for allegedly biting off the female plaintiff's pinky finger. Allegedly, the president of the fraternity (the defendant) was fighting the plaintiff's boyfriend at a fraternity party at the fraternity house when the plaintiff grabbed the defendant from behind, and he bit off her finger and spit it out. She alleged in the petition that the defendant negligently inflicted the injury. The defendant was defended by his parents' homeowners' insurer. This shows how far reaching homeowners' liability coverage can be. The defendant was covered under the policy since he was a member of the household.

B. Foundation Claims

As stated above, insurance coverage will be determined by the terms of any specific policy. In general, however, a standard Texas homeowners' policy may provide coverage for foundation damage and ensuing damage depending on the circumstances.

Pursuant to the terms of most standard Texas homeowners' policies, foundation damage and ensuing damage is not covered if the foundation damages is caused by normal wear and tear, settling and/or movement of the earth. However, if the movement of the foundation is caused by a plumbing leak or other leak from a pipe or plumbing system, the policy likely provides coverage. ***See for example Balandran v. Safeco Ins. Co. of America*, 972 S.W.2d 738 (Tex. 1998)**.

C. No Coverage for Floods

A homeowner's policy excludes damage resulting from flood, surface water, waves, overflow of streams, etc. To be covered for damage caused by flooding, the owner must purchase a separate flood policy.

However, the standard homeowner's policy does provide coverage for loss caused by windstorm, hurricane and hail. Thus, damage caused by wind-driven rain is covered, but damage caused by rising water is not covered.

IV. AUTOMOBILE INSURANCE

An automobile liability policy applies to liability arising from auto accidents. Duh! But there are issues of which every practitioner should be aware.

A. What Is Use of an Auto?

First, it should be noted that the auto policy only applies if the alleged injury arises from the use of the auto. This seems black and white, but not always. For example, what if the insured driver of a covered auto pulls out his gun to show his passenger, and the gun is accidentally discharged injuring the passenger. If the passenger files suit against the insured alleging negligence, would this claim be covered by the driver's auto liability policy? According to Texas courts, the answer is "no". ***See National Union Fire Ins. Co. v. Merchants Fast Motor Lines, Inc.*, 939 S.W.2d 139, 142 (Tex. 1997)**. However, when a child was injured while climbing through a rear sliding window of a truck accidentally causing discharge of a mounted rifle, the Texas Supreme Court held that the injury did result from the use of the auto. ***See Mid-Century Ins. Co. v. Lindsey*, 997 S.W.2d 153, 154 (Tex. 1999)**.

The factors considered by Texas courts to determine if an accident arises from the use of an auto are: (1) the accident must have arisen out of the inherent nature of the automobile, as such; (2) the accident must have arisen within the natural territorial limits of an automobile, and the actual use must not have terminated; and (3) the automobile must not merely contribute to cause the condition which produces the injury, but must itself produce the injury. ***See Lancer Ins. Co. v. Garcia Holiday Tours*, 345 S.W.3d 50, 51 (Tex. 2011)(holding claim by bus passengers that they contracted tuberculosis from bus driver did not arise from use of auto)**.

B. Claims by Family Members Against Family Members

Prior to 1993, standard Texas personal auto policies excluded coverage for a claim by a family member against another family member arising from an auto accident. Obviously, the purpose of the exclusion was to prevent collusion and fraudulent claims.

In 1993, the Texas Supreme Court held that the exclusion violated the intent of the Texas Safety Responsibility Act (i.e., the mandatory insurance statute). Only four justices voted to completely invalidate the exclusion. Justice Cornyn was the fifth vote for invalidation of the exclusion, but in his concurring opinion, he stated that the exclusion should only be invalid up to the minimum statutorily-required insurance limit. Above the minimum limits, according to Cornyn, the exclusion should be valid and enforceable. ***See National County Mutual Fire Ins. Co. v. Johnson*, 879 S.W.2d 1 (Tex. 1993)**. This is the current state of the

law in Texas, and standard Texas personal auto policies now expressly state that claims by family members against family members are excluded only for amounts above the minimum limits of insurance required by the state.

C. Primary vs. Excess Issue

The standard "other insurance" clause in a Texas personal auto policy states that if there is other applicable liability insurance, the insurance provided to a "covered person" for the use of an auto which the named insured does not own is excess over any other applicable liability insurance.

If a person is driving another person's auto with permission and is sued as a result of an auto accident, the "other insurance" provisions in the policies will determine which insurance company should defend the driver. As a permissive user of the auto, the driver is a "covered person". In this example, there will be one insurance policy covering the automobile and another insurance policy covering the driver. If you apply the standard "other insurance" clause in the two policies, you will see that the policy covering the auto is primary, and the policy covering the driver is excess. Thus, the insurer covering the auto should assume the defense of the driver. An easy way to remember this is the old phrase that "the insurance goes with the car" meaning that the policy covering the auto is primary.

D. Uninsured Motorist Coverage

1. What Is It?

Every Texas auto policy is required by statute to provide uninsured motorist coverage and personal injury protection coverage unless such coverages are rejected by the insured in writing.

Uninsured motorist coverage (UM) includes underinsured motorist coverage (UIM). Thus, the coverage is triggered if the named insured or other "covered person" sustains damage and/or injury by an at-fault uninsured driver or underinsured driver.

According to the terms of the Texas auto policy, an underinsured vehicle is one which is covered by a liability policy but the limit of liability is not sufficient to pay the full amount the "covered person" is legally entitled to recover as damages.

An uninsured vehicle is one which is not covered by any insurance. The definition of uninsured vehicle also includes a vehicle which is a hit-and-run vehicle whose driver cannot be identified.

It is important to remember that UM/UIM coverage applies whether the insured is injured while occupying his vehicle, another vehicle, or no vehicle. In other words, if a person has UM/UIM coverage on his auto policy, the coverage applies even if the insured is injured while riding his bicycle or as a pedestrian. As long as the insured is struck by an auto, the coverage may apply.

2. Physical Contact Rule / Indirect Contact Rule

There are two doctrines or rules of which practitioners should be aware when dealing with an accident caused by an unidentified vehicle: 1) the physical contact rule; and 2) the indirect contact rule.

The physical contact rule states that the unidentified vehicle must make physical contact with the claimant or the claimant's vehicle to come within the uninsured coverage for the personal auto policy. ***See Mayer v. State Farm***

***Mut. Auto. Ins. Co.*, 870 S.W.2d 623 (Tex. App.–Houston [1st Dist.] 1994, no writ)**. Thus, if a claimant is forced off the road by a vehicle which makes no contact with him or if something falls from an unidentified vehicle causing injury or damage, the uninsured motorist coverage does not apply. ***See Nationwide Ins. Co. v. Elchehimi*, 249 S.W.3d 430 (Tex. 2008)**.

The indirect contact rule applies when an unidentified vehicle strikes a second vehicle causing the second vehicle to strike the claimant's vehicle. In this situation, since there is contact between the unidentified vehicle and another vehicle, this satisfies the physical contact rule, and the uninsured motorist coverage is applicable. ***See Latham v. Mountain States Mutual Casualty Co.*, 482 S.W.2d 655 (Tex. Civ. App.–Houston [1st Dist.] 1972, writ denied)**.

3. Accident While In Course and Scope

A standard exclusion in the UM section of the Texas personal auto policy states that UM coverage does not apply directly or indirectly to benefit any insurer under workers' compensation law. This exclusion has been applied differently by the courts depending the circumstances.

If a person receives workers' compensation benefits as a result of an auto accident, and the person *receives UM benefits from her own auto policy*, the workers' compensation insurer cannot subrogate against the UM benefits. ***See Liberty Mutual v. Kinser*, 82 S.W.3d 71 (Tex. App.–San Antonio 2002, no pet.)**. However, if a person receives workers' compensation benefits as a result of an auto accident and *receives UM benefits from his employer's auto policy*, the workers' compensation can subrogate against the UM benefits. ***See Erivas v. State Farm Mutual Auto. Ins. Co.*, 141 S.W.3d 671 (Tex. App.–El Paso 2004, no pet.)**.

There is an exclusion in the standard Texas personal auto policy which states that the insurer will only pay UM/UIM benefits not paid or payable under any workers' compensation law. This exclusion, however, has been held to be invalid or ineffective to the extent it reduces UM/UIM protection below the minimum limits required by statute. ***See Mid-Century Insurance Co. of Texas v. Kidd*, 997 S.W.2d 265 (Tex. 1999)**.

4. Settling Liability Claim and Pursuing UIM Claim

In an underinsured situation, the injured party may want to settle with the underinsured motorist's insurer and then pursue a claim for UIM benefits under her own policy. However, the UIM claimant must get permission from his insurer before settling and releasing her claims against the underinsured motorist. This is because the UIM insurer has a right to subrogate against the underinsured motorist.

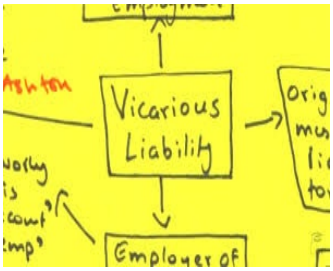
It should be noted that although consent to settle and release the underinsured motorist is required, failure to get consent from the UIM insurer will not bar the claim for benefits unless the UIM insurer is prejudiced by the release of the claims against the underinsured motorist.

***See Hernandez v. Gulf Group Lloyds*, 875 S.W.2d 691 (Tex. 1994)**.

5. Coverage for Punitive Damages Under UM Section of Auto Policy

Although it has been held that Texas public policy generally does not prohibit coverage for punitive damages in a liability policy, several appellate courts have held that it is against public policy to insure for punitive damages in the uninsured motorist context. ***See Milligan v. State Farm Mut. Auto. Ins. Co.*, 940 S.W.2d 228 (Tex. App.–Houston [14th Dist.] 1997, pet. denied); *State Farm Mut. Auto. Ins. Co. v. Shaffer*, 888 S.W.2d 146 (Tex. App.–Houston [1st Dist.] 1994, pet. denied); *Vanderlinden v. USAA Prop. & Cas. Ins. Co.*, 885 S.W.2d 239 (Tex. App.–Texarkana 1994, pet. denied)**. These courts hold that the objectives of punishment and deterrence cannot be accomplished in an uninsured motorist claim because the wrongdoer is not even involved.

E. Employer May Be Covered Under Employee's Personal Auto Policy



A standard personal auto policy has an omnibus clause which states that "covered person" includes for the named insured's covered auto "any person or organization . . . with respect to legal responsibility for acts or omissions of a person for whom coverage is afforded . . ." under the policy. In other words, if a person is involved in an accident while driving her insured vehicle in the course and scope of employment and her employer is sued on a theory of vicarious liability, the employer is insured under the employee's personal auto policy.

V. COMMERCIAL GENERAL LIABILITY INSURANCE (CGL)

A commercial general liability policy (CGL) provides coverage for liability arising from the operation of a business.

Usually, a CGL policy is "occurrence" based meaning that the policy covers damage or injury which occurs during the policy period (as opposed to a claims-made policy which provides coverage for a claim made during the policy period).

A. No Coverage for Injury to Employee

A standard exclusion in a CGL policy is an exclusion which states that the coverage does not apply to injury to an employee. The reason, of course, for such an exclusion is that if the CGL policy provided such coverage, it would essentially convert the policy into a workers' compensation policy. If the insured wants to be protected for injuries to employees, it needs to purchase workers' compensation insurance which is much more expensive.

Many companies today attempt to control risk by contracting with a staff leasing company to provide workers. However, this can be dangerous. If the company controls the details of the work of the leased workers, the workers may become the "borrowed employees" of the company. If the "borrowed employee" files suit against the company for injury sustained in the course and scope of his work (assuming the client company is not a workers' compensation subscriber), the company's CGL insurer could deny coverage based on the "injury to employee" exclusion.

It should be noted that if the employee leasing company is licensed under the Staff Leasing Services Act, §91.042, Texas Labor Code, different rules apply. If the company is licensed, and if it is covered by a valid Texas workers' compensation policy, then both it and the client company get the protection of the exclusive remedy defense. However, the CGL would still provide no coverage.

B. Care, Custody, and Control Exclusion

If an insured conducts a business in which it has possession of a customer's property either for repair or storage, it may not be covered if the customer files suit for damage to the property while in the insured's possession. The standard CGL policy excludes coverage for property damage to property in the care, custody; and control of the insured. Special coverage would be required to protect the insured. For example, a garage would need to be covered by a garagekeeper's policy to have coverage for damage to its customer's autos. ***See Frito-Lay, Inc. v. Trinity Universal Ins. Co.*, 2010 Tex. App. LEXIS 9271 (Tex. App.–Dallas 2010, pet. denied)**.

C. What is "Bodily Injury" and "Property Damage"

In the standard CGL policy, "bodily injury" is defined as "bodily injury, sickness or disease sustained by a person, including death resulting from any of these at any time". This seems straight forward, but what about a claim against the insured for mental anguish?

Texas courts have addressed whether pure mental anguish comes within the definition of "bodily injury" more than once. The seminal case is ***Trinity Universal Ins. Co. v. Cowan*, 945 S.W.2d 819 (Tex. 1997)**. In *Trinity Universal*, the Texas Supreme Court held that a claim for purely emotional injury unaccompanied by any physical manifestations did not come within the definition of "bodily injury" where "bodily injury" was defined as "bodily harm, sickness or disease". ***See also Evanston Ins. Co. v. Legacy of Life, Inc.*, 370 S.W.3d 377 (Tex. 2012)**.

"Property damage" is defined in the standard CGL policy as "physical injury to tangible property, including all resulting loss of use of that property . . . and loss of use of tangible property that is not physically injured." If a claim is made against the insured for loss of use of tangible property as a result of conduct of the insured, the claim constitutes "property damage" whether it is physically damaged or not. ***See for example Mid-Continent Casualty Co. v. Camaley Energy Co.*, 364 F. Supp. 2nd 600 (N.D. Tex. 2005)(plaintiff's claim that it was evicted from leasehold because driller drilled well in easement owned by another party was a claim of "loss of use of tangible property" and therefore property damage as defined in policy)**.

However, if the claim is actually one for an economic loss (e.g., loss in value or benefit of the bargain due to an alleged misrepresentation of the insured), then the claim is not one for "property damage". ***See Lay v. Aetna Ins. Co.*, 599 S.W.2d 684 (Tex. Civ. App.–Austin 1980, pet. denied)**.

D. Coverage for Punitive Damages

Does Texas public policy prohibit a

liability insurance provider from indemnifying an award for punitive damages imposed on its insured because of gross negligence? No.

In ***Fairfield Ins. Co. v. Stephens Martin Paving, LP*, 246 S.W.3d 653 (Tex. 2008)**, the Texas Supreme Court held that because parties have the freedom of contract, Texas public policy generally does not prohibit coverage for punitive damages. However, an insurer can exclude coverage for punitive damages if it so wishes. It is a matter of contract. This holding follows the majority of jurisdictions. ***See also American Home Assurance Co. v. Safway Steel Products Co.*, 743 S.W.2d 693 (Tex. App.–Austin 1987, pet. denied)**.

THOMISEE & THOMISEE

A Professional Corporation
Attorneys At Law

806 Austin St.
Richmond, TX 77469
Tel. 281-341-5722
Fax 281-341-5755
dthomisee@thomiseelaw.com
jthomisee@thomiseelaw.com