NO. 13-0670

IN THE
SUPREME COURT OF TEXAS

IN RE DEEPWATER HORIZON

BRIEF OF AMICUS CURIAE

THE NATIONAL ASSOCIATION OF MANUFACTURERS

URGING AFFIRMATIVE ANSWERS TO BOTH QUESTIONS CERTIFIED BY THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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TO THE HONORABLE SUPREME COURT OF TEXAS:

Amicus Curiae The National Association of Manufacturers submits this brief to urge the Court to adhere to two fundamental propositions of insurance law recognized by this Court for more than 125 years: (1) the scope of insurance coverage must be determined from the face of the policy itself and not from external documents, unless the intent to incorporate other terms is unambiguously clear and not dependent on implication[1]; and (2) if an insurance coverage provision is susceptible to more than one reasonable interpretation, the court must interpret the provisions in favor of the insured, so long as that interpretation is reasonable.[2] The Court should not create new exceptions to these firmly-entrenched rules in this case. Accordingly, the Court should answer both certified questions "yes."

[1] *See, e.g., Goddard v. East Tex. Fire Ins. Co.*, 1 S.W. 906, 907 (Tex. 1886) ("The policy is the contract; and if outside papers are to be imported into it, this must be done in so clear a manner as to leave no doubt of the intention of the parties."); *Urrutia v. Decker*, 992 S.W.2d 440, 442 (Tex. 1999) (External terms are incorporated into an insurance policy only "by an explicit reference clearly indicating the parties' intention to include that contract as part of their agreement.").

[2] *See, e.g., Goddard*, 1 S.W. at 909 ("when an instrument of this character is inconsistent or ambiguous in its provisions, it must be construed most favorably for the assured"); *Hibernia Ins. Co. v. Bills*, 29 S.W. 1063, 1065 (Tex. 1895) ("every doubt arising upon the terms of the instrument must be resolved against the insurer"); *Brown v. Palatine Ins. Co.*, 35 S.W. 1060, 1061 (Tex. 1896) ("If the words admit of two constructions, that one will be adopted most favorable to the insured."); *Evanston Ins. Co. v. Legacy of Life, Inc.*, 370 S.W.3d 377, 380 (Tex. 2012) ("As to the policy, if a term is susceptible to more than one reasonable interpretation, we must resolve that uncertainty in favor of the insured.").

INTEREST OF AMICUS

The National Association of Manufacturers (NAM) is the largest manufacturing association in the United States, representing small and large manufacturers in every industrial sector and in all 50 states. Manufacturing employs nearly 12 million men and women, contributes more than $1.8 trillion to the U.S. economy annually, has the largest economic impact of any major sector, and accounts for two-thirds of private-sector research and development. The NAM is the powerful voice of the manufacturing community and the leading advocate for a policy agenda that helps manufacturers compete in the global economy and create jobs across the United States.

NAM's members, both in Texas and nationwide, have a vital interest in the predictable and consistent interpretation of insurance policies and thus in maintaining the clear rules in place for more than 125 years. Any change to those rules will have an adverse effect on the manufacturing industry.

Amicus has no direct financial interest in the outcome of this litigation. The BP Appellants are members of NAM. No financial contributions have been or will be made to amicus by the BP Appellants or their affiliates in connection with the preparation of this brief. The fees for this brief will be paid solely by amicus.

SUMMARY OF THE ARGUMENT OF AMICUS

At issue in this case is whether, with respect to pollution claims against BP for oil emanating from the Deepwater Horizon oil spill, BP is entitled to coverage as an additional insured under primary and excess policies issued to Transocean for the benefit of both BP and Transocean, or whether the additional insured coverage is limited to Transocean's contractual indemnity obligation to BP. The Fifth Circuit has certified two questions to this Court:

> 1. Whether *Evanston Ins. Co. v. ATOFINA Petrochems., Inc.*, 256 S.W.3d 660 (Tex. 2008), compels a finding that BP is covered for the damages at issue, because the language of the umbrella policies alone determines the extent of BP's coverage as an additional insured if, and so long as, the additional insured and indemnity provisions of the Drilling Contract are "separate and independent"?
>
> 2. Whether the doctrine of *contra proferentem* applies to the interpretation of the insurance coverage provision of the Drilling Contract under the *ATOFINA* case, 256 S.W.3d at 668, given the facts of this case?

In re Deepwater Horizon, 728 F.3d 491, 500 (5th Cir. 2013). Both questions should be answered "yes." Affirmative answers are mandated by fundamental tenets of insurance law consistently recognized and applied by this Court for more than 125 years.

Question 1. The scope of insurance coverage must be determined from the face of the policy alone. An intent to incorporate other terms from external documents must be stated in the policy in unambiguously clear language, and

external terms will not be imported by implication. Here, nothing on the face of the policy unambiguously limits the scope of additional insured coverage or clearly imports any potentially limiting language from the drilling contract.

Express language is commonly used in policies to limit the scope or amount of additional insured coverage. No express language was used in this case, and it should not be implied by the courts. Question 1 should be answered "yes."

Question 2. If an insurance coverage provision is susceptible to more than one reasonable interpretation, the court must interpret the provision in favor of the insured, so long as that interpretation is reasonable. This rule is better labelled as the Ambiguity Rule rather than the rule of *contra proferetem*, because it is not based exclusively on the premise that a writing is construed against the drafter. Nor is it based principally on the concept that an insurance policy is a contract of adhesion between parties with unequal bargaining power. Instead, the Ambiguity Rule – from the time it was first adopted by this Court in the 1800s to the present day – is founded on an amalgamation of general contract-interpretation rules and rules developed specifically in the context of insurance.

The multi-premised Ambiguity Rule has been consistently recognized and applied by this Court for more than 125 years, and is in place in 49 states. It is universally understood in the insurance industry and incentivizes insurers to issue policies that clearly and unambiguously delineate any limits on and exceptions to

coverage. Insurers have known for more than a century that they bear the risk of ambiguity in the policies they issue. Their business is assessing and accepting risk through insurance policy language. The Ambiguity Rule is an objective rule that avoids expensive, time-consuming, and fact-intensive litigation over coverage disputes by allowing many cases to be determined as a question of law from the four corners of the policy. The Court should not create a subjective and problematic "sophisticated insured" exception to the venerable Ambiguity Rule. Question 2 should be answered "yes."

ARGUMENT OF AMICUS

I. Question 1: The scope of insurance coverage must be determined from the four corners of the policy, and this Court should not imply limitations or exceptions from external documents in the absence of clear and express language.

Under the four corners rule, coverage is determined from the face of the policy. Any incorporation of external terms must be clear and manifest, and the courts may not add those terms by implication. Here, the policies did not expressly limit the scope or amount of additional insured coverage nor did they expressly incorporate external terms as to the scope or amount of coverage from the drilling contract.

A. The four corners rule: the scope of coverage must be determined from the face of the policy.

When analyzing an insurance contract, the court's "primary goal is to determine the contracting parties' intent *through the policy's written language*." *State Farm Lloyds v. Page*, 315 S.W.3d 525, 527 (Tex. 2010) (emphasis added). That analysis "is confined within the four corners of the policy itself." *Id.* The court thus ascertains the parties' intent by looking only to the face of the policy to see what is actually stated and does not consider what was allegedly meant. *Fiess v. State Farm Lloyds*, 202 S.W.3d 744, 746 (Tex. 2006).

B. Adoption of external terms must be clear and unambiguous.

Sometimes either the insurance company or the insured will contend that an insurance policy incorporates another document. The four corners rule also applies when a court must decide whether the parties intended to incorporate the terms of external documents into an insurance policy. As this Court recognized more than 125 years ago: "The policy is the contract; and if outside papers are to be imported into it, this must be done *in so clear a manner as to leave no doubt* of the intention of the parties." *Goddard v. East Tex. Fire Ins. Co.*, 1 S.W. 906, 907 (Tex. 1886) (emphasis added). External terms are incorporated into an insurance policy only "by an *explicit reference clearly indicating* the parties' intention to include that contract as part of their agreement." *Urrutia v. Decker*, 992 S.W.2d 440, 442 (Tex. 1999) (emphasis added).

The intent to incorporate external terms thus must be clear and manifest, and it will not be imported by implication:

> Separate documents may become a part of a contract of insurance by law, by being annexed or attached to the policy, or by a clear reference in the policy that they are intended to be a part thereof. *To have this effect, the intent to incorporate them should be plainly manifest and not dependent upon implication*.

2 COUCH ON INSURANCE 3D § 18:23 (2010 rev. ed.) (emphasis added); *see also* 1A COUCH ON INSURANCE 3D § 17:16 ("[S]tatements in a collateral document do not become a part of the contract of insurance unless they are referred to in a sufficiently clear manner to indicate that the parties intended to make them a part of the contract.").

Clear and manifest language of incorporation requires more than merely mentioning an external document. *Bob Montgomery Chevrolet, Inc. v. Dent Zone Cos.*, 409 S.W.3d 181, 189 (Tex. App.—Dallas 2013, no pet.). There must be no doubt that the parties intended for the specific terms of the other document to become part of the contract. *See id.*

In addition, reference to a document for a particular purpose incorporates that document only for the specified purpose, absent clear language that imports all of the terms and provisions of the external agreement. *Id.* at 189-90; *see, e.g.*, *Phillips Petroleum Co. v. St. Paul Fire & Marine Ins. Co.*, 113 S.W.3d 37, 44 (Tex. App.—Houston [1st Dist.] 2003, pet. denied) (policy reference to external

contract was to clarify who was an additional insured under the policy, but did not incorporate external terms to vary coverage as stated on the face of the policy); *Valero Mktg. & Supp. Co. v. Baldwin Contracting Co.*, No. H-09-2957, 2010 WL 1068105, at *5 (S.D. Tex. Mar. 19, 2010) (applying Texas law) (statement that price quote subject to general terms and conditions in another agreement incorporated that agreement only with respect to pricing, and did not reflect clear intent to incorporate other terms, including a forum-selection clause); 17A C.J.S. *Contracts* § 402 (2013) ("if a written contract refers to another writing for a particularly designated purpose, the other writing becomes a part of the contract only for the purpose specified").

In the absence of clear and express language, the external terms do not become part of the contract. *See, e.g., Phillips Petroleum Co. v. St. Paul Fire & Marine Ins. Co.*, 113 S.W.3d at 44 (policy providing that Phillips was an additional insured under the policy "as required by contract" with the named insured did not evidence clear intent to incorporate the terms of the external contract into the policy); *Schneider Nat'l Transp. v. Ford Motor Co.*, 280 F.3d 532, 538-39 (5th Cir. 2002) (applying Texas law) (reference in excess policy to "underlying insurance" did not incorporate into excess policy provisions of primary policy providing for defense costs); *Rutter v. Conseco Life Ins. Co.*, Civ. Action No. 3:09-CV-680-DPJ-JCS, 2011 WL 2532467, at *4 (S.D. Miss. June 24, 2011) (applying Mississippi

law) (insurance policy's reference to grace notices to be issued in the event of a late payment did not incorporate terms of those notices into policy); *M.J. Delaney Co. v. Murchison*, 393 S.W.2d 705, 709 (Tex. Civ. App.—Tyler 1965, no writ) (statement that stipulations, responsibilities, billing, and payments on a well would be the same as those on two prior completed wells did not incorporate the terms of the contract for the prior wells); *Bob Montgomery Chevrolet, Inc. v. Dent Zone Cos.*, 409 S.W.3d at 193 (reference in contract to terms on internet site did not evidence a clear intent to incorporate those terms into the contract); *cf. Berwick v. Wagner*, 336 S.W.3d 805, 810 (Tex. App.—Houston [1st Dist. 2011, pet. denied) (statement that the judgment was issued "pursuant to" the parties' stipulation did not incorporate the terms of the stipulation).

The *Phillips Petroleum* case is illustrative. There, a Master Service Agreement (MSA) required the general contractor, Zachry, to obtain comprehensive general liability (CGL) insurance with a combined single limit of $1,000,000 per occurrence and to name Phillips, the refinery owner, as an additional insured. The policy extended coverage to any organization "required to be made an additional protected person in a written contract" and to "an additional protected person as required by contract." *Phillips Petroleum Co. v. St. Paul Fire & Marine Ins. Co.*, 113 S.W.3d at 41-42 (emphasis deleted). While the Zachry policy provided for $1,000,000 in coverage, that amount was subject to erosion for

defense costs and a $1,000,000 deductible. *Id.* at 42-43. After a refinery explosion injured Zachry employees, Phillips sought a defense and coverage under the policy.

Phillips asserted that language in the policy that it was an additional insured "as required by contract with" Zachry incorporated all of the terms of the MSA into the policy. *Id.* at 43. Because the MSA required traditional CGL coverage, Phillips asserted it was entitled to an unlimited defense until policy limits were exhausted by settlement or judgment, in other words, coverage not subject to a deductible or erosion based on defense costs. *Id.*

The court of appeals rejected Phillips' incorporation-by-reference argument. The court held that the reference to the MSA merely clarified who was covered as an additional insured but did not evidence a clear intent to incorporate the specific terms of the MSA into the policy:

> Moreover, the policy's additional insured endorsement language, set out above, naming Phillips as an additional insured under the policy "as required by contract with you [Zachry]," is not, as argued by Phillips, "an explicit reference clearly indicating the parties' intention" to include the terms and provisions of the M.S.A. § as part of the policy. *See Urrutia*, 992 S.W.3d at 442. *This language merely clarifies which persons or entities are to be additional insureds under the policy*, namely, those persons "required to be made an additional protected person in a written contract executed prior to a loss."

Id. at 44 (brackets in original; emphasis added).

The same analysis applies here. The policies at issue extend additional insured coverage to any entity that the named insured is obligated by "any oral or written 'Insured Contract' . . . to provide insurance such as is afforded by this Policy." It further defines the term "Insured Contract" to be a written or oral contract under which the name insured assumes the tort liability of another party.[3] As in *Phillips Petroleum*, the policies reference the external document (here, the drilling contract) for the purpose of identifying who is an additional insured. And, also as in *Phillips Petroleum*, there is no explicit reference clearly indicating an intent to import the terms of the drilling contract into the policies.

The mischief caused by allowing such a loose reference to incorporate the terms of an external document into an insurance policy is manifest. In *Phillips Petroleum*, it would have excluded the $1,000,000 deductible and the provision that defense costs eroded policy limits – in other words, completely rewritten the policy. Many external agreements executed by the named insured will have provisions that the insurer (and insured) would never agree to if those terms had been included in the policy. Insured Contracts are likely to contain provisions

[3] The definition of "Insured Contract" is commonly included in insurance policies not for the purpose of limiting additional insured coverage but to expand contractual-liability coverage for the named insured to include any contractual obligation to indemnify third parties. *See* Am. Bar Ass'n, THE HANDBOOK ON ADDITIONAL INSUREDS § 3.V (2012); *see also, e.g., Gilbert Tex. Constr., L.P. v. Underwriters at Lloyd's London*, 327 S.W.3d 118, 133 (Tex. 2010) (examining scope of "insured contract" exception to contractual-liability exclusion). The policies here contain an "Insured Contract" exception to the contractual-liability exclusion. Appellants' Appendix at AA19, 27, 39, 49, 57, 84.

relating to forum and resolution of disputes. If a reference to an Insured Contract imports other terms of that contract, is the insurer then bound by an arbitration clause, a forum-selection clause, a choice-of-law clause, or similar provisions contained in the contract? The rule adopted by this Court more than 125 years ago – that external terms will not be imported into the policy absent clear and manifest intent – is sound. The Court should not create an exception to that rule in this case.

The policies at issue here do not meet the standard for clear and manifest incorporation by reference. Nothing on the face of the policies unambiguously limits the scope of additional insured coverage or clearly imports any potentially limiting language from the drilling contract.

C. Express language is commonly used in policies to limit the scope or amount of additional insured coverage.

Additional insured endorsements are common. Express language is routinely used in policies to limit the scope or amount of additional insured coverage, including expressly limiting coverage to the scope and amount of the indemnity obligation of the named insured. *See, e.g.*, *Urrutia v. Decker*, 992 S.W.2d at 441 (policy expressly provided additional insured coverage "only to the extent and for the limits of liability agreed to under contractual agreement with the named insured"); *United Nat'l Ins. Co. v. Motiva Enters., L.L.C.*, No. Civ. A. H-04-2924, 2006 WL 83482, at *3 (S.D. Tex. Jan. 12, 2006) ("the extent and scope of coverage under this insurance for the additional insured will be no greater than

the extent and scope of indemnification of the additional insured which was agreed to by the named insured"); *Clayton Williams Energy, Inc. v. Nat'l Union Fire Ins. Co.*, No. Civ. A. 03-2980, 2004 WL 2452780, at *1 n.14 (E.D. La. Nov. 1, 2004) (additional insured endorsement stating that "the insurance provided will not exceed the lesser of: 1. The coverage and/or limits of this policy, or 2. The coverage and/or limits required by said contract or agreement."); *CertainTeed Corp. v. Employers Ins. of Wausau*, 939 F. Supp. 826, 829 (D. Kan. 1996) (policy provided that additional insured coverage "shall include only the insurance that is required to be provided by the terms of such agreement to procure insurance"); *see also, e.g., Shell Chem. L.P. v. Discover Prop. & Cas. Ins. Co.*, No. H-09-2583, 2010 WL 1338068, at *2 (S.D. Tex. Mar. 29, 2010) (policy provided for additional insured coverage "but only with respect to their legal liability for acts or omissions of" the named insured).

The Insurance Service Organization (ISO), a leading developer of standardized insurance policy language, has issued additional insured endorsement forms that contain express language, similar to that in the cases cited above, offering parties the option to limit the scope or amount of additional insured

liability where so intended.[4] No limiting language was included in the Transocean policies at issue here.

The Fifth Circuit addressed an analogous situation in *Schneider Nat'l Transport v. Ford Motor Co.*, 280 F.3d at 538-39 (applying Texas law). There the excess insurance policy provided that it was to continue "as underlying insurance" after the primary policy limits had been exhausted. The insured argued that the excess policy incorporated the terms of the primary policy, and that the excess insurer was therefore required to provide coverage for defense costs to the same degree as provided in the primary policy. The court rejected the argument. The court noted that excess policies commonly contain express language specifically incorporating the terms of the primary policy, but the policy at issue before the court did not. The court held that the reference to "underlying insurance," without more, was insufficient to incorporate the terms of the underlying policy:

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[4] Standard ISO Additional Insured Endorsement CG 20 38 04 13 includes the following:

> [T]he insurance afforded to such additional insured described above . . . will not be broader than that which you [the insured] are required by the contract or agreement to provide for such additional insured.
>
> The most we [the insurer] will pay on behalf of the additional insured is the amount of insurance: 1. Required by the contract or agreement described in Paragraph A.1.; or 2. Available under the applicable Limits of Insurance shown in the Declarations; whichever is less.

Donald S. Malecki & Jack P. Gibson, THE ADDITIONAL INSURED BOOK 454-55 (7th ed. 2013).

> An incorporation by reference must be sufficiently clear for this court to conclude the parties intended the incorporation. . . .
>
> There is nothing in appellants' policy here that uses the term "incorporation" or "incorporation by reference" or "follow form" language. Nor is there any other express terminology stating that the provisions of the underlying policy are in some way to be a part of the terms of the excess policy, or that the parties intended this result. Absent such language, this Court is unable to hold that the parties intended, much less inferred, the defense cost burden be pro rated between all carriers as was provided for in the policy of Planet, one of the underlying carriers.

Id. at 538-39.

Like the excess policy in *Schneider*, the policies here do not expressly use the terms "incorporation" or "incorporation by reference," nor is there other express terminology that would incorporate any potentially limiting language from the drilling contract. The Court should not correct this failure by implying terms not stated in the four corners of the policies. As the Fifth Circuit recognized in its certification order, "the Insurers were involved in drafting the umbrella policy language at issue, and the failure of that policy language to limit coverage in underlying 'Insured Contracts' to the liabilities assumed by the named insured in those contracts is part of what ails the Insurers now." *In re Deepwater Horizon*, 728 F.3d at 500.

D. Question 1 should be answered "yes."

While Question 1 appears to pose a complex question of additional insured coverage and indemnity, its answer is governed by first principles. The scope of

insurance coverage must be determined from the face of the policy alone. An intent to incorporate other terms from external documents must be stated in the policy in unambiguously clear language, and external terms will not be imported by implication. Here, nothing on the face of the policies unambiguously limits the scope of additional insured coverage or clearly imports any potentially limiting language from the drilling contract. No express language was used in this case, and it should not be implied by the courts. Question 1 should be answered "yes."

II. Question 2: This Court should not create a "sophisticated insured" exception to the Ambiguity Rule, under which a court must interpret an ambiguous insurance coverage provision in favor of the insured.

The Court does not need to reach Question 2 if it answers Question 1 "yes." If the Court chooses to reach Question 2, it should also be answered "yes."

The Ambiguity Rule has been part of the fabric of Texas insurance jurisprudence for more than 125 years and reflects an amalgamation of contract and insurance principles. The multi-premised Ambiguity Rule is universally understood in the insurance industry and incentivizes insurers to issue policies that clearly and unambiguously delineate any limits on and exceptions to coverage. It also expedites coverage disputes by allowing many cases to be determined as a question of law from the four corners of the policy. The Court should not create an exception to the Ambiguity Rule for so-called "sophisticated" insureds – a

subjective and problematic test that ignores the multiple bases for the Ambiguity Rule, and that will increase the cost and time to resolve coverage disputes.

A. The Ambiguity Rule has been consistently recognized and applied by this Court for more than 125 years.

The Ambiguity Rule is bedrock law in Texas. Since 1886, this Court has repeatedly recognized and applied the rule to insurance coverage disputes. The following cases demonstrate this Court's consistently-held view that construing ambiguities against the insurer is a settled rule of Texas insurance law:

- *Goddard v. East Tex. Fire Ins. Co.*, 1 S.W. 906, 909 (Tex. 1886) ("when an instrument of this character is inconsistent or ambiguous in its provisions, it must be construed most favorably for the assured").

- *Hibernia Ins. Co. v. Bills*, 29 S.W. 1063, 1065 (Tex. 1895) ("These authorities suffice to illustrate the rule that the terms of the policy must be broad enough to cover, under a strict construction, the facts of the case under consideration, and that every doubt arising upon the terms of the instrument must be resolved against the insurer.").

- *Brown v. Palatine Ins. Co.*, 35 S.W. 1060, 1061 (Tex. 1896) ("If the words admit of two constructions, that one will be adopted most favorable to the insured.").

- *McCaleb v. Cont'l Cas. Co.*, 116 S.W.2d 679, 682 (Tex. 1938) ("In construing the language used in a policy, if it is ambiguous or contains inconsistent terms, in order to arrive at the true intention of the parties expressed therein, the well-known rule that insurance contracts should be construed strictly against the insurer, and in favor of the insured, will control.").

- *United Serv. Auto Ass'n v. Miles*, 161 S.W.2d 1048, 1050 (Tex. 1942) ("It would ignore 'a settled principle of insurance law, laid down in a host of decisions, that language of a policy which is susceptible of more than one construction should be interpreted strictly against the insurer and liberally in

favor of the insured.' 24 Tex. Jur., sec. 29, p. 705, citing twenty nine Texas cases.").

- *Davis v. Nat'l Cas. Co.*, 175 S.W.2d 957, 960 (Tex. 1943) ("If it may be said that the language of the policy, which was selected by the insurer, is in its use of the word . . . ambiguous or of uncertain meaning, it is at least fairly susceptible of the construction that we have given it and that construction should be adopted because it is favorable to the insured.").

- *Lloyds Cas. Insurer v. McCrary*, 229 S.W.2d 605, 609 (Tex. 1950) ("[A]mbiguous terms of an insurance policy should be construed in favor of the insured where they are reasonably susceptible of such a construction.").

- *Providence Washington Ins. Co. v. Proffitt*, 239 S.W.2d 379, 381 (Tex. 1951) ("It is a settled rule in this state that policies of insurance will be interpreted and construed liberally in favor of the insured and strictly against the insurer. It is also well settled that exceptions and words of limitation will be strictly construed against the insurer.") (citations omitted).

- *Cont'l Cas. Co. v. Warren*, 254 S.W.2d 762, 763 (Tex. 1953) ("[T]he insurer may not escape liability merely because his or its interpretation should appear to us a more likely reflection of the intent of the parties than the interpretation urged by the insured. The latter has to be no more than one which is not itself unreasonable. A related or subsidiary rule is 'that exception and words of limitation will be construed against the insurer.'") (citations omitted).

- *Ramsay v. Md. Am. Gen. Ins. Co.*, 533 S.W.2d 344, 349 (Tex. 1976) ("It is a settled rule that policies of insurance will be interpreted and construed liberally in favor of the insured and strictly against the insurer, and especially so when dealing with exceptions and words of limitation. When the language of a policy is susceptible of more than one reasonable construction, the courts will apply the construction which favors the insured and permits recovery.") (citations omitted).

- *Glover v. Nat'l Ins. Underwriters*, 545 S.W.2d 755, 761 (Tex. 1977) ("[W]e must adopt the construction of an exclusionary clause urged by the insured as long as that construction is not itself unreasonable, even if the construction urged by the insurer appears to be more reasonable or a more accurate reflection of the parties' intent. . . . But when the language of an insurance contract is ambiguous, that is, is subject to two or more reasonable

interpretations, then that construction which affords coverage will be the one adopted.").

- *Blaylock v. Am. Guarantee Bank Liab. Ins. Co.*, 632 S.W.2d 719, 721 (Tex. 1982) ("[W]hen the language used is subject to two or more reasonable interpretations, the construction which affords coverage will be adopted. The policy of strict construction against the insurer is especially strong when the court is dealing with exceptions and words of limitation.") (citations omitted).

- *Kelly Assocs., Ltd. v. Aetna Cas. & Sur. Co.*, 681 S.W.2d 593, 596 (Tex. 1984) ("'But when the language of an insurance contract is ambiguous, that is, is subject to two or more reasonable interpretations, then that construction which affords coverage will be the one adopted.'") (quoting *Glover*, 545 S.W.2d at 761).

- *Gonzalez v. Mission Am. Ins. Co.*, 795 S.W.2d 734, 737 (Tex. 1990) ("Where an insurance policy's provisions are ambiguous or inconsistent, and is subject to two or more reasonable interpretations, then that construction which affords coverage will be the one adopted.").

- *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Hudson Energy Co.*, 811 S.W.2d 552, 555 (Tex. 1991) ("[I]f a contract of insurance is susceptible of more than one reasonable interpretation, we must resolve the uncertainty by adopting the construction that most favors the insured. The court must adopt the construction of an exclusionary clause urged by the insured as long as that construction is not unreasonable, even if the construction urged by the insurer appears to be more reasonable or a more accurate reflection of the parties' intent. In particular, exceptions or limitations on liability are strictly construed against the insurer and in favor of the insured.") (citations omitted).

- *State Farm Fire & Cas. Co. v. Reed*, 873 S.W.2d 698, 699 (Tex. 1993) ("[I]f a contract of insurance is susceptible to more than one reasonable interpretation, we must resolve the uncertainty by adopting the construction most favorable to the insured.").

- *Grain Dealers Mut. Ins. Co. v. McKee*, 943 S.W.2d 455, 458 (Tex. 1997) ("Conversely, if an insurance contract is subject to more than one reasonable interpretation, the contract is ambiguous and the interpretation that most favors coverage for the insured will be adopted.").

- *Balandran v. Safeco Ins. Co. of Am.*, 972 S.W.2d 738, 741 (Tex. 1998) ("Where an ambiguity involves an exclusionary provision of an insurance policy, we 'must adopt the construction . . . urged by the insured as long as that construction is not unreasonable, even if the construction urged by the insurer appears to be more reasonable or a more accurate reflection of the parties' intent.'") (quoting *Hudson Energy*, 811 S.W.2d at 555).

- *ATOFINA Petrochems., Inc. v. Cont'l Cas. Co.*, 185 S.W.3d 440, 444 (Tex. 2005) (per curiam) ("We adopt this [the insured's] reasonable construction.") (involving a claim by an additional insured).

- *Evanston Ins. Co. v. ATOFINA Petrochems., Inc.*, 256 S.W.3d 660, 668 (Tex. 2008) ("When interpreting an insurance contract, we 'must adopt the construction of an exclusionary clause urged by the insured as long as that construction is not unreasonable, even if the construction urged by the insurer appears to be more reasonable or a more accurate reflection of the parties' intent.' 'Exceptions or limitations on liability are strictly construed against the insurer and in favor of the insured,' and '[a]n intent to exclude coverage must be expressed in clear and unambiguous language.'") (quoting *Hudson Energy*, 811 S.W.2d at 555) (involving a claim by an additional insured).

- *Gilbert Tex. Constr., L.P. v. Underwriters at Lloyd's London*, 327 S.W.3d 118, 133 (Tex. 2010) ("Terms in insurance policies that are subject to more than one reasonable construction are interpreted in favor of coverage. 'Where an ambiguity involves an exclusionary provision of an insurance policy, we "must adopt the construction . . . urged by the insured as long as that construction is not unreasonable, even if the construction urged by the insurer appears to be more reasonable or a more accurate reflection of the parties' intent. . . ."'") (quoting *Balandran*, 972 S.W.2d at 741) (citations omitted).

- *Evanston Ins. Co. v. Legacy of Life, Inc.*, 370 S.W.3d 377, 380 (Tex. 2012) ("As to the policy, if a term is susceptible to more than one reasonable interpretation, we must resolve that uncertainty in favor of the insured.").

This list of cases from this Court does not purport to be complete; there are other cases invoking the Ambiguity Rule. There are also many more, too

numerous to list, from the intermediate courts of appeals. But the partial list above more than amply demonstrates that the Ambiguity Rule is fundamental law in Texas. It is an objective rule applied as a matter of law by this Court without factual inquiry into the sophistication or bargaining power of the parties or the negotiation and drafting history of the policy. As shown in the following section, that objective approach properly respects the multiple contract and insurance law principles on which the Ambiguity Rule is based.

B. The Ambiguity Rule is an amalgamation of many contract and insurance law principles.

The certification order from the Fifth Circuit assumes that the Ambiguity Rule rests on only two underlying public policies: (1) the rule of *contra proferentem*, under which an insurance contract is construed against the insurer as the party that drafted it; and (2) the view that insurance policies are contracts between parties with unequal bargaining power. *In re Deepwater Horizon*, 728 F.3d at 500. That assumption is incorrect.

As an examination of this Court's early jurisprudence adopting the Ambiguity Rule in Texas demonstrates, the rule construing ambiguities against the insurer is not so readily compartmentalized, and the term *contra proferentem* is a misleading misnomer for a more complex rule. The Ambiguity Rule is a multi-dimensional rule founded on an amalgamation of general contract-interpretation rules and rules developed specifically in the context of insurance.

The Ambiguity Rule in Texas is rooted in a triptych of cases decided by this Court in the late 1800s – *Goddard v. East Tex. Fire Ins. Co.*, *Hibernia Ins. Co. v. Bills*, and *Brown v. Palatine Ins. Co.* In adopting the Ambiguity Rule as a fundamental rule of Texas insurance law, this Court, in turn, relied on the two leading insurance treatises of the day (by H.G. Wood and John Wilder May) as well as opinions from the highest courts of other states. Focusing on this Court's three opinions and their cited sources, it is evident that the Ambiguity Rule is not based solely on *contra proferentem* and has little if any connection to a concern about unequal bargaining power. Instead, it is a multi-premised rule based on a least seven concepts:

1. Construction against the drafter. The rule of *contra proferentem* construing a contract against its drafter is one basis for the Ambiguity Rule identified in this Court's opinions in *Goddard*, *Hibernia*, and *Palatine*. As this Court stated in *Brown v. Palatine Ins. Co.*, 35 S.W. at 1061, "The language being selected and used by the insurer to express the terms and conditions upon which it issued, the policy will be strictly construed against it, and liberally in favor of the insured." *Accord, Hibernia Ins. Co. v. Bills*, 29 S.W. at 1064 ("The insurance company selected the words in which to express the terms and conditions upon which the forfeiture could be enforced, and must abide by the effect to which they are entitled under the established rules of construction.").

Construction against the drafter is also discussed in the authorities on which this Court relied in adopting the Ambiguity Rule. H.G. Wood, 1 A TREATISE ON THE LAW OF FIRE INSURANCE § 58 at 141 (1886) ("[A]s the insurer makes the policy, and selects his own language, he is presumed to have employed that which expresses his real intention and the actual contract entered into, and has left nothing to be inferred or supplied by reference to extraneous matters.")[5]; *Aetna Ins. Co. v. Jackson, Owsley & Co.*, 55 Ky. 242, 1855 WL 4204, at *10 (Ky. 1855) ("as the language of the policy in all its parts is framed by the insurer, and not by the insured, it is the duty of the former . . . to frame the policy as to cover the intended subject and to furnish the expected indemnity against loss upon that subject").[6]

But, while *contra proferentem* is an important policy underlying the Ambiguity Rule, it is not the sole basis for the rule.

2. Construction against the promisor and in favor of the promisee. The authorities on which this Court relied in first adopting the Ambiguity Rule show the rule is based on another important tenet of contract construction – that words of promise are construed against the promisor and in favor of the promisee.

[5] The Wood treatise was cited by this Court as a basis for the Ambiguity Rule in all three cases adopting the rule. *Goddard*, 1 S.W. at 909; *Hibernia*, 29 S.W. at 1064, 1065; *Palatine*, 35 S.W. at 1061. While the Court likely referred to the 1878 edition of the treatise in the earlier opinion and the 1886 editions in the later opinions, for simplicity this amicus brief will cite to the later edition.

[6] The Kentucky Supreme Court decision was cited by this Court as support for the Ambiguity Rule in *Goddard*, 1 S.W. at 909.

The two leading treatises of the day both embraced this tenet as support for construing insurance policies against the insurer, because the insurer is making a promise of coverage. Wood, 1 A TREATISE ON THE LAW OF FIRE INSURANCE § 58 at 145 ("that construction should be taken which is most beneficial to the promisee"); John Wilder May, THE LAW OF INSURANCE § 175 at 182-83 (1873) ("Language taken most strongly against those for whose Benefit it is. . . . The words of a promise, with its exceptions and qualifications, are to be considered as those of the promisor . . . .").[7]

The same view is reflected in *Hoffman v. Aetna Fire Ins Co.*, 32 N.Y. 405, 1865 WL 3325 (N.Y. 1865), cited by the Court in *Goddard*, 1 S.W. at 909. *Hoffman* states that: "It is also a familiar rule of law, that if it be left in doubt . . . whether given words were used in an enlarged or a restricted sense, other things being equal, that construction should be adopted which is most *beneficial* to the promisee." 1865 WL 3325, at *6 (emphasis in original).

3. Construction of words of limitation and exception against the promisor. The Ambiguity Rule is also grounded on the principle that words that limit a contractual promise are construed narrowly and against the promisor. May, THE LAW OF INSURANCE § 175 at 184 ("So words of exception, if of doubtful import,

[7] The May treatise was cited by this Court as a basis for the Ambiguity Rule in *Goddard*, 1 S.W. at 909.

are to be construed most strongly against the party in whose interest they are introduced."); *Hoffman v. Aetna Fire Ins. Co.*, 1865 WL 3325, at *6 ("This [ambiguity] rule has been very uniformly applied to conditions and provisos in policies of insurance, on the ground that though they are inserted for the benefit of underwriters, their office is to limit the force of the principal obligation."); *Boon v. Aetna Ins. Co.*, 40 Conn. 575, 1874 WL 3166, *9 (Conn. 1873) ("it is the duty of an insurance company seeking to limit the operation of its contract of insurance by special provisos or exceptions, to make such limitations in clear terms and not leave the insured in a condition to be misled").[8]

4. Construction of insurance policies in favor of coverage. The Ambiguity Rule also rests on the principle that contracts are interpreted to give effect to the parties' intent, and that the primary intent of the parties to an insurance policy is to provide insurance coverage. As the leading treatise of the day stated:

> Indemnity is the real object and purpose of all insurance; that is what the assured bargains for, and what the assurer intends to provide. *The predominant intentions of the parties in a contract of insurance is indemnity, and this is to be kept in view and favored in putting a construction upon a policy*.

Wood, 1 A TREATISE ON THE LAW OF FIRE INSURANCE § 58 at 146 (emphasis added).

[8] The Connecticut Supreme Court decision was cited by this Court in *Hibernia*, 29 S.W. at 1064.

This core principle is similarly reflected in other sources cited by the Court in adopting the Ambiguity Rule. May, THE LAW OF INSURANCE § 174 at 181-82 ("The Contract will be construed liberally in favor of the Object to be accomplished. . . . Having indemnity for its object, the contract is to be construed liberally to that end, and it is presumably the intention of the insurer that the insured shall understand that in case of loss he is to be protected to the full extent which any fair interpretation will give."); *Aetna Ins. Co. v. Jackson, Owsley & Co.*, 1855 WL 4204, at *10 (the policy "should be construed liberally for [the insured's] benefit, and so as to effectuate, as far as may reasonably be done, the indemnity which he justly expected"); *Commercial Ins. Co. v. Robinson*, 64 Ill. 265, 1872 WL 8304, at *2 (Ill. 1872) ("[I]t is reasonable to resolve any doubt against the company. The object of the company's existence is to insure against fire. That is what it holds itself out to the public as able and willing to do.")[9]; Wood, 1 A TREATISE ON THE LAW OF FIRE INSURANCE § 58 at 146 ("The spirit of the rule is, that when two interpretations, equally fair, may be given, that which gives the greater indemnity shall prevail.").

5. Placement of risk of ambiguity on the insurer because of its expertise. The sources cited by the Court in support of the Ambiguity Rule also recognize that

[9] The Illinois Supreme Court decision was cited by this Court in *Hibernia*, 29 S.W. at 1064.

insurers are experts in their field and in the best position to ensure clarity and to avoid ambiguity. Wood, 1 A TREATISE ON THE LAW OF FIRE INSURANCE § 58 at 145 ("the provisions and conditions" of the policy are "prepared by the assurers themselves, and their advisers, persons thoroughly conversant with the principles and practice of insurance, with the utmost deliberation, 'every word being weighed, and every contingency debated'"); *Aetna Ins. Co. v. Jackson, Owsley & Co.*, 1855 WL 4204, at *10 ("The insurer has printed policies incumbered with numerous and complicated provisos and conditions, and is presumed not only to understand their meaning, but to know the intended effect upon the forms of expression to be used in the policy, and upon the consequent right of the parties.").

6. Construction against forfeiture. In construing ambiguities against the insurer, this Court in *Palatine* and *Hibernia* invoked the rule that construes language in a contract against forfeiture. The Court adapted the rule to the insurance context to prevent forfeiture of coverage under the policy. *Brown v. Palatine Ins. Co.*, 35 S.W. at 1061 ("Forfeitures are not favored by the law, and if the language used is fairly susceptible of an interpretation which will prevent a forfeiture, it will be so construed."); *Hibernia Ins. Co. v. Bills*, 29 S.W. at 1064 ("the language will be strictly construed against [the insurer] . . . for the additional reason that forfeitures are not favored, and will not be declared, unless the case comes within the terms prescribed"). The Court's supporting authority also

invoked the anti-forfeiture rule to uphold coverage. *Hoffman v. Aetna Fire Ins. Co.*, 1865 WL 3325, at *7 ("'Conditions providing for disabilities and forfeitures are to receive, where the intent is doubtful, a strict construction against those for whose benefit they are introduced.'").

7. A belated concern about unequal bargaining power. Nothing in *Goddard*, *Hibernia*, or *Palatine* suggests that the Ambiguity Rule was rooted in a concern that insurance policies are contracts between parties with unequal bargaining power. The authorities they cite do not discuss this proposition either. At most, one authority expresses concern that an insured may be duped by an insurer into believing there is coverage when there is none. Wood, 1 A TREATISE ON THE LAW OF FIRE INSURANCE § 60 at 161 ("A contract drawn by one party, who makes his own terms, and imposes his own conditions, will not be tolerated as a snare to the unwary . . . .").

Rather than being a firm basis for the Ambiguity Rule, the first direct reference by this Court to unequal bargaining power came more than 100 years after the rule was first adopted. In a footnote in *Balandran v. Safeco Ins. Co. of Am.*, 972 S.W.2d 738, 741 n.1 (Tex. 1998), the Court stated that the Ambiguity Rule "is also justified by the special relationship between insurers and insureds arising from the parties' unequal bargaining power." But, in support, it cited *Arnold v. Nat'l Cty. Mut. Fire Ins. Co.*, 725 S.W.2d 165, 167 (Tex. 1987), a case

that did not even address, much less apply, the Ambiguity Rule. *Arnold* and its supporting authority, *G.A. Stowers Furniture Co. v. Am. Indem. Co.*, 15 S.W.2d 544, 548 (Tex. Comm'n App. 1929, holding approved), both recognized that an insurer owes a special duty of care to the insured in the settlement and resolution of claims. Neither involved construction of an insurance policy or a dispute over coverage.

The Ambiguity Rule as adopted in Texas thus has little if any connection to a concern about unequal bargaining power.

C. Appellees' claim to a sophisticated-insured exception to the Ambiguity Rule lacks support.

The Ambiguity Rule is fundamental insurance law not just in Texas, but in 49 of the 50 states. In urging this Court to create a sophisticated-insured exception to that rule, Appellees claim such an exception has been recognized in 10 states. It has not. The authorities they cite do not support that claim, nor is their reliance on a single Texas federal district court opinion persuasive.

1. The Ambiguity Rule is recognized by the highest courts of 49 states. As the survey attached as Appendix A demonstrates, the highest courts of 49 states recognize some version of the Ambiguity Rule as a fundamental tenet of

insurance-policy construction. App. A.[10] The Ambiguity Rule is overwhelmingly the majority rule in this country.

2. Authorities cited by Appellees do not support their claim of a nationally-recognized sophisticated-insured exception to the Ambiguity Rule. Contrary to the arguments of Appellees, there is no national groundswell movement toward abandoning the Ambiguity Rule when the insured is subjectively determined to be "sophisticated." In support of creating a "sophisticated-insured" exception, Appellees cite only a handful of cases, mostly from federal district courts and many of which contain only dicta. When the cited authorities are closely examined, Appellees can show that at most one of the nation's highest courts has recognized a limited exception to the Ambiguity Rule.

In its brief, Ranger asserts that ten states have recognized a "sophisticated-insured" exception to the Ambiguity Rule. Ranger Br. at 56 n.19. Most of the footnoted authorities do not support Ranger's claim:

> **Illinois.** The cited case, *Baxter Int'l, Inc. v. Am. Guar. & Liab. Ins. Co.*, 861 N.E.2d 263, 268-69 (Ill. App. Ct. 2006), is an intermediate Illinois court decision. The Supreme Court of Illinois has refused to recognize a sophisticated-insured exception to the Ambiguity Rule. *Outboard Marine Corp. v. Liberty Mut. Ins. Co.*, 607 N.E.2d 1204, 1218 (Ill. 1992) ("The insurers argue that it should not apply here because OMC is a large corporation, sophisticated and counseled in insurance matters. We disagree

[10] Maryland does not recognize a special rule of construction for insurance policies but applies the traditional contract rule of *contra proferentem* when the insurer has drafted the policy language. *See* App. A.

with this contention."); *see also Homeowners Choice, Inc. v. Aon Benfield, Inc.*, 938 F. Supp. 2d 749, 758 (N.D. Ill. 2013) ("the Illinois courts apply the doctrine of *contra proferentum* [sic] even with sophisticated parties").

Indiana. The cited case, *Beanstalk Group, Inc. v. AM Gen. Corp.*, 283 F.3d 856, 858-59 (7th Cir. 2002), does not support Ranger's statement that Indiana recognizes a sophisticated-insured exception to the Ambiguity Rule. To begin with, it is not an insurance case, but involves a breach of a licensing agreement. It thus did not involve the Ambiguity Rule, but the contract rule of *contra proferentem*. Second, the federal court's discussion of a sophisticated contracting party exception to the rule of *contra proferentem* is dicta. 283 F.3d at 859 (no matter whether an exception to the rule applied, "AM does not need the rule in order to prevail"). Third, and most importantly, the federal court noted that "Indiana has yet to take a stand on the exception" and the only case "leans in favor of rejecting it." *Id*.

Iowa. The federal court in *Penford Corp. v. Nat'l Union Fire Ins. Co.*, 662 F.3d 497, 505 (8th Cir. 2011), did refuse to apply the doctrine of *contra proferentem* to an ambiguous insurance policy. However, it did not purport to be announcing Iowa law – it cited no Iowa authority. Further, it cited only federal cases that did not involve insurance policies. It thus did not address the Ambiguity Rule, but the pure contract rule of *contra proferentem*, and focused on the "back-and-forth nature of the drafting process." *Penford* does not state Iowa law on the issue.

Kansas. The cited case, *Payless Shoesource, Inc. v. Travelers Cos.*, 585 F.3d 1366, 1372 (10th Cir. 2009), does not support Ranger's statement that Kansas recognizes a sophisticated-insured exception to the Ambiguity Rule. To begin with, the federal court did not purport to announce Kansas law, instead concluding that "Kansas courts seem to have begun wrestling" with the question. *Id.* at 1372. Further, the discussion is dicta, as the court concluded the policy was not ambiguous and thus the rule of *contra proferentem* "holds no sway." *Id.* at 1373.

Louisiana. The federal district court in *Indus. Risk Insurers v. New Orleans Pub. Serv., Inc.*, 666 F. Supp. 874, 881 (E.D. La. 1987), stated in Conclusion of Law 10 that the doctrine of *contra proferentem* did not apply to an ambiguous policy issued to a large municipality represented by professionals. However, the court did not purport to be announcing Louisiana law – it cited no Louisiana authority.

Maryland. The cited case, *Rouse Co. v. Fed. Ins. Co.*, 991 F. Supp. 460, 466 (D. Md. 1998), does not establish a sophisticated-insured exception in Maryland because it is a decision of a federal district court that fails to cite any supporting Maryland case law. The federal court refused to apply the traditional contract rule of *contra proferentem* because it was unclear which party had drafted the policy language at issue.

New Jersey. Ranger is correct that the Supreme Court of New Jersey in *Benjamin Moore & Co. v. Aetna Cas. & Sur. Co.*, 843 A.2d 1094, 1103-04 (N.J. 2004), stated that the Ambiguity Rule does not apply to "sophisticated commercial entities that do not suffer from the same inadequacies as the ordinary unschooled policyholder and that have participated in the drafting of the insurance contract." However, that statement was dicta because the court determined the policy was unambiguous and the rule and its exception "played no part in the ultimate outcome of the case." *Id.* at 1104. Further, the high court questioned whether a sophisticated-insured exception would even apply to the facts of the case where the insured was not a "meaningful participant" in the drafting of the policy language at issue. *Id.*

New York. The cited case, *Cummins, Inc. v. Atl. Mut. Ins. Co.*, 867 N.Y.S.2d 81, 83 (N.Y. App. Div. 2008), is a three-paragraph opinion from an intermediate appellate court that refused to apply the Ambiguity Rule when "the basic concept and terms" of the loss conversion factor in the policy "originated with" a sophisticated insured with equal bargaining power. In support, it cites two inapt intermediate court cases – one involving a lease, not an insurance policy, and the other involving a dispute between an excess insurer and an insured that was acting as its own primary insurer. A federal court of appeals' decision reviewing New York law has concluded that "there is no general rule in New York denying sophisticated businesses the benefit of contra proferentem" and it is "unsettled in New York whether contra proferentem applies if the policyholder is a sophisticated entity that negotiated contract terms." *Morgan Stanley Group Inc. v. New England Ins. Co.*, 225 F.3d 270, 279 (2d Cir. 2000). The *Cummins* case is not a dispositive statement of New York law. And, very recently, New York's highest court indicated it would apply the Ambiguity Rule to a policy issued to IBM. *Fed. Ins. Co. v. Int'l Bus. Machs. Corp.*, 965 N.E.2d 934, 936 (N.Y. 2012) ("the language at issue would be deemed to be ambiguous and thus interpreted in favor of the insured") (citation omitted).

> **South Dakota.** Ranger correctly states that the South Dakota Supreme Court held in *Union Pac. R.R. v. Certain Underwriters at Lloyd's London*, 771 N.W.2d 611, 616-17 (S.D. 2009), that it would not apply the Ambiguity Rule to the specific commercial insurance policy at issue in that case. The court based its decision on several factors: the policies were non-standard manuscripted documents; the insurer and insured were sophisticated parties negotiating on a level playing field; and the insured had hired insurance brokers in Chicago to negotiate the terms of the policies at arms' length with the insurer. The court reasoned the Ambiguity Rule should not apply because there was no contract of adhesion.
>
> **Vermont.** The cited case, *Prof. Consultants Ins. Co. v. Employers Reinsurance Co.*, No. 1:03-CV-216, 2006 WL 751244, *3 n.5 (D. Vt. Mar. 8, 2006), does not support Ranger's statement that Vermont recognizes a sophisticated-insured exception to the Ambiguity Rule. To begin with, the federal district court examined the exception in a very limited context – reinsurance – where the dispute is between two insurance companies and no insured is involved. Second, the court recognized that the Vermont courts had not spoken on the issue. *Id.* ("No Vermont [case] . . . provides guidance on whether Vermont courts would apply the rule [of *contra proferentem*] to reinsurance contracts."). The court, making an *Erie* guess on what it termed a "close question" under Vermont law, held that the rule would not apply in the limited context of reinsurance.

Summed up, then, the highest court of only one of Ranger's claimed ten states – South Dakota – has adopted a sophisticated-insured exception to the Ambiguity Rule, and in one of those ten states, Illinois, the highest court has in fact rejected such an exception. There is no definitive holding in the other eight claimed states.

Moreover, the Ranger list ignores decisions from other states that have rejected a sophisticated-insured exception to the Ambiguity Rule:

> **California.** The California Supreme Court applied the Ambiguity Rule to an insured that "unquestionably possesse[d] both legal sophistication and substantial bargaining power" in *AIU Ins. Co. v. Superior Ct. of Santa Clara*

Cty., 51 Cal. 3d 807, 823 (1990). It rejected the insurers' argument that the rule should not apply to a sophisticated insured.

Minnesota. The Minnesota Supreme Court rejected differential treatment of a sophisticated insured in *Home Ins. Co. v. Nat'l Union Fire Ins. Co.*, 658 N.W.2d 522, 533 (Minn. 2003) ("We will not create a legal rule that presumes an insured, whether a company or an individual, is equally sophisticated . . . ."). The Ambiguity Rule "applies even to disputes involving a sophisticated insured with equal bargaining power." *Econ. Premier Assurance Co. v. W. Nat'l Mut. Ins. Co.*, 839 N.W.2d 749, 755 (Minn. Ct. App. 2013). The Minnesota appellate court recognized that applying the rule "provides an incentive, especially for insurance companies who are in a better position to prevent misunderstandings, to avoid including ambiguities." *Id.*

Rhode Island. The Rhode Island Supreme Court discussed the "sophisticated consumer" exception but refused to adopt it in *Textron, Inc. v. Aetna Cas. & Sur. Co.*, 754 A.2d 742, 749 (R.I. 2000). The court followed the view that the Ambiguity Rule applies "not only when the insured is an unsophisticated consumer, but also when, as here, the insured is a corporation that might presumably have more business acumen and bargaining power." *Id.*

Washington. The Washington Supreme Court rejected the argument that an insurance policy should be interpreted differently when the insured was a sophisticated corporation. *Boeing Co. v. Aetna Cas. & Sur. Co.*, 784 P.2d 507, 514 (Wash. 1990) (en banc) (the "standard rules of construction are no less applicable merely because the insured is itself a corporate giant"). *See also Liberty Mut. Fire Ins. Co. v. Costco Wholesale Corp.*, No. C07-1499RAJ, 2009 WL 13069, at *4 n.2 (W.D. Wash. Apr. 30, 2009) ("To the extent Liberty suggests that the court should not construe the Policy in Costco's favor merely because a large corporation like Costco has sufficient power to bargain for a favorable policy, it is mistaken.").

Ranger's list in no way evidences a national trend among the 50 states toward adoption of a sophisticated-insured exception to the Ambiguity Rule.

3. Appellees' reliance on a single Texas federal district court opinion is unpersuasive. Both Ranger and the Certain Underwriters Appellees place great reliance on the federal district court's opinion in *Vought Aircraft Indus., Inc. v. Falvey Cargo Underwriting, Ltd.*, 729 F. Supp. 2d 814 (N.D. Tex. 2010). In holding that "the sophisticated insureds exception can conceivably apply" to the specific facts of that case, the *Vought* opinion fails to cite any supporting Texas authority and further fails to consider the multiple foundations for the Ambiguity Rule. *Id.* at 826.[11]

The *Vought* opinion is unpersuasive because it cites no Texas authority in support of a sophisticated-insured exception. To the contrary, it candidly admits that no such authority exists: "Neither the court nor the parties are aware of a Texas case that addresses the sophisticated insureds exception." *Id.* at 824.

Moreover, the *Vought* opinion acknowledges only two of the seven bases for adoption of the Ambiguity Rule in Texas – "an insured's unequal bargaining power, the special relationship between the insured and the insurer, and the general principle that contracts are construed against the drafting party." *Id.* at 824-25. And, in fact, the *Vought* opinion turns solely on the traditional contract rule of

[11] Ranger also cites to *In re Enron Corp. Sec. Litig.*, 391 F. Supp. 2d 541 (S.D. Tex. 2005), as recognizing a sophisticated-insured exception to the Ambiguity Rule. Any discussion in *Enron* is dicta, as the court found the policy language unambiguous and the policy contained a provision expressly negating the Ambiguity Rule. 391 F. Supp. 2d at 578.

contra proferentem construing language against its drafter. In holding that the "the sophisticated insureds exception can conceivably apply," the *Vought* opinion rejected a broad formulation that would focus on the corporate status of the insured. *Id.* at 825 n.11 ("But the sophisticated insureds exception is not based on the corporate nature of the insured."). The court further required more than equal bargaining power or the existence of negotiations between the insurer and insured. Instead, the *Vought* exception is premised solely on the fact that the insured played a significant role in the actual drafting of the policy itself. *Id.* (the sophisticated insureds exception "rests instead on the insured's role in drafting the policy").

In focusing on a single question – who drafted the language – the *Vought* opinion fails to consider the other bases for the Ambiguity Rule: construction of a promise against the promisor, narrow interpretation of words of limitation, construction of a policy in favor of coverage, construction of provisions against forfeiture, and placement of the risk of ambiguity on the insurer as issuer of the policy and expert in the field. In fact, after *Vought* was decided, this Court applied the rule narrowly construing words of exception and limitation to a negotiated policy issued to a sophisticated insured. *Houston Exploration Co. v. Wellington Underwriting Agencies, Ltd.*, 352 S.W.3d 462, 472 (Tex. 2011) (language must be "'strictly construed against the insurer and in favor of the insured'").

Vought, then, is not persuasive authority, as it fails to consider the many reasons – beyond draftsmanship – that courts across the nation apply the Ambiguity Rule in the specific context of insurance.[12]

D. The Court should not craft a new exception to the Ambiguity Rule for so-called "sophisticated insureds."

This Court should not adopt a sophisticated-insured exception to the Ambiguity Rule. Such an exception, as shown above, lacks national support and represents a distinct minority view. Moreover, a sophisticated-insured exception would be subjective and problematic, would ignore important grounds on which the Ambiguity Rule is premised, would result in time-consuming and fact-intensive disputes over coverage issues, and de-incentivize insurers to issue clear and unambiguous policies to commercial insureds. More specifically, the Court should reject a sophisticated-insured exception on at least six grounds:

[12] Even were this Court to consider the narrow exception discussed in the *Vought* case, it would not apply to the facts here. As the Fifth Circuit recognized in its certification order, "the Insurers were involved in drafting the umbrella policy language at issue, and the failure of that policy language to limit coverage in underlying 'Insured Contracts' to the liabilities assumed by the named insured in those contracts is part of what ails the Insurers now." *In re Deepwater Horizon*, 728 F.3d at 500. *See also Jefferson Block 24 Oil & Gas, L.L.C. v. Aspen Ins. UK Ltd.*, 652 F.3d 584, 599 (5th Cir. 2011) (applying New York law) (holding that an ambiguity arose when the insurers, after receiving external document from the insured, made it a part of the contract without further alteration or specification and that, as a result, the ambiguity would be construed against the insurers because "the causal link is one wholly of [the insurers'] own creation"). It is also undisputed that the BP Appellants played no role in drafting the policy language.

1. Rules of construction should be objective and uniform. Rules of construction are legal rules adopted and applied by the courts as a matter of law. Like all legal rules, rules of construction are objective and uniform; they do not change with the identity of the party invoking them.

The Ambiguity Rule serves an important function by providing for the uniform construction of insurance policies. The same words in different policies have the same meaning whether the insured is an individual or a corporation, wealthy or poor, sophisticated or unsophisticated. This makes sense because, under the doctrine of stare decisis, an interpretation of policy language will establish its meaning in all policies, not just the one before the court:

> [I]t would be incongruous for the court to apply different rules of construction based on the policyholder because once the court construes the standard form coverage clause as a matter of law, the court's construction will bind policyholders through the state regardless of the size of their business.

Boeing Co. v. Aetna Cas. & Sur. Co., 784 P.2d at 514.

An objective and uniform application of the Ambiguity Rule ensures consistent and predictable results in Texas courts, which in turn ensures confidence in our judicial system. Creating an exception for sophisticated insureds would mean two sets of rules in insurance cases. "It gives sophisticated insureds inferior product and treats them differently from other insureds." Hazel Glenn Beh, *Reassessing the Sophisticated Insured Exception*, 39 TORT TRIAL & INS. PRAC. L.J.

85, 118 (2003) ("Beh"). Changing established interpretation rules based on the wealth or sophistication of the insured "threatens mischief where predictability, equality, and uniformity are desirable." *Id.*[13]

2. A new exception would be inconsistent with the multiple bases for the Ambiguity Rule. However defined, a new exception for sophisticated insureds would ignore important policy grounds for the adoption of the Ambiguity Rule in Texas. An exception based solely on sophistication would address only the relatively-recent concern about unequal bargaining power between insurers and insureds giving rise to a special relationship. But, as demonstrated above, for more than 100 years, the Ambiguity Rule was based on six other, equally-important rules of construction: construction against the drafter, construction against the promisor, narrow construction of words of limitation and exception, construction in favor of coverage, construction against the insurer as expert in the field, and construction against forfeiture.

Further, a new exception based solely on drafting responsibility would incorrectly equate the multi-foundational, insurance-specific Ambiguity Rule with the single-based contract rule of *contra proferentem*. This exception, like one

[13] The Ambiguity Rule is a tie-breaker rule similar to the rule in baseball that the tie goes to the runner – both provide a clear and consistent answer in close cases. The rule does not change depending on whether the runner is Derek Jeter playing at Yankee Stadium or an 8-year old playing ball on a local vacant lot.

based solely on sophistication, would ignore six other grounds for construing ambiguous words in a policy against the insurer.

The Court should not adopt an exception that is inconsistent with the many important policy grounds on which the 125-year Ambiguity Rule is founded.

3. A new exception would fail to recognize that the insurer is always ultimately responsible for the language in the policies it issues, even in so-called "manuscripted" policies. It is the insurer that issues the policy. It must stand behind the risks it has accepted in the policy, or decline to issue it. For more than 125 years, insurers in Texas have known that they bear the risk of any ambiguity. The Ambiguity Rule has incentivized insurers to issue policies that clearly and unambiguously delineate any limits on and exceptions to coverage.

Almost without exception, it is the insurer that has supplied the particular language included in the policy and that language will be standard in all of the policies of the type or types it issues. *See* David B. Goodwin, *Disputing Insurance Coverage Disputes*, 43 STAN. L. REV. 779, 796 (1991) ("Goodwin") ("Even the most sophisticated insureds normally purchase standard policy language . . . ."); Eugene R. Anderson & James J. Fournier, *Why Courts Enforce Insurance Policyholders' Objectively Reasonable Expectations of Insurance Coverage*, 5 CONN. INS. L. J. 335, 371 (1998) ("Anderson & Fournier") ("The truth is that America's largest corporations purchase standard form policy language just like

everybody else."). Even large corporate insureds with substantial bargaining power are most likely to exercise that leverage to obtain greater coverage, higher limits, or lower rates rather than to negotiate specific wording of policy provisions. Goodwin, 43 STAN. L. REV. at 797.

Labelling a policy as "manuscripted" does not change the responsibility for the language. Most policies are not written from scratch, but assemble standard provisions to fit the particular circumstances of the insured. Anderson & Fournier, 5 CONN. INS. L. J. at 371 ("Even large commercial policyholders who work with brokers are only paying to have *segments* of yet more standard-form language *assembled* – terms are rarely rewritten.") (emphasis in original); Beh, 39 TORT TRIAL & INS. PRAC. L.J. at 104 ("the characterization may merely mean that the insurer created a customized policy from a menu of standard terms drafted by it, rather than actually negotiated terms"); Leo P. Martinez, Marc S. Mayerson & Douglas R. Richmond, 1 NEW APPLEMAN INS. LAW PRAC. GUIDE § 3.05[3] (2014) (Some policies, "while described as 'manuscripted,' are in fact more of a collage of form provisions from other policies.").

Negotiating over which standard provisions to be included in a policy does not transform the insured into the drafter any more than choosing one menu item from Column A and one from Column B at a Chinese restaurant transforms the

diner into the chef. The ultimate responsibility for the language – and the risk of any ambiguity in the way it is framed – remains with the insurer.

4. A new sophisticated-insured exception would be too amorphous and subjective. It is difficult, if not impossible, to draw a clear distinction between a sophisticated and an unsophisticated insured. *See* Beh, 39 TORT TRIAL & INS. PRAC. L.J. at 92 ("[A] precise definition of 'sophisticated' is elusive."). If it is based on corporate status, does that mean that all commercial insureds – from mom and pop enterprises to multinational corporations – are sophisticated? Or will courts be engage in examining the staffing, knowledge, and experience of each commercial insured on a case-by-case basis? This Court has applied the Ambiguity Rule to many insurance policies issued to commercial entities.[14] Will all of these now be subject to a fact-intensive jury trial on "sophistication"?

[14] *Evanston Ins. Co. v. Legacy of Life, Inc.*, 370 S.W.3d at 379 (policy issued to organ donation charity); *Gilbert Tex. Constr., L.P. v. Underwriters at Lloyd's London*, 327 S.W.3d at 121 (commercial contractor); *Evanston Ins. Co. v. ATOFINA Petrochems., Inc.*, 256 S.W.3d at 661 (commercial contractor and major refinery owner); *ATOFINA Petrochems., Inc. v. Cont'l Cas. Co.*, 185 S.W.3d at 441 (commercial contractor and major refinery owner); *Grain Dealers Mut. Ins. Co. v. McKee*, 943 S.W.2d at 456 (commercial business auto policy); *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Hudson Energy Co.*, 811 S.W.2d at 553 (commercial business aviation policy); *Kelly Assocs., Ltd. v. Aetna Cas. & Surety Co.*, 681 S.W.2d at 594 (stock brokerage firm); *Glover v. Nat'l Ins. Underwriters*, 545 S.W.2d at 757 (commercial business aviation policy); *Cont'l Cas. Co. v. Warren*, 254 S.W.2d at 762 (commercial business aviation policy); *Lloyds Cas. Insurer v. McCrary*, 229 S.W.2d at 606 (butane gas dealership); *McCaleb v. Cont'l Cas. Co.*, 116 S.W.2d at 680 (Texas municipality); *Brown v. Palatine Ins. Co.*, 35 S.W. at 1060 (commercial policy covering stock in trade); *Hibernia Ins. Co. v. Bills*, 29 S.W. at 1064 (commercial policy covering cotton gin house and machinery).

And why would the exception stop at corporations? Very wealthy individuals may have more sophistication than a commercial insured – Warren Buffett no doubt owns several insurance companies. Does the language in his homeowner's policy mean something different than the same policy issued to his next-door neighbor? Or what about insureds in the learned professions, like lawyers and judges? Given their level of sophistication, do their policies mean something different than the same policies issued to other, less-educated insureds?

As one commentary has aptly observed, "The slippery slope character of the 'sophisticated' policyholder argument is self-evident." Anderson & Fournier, 5 CONN. INS. L. J. at 370. The Court should not create a subjective and amorphous exception to the Ambiguity Rule, which has been uniformly applied to all insureds – without exception – for more than 125 years.

5. A new exception would undermine the efficient resolution of coverage disputes. The Ambiguity Rule allows for efficient resolution of coverage disputes as a matter of law. Recognizing a sophisticated-insured exception would result in fact-intensive disputes over coverage that in many cases would require trial to a jury after extensive discovery. Insurers would likely attempt to invoke the exception in any coverage dispute involving a commercial business or whenever any negotiation of the policy, no matter how minor, had occurred.

An insured would be placed in a war on two fronts, defending itself in the third-party suit seeking to impose liability and at the same time engaging in litigation with the insurer over coverage. The result will be more expensive, time-consuming, and more protracted litigation that is a burden not just on the parties but on the Texas courts as well. *See* Goodwin, 43 STAN. L. REV. at 797-98.

6. A new exception would fail to recognize that the insurer will always have more expertise in the field of insurance. Even the most sophisticated insured will not have the same level of expertise in the field of insurance as an insurance company that devotes all of its time and resources to specialization in that field. As the Minnesota Supreme Court correctly observed in rejecting a sophisticated-insured exception, "Both primary and umbrella insurers are typically more sophisticated than the insured – they know their policies intimately, including their duties under the contract and how courts have interpreted language in the policies." *Home Ins. Co. v. Nat'l Union Fire Ins. Co.*, 658 N.W.2d at 533.

ATOFINA may have great expertise in operating a refinery, and BP may have great expertise in oil and gas exploration, but that does not make them experts in insurance. "Insurance companies simply have no reason to believe that policyholders sophisticated [in a particular line of business] are equally sophisticated about insurance." Anderson & Fournier at 372; *cf. Union Nat'l Bank of Little Rock v. Moriarty*, 746 S.W.2d 249, 250–51 (Tex. App.—Texarkana 1987,

writ denied) (explaining that an "insured is allowed to rely on the knowledge and expertise of the insurer").

This case involves policies issued through Lloyd's of London, one of the largest and most sophisticated insurance markets in the world. *See Houston Exploration Co. v. Wellington Underwriting Agencies, Ltd.*, 352 S.W.3d 464-65 (describing operations). The Lloyd's of London market assesses and accepts risks both ordinary and extraordinary. In issuing the policies in this case, the insurers accepted the risk of ambiguity under 125 years of Texas law. They also are charged with knowledge of this Court's decision in *Evanston Ins. Co. v. ATOFINA Petrochems., Inc.* The policies in dispute in this case were issued almost a year after the *ATOFINA* decision and nine and one-half years after the drilling contract was signed. The insurers thus knew that a policy issued under Texas law would not import limitations from a separate indemnification agreement in the drilling contract absent clear and express language in the policy. That was part of the risk they accepted. They were compensated for that risk through the rates they charged.

E. Question 2 should be answered "yes."

If the Court reaches Question 2, it should also be answered "yes." The multi-premised Ambiguity Rule, recognized by this Court for more than 125 years, incentivizes insurers to issue policies that clearly and unambiguously delineate any

limits on and exceptions to coverage. It expedites coverage disputes by allowing many cases to be determined as a question of law from the four corners of the policy. The Court should not create an exception to the Ambiguity Rule for so-called "sophisticated" insureds – a subjective and problematic test that ignores the multiple bases for the Ambiguity Rule and that will increase the cost and time to resolve coverage disputes.

CONCLUSION AND PRAYER

Amicus The National Association of Manufacturers urges this Court to adhere to fundamental propositions of insurance law recognized by this Court for more than 125 years. The Court should not create new exceptions to the four corners rule and the Ambiguity Rule in this case. Accordingly, the Court should answer both certified questions "yes."

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I hereby certify that: (1) the word count of this document is 12,571 words according to Microsoft Word 2007 and excluding those parts of the document specified in TEX. R. APP. P. 9.4(i)(1); and (2) this document has been prepared in a conventional typeface no smaller than 14-point for text and 12-point for footnotes.

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CERTIFICATE OF SERVICE

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APPENDIX A:
AMBIGUITY RULE 50-STATE SURVEY

- **Alabama:** *State Farm Mut. Auto. Ins. Co. v. Brown*, 26 So. 3d 1167, 1169-70 (Ala. 2009) ("'[I]f a provision in an insurance policy is found to be genuinely ambiguous, policies of insurance should be construed liberally in respect to persons insured and strictly with respect to the insurer.'").

- **Alaska:** *Whittier Props., Inc. v. Alaska Nat'l Ins. Co.*, 185 P.3d 84, 90 (Alaska 2008) ("[W]hen a clause in an insurance policy is ambiguous, we must accept the interpretation that most favors the insured.").

- **Arizona:** *First Am. Title Ins. Co. v. Action Acquisitions, LLC*, 187 P.3d 1107, 1110 (Ariz. 2008) ("If a clause appears ambiguous, we interpret it by looking to legislative goals, social policy, and the transaction as a whole. If an ambiguity remains after considering these factors, we construe it against the insurer.") (citation omitted).

- **Arkansas:** *Smith v. Prudential Prop. & Cas. Ins. Co.*, 10 S.W.3d 846, 850 (Ark. 2000) ("It is also a cardinal rule of insurance law that a policy of insurance is to be construed liberally in favor of the insured and strictly against the insurer . . . .").

- **California:** *Ameron Int'l Corp. v. Ins. Co. of State of Pa.*, 242 P.3d 1020, 1024 (Cal. 2010) ("Particularly, 'in the insurance context, . . . ambiguities [are resolved] in favor of coverage' so as to protect the insured's reasonable expectation of coverage.") (brackets and ellipses in original).

- **Colorado:** *Cary v. United of Omaha Life Ins. Co.*, 108 P.3d 288, 290 (Colo. 2005) (en banc) ("Any ambiguity in an insurance policy is construed in favor of providing coverage to the insured.").

- **Connecticut:** *Johnson v. Conn. Ins. Guaranty Ass'n*, 31 A.3d 1004, 1007 (Conn. 2011) ("'[A]ny ambiguity in the terms of an insurance policy must be construed in favor of the insured because the insurance company drafted the policy.'").

- **Delaware:** *Emmons v. Hartford Underwriters Ins. Co.*, 697 A.2d 742, 745 (Del. 1997) ("If ambiguity exists in the contract, it 'is construed strongly

against the insurer, and in favor of the insured, because the insurer drafted the language that is interpreted.'").

- **Florida:** *Garcia v. Fed. Ins. Co.*, 969 So. 2d 288, 291 (Fla. 2007) ("Ambiguities in insurance contracts are interpreted against the insurer and in favor of the insured.").

- **Georgia:** *State Farm Mut. Auto. Ins. Co. v. Staton*, 685 S.E.2d 263, 265 (Ga. 2009) ("When an insurance contract is deemed to be ambiguous, it will be construed liberally against the insurer and most favorably for the insured.").

- **Hawaii:** *Hart v. Ticor Title Ins. Co.*, 272 P.3d 1215, 1224 (Haw. 2012) ("'Insurance policies are contracts of adhesion . . . [;] they must be construed liberally in favor of the insured and [any] ambiguities [must be] resolved against the insurer.'") (brackets and ellipses in original).

- **Idaho:** *AMCO Ins. Co. v. Tri-Spur Inv. Co.*, 101 P.3d 226, 232 (Idaho 2004) ("If a policy term is ambiguous, this Court construes it 'liberally in favor of recovery, with all ambiguities being resolved against the insurer.'").

- **Illinois:** *Gillen v. State Farm Mut. Auto. Ins. Co.*, 830 N.E.2d 575, 582 (Ill. 2005) ("If the policy language is susceptible to more than one reasonable meaning, it is considered ambiguous and will be construed against the insurer.").

- **Indiana:** *State Auto. Mut. Ins. Co. v. Flexdar, Inc.*, 964 N.E.2d 845, 848 (Ind. 2012) ("'It is well settled that where there is ambiguity, insurance policies are to be construed strictly against the insurer and the policy language is viewed from the standpoint of the insured.' This is especially true where the language in question purports to exclude coverage.") (citation omitted).

- **Iowa:** *Bituminous Cas. Corp. v. Sand Livestock Sys., Inc.*, 728 N.W.2d 216, 221 (Iowa 2007) ("'Where the meaning of terms in an insurance policy is susceptible to two interpretations, the one favoring the insured is adopted.'").

- **Kansas:** *Brumley v. Lee*, 963 P.2d 1224, 1226 (Kan. 1998) ("We construe an insurance policy in a way that will give effect to the intention of the parties.

If the language is ambiguous, the construction most favorable to the insured must prevail.").

- **Kentucky:** *Bituminous Cas. Corp. v. Kenway Contracting, Inc.*, 240 S.W.3d 633, 638 (Ky. 2007) ("[A]mbiguous language must be liberally construed so as to resolve all doubts in favor of the insured.").

- **Louisiana:** *Cadwallader v. Allstate Ins. Co.*, 848 So. 2d 577, 580 (La. 2003) ("Ambiguous policy provisions are generally construed against the insurer and in favor of coverage.").

- **Maine:** *Cox v. Commonwealth Land Title Ins. Co.*, 59 A.3d 1280, 1283 (Me. 2013) ("We construe ambiguous policy language strictly against the insurance company and liberally in favor of the policyholder.").

- **Maryland:** *Megonnell v. United Servs. Auto. Ass'n*, 796 A.2d 758, 772 (Md. 2002) ("Maryland does not follow the rule that insurance policies should, as a matter of course, be construed against the insurer . . . . Nevertheless, under general principles of contract construction, if an insurance policy is ambiguous, it will be construed liberally in favor of the insured and against the insurer as drafter of the instrument.") (citations and internal quotation marks omitted).

- **Massachusetts:** *Boston Gas Co. v. Century Indem. Co.*, 910 N.E.2d 290, 304 (Mass. 2009) ("'[a]ny ambiguities in the language of an insurance contract are interpreted against the insurer who used them and in favor of the insured'").

- **Michigan:** *Fire Ins. Exch. v. Diehl*, 545 N.W.2d 602, 606 (Mich. 1996) ("if the policy contains an ambiguity, the ambiguity will be resolved in favor of the insured"), *overruled on other grounds by Wilkie v. Auto-Owners Ins. Co.*, 664 N.W.2d 776 (Mich. 2003); *see also Wilkie*, 664 N.W.2d at 787 ("[a]mbiguous language should be construed against the drafter, i.e., the insurer.").

- **Minnesota:** *Eng'g & Constr. Innovations, Inc. v. L.H. Bolduc Co.*, 825 N.W.2d 695, 705 (Minn. 2013) ("An insurance policy is ambiguous . . . 'if it is susceptible to two or more reasonable interpretations.' We resolve

ambiguous terms against the insurer, and construe such terms in favor of providing coverage to the insured.").

- **Mississippi:** *U.S. Fid. & Guar. Co. of Miss. v. Martin*, 998 So. 2d 956, 963 (Miss. 2008) ("If a contract contains ambiguous or unclear language, then ambiguities must be resolved in favor of the non-drafting party. . . . Exclusions and limitations on coverage are also construed in favor of the insured.").

- **Missouri:** *Ritchie v. Allied Prop. & Cas. Ins. Co.*, 307 S.W.3d 132, 138 (Mo. 2009) (en banc) ("Any conflict between these provisions creates an ambiguity that is resolved in favor of the insureds.").

- **Montana:** *Swank Enters., Inc. v. All Purpose Servs., Ltd.*, 154 P.3d 52, 57 (Mont. 2007) ("Ambiguities in the language of the contract will be construed against the insurer.").

- **Nebraska:** *Guerrier v. Mid-Century Ins. Co.*, 663 N.W.2d 131, 154 (Neb. 2003) ("An ambiguous insurance policy will be construed in favor of the insured.").

- **Nevada:** *Fed. Ins. Co. v. Am. Hardware Mut. Ins. Co.*, 184 P.3d 390, 393 (Nev. 2008) ("Applying our contract and insurance policy construction rules, under which we broadly interpret clauses providing coverage and generally interpret ambiguous terms in favor of the insured, we construe the endorsement here as providing coverage for the additional insured . . . . .").

- **New Hampshire:** *Great Am. Dining, Inc. v. Philadelphia Indem. Ins. Co.*, 62 A.3d 843, 846 (N.H. 2013) ("'If more than one reasonable interpretation is possible, and an interpretation provides coverage, the policy contains an ambiguity and will be construed against the insurer.'").

- **New Jersey:** *Passaic Valley Sewerage Commn'rs v. St. Paul Fire & Marine Ins. Co.*, 21 A.3d 1151, 1158 (N.J. 2011) ("If the terms are not clear, but instead are ambiguous, we construe them against the insurer and in favor of the insured to give effect to the insured's reasonable expectations.").

- **New Mexico:** *Battishill v. Farmers Alliance Ins. Co.*, 127 P.3d 1111, 1115 (N.M. 2006) ("We recognize that it is the law in New Mexico that 'an

insurance policy which may reasonably be construed in more than one way should be construed liberally in favor of the insured.'").

- **New York:** *Fed. Ins. Co. v. Int'l Bus. Machs. Corp.*, 965 N.E.2d 934, 936 (N.Y. 2012) ("If this is the case, the language at issue would be deemed to be ambiguous and thus interpreted in favor of the insured.") (citation omitted).

- **North Carolina:** *Register v. White*, 599 S.E.2d 549, 553 (N.C. 2004) ("If . . . the meaning of words or the effect of provisions is uncertain or capable of several reasonable interpretations, the doubts will be resolved against the insurance company and in favor of the policyholder.") (internal quotation marks omitted).

- **North Dakota:** *Fisher v. Am. Fam. Mut. Ins. Co.*, 579 N.W.2d 599, 602 (N.D. 1998) ("[A]ny ambiguity or reasonable doubt as to the meaning of an insurance policy is strictly construed against the insurer and in favor of the insured.").

- **Ohio:** *Westfield Ins. Co. v. Galatis*, 797 N.E.2d 1256, 1262 (Ohio 2003) ("[A]n ambiguity in an insurance contract is ordinarily interpreted against the insurer and in favor of the insured.").

- **Oklahoma:** *Haworth v. Jantzen*, 172 P.3d 193, 197 (Okla. 2006) ("When an insurance contract provision is ambiguous, words of inclusion will be liberally construed in favor the insured, and words of exclusion will be strictly construed against the insurer.").

- **Oregon:** *Shadbolt v. Farmers Ins. Exh.*, 551 P.2d 478, 480 (Or. 1976) ("[W]e have said many times that if there is an ambiguity in the terms of an insurance policy, any reasonable doubt to the intended meaning of such terms will be resolved against the insurance company and in favor of extending coverage to the insured.").

- **Pennsylvania:** *Prudential Prop. & Cas. Ins. Co. v. Sartno*, 903 A.2d 1170, 1175 (Pa. 2006) ("'Where a provision of a policy is ambiguous, the policy provision is to be construed in favor of the insured and against the insurer, the drafter of the agreement.'").

- **Rhode Island:** *Textron, Inc. v. Aetna Cas. & Sur. Co.*, 754 A.2d 742, 748 (R.I. 2000) ("[W]e strictly construe any ambiguous policy language in favor of the insured.").

- **South Carolina:** *Whitlock v. Stewart Title Guar. Co.*, 732 S.E.2d 626, 628 (S.C. 2012) ("Ambiguous or conflicting terms in an insurance policy must be construed liberally in favor of the insured and strictly against the insurer.") (internal quotation marks omitted).

- **South Dakota:** *Alverson v. Nw. Nat'l Cas. Co.*, 559 N.W.2d 234, 238 (S.D. 1997) ("When a policy is ambiguous, we should liberally construe the policy 'in favor of the insured and strictly against the insurer.'").

- **Tennessee:** *Garrison v. Bickford*, 377 S.W.3d 659, 664 (Tenn. 2012) ("In addition, contracts of insurance are strictly construed in favor of the insured, and if the disputed provision is susceptible to more than one plausible meaning, the meaning favorable to the insured controls.").

- **Texas:** *Evanston Ins. Co. v. Legacy of Life, Inc.*, 370 S.W.3d 377, 380 (Tex. 2012) ("As to the policy, if a term is susceptible to more than one reasonable interpretation, we must resolve that uncertainty in favor of the insured.").

- **Utah:** *Farmers Ins. Exch. v. Versaw*, 99 P.3d 796, 800 (Utah 2004) ("We have also stated that 'ambiguous or uncertain language in an insurance contract that is fairly susceptible to different interpretations should be construed in favor of coverage. . . . [I]f an insurance contract has inconsistent provisions, one which can be construed against coverage and one which can be construed in favor of coverage, the contract should be construed in favor of coverage.'") (brackets and ellipses in original).

- **Vermont:** *N. Sec. Ins. Co. v. Doherty*, 987 A.2d 253, 257 (Vt. 2009) ("Because the policy language is ambiguous, we construe it in favor of providing coverage . . . .").

- **Virginia:** *Smith v. Allstate Ins. Co.*, 403 S.E.2d 696, 697 (Va. 1991) ("'[D]oubtful, ambiguous language in an insurance policy will be given an interpretation which grants coverage, rather than one which withholds it.'").

- **Washington:** *Queen City Farms, Inc. v. Cent. Nat'l Ins. Co. of Omaha*, 882 P.2d 703, 721 (Wash. 1994) ("Unresolved ambiguity in insurance contract language is resolved against the insurer. Where exceptions to or limitations upon coverage are concerned, this principle applies with added force.") (citation omitted).

- **West Virginia:** *Wehner v. Weinstein*, 607 S.E.2d 415, 422 (W.Va. 2004) (This "Court stated that '"[i]t is well[-]settled law in West Virginia that ambiguous terms in insurance contracts are to be strictly construed against the insurance company and in favor of the insured."'") (citation omitted; brackets in original).

- **Wisconsin:** *Dowhower v. W. Bend Mut. Ins. Co.*, 613 N.W.2d 557, 565 (Wis. 2000) ("'Ambiguities in coverage are to be construed in favor of coverage, while exclusions are narrowly construed against the insurer.'").

- **Wyoming:** *Shaffer v. WINhealth Partners*, 261 P.3d 708, 713 (Wyo. 2011) ("Where insurance contracts are drawn so as to be ambiguous and uncertain and require construction, the contract will be construed liberally in favor of the insured and strictly against the insurer. Consequently, if the contract is fairly susceptible of two constructions, the one favorable to the insured will be adopted.").

HYPERLINKED AUTHORITIES

16 B.Mon. 242, 55 Ky. 242, 1855 WL 4204 (Ky.)
(Cite as: 16 B.Mon. 242, 55 Ky. 242 (Ky.), 1855 WL 4204 (Ky.))

Court of Appeals of Kentucky.
ÆTNA INSURANCE COMPANY
v.
JACKSON, OWSLEY & CO.
JACKSON, OWSLEY & CO.
v.
ÆTNA INSURANCE COMPANY.

Summer Term, 1855.

Appeal from Louisville Chancery Court.
On Cross-Errors.

***1** 1. An agent or consignee, having the property of his principal in his possession, and responsible for it, may, and especially if he have an interest in it, though it may be only for his commissions, insure it in his own name, and in case of loss recover its full value--holding all beyond his own interest in trust for the owners of the property. (Story Agency, sec. 111; *Hewitt, Allison & Co. v. Franklin Ins. Co.* 3 B. Mon. 231; 1 Hall, 189.)

2. Policies of insurance should be liberally construed to effectuate the intention of the assured.

3. A policy insuring all the articles constituting the stock of a pork house, and all articles contained within the building described and appurtenent thereto, covers all within those buildings without regard to the particular ownership of each or any article which was at the risk of the insured.

4. Contracts are to be construed according to the intention of the parties thereto. A contract to sell 40,000 hams, to be paid for on delivery; the hams were inspected and invoiced, but not delivered or paid for: *Held,* that the contract was executory, and property not changed, and if insured portected by the policy. (1 Phillips Ins. 27; 4 Mass. 336.)

5. A vendor of personal property, to be paid for on delivery, parts not with the title until payment; if the price is not paid in a reasonable time he may resume his original ownership, as upon a rescission of the contract. (Story Contr. sec. 809; Chitty Contr. 427, and authorities there cited.)

6. A vendor of goods not delivered, but to be paid for on delivery, has a lien on the property retained in possession for securing payment, and it is upon the presumption that the agreed price is the fair value, and can not be enhanced by any fluctuation in the value; and if the goods be insured the vendor is entitled to the insurance corresponding with interest insured. Any interest remaining in a vendor, who has made a contract of sale, remains protected under an existing insurance. (8 Mass. 516; 5 Pick. 76; 19 Ib. 81; Am. Lead. Cas. in note to the case in 8 Mass.)

The facts of the case are stated in the opinion of the court.

West Headnotes

Insurance 217 ⚿1790(3)

217 Insurance
217XIII Contracts and Policies
217XIII(D) Insurable Interest
217k1788 Particular Types of Coverage
217k1790 Property and Title Insurance
217k1790(3) k. Agents, consignees, factors or bailees. Most Cited Cases
(Formerly 217k115(3))

A consignee having property of his principal in his possession, and responsible for it, and especially if he has an interest in it, though only for his commissions, can insure it in his own name, and in case of loss recover its full value, holding all beyond his own interest in trust for the owners of the property.

Insurance 217 ⚿1831

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1831 k. In general. Most Cited Cases
(Formerly 217k146.7(1))

A contract of insurance will be construed strictly against the insurer and liberally in favor of the insured.

Insurance 217 ⚿2090

217 Insurance
217XV Coverage—in General
217k2090 k. In general. Most Cited Cases
(Formerly 217k157)

The language of the policy being framed in all its parts by the insurer, it is his duty, when apprised of the subject intended to be insured, so to frame his policy as to cover the intended subject.

Insurance 217 ⚿2136(3)

217 Insurance
217XVI Coverage—Property Insurance
217XVI(A) In General
217k2130 Property Covered or Excluded

217k2136 Personal Property
217k2136(3) k. Merchandise or stock in trade. Most Cited Cases
(Formerly 217k163(.5), 217k163)

A policy insuring all articles making up the stock of a pork house, and all within and appurtenant to the building, covers everything in the building, properly belonging to a pork house, without regard to the particular ownership of each and every article contained in or appurtenant to the building.

G. A. and I. CALDWELL for appellants:

***2** Argued: 1. That the third condition of the policy of the Ætna Insurance Company only bound the company to become ratably responsible, in case of loss, on the absolute property of Jackson, Owsley & Co. There is no such provision in this policy, as is contained in other policies, for liability for the loss of property belonging to others. There is no such provision as "or whom it may concern."

There was taken by the assured eight policies, covering $60,000 worth of property--five of the policies covering $25,000 to Jackson, Owsley & Co.; three to Jackson, Owsley & Co., "or whom it might (may) concern," covering $35,000. The undertaking in the policy, in this suit, is to pay a ratable share of the loss to the extent of $25,000--the real loss by Jackson, Owsley & Co. This is shown to be $8,009.92. The other insurances pay, of that sum, $1,416.16. The balance is $6,548.76, and for one-fifth of this sum is the Ætna Insurance Company liable in this suit, and no more.

We insist that by the third condition of the policy, in these words: "Goods held in trust or on commission are to be insured as such, otherwise the policy will not cover such property * * * Goods on storage must be separately and specifically insured," that the $18,000 worth of pork sold to Harbison & Hansboro, but still remaining in the house, was not covered by the policy in this case, but excluded by the terms of this third condition. (*Brichta v. The N. Y. Lafayette Ins. Co.,* 2 Hall N. Y. 372.) This case is not contradicted by the case of *Hewitt, Allison & Co. v. The Franklin Ins. Co.,* 3 B. Mon. 231, or *DeForest v. The Fulton Ins. Co.,* 1 Hall N. Y. 81.

The three policies covering property to the amount of $35,000 embrace as well the property of Jackson, Owsley & Co. as of others; the five covering $25,000 apply to the property of Jackson, Owsley & Co., and none others. The first three policies pay their proportion upon the whole loss of property in the pork house. The five insuring $25,000 pay only their proportion of the loss on $25,000 of the property of Jackson, Owsley & Co., and not of others. It is insisted that any other apportionment of the loss would be to make a new contract for the parties.

The case in 5 Hill, referred to by appellees, is believed to be unsound, not law, and repugnant to common sense.

2. It is insisted, for appellants, that the view of the chancellor, in respect to the $18,000

worth of meat sold by Jackson, Owsley & Co. to Harbison & Hansboro, is correct; that it constituted no part of the stock of the pork house after the sale, and therefore not protected by the policy. (See *Willis v. Willis,* 6 Dana, 48; *Crawford v. Smith,* 7 Dana, 59; *Owsley v. Sweeney,* 4 B. Mon. 413.)

It is urged, on behalf of the appellees, that though the title to the property may have vested in the vendees, Harbison & Hansboro, yet that appellees had still an insurable interest, and that they may recover to the extent of the injury they may have sustained. This is not admitted. If the appellees wished to protect any insurable interest which they believed they had, they ought to have taken out a new policy--the old policy no longer covered it after the sale--1st. Because it ceased, when sold, to constitute part of the stock of the pork house, which was the only property covered by the policy. 2d. Because after the sale it was held in trust, and not covered by the policy any more than was the meat slaughtered for others. 3d. Because it is the well established doctrine that "a sale of the interest insured during the continuance of the risk, divests the right of recovery under the policy." (8 Mass. 115; *Carrol v. The Boston Marine Ins. Co.* 2 Am. Lead. Cas.; 11 John. 302; Phillips Ins. 108, and authorities before cited.)

***3** The authorities relied on to show that an insurable interest remains protected after sale, apply to cases either where the sale is conditional, or where the legal title was retained by the vendor, to secure the purchase money. This case presents neither state of case. The sale was absolute. They had no right to retain the property except perhaps an equitable right to hold it to secure the payment of the price.

We ask a reversal.

O. G. CATES on the same side:

This record presents three questions, two of law and one of fact.

1. Was there, at the date of the policy in this case, any custom or usage in existence in Louisville giving the appellees, as the owners of a pork house, upon an insurance thereof, indemnity for loss of property held by them in trust for others? 2. Is the testimony of persons engaged in the business of insurance, and those engaged in pork packing, admissible in the construction of contracts of insurance? 3. Is the written part of insurance to have the effect to render inoperative the printed conditions annexed thereto? If so, does the written covenant cover property held by the assured in trust for others, and to what extent?

The chancellor correctly decided that there existed no custom in Louisville where the policy was to operate in regard to the rule of adjusting loss in a pork house, as none other had ever taken place.

I do not concur with the chancellor in regard to the second proposition.

In respect to the construction of the policy, and the force of the term, "for account of whom it may concern," used in policies from the earliest times, and the effect of such words in securing property of third persons in the house insured, the court is referred to Angell Ins.

p. 47, secs. 11, 12; Park Ins. 2, 3; Ellis Ins. 91. The insured in this case regarded these words as im portant, or why so soon after the fire show such anxiety to have them inserted in the two policies issued by the agents, Kennedy and Atwood? But it is insisted that the policy is to be construed by its own terms, without the aid of extrinsic evidence, as show no charge of fraud in this case. (See 5 Wend. 541; 6 Ib. 548; 16 Ib. 399; Angell, sec. 12; 2 Hall, 375; 3 Hill, 501, 161; 4 N. H. 171; 5 Pick. 181.)

I do not concur with the chancellor in his construction of the policy. Its terms are these: "Do insure Jackson, Owsley & Co., against loss or damage by fire, to the amount of $5,000 on pork, lard, bacon, bulk meat, hogs hanging, or otherwise, salt, bags, kegs or barrels, and all other articles composing the stock of a pork house, contained in their pork packing, lard, and smoke houses." It is not supposed that pork, lard, bacon, etc., constitute part of the stock of a pork house, but that the stock of a pork house consists of salt, barrels, kegs, and other articles; in other words, all such articles as are necessary to convert live stock into pork, lard, and bacon. The case in 3 B. Mon. cited by the chancellor, does not apply.

***4** Though contracts of insurance are to be liberally construed to effect the purpose for which they were designed, yet this rule of construction does not authorize the rejection of one part of the instrument to give undue effect to another part. It is not denied that more effect may generally be given to the written than the printed clauses of a policy, because they are descriptive of the person insured, and subject matter of the insurance; and, if in this case words had been written, giving insurance on property in the pork house of the assured and "others," or property generally "contained in their pork house," or on "pork as it might be from time to time in their pork house," such, and similar words might have been sufficient to control the printed words, "that property held in trust for others is to be insured separately, otherwise not covered."

No case has been found in which a policy containing words of like import with the one in this case has been held to cover property on storage, though there are cases which recognize the rule, that if a party has an interest in *different capacities,* he may insure both interests under a general policy, or under a general description.

The contract of insurance is one thing, and the rules which are to govern the adjustment of loss is another thing. They are the conditions annexed--the land-marks--the beacon-lights--to direct the mind of the court in adjusting the rights of the parties. (1 Duer Ins. 19; 5 Hill, 188; 13 Wend. 92; Angell Ins. 50; Park Ins. 2, 3; 13 Mass. 172; 5 Pick. 181.)

The sale by appellees of 40,000 hams to Harbison & Hansboro, worth $17,938, is proved, yet the credit in the adjustment was only for $13,000, and should have been for the entire sum of $17,938, and upon an agreed case the costs should have been divided.

RIPLEY and LOGAN for appellees:

This is in part an agreed case. It is admitted that in the pork house of appellees there was a loss by fire to the amount of $56,514.68, and they are entitled to recover. The amount of the recovery is the subject of controversy. The loss of Jackson, Owsley & Co., in their own right,

was $19,938.98, and the loss as consignees and bailees was $96,756.70, on which they had made large advances, and in which they were interested to the full value at the time of the fire.

Jackson, Owsley & Co., had made a contract to sell Harbison & Hansboro 40,000 bulk shoulders of hog meat for cash, payable on delivery. That 18,152 of these shoulders were not paid for nor delivered, and that they were destroyed by the fire, constituting part of the loss.

The aggregate amount of insurance on the entire stock of the pork house was $60,000, effected by various insurance companies by open policies, in the following proportions: one an open policy with Fellows & Co., for $25,000; two others in the name of "Jackson, Owsley & Co., and whom it may concern," for $5,000 each, and five of the policies were in the name of Jackson, Owsley & Co., for $5,000 each. The appellants' policy is one of the last mentioned five, not containing the words "or whom it may concern," but describing in *writing* the stock insured in the following comprehensive language: "Pork, lard, bacon, bulk meat, hogs hanging or otherwise, salt, barrels, kegs, and all other articles composing the stock of a pork house, contained in their pork packing, lard, and smoke houses, situated on the Bardstown turnpike, near the city limits."

***5** 2. The appellees insist that the appellants are liable for one-twelfth part of the $56,514.68, including the loss of the shoulders not delivered to, or paid for, by Harbison & Hansboro; and that there is no essential difference in the policies which do not contain the words "or whom it may concern," and those which do contain those words. In this construction the chancellor concurs, though he held that the appellants were not liable for the shoulders contracted for by Harbison & Hansboro, and gave judgment for only $3,737 and costs.

It is here insisted on the part of the appellees that if there be any difference between the two sets of policies, that they have the right to apply the policies containing the words "or whom it may concern," to the loss on the *consigned* and *trust* property, and leave the other policies to be in like manner applied exclusively to the loss on the property of the appellees. If it be considered that the policies which do not contain these words can not cover the *consigned* or *trust* property, and that the other policies do cover such property, then it would seem equitable (as the entire property has been insured), to exhaust the policies containing these words, by applying them to the *consigned* or *trust* property, and the other policies to the particular property of the appellees. This would be analogous to the equitable principle of applying securities, in such manner as to secure all; any other principle would convert a second insurance to the benefit of the first underwriter, than to the benefit of the insured, and in many cases leave the insured in a worse condition than if he had not made a second insurance.

Before the introduction of the clause into policies in regard to contribution, the course was for the assured to sue the *first* of the underwriters whose policy covered the loss, and leave him to seek contribution from the others. The object of this clause was to prevent circuity of action, and by *abatement* to make *contribution*, and not to establish any new rule; but the clause has no application except in cases where the risk is the same. If they be the same, the underwriters are treated as joint securities for the same debt. If they be not the same, each is

bound by his own policy for the entire amount, not exceeding the amount insured, and can compel no contribution.

If there is any difference in the policies, the risk insured against is not the same. By one set of policies the risk insured against would be the loss of appellees in their own right, which was $19,938.98, and by the other set of policies the loss insured against would be by the appellees, "or whom it may concern," which embrace not only the $19,938.98 but also the $36,575.70. It is obvious that the risks here are not the same on a hypothesis of a difference in the policies, and consequently the principle of contribution would not apply. The result would be that the policies in the name of appellees would have been applied to the $19,938.98, and the other policies exclusively to the $36,575.70. See the case of *Scribner v. Howard Ins. Co.* 5 Hill, for an express authority on this point.

***6** 3. But it seems to appellees' counsel that there is no difference between the two sets of policies, as to the liability of the appellants. Insurance was taken on the aggregate of $60,000 worth of property, by a description essentially identical in all the policies. The object was to secure all the property whatever constituting the stock of a pork house. The written description of the stock in all the policies is in substance the same, embracing *all the contents* of the pork house, which is as comprehensive as the term "or whom it may concern;" and the omission of those cabalistic words neither enlarges or impairs the effect of the policies on the subject matter insured. The terms are broad enough to embrace meat on consignment, or otherwise held in trust or on commission.

4. But it is insisted by appellants that the printed conditions in the policy are opposed to our view, and must so be regarded, and that goods held in trust or on commission must be insured as such, and that the consigned meat is no where insured as such in the Ætna policy, and consequently that the policy (despite the aforesaid written description), must be restricted by construction to apply only to the *peculiar* and absolute property of the appellees. To this we reply, that consigned property is no where insured as such--that is to say by name--even in those policies which use the words "or whom it may concern;" nor do we conceive it necessary to describe by name consigned meat in a pork house, in order to its protection. It is sufficient if the terms of the policy be clear and explicit enough to embrace it. Nothing more is required by the printed conditions. This is rendered more clearly evident from the nature of the business of the pork house. The testimony shows it to be the very business of a pork house in Louisville to receive and slaughter and pack pork and smoke it. It further shows that appellees were instructed to insure; that appellees made advances on hogs, and held an interest in the entire stock of pork at the time of the loss.

It was, therefore, their duty and their interest and right to insure the entire stock, and not merely their own peculiar interest. And it must have been understood at the Ætna office that the application was for insurance upon the consigned stock, as well as the particular property of the consignees. Their ""stock of meat" must have meant all the meat in the pork house of whatever description, in which they had, or thereafter might have, an interest, through all the shifting changes and operations of the business.

The testimony shows that no additional premium is demanded by insurers for the addition

of the words "or whom it may concern," in pork house policies. We insist, therefore, that the policy is as broad as though these words had been inserted, and was so understood by the parties. (*Hewitt, Allison & Co. v. Franklin Ins. Co.* 3 B. Mon. 231.)

5. The printed conditions in this policy should not prevail over the written description. There is reason to believe that the printed conditions are never intended to apply, in any case to a policy on the stock of a pork house, but only to *goods* (that is the word), held in trust or on commission. That printed condition is rarely if ever erased, even when inapplicable to the subject--as a building. The failure, therefore, to erase it in this case, when it has no application, should have no weight.

***7** It is further stipulated in the body of the policy that the printed conditions are to have no effect when therein provided against, which means nothing more than that they have no effect when inapplicable, as is the case here.

6. But the printed conditions are not regarded as presenting any obstacle to the recovery sought in this case for another reason. It is in proof that the whole stock of meat was at the risk of the appellees, and that they were virtually the *owners* thereof. Aside from the printed condition, although a mere naked consignee may have no insurable interest, a party holding goods in trust or on commission, with power to sell, or an interest however small, has, by law, the right to insure them, and in case of loss may recover the full value of the goods, being liable, after indemnifying himself, to the real owner for the surplus. In this case Jackson, Owsley & Co., had an interest in the pork contracted to Harbison & Hansboro, equal to the full value thereof; it was held at their risk, and they had a right to recover the full value of the whole. (Arnould Ins. 165, 5, 6, 252-3.)

7. The shoulders sold were never paid for, never delivered; no notice that an invoice was made out was ever given to the purchasers. The contract was for cash, to be paid on delivery. The facts show a contract for sale, with mutual conditions; neither party could compel performance without offer to perform, on his own part, and this not having been done the sale was incomplete, and the right of property was in the appellees. (Addison Contr. 41.)

8. The right of property not having passed, the appellees, had more than a lien right. They had a right of *dominion* over it, superior to a mere *lien,* growing out of his original ownership, and the buyer has no right in the thing purchased until tender of the price. (Smith Contr. 431.)

9. But if the right of property passed in a qualified sense, there can be no doubt of the right of appellees to retain the possession, in virtue of the lien, for the unpaid price, and this gave the appellees an insurable interest. (1 Phillips Ins. 27; *Stitson v. Mass. Ins. Co.* 4 Mass. 330; 1 Phillips Ins. 3d ed. 122; *Warder v. Horton,* 4 Binney, 529.) A vendor has an insurable interest. (*Fittermore v. Vermont M. F. Ins. Co.* 20 Vt.) So a vender of real estate may recover for a loss happening after a contract of sale, where he retains the title to secure the purchase money. This does not conflict with the rule that an absolute sale of property (which divests the seller of *all* interest), will prevent a recovery on a policy of insurance. (2 Am. Lead. Cas. 402: *Gordon v. F. & M. Ins. Co.* 2 Pick. 258.)

10. Suppose all interest in the pork contracted to Harbison & Hansboro to have passed by

the sale, still it was competent for appellees to make a contract to smoke them. This gave to appellees a right to retain them for that purpose, and until paid for that as well as the contract price, was an insurable interest. (1 Arnould Ins. 229-252; Phillips Ins. 3d ed. 166-175.)

***8** 11. It is not necessary that the court should believe that the whole stock in the pork house was at the risk of the appellees to entitle them to a full recovery for the lost property, if they were interested to a limited extent for advances made, or held the property for the purpose of sale, or otherwise controlling it, and especially if they had authority to insure it, and in the case of loss to recover the full value of both their own and the interest of the owners. (Story Agency, sec. 111; *Franklin Ins. Co. v. Hewitt & Allison, supra; DeForest v. Fulton Ins. Co.* 1 Hall, 84, which Judge Story approved.)

We think the judgment of the lower court is for too small a sum, and ask that it be reversed on cross-errors, and that a judgment be rendered for $4,709.55, with interest--being one-twelfth part of the loss of the appellees, including the loss on the shoulders qualifiedly sold to Harbison & Hansboro.

Chief Justice MARSHALL delivered the opinion of the court.

By an agreed case made in the Louisville chancery court, between Jackson, Owsley & Co. as plaintiffs, and the Ætna Insurance Company, defendant, it appears that in 1850 the defendant issued a policy for one year, but annually renewed by payment of the premium, insuring Jackson, Owsley & Co. against loss or damage by fire, to the amount of $5,000 on pork, lard, bacon, bulk meat, hogs hanging and otherways, salt, barrels, kegs, and all other articles composing the stock of a pork house, contained in their pork packing, lard, and smoke houses, situated on the Bardstown turnpike, near the city of Louisville, with the privilege of rendering lard and smoking meat; also to effect additional insurance without further notice to that office, unless called for. But it was stipulated that if there were other insurance prior or subsequent, the insured, in case of loss or damage, should not recover of this company a greater portion of the loss or damage sustained than the amount hereby insured shall bear to the whole amount insured on said property. The third printed condition annexed to the policy provides that goods held in trust or on commission, are to be insured as such, otherwise the policy will not cover such property; and that in the case of loss the names of the respective owners shall be set forth in the preliminary proofs, together with their respective interests therein; and that goods on storage must be separately and specifically insured. The fourth condition is to the effect that if a policy be assigned without consent of the company, the liability thereon shall cease. And that in case of any transfer or change of title in the property insured by this company, such insurance shall be void and cease.

The above mentioned policy was in force at the time of the fire, on the _____ day of _____, 1853, when a large portion of the meat and other articles in the pork house was destroyed. At the same time seven other policies were in force, of which four insured Jackson, Owsley & Co., to the amount of $5,000 each; two insured Jackson, Owsley & Co., or whom it may concern, to the amount of $5,000 each, and one for $25,000 in substantially the same form. The sum covered by all of the policies together was $60,000. The description of the property insured by each was in substance the same. It appears, however, that a large part of the pork, etc., in the house belonged to others than Jackson, Owsley & Co., the proprietors of

the house. That the total loss of these articles by the fire was about $56,500, of which property, to the value of $19,938.98, was claimed by the plaintiffs as theirs, and the other property lost amounted to $36,575.70. It appears, also, that a short time before the fire occurred, Jackson, Owsley & Co., had made a sale or an agreement for the sale of 40,000 shoulders of meat in the pork house, part of that now claimed as their own, to Harbison & Hansboro, the terms and circumstances of which will be hereafter further noticed; and the defendants insist that the value of such part of these shoulders as was destroyed by the fire, amounting, as they claim, to about $13,000, should be deducted from the claim of the plaintiffs for their own property destroyed. The defendants further insist that they are liable for nothing more than a ratable proportion of the loss upon the specific and peculiar property of the plaintiffs, whose property alone they say they insured; that the loss for which they are ratably liable is to be ascertained by first excluding from the estimate of the loss of the plaintiffs the value of the shoulders sold to H. & H. and destroyed by the fire, and then by applying to the residue of their claim for themselves, a ratable indemnity due from the three policies which insured Jackson, Owsley & Co., or whom it may concern, to the amount of $35,000, and that their liability is only for one-fifth of the remaining loss. The plaintiffs insist upon the opposite of each of these positions, and claim that in each of the eight policies, whether the words “or for whom it may concern,” be contained in it or not, the entire property comprising the stock of the pork house, whether belonging strictly to themselves, or held by them for others, is covered to the aggregate value of $60,000, that the defendants are liable for the ratable proportion of the whole loss estimated upon this basis, or that if there be the difference contended for between the effect of the policies, with or without the words “or whom it may concern,” the five policies which do not contain those words should be applied without any aid from the others, to the peculiar loss of the plaintiffs, leaving the other policies to cover the remaining loss; and further, that notwithstanding the sale of the shoulders to H. & H., such interest, property, and risk remained in the plaintiffs, as that they continued to be covered and protected by the policy of the defendants, and by the other policies before referred to.

***9** It will be seen from this statement, that the case presents two principal questions; the first upon the construction and effect of the policy on which the claim is founded: the second upon the effect of the sale to Harbison & Hansboro. Upon each of these questions, so far as extraneous facts might be applicable, there was a contest, and evidence was adduced by the parties; and the chancellor having decided the question upon the construction of the policy in favor of the plaintiffs, and that upon the effect of the sale to Harbison & Hansboro in favor of the defendants, and having decided against the latter, a sum ascertained on this basis, the defendants by their appeal, and the plaintiffs by cross errors complain--the former that the decree is for too great, and the latter that it is for too small a sum.

In reference to the first of these questions, it is proved that at all the pork houses in Louisville, and the adjacent cities of New Albany and Jeffersonville, eleven in number, and of which eight are in Louisville, it is a large part of the regular business of the establishment to receive the hogs of other persons, to be slaughtered, cut up, packed or smoked, or otherwise disposed of, as may be directed or agreed on; and that a large, often, perhaps, the largest part of the meat contained in the pork house belongs to other persons than the owners of the pork

house; and the evidence authorizes the assumption that in Louisville the term pork house is understood to denote an establishment in which the slaughtering of hogs, belonging to various owners, and the preparation of the pork, and lard or bacon to be made from them, is carried on, and the custody and care of the whole is undertaken; and that the stock of a pork house is understood as including the hogs and meat of the various owners placed and contained in it, as well as the instruments and materials necessary for carrying on the business in its various stages. The terms used in the policy to describe the different subjects of the insurance, are comprehensive enough to embrace all the subjects of the kind mentioned which might be contained in the pork packing, lard, and smoke houses of the plaintiffs. And, although, if there were nothing to indicate a contrary intention, the insurance might, under the third condition attached to the policy, be restricted to such of the articles described as properly belonging to the insured themselves; yet as the words, "and all other articles comprising the stock of a pork house," refer grammatically and properly not only to salt, barrels, and kegs, but also to all of the articles previously enumerated (as pork, lard, etc.), there would seem to be clear indication of intention to embrace in the description of everything constituting the stock of a pork house, which might be contained in the packing, lard, and smoke houses referred to.

It is proved that persons sending their hogs to the pork house of Jackson, Owsley & Co., to be slaughtered, etc., generally directed insurance to be made; that all the property in the establishment was considered to be at the risk of the plaintiffs; that they generally made advances on, and had charges against it; that it was their object to keep it all insured, as is usual among those engaged in the same business, and that their clerk, who obtained this policy, intended to get insurance applicable to the property of others, as well as that of the plaintiffs, and so understood his own application and the policy issued by the defendants.

***10** (1.) It seems to be the established law that an agent or consignee, having the property of his principals in his possession, and responsible for it, may, and especially if he have an interest in it, though it be only for his commissions, insure it in his own name, and in case of loss recover its full value, holding all beyond his own interest in trust for the owners of the property. (Story Agency, sec. 111; *Hewitt, Allison & Co. v. Franklin Ins. Co.* 3 B Mon. 231; *De Forest v. Fulton Ins. Co.* 1 Hall, 84.)

This principle is recognized by the third condition of the policy before us, which is relied on to exclude from the insurance all the property in the pork house establishment, except that which properly belonged to the plaintiffs themselves. And the question is, what form of expression should be deemed sufficient to comply with the requisition that goods held in trust or on commission must be insured as such, or will not be embraced in the policy? A general answer to this question is, that as the language of the policy in all its parts is framed by the insurer, and not by the insured, it is the duty of the former, when fully apprised of the subject intended and expected to be insured, so to frame the policy as to cover the intended subject, and to furnish the expected indemnity against loss upon that subject. And if the description given by the applicant, though sufficient by its comprehensiveness to cover all the property of the kind, and in the situation described, and which it may be his right and interest to insure, may yet, by the usage of insurance, or by the effect of a condition annexed to the policy, be subject, for want of particular words, to a restriction by which a portion of the property may be excluded; good faith requires that the insurer shall apprize the applicant of the ambiguity or

other defect, or by the inquiry ascertain his real intention. The insurer has printed policies incumbered with numerous and complicated provisos and conditions, and is presumed not only to understand their meaning, but to know their intended effect upon the forms of expression to be used in the policy, and upon the consequent rights of the parties. The insured, unfamiliar with these particulars, if not wholly ignorant of them, relies upon the written terms of insurance adopted for the actual case, and confides, as he has a right to do, in the skill and good faith of the insurer, for making the insurance effectual under the conditions of the policy to cover the subjects known to be intended. And although the insured by accepting the policy takes it with the description, provisos and conditions, which form a part of it, yet if he has himself acted in good faith, the considerations just adverted to require that the terms of the policy, both written and printed, should be construed liberally for his benefit, and so as to effectuate, as far as may reasonably be done, the indemnity which he justly expected.

(2.) Upon the question above stated, as to the form of expression necessary to effect an insurance upon goods held in trust or on consignment, several witnesses who had been engaged in the business of making insurance and issuing policies in Louisville, as agents for different insurance companies, were examined on each side. Several testified, on the part of the plaintiffs, to the effect that the description of property insured, as constituting the stock of a pork house, was sufficient to embrace the property constituting such stock, though it belonged to various persons; and that the additional words “or whom it may concern” were, in their opinion, immaterial, and gave no additional or different effect to the policy. Several witnesses for the defendant considered those words as material, and were of opinion that without these or other words indicating the ownership of others besides the insured, the policy would not embrace the property of others. Even these witnesses considered that the additional words “or whom it may concern,” would suffice to extend the insurance to property held in trust or on consignment, at least in an insurance on stock of a pork house; and we understand it to be proved that any of the insurers would insert these words simply upon request at the time of making up the policy, and without increase of the premiums; and that upon the policies executed to Jackson, Owsley & Co., not containing those words, all except two had been settled according to the claim of the plaintiffs in this case.

***11** This evidence does not, it is true, establish a uniform custom or usage in Louisville, for the adjustment of loss upon policies such as that now in question, nor even a uniform practice in adapting the terms of the policy to the protection of the different owners of property under the care and custody of the proprietors of a pork house; but it shows that while some, perhaps a majority, would deem it sufficient for this purpose to describe the property as constituting the stock of a pork house; others, who would deem it necessary to say nothing more, would still be content with the additional words “or whom it may concern,” following the name of the insured, and would themselves use these words as sufficient to include in the indemnity the property of the various owners. None of them intimate that they would deem it necessary to use more than these latter words for the purpose. And as these words, which indicate nothing more than that other persons besides those specially named as the insured, are or may be interested in the subject, and may be entitled to the benefit of the promised indemnity, would be used by the strictest constructionists among the insurers themselves, as a sufficient compliance with the requisition of the third condition of the policy; any other words

or phrase, importing the same thing, must, in reason, be deemed equally a compliance with the same requisition.

The policy itself shows that pork, lard, etc., and the other articles enumerated in it, do compose a part of the stock of a pork house; the enumeration and description are sufficient to embrace all articles of the kind referred to, whether belonging to the owners of the pork house or to others, and do embrace all unless restricted by the third condition. But as the term ""pork house," as understood in Louisville, designates an establishment and a business, in which hogs of various owners are slaughtered and undergo various operations by which they are prepared for market; and as the stock of a pork house being composed of the same articles, in their various forms, includes the property of various owners, and as the phrase itself carries with it the idea of this various ownership, and clearly denotes it, we think the enumeration of the various articles which might compose the stock of a pork house, with the additional characteristic that they do compose the stock of a pork house belonging to the plaintiffs, denotes sufficiently, and as certainly as the words "or whom it may concern," that others besides the insured themselves are interested in the property, and are intended to have the benefit of the insurance to the extent of their interests, and should therefore be deemed a compliance with the third condition.

If it were admitted that the application to insure in the names of Jackson, Owsley & Co. pork, lard, etc., and all other articles composing the stock of a pork house, contained in the buildings described, did not indicate unequivocally the desire to insure the entire stock of the pork house to whomsoever the articles composing it might belong, it might well have been deemed sufficient for that purpose by the applicant, as it would have been, and in fact was so deemed by several insurers in Louisville. And with such knowledge of the business and usages of a pork house as every insurer there must be presumed to have had, the application in these terms was at least sufficient to apprise any one applied to for insurance, that it was probably, if not certainly, the design of the applicant to obtain insurance upon the entire stock, though the articles composing it might belong to different owners. If, according to the opinions and practice or usage of the particular insurer to whom the application was made, a further specification of this intention were deemed necessary, good faith, as we have already said, required that he should have so informed the applicant, or that he should by inquiry (as one of the witnesses says would be proper), have turned his attention to what was deemed an ambiguity, and have thus ascertained what he intended; having failed to do so, and having drawn up for an applicant who, as indicated by the terms of the application, intended to describe, and desired to insure the entire stock, a policy, which presenting the same ambiguity (if it be one), will be effectual or ineffectual for the purpose intended; as it may be construed in favor of one or the other parties, common justice requires that the consequences of the failure should fall upon the party who, under the circumstances, might and should have removed the ambiguity; and an applicant for insurance having indicated, with reasonable certainty, the extent of the insurance desired, should not, after a loss has occurred, be disappointed in his just expectation of indemnity by an objection of which the insurer was apprised when the policy was issued, while its existence and effects may, for all that appears, have been unknown to the party insured.

***12** (3.) But the objection is not in any view sustainable. The object of the third condition

of the policy, as shown by the practice of insurers at Louisville, is accomplished by any sufficient indication in the policy that the property described, to whomsoever belonging, is intended to be insured. And upon the evidence respecting the nature and business of a pork house in Louisville, we are of opinion that the description of the subjects insured, as all being the articles constituting the stock of a pork house, and contained in the buildings described, which are evidently appurtenant to the pork house, is a reasonably certain indication that all articles of the kind mentioned and situated or contained in the buildings described, are, without regard to the actual or peculiar ownership of each or any of them, intended to be insured. The hogs and meat in the establishment, and the ownership of them, would of course vary from time to time. At particular periods Jackson, Owsley & Co., the proprietors of the pork house, might own none or but a small portion of the hogs or meat in it, but all being at their risk, they had the strongest motives of duty and interest to keep it insured. And this fact, growing out of the nature of the business, tends strongly to prove, not only that the plaintiffs intended to cover all by insurance, but that this intention was known to the insurers.

We are of opinion, therefore, that the first of the two questions stated was properly decided by the chancellor, and that the loss upon the articles constituting the stock of the pork house should be borne ratably by all the insurers, although the articles did not all belong to Jackson, Owsley & Co., and, although the policies do not all contain the words “or whom it may concern.”

Upon the second question, which relates to the sale to Harbison & Hansboro, and its proper effect in this case, it is to be remarked, that although in strictness a sale imports a complete and executed contract, by which the title and possession, or right of possession, are transferred from the vendor to the vendee, the term itself is often applied to transactions in which the transfer is not thus comprehensive and complete, and in which the contract, in some respects, seems to be executory. The criterion established for determining whether, in a particular case, the property has passed by the sale so as to be thenceforth at the risk of the vendee, refers of course to the particular facts which characterize the transaction. The facts in the present case are substantially the following: In February, 1853, some two or three weeks before the fire occurred, Harbison & Hansboro purchased from Jackson, Owsley & Co., 40,000 green or bulk shoulders of pork, on the terms that they were to be paid for in cash on delivery. On the same day of the purchase the vendors ascertained that they had not that number of shoulders in the condition called for by the contract, but having shoulders which had been hung up and were being smoked, it was agreed that the deficiency should be made up in shoulders of this latter description. The shoulders, all of which were in the pork house buildings, were to be weighed by the vendors, and were to be sound and merchantable. The vendees were to employ an inspector to inspect them. The shoulders appeared to have been weighed and inspected some ten or fifteen days before the fire. But it does not appear that either of the vendees, of whom both resided at the distance of about thirty miles, were at the pork house, either at the time of the weighing or afterward, before the fire, to receive and pay for the shoulders, though one of them had gone to Louisville to see about it, and while there, probably about the time of the weighing, had advanced, by way of accommodation, and not of obligation, $17,000 to the vendors; which sum did not equal one-half of the entire price to be paid. A very large proportion of the green shoulders was destroyed by the fire. The residue,

together with those which were smoked, were afterward delivered, and the price of those delivered, amounting to about $3,000 in addition to the $17,000 previously advanced, was then paid. The clerk of the vendors states that it was the general usage on such sales, to make out an invoice, on the delivery of which to the vendees, the price was to be paid; that the meat, until paid for, was considered to be the property, and at the risk of the vendors, and we infer from the evidence that the parties understood that it was to be kept under insurance by the vendors. The invoice was made out on the meat being weighed, or as it was weighed, sometime before the fire, but had not been delivered to the vendees, nor had any payment been made by them beyond the advance of $17,000 as before stated. The plaintiffs made no claim upon the vendees for the shoulders which were burnt, but look to the insurance upon the stock in the pork house for indemnity.

***13** The first question upon this evidence is, whether the vendors had, on their part, done all that was to have been done preparatory to the final execution of the contract, and before the vendees were bound to pay for the articles purchased, since no invoice was ever delivered, and it does not appear that the inspector of the vendors had anything to do with the weighing or counting of the pieces, or took any notice of either. Nor, indeed, is there any distinct and precise proof of the price per pound agreed to be paid, nor of the allowance to be made in taking the smoked instead of the green shoulders. If these matters remained to be adjusted before the aggregate sum to be paid could be certainly determined, it would seem that the articles sold did not, according to the general rule applicable to the ordinary sales of goods, for cash, to be paid for on delivery, become the property of the vendees, and at their risk, before a large portion of them was destroyed by fire. And even if the matters just referred to were so agreed on in the contract that nothing remained to be done for their final ascertainment after the articles were counted, weighed, and inspected, it would be just, and would seem to be requisite, that before the vendees should be involved in the hazard consequent upon ownership, they should be apprized of the facts necessary to be known before they could, by making payment, be entitled to assume the authority and control pertaining to ownership. This knowledge, according to the usage of the vendors in such sales, and the understanding of the parties in this particular case, was to be communicated by delivery of the invoice. And although the vendees might, at any time after the weighing, etc., was completed, which would necessarily take several days, have demanded the invoice, and upon that or such other knowledge as they had, might have offered payment and demanded or taken the goods (as the vendors might on their part have delivered the invoice and demanded payment), the delay of each party to exercise these rights important to each, if the ownership and risk were already devolved on the vendees, who had failed to insure, tends strongly to prove in corroboration of the statement of the witness, that it was the understanding and intention of the parties that the ownership and risk were to remain, and did remain, with the vendors, and under the protection of their insurance until payment or delivery. If, as we may think may be assumed, as fairly deducible from the facts, such was the intent of the contract, there is no doubt that such intention, whether expressed in words or implied from its nature and the attendant circumstances, would give character to the transaction and determine the rights of the parties. And there is as little doubt that the insurers, setting up this contract between the insured and others to protect themselves from loss, upon the very articles insured, occurring during the very period of their insurance, must abide by the nature and effect of that

contract, as between the parties, to be determined upon the evidence in the case against the insurers.

***14** (4.) There is no rule of law more universal or more inflexible than that contracts are to be effectuated according to the lawful intention of the parties. There is none more certain than that the parties themselves may determine by their contract, whether on a sale of property for cash on delivery, the title and ownership shall pass immediately on the making of the contract, or on the identification of the articles sold and the price, or not until payment or delivery. The contract in this case being in parol, is more open than if it had been in writing to implications, and to the proof of facts and circumstances, for ascertaining its terms and effect; and certainly there is no principle, either of reason or of law, which requires that in the present contest with the insurers there should be a different rule, either of evidence or of construction, from that which would prevail between the parties themselves. The insurers put their case and the question upon the right of the parties under the contract, and they must abide by those rights as they existed, and would be determined between the parties.

Then notwithstanding this nominal sale to Harbison & Hansboro, the plaintiffs, according to the view of the facts and law just presented, had not only the possession and the right of possession, but the property or ownership itself, in substantially the same plight as before, except that their obligation to deliver the articles to these purchasers on payment of the price, restricted them from selling the same articles to others. And as their interest in the safety of the property was equivalent to the entire price (for under the view now taken, they were bound to account for the $17,000, and would lose the entire benefit of the sale, in case of non-delivery, unless they could show a default on the part of the vendees), there seems to be no reason, according to the general law of insurance, why they should not recover for the loss of the articles counted and weighed under the contract, just as if the contract had not been made; nor is their right thus to recover affected, as we think, by the fourth condition of the policy, declaring that a transfer or change of title in the property insured shall avoid the insurance upon it. The only legitimate or supposable object of that clause is to prevent the continuance of the insurance, and the liability of the insurers, after the property ceases to be at the risk of the insured, when it would in effect be but a wagering policy. And notwithstanding the vagueness of the expression, “any change of title,” it would be understood by common men, and should be construed with reference to its object, as meaning such transfer or change of title from one to another, as would terminate the interest and risk of the insured in the property transferred.

(5.) But if the preceding view, with regard to the nature and effect of the contract, for the sale of 40,000 shoulders to Harbison & Hansboro be incorrect, if the right of property passed to them as soon as the shoulders were identified by counting and weighing them, the vendees were of course then bound to make payment, and the vendors had still not only the right to retain the possession until payment, but had also the further right if payment should not be made in reasonable time, and especially after notice, to sell the same articles to another at the risk of the vendees, or to resume their own absolute dominion, as upon a rescission or abandonment of the contract. (Story Contr. sec. 809, 812; Chitty Contr. 427, and cases cited by both authors.) If these rights, which seem to be more than a mere lien, amounting in fact to nothing more, the lien did not, like the right of the vendees to demand, and the obligation of

the vendors to deliver possession in payment of the price, grow out of the contract which conferred upon the vendors no other right but that of demanding payment. It grew out of their original ownership and dominion, and was a remnant of their original possession and property, or interest, precisely equal in value to the unpaid price to become due on delivery. And as this lien was retained as the chosen security, its value as property or as an interest in property is wholly independent of the solvency or insolvency of the debtor, and is precisely measured by the sum due, and the adequacy of the lien to secure it. The insolvency of the debtor would, it is true, render more apparent the importance of the lien as being the only security, but would not affect its intrinsic value, nor the creditors' right to look to it for securing payment.

***15** (6.) If no part of the price be paid, this lien of the vendor, which is an interest or property in the articles sold but retained in possession for securing payment, is upon the presumption that the agreed price is the fair value, to be regarded as equivalent in value to the articles themselves, and to the absolute ownership of them, except that although it may be depreciated it can not be enhanced by the fluctuations of the market; and as the vendor, whether the vendee be solvent or insolvent, has a right to look to the goods and his lien upon them for securing payment, and is not bound to resort to the personal responsibility of the vendee, so if his lien or interest in the articles sold be protected by insurance, that insurance being, in case of a destruction of the goods, and consequently of the lien, by a casualty insured against, substituted by the very nature and effect of the transaction, to the extent of the interest insured, in place of the goods themselves, he must have the same right to look to it, instead of resorting to the personal responsibility of the vendee, as he would have had to look to the goods themselves had they remained.

That the interest of the vendors, as above stated, was a proper subject of insurance, is not denied; and if they had insured that interest specifically, after the contract with Harbison & Hansboro, we suppose the consequence, as above stated, would be alike unquestioned. But it is contended that without such subsequent and specific insurance the vendors, notwithstanding the previous insurance upon the same articles as their property, have no recourse upon the policy on account of the impairment or destruction of their lien by a casualty insured against, and that having lost their lien by the destruction of the goods, they have no other resource for payment but in the personal responsibility of the vendees, whose insolvency would subject them to precisely the same loss, and upon precisely the same subject, as if there had been no sale. And this consequence is insisted on in a case in which the very terms of the contract indicate clearly that there was no substantial transfer or change of the title, and that the vendors retaining, and entitled to retain, the goods as a security for the price, retain an interest in them equal to their value, and when the vendees at most acquire but nominal title, unaccompanied by possession, or the right of possession, arising not from any positive act or intention of the parties having that object directly in view, but by mere operation of law, and encumbered by an interest of the vendors equivalent to the value of the subject, and clothed with the possession and the right of possession.

Waiving the objection founded on the inconvenience of requiring, and especially in the business of a pork house, a new insurance after every transaction by which the title to property remaining in the establishment may be immediately or ultimately affected, and waiving also

the considerations which tend to show that the parties to this sale did not intend that the right of property should pass until payment of the price, but intended and expected it to remain as the property of the vendors, subject to the insurance already on it, we are of opinion that under the general law of insurance the interest remaining in the vendors after the sale, though not the same as that which existed before, was still protected by the previous policy, unless excluded from protection by the terms of that instrument; and that the fourth condition of the policy does not apply to a case in which, although there was in name a sale, there was in fact neither an absolute transfer of property or change of title, nor a substantial transfer or change of interest.

***16** Upon the first branch of this proposition the authorities are abundant and decisive. Phillips, in his treatise on insurance (vol. 1, p. 27), says it has been held "that the sale and conveyance in fee of a house insured, which the purchaser at the same time mortgages back to the vendor, did not divest the assured of his interest under the policy." In the case to which he refers (*Stetson v. The Mass. Mut. Ins. Co.*, 4 Mass. 336), the plaintiff, after the issuing of the policy, sold and conveyed a part of the building insured, reserving to himself a term of seven years in the premises, and the grantee at the same time reconveyed them to the grantor, in mortgage, to secure the purchase money; it was objected that by the act of incorporation, and by the very nature of a mutual insurance company, the members of the company must be the owners of buildings--it was in virtue only of those buildings being insured that the owners can become members of the company. The objection seems to have been considered by the court principally with reference to the principle of policy which prohibits gambling insurances, insurances without interest. The objection was overruled by a majority of the court, as not being supported by showing contracts affecting the formal title of the plaintiff, in parts only of the subject of the insurance. And it is said in the opinion "his interest in a part remains the same, and perhaps substantially, and for the purpose of repelling this objection, is to be considered as unaltered in the whole of the premises insured. It had been before said, that taking the writings together, the transaction might be considered as a conditional sale after the expiration of seven years.

In *Carrol, etc. v. The Boston Mut. Ins. Co.,* 8 Mass. 516, the principle seems to be recognized that if any interest remain in the insured at the time of the loss it is sufficient, and that if a conveyance made after the insurance, which was in fact absolute, had been a mortgage, there would still have been an interest on which there might have been a recovery. This principle is more distinctly stated in the case of *Lazarus v. The Commonwealth Ins. Co.,* in which several cases in the Supreme Court of Massachusetts are referred to as sustaining it. (5 Pick. 76.) And in the same case again reported (after a second trial), in 18 Pick. 81, the principle was discussed and decided, that notwithstanding a conveyance (after the insurance), if it be in the nature of a mortgage or in trust, with a resulting trust to the insured, so that he has in truth an insurable interest in the property, he may nevertheless recover to the extent of his actual loss. The transfer of the vessel insured with other property, was in trust to pay over the proceeds to certain creditors of the plaintiff, who would of course be entitled to the surplus if any. A new trial was granted because a verdict had been found for the plaintiff, when there was no evidence of a probable surplus after payment of the debts. On the subsequent trial it was proved that the debts had been paid, and on the ground that the transfer was not absolute,

and the insurable interest only conditionally affected by it, and that it left the plaintiff entitled to the surplus, the verdict for him was sustained, and he had judgment accordingly.

***17** In 2 American Leading Cases, 435, in a note to the case of *The Boston Mut. Ins. Co.*, before cited from 8 Mass., it is said to be universally admitted that a sale or assignment of the property will only defeat the recovery of the assignor on the policy, when and so far as it strips him of insurable interest, without regard to whether the interest which survives the conveyance be of the same nature or character as that which existed before the conveyance was made, to which the author adds: "It is consequently well settled that a vendor either of real or personal property, who has retained the legal title as a security for the purchase money, may recover for a loss which has happened subsequently to the execution of the contract of sale," and a number of cases decided by different courts are referred to. These cases, with few exceptions, we have not had an opportunity of examining. But the principle last stated is directly sustained by the case cited above from 4 Mass. and the principle first stated is sustained by all of the above cited cases, to which others might be added.

The cases, and especially the cases in 4 Mass. and that in 5 and 19 Pick., have also a bearing upon the construction of the fourth condition of the policy now in question, which being supposed to have been founded upon some just principle, and to have been intended for the attainment of some substantial object, and as a security to the insurer against unfair claims rather than as a protection against such as are just and equitable, we are of opinion that it does not apply to such contracts or transactions as affect merely the formal title of the assured, leaving in him an insurable interest of substantial value in the subject or a part of it, and especially where that interest is equivalent in value to that which existed before, and is only distinguishable from it by subtle and nice discrimination, or by artificial rules of construction.

Being of opinion, therefore, that under any view of the effect of the sale to Harbison & Hansboro, and of the transactions relating to it, the policy covered the interest of the plaintiffs in the articles sold, so long as they remained in the pork house unpaid for, and not actually delivered; and being further satisfied that this interest of the plaintiffs was equal in value to the whole of said articles which were consumed by the fire, we conclude that the various insurers being, as now appears, responsible for the entire loss, the defendants are responsible for one-twelfth part thereof.

Wherefore, the judgment upon the original errors assigned by the defendants is affirmed, but upon the cross-errors of the plaintiffs it is reversed, and the cause is remanded, with directions to render a judgment in favor of the plaintiffs for one-twelfth part of the entire loss, including that occasioned by the destruction of a part of the shoulders sold to Harbison & Hansboro.

Ky.App. 1855.
Aetna Ins. Co. v. Jackson
16 B.Mon. 242, 55 Ky. 242, 1855 WL 4204 (Ky.)

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725 S.W.2d 165
(Cite as: 725 S.W.2d 165)

Supreme Court of Texas.
Glen ARNOLD, Petitioner,
v.
NATIONAL COUNTY MUTUAL FIRE INSURANCE COMPANY, Respondent.

No. C–4674.
Jan. 28, 1987.
Rehearing Denied March 25, 1987.

After injured motorcyclist had been successful in action against insurer providing motorcyclist uninsured motorist protection and uninsured motorist, and insurer had paid motorcyclist policy limit, motorcyclist brought action against insurer alleging various statutory causes of action and common-law cause of action for insurer's breach of its duty of good faith and fair dealing in handling motorcyclist's claim. The District Court No. 151st, Harris County, Anthony J.P. Farris, J., granted summary judgment for insurer. The Houston Court of Appeals, First Supreme Judicial District, in unpublished opinion, affirmed, and motorcyclist appealed. The Supreme Court, Ray, J., held that: (1) motorcyclist's causes of action against insurer under Insurance Code, both independently and as pleaded through Deceptive Trade Practices Act, were barred by Insurance Code article which exempted county mutual insurers from particular Insurance Code articles at time action was brought; (2) insurers had duty to deal fairly and in good faith with their insureds, and cause of action for breach of that duty was stated when it was alleged there was no reasonable basis for denial of claim or delay in payment or failure on part of insurer to determine whether there was any reasonable basis for denial or delay; and (3) statute of limitations did not begin to run on good faith and fair dealing claim until underlying insurance contract claims were finally resolved.

Judgment of Court of Appeals affirmed in part and reversed in part; cause remanded to trial court.

Gonzalez, J., filed concurring opinion.

West Headnotes

[1] Insurance 217 ⚿1070

217 Insurance
217II Regulation in General
217II(C) State Agencies and Regulation
217k1070 k. Judicial remedies and review. Most Cited Cases
(Formerly 217k4.3)

Injured motorcyclist's causes of action under the Insurance Code against insurer which provided motorcyclist uninsured motorist protection were barred by Insurance Code article which exempted county mutual insurers from particular Insurance Code articles at time suit

was brought, as causes of action were pleaded independently and as they were pleaded through Deceptive Trade Practices Act. V.T.C.A., Bus. & C. § 17.41 et seq.; V.A.T.S. Insurance Code, arts. 17.22, 21.21, 21.21–2.

[2] Limitation of Actions 241 ⚿99(1)

241 Limitation of Actions
241II Computation of Period of Limitation
241II(F) Ignorance, Mistake, Trust, Fraud, and Concealment or Discovery of Cause of Action
241k98 Fraud as Ground for Relief
241k99 In General
241k99(1) k. In general. Most Cited Cases

Any cause of action for misrepresentation which injured motorcyclist had against insurer that provided motorcyclist uninsured motorist protection, based on representation that policy would pay uninsured motorist benefits if prerequisites were fulfilled and fact no payment of benefits was made until judgment after jury verdict in action by motorcyclist against uninsured motorist and insurer, was barred by statute of limitations, where injuries occurred in June 1974, uninsured motorist and insurer were sued in June 1974, judgment was obtained in December 1977 and insurer then paid policy limit, and action alleging misrepresentation was filed in December 1978. V.T.C.A., Bus. & C. § 17.46(a), (b)(5, 12).

[3] Insurance 217 ⚿1867

217 Insurance
217XIII Contracts and Policies
217XIII(H) Relations Between Parties; Implied Terms
217k1867 k. Good faith and fair dealing. Most Cited Cases
(Formerly 217k156(1))

Insurers have duty to deal fairly and in good faith with their insureds.

[4] Insurance 217 ⚿3336

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3334 In General
217k3336 k. Reasonableness of insurer's conduct in general. Most Cited Cases
(Formerly 217k602.2(1))

Cause of action for insurer's breach of duty of good faith and fair dealing with respect to insureds is stated when it is alleged there is no reasonable basis for denial of claim or delay in payment or failure on part of insurer to determine whether there is any reasonable basis for denial or delay.

[5] Judgment 228 ⚿181(23)

228 Judgment
228V On Motion or Summary Proceeding
228k181 Grounds for Summary Judgment
228k181(15) Particular Cases
228k181(23) k. Insurance cases. Most Cited Cases

Genuine issue of material fact existed as to whether insurer had reasonable basis for refusal to pay injured insured's uninsured motorist claim and with actual knowledge of that fact forced insured to trial on accident before it would pay claim, so as to preclude summary judgment for insurer in action by insured alleging breach of duty of good faith and fair dealing.

[6] Insurance 217 ⚿3419

217 Insurance
217XXVIII Miscellaneous Duties and Liabilities
217k3416 Of Insurers
217k3419 k. Bad faith in general. Most Cited Cases
(Formerly 217k602.1)

Exemplary damages and mental anguish damages are recoverable for insurer's breach of duty of good faith and fair dealing with respect to insureds under same principles allowing recovery of such damages in other tort actions.

[7] Limitation of Actions 241 ⚿55(1)

241 Limitation of Actions
241II Computation of Period of Limitation
241II(A) Accrual of Right of Action or Defense
241k55 Torts
241k55(1) k. In general. Most Cited Cases

Statute of limitations does not begin to run on insured's good faith and fair dealing claim against insurer until underlying insurance contract claims are finally resolved.

[8] Limitation of Actions 241 ⚿55(1)

241 Limitation of Actions
241II Computation of Period of Limitation
241II(A) Accrual of Right of Action or Defense
241k55 Torts
241k55(1) k. In general. Most Cited Cases

Injured motorcyclist's cause of action against insurer providing uninsured motorist protection for breach of duty of good faith and fair dealing was not barred by two-year statute of limitations governing actions for personal injury, on theory that motorcyclist's rights were

invaded at time his claim was rejected in 1974, where motorcyclist obtained judgment against his insurer and uninsured motorist in December 1977 and brought action alleging breach of good faith and fair dealing in December 1978. Vernon's Ann.Texas Civ.St. art. 5526 (Repealed); V.T.C.A., Civil Practice & Remedies Code § 16.003.

***166** Dale W. Felton, Felton & Associates, Stan Pfeiffer, Whittington, Pfeiffer & Vacek, Houston, for petitioner.

Larry Funderburk, Kurt Groten, Funderburk & Funderburk, Houston, for respondent.

OPINION

RAY, Justice.

Glen Arnold appeals from a summary judgment granted defendant National County Mutual Insurance Company. The court of appeals, in an unpublished opinion, affirmed the trial court's judgment on the grounds that Arnold's common law and statutory causes of action, if valid, were barred by limitations. We reverse that part of the judgment denying the common law cause of action and remand the cause to the trial court.

This is a suit on an insurance contract. In June 1974, Arnold was severely injured when the motorcycle he was operating was struck by a car driven by an uninsured motorist. Arnold was insured by NCM under a policy that included “uninsured motorist” protection with a limit of $10,000. Arnold made timely demand for payments up to the limit and an independent insurance adjusting firm recommended, within six months following the date of the accident, that NCM pay the entire policy limit to Arnold. NCM refused to pay although it is not clear when it specifically denied the claim.

Arnold sued both the uninsured motorist and the insurance company in late June 1974. In December 1977, Arnold obtained a judgment against both defendants for approximately $17,975. NCM then paid Arnold the $10,000 policy limit. Arnold filed this suit on December 27, 1978, alleging various statutory causes of action and a common law cause of action for NCM's breach of its duty of good faith and fair dealing in its handling of his claim. The trial court granted summary judgment in favor of NCM on all of Arnold's causes of action.

Summary judgment evidence shows that NCM based its decision to deny the claim on the advice of its agent, who was the attorney handling the file. Even though the uninsured motorist admitted that the collision was his fault, NCM refused to negotiate a settlement. In his deposition the attorney handling the file admitted that he was inexperienced in insurance matters and based his recommendation on his perception that a jury would be prejudiced against motorcyclists, that Arnold was driving too fast under the existing conditions and that Arnold was intoxicated. The summary judgment evidence relied on by Arnold also showed that the defenses of ***167** speed and intoxication proferred by the attorney were very weak at best and ultimately intoxication was not pleaded. NCM failed to investigate the facts supporting the attorney's contentions. An issue of fact was raised as to NCM's reasonableness in failing to settle the claim and forcing Arnold to trial.

In order to decide if the court of appeals erred in upholding the summary judgment on

limitations grounds, we must first resolve those points of error directed to the underlying causes of action.

STATUTORY CAUSES OF ACTION

[1] The court of appeals did not err in upholding the trial court's rendition of summary judgment on Arnold's causes of action under the Deceptive Trade Practices Act (DTPA) and articles 21.21 and 21.21–2 of the Texas Insurance Code. His causes of action under the Texas Insurance Code, both independently and as pleaded through the DTPA, are barred by article 17.22 of the Texas Insurance Code which exempted county mutual insurance companies from articles 21.21 and 21.21–2 at the time this suit was brought. *Jewell v. Mobile County Mutual Insurance Company,* 566 S.W.2d 295 (Tex.1978).

[2] Arnold also pleaded that NCM violated § 17.46(a) and (b)(5) and (12) of the DTPA "by representing that the policy would pay uninsured motorist benefits when certain prerequisites were fulfilled and when, in fact, no payment of those benefits was made after complete compliance by Plaintiff of the prerequisites until judgment after jury verdict." Arnold did not plead and there is no summary judgment evidence that NCM made any misrepresentations. Even if Arnold had stated a cause of action for misrepresentation, it was barred by limitations.

COMMON LAW CAUSE OF ACTION–DUTY OF GOOD FAITH AND FAIR DEALING

[3] Arnold raises the issue of whether there is a duty on the part of insurers to deal fairly and in good faith with their insureds. We hold that such a duty of good faith and fair dealing exists. *See,* Zupanec, *Cause of Action in Tort for Bad Faith Refusal of Insurer to Pay Claim of Insured* § 2, in Vol. 1 Shepard's Causes of Action 205 (1983).

While this court has declined to impose an implied *covenant* of good faith and fair dealing in every contract, we have recognized that a duty of good faith and fair dealing may arise as a result of a special relationship between the parties governed or created by a contract. *Manges v. Guerra,* 673 S.W.2d 180, 183 (Tex.1984); *See, English v. Fischer,* 660 S.W.2d 521, 524 (Tex.1983) (Spears, J., concurring).

In the insurance context a special relationship arises out of the parties' unequal bargaining power and the nature of insurance contracts which would allow unscrupulous insurers to take advantage of their insureds' misfortunes in bargaining for settlement or resolution of claims. In addition, without such a cause of action insurers can arbitrarily deny coverage and delay payment of a claim with no more penalty than interest on the amount owed. An insurance company has exclusive control over the evaluation, processing and denial of claims. For these reasons a duty is imposed that "[An] indemnity company is held to that degree of care and diligence which a man of ordinary care and prudence would exercise in the management of his own business." *G.A. Stowers Furniture Company v. American Indemnity Company,* 15 S.W.2d 544, 548 (Tex.Comm'n App.1929, holding approved).

[4][5] A cause of action for breach of the duty of good faith and fair dealing is stated when it is alleged that there is no reasonable basis for denial of a claim or delay in payment or a failure on the part of the insurer to determine whether there is any reasonable basis for the

denial or delay. Arnold pleaded and produced sufficient summary judgment proof to raise an issue of material fact that NCM had no reasonable basis for its refusal to pay his uninsured motorist claim and with actual knowledge of that, forced him to a trial on the accident before it would pay the claim.

***168** EXEMPLARY DAMAGES

[6] Arnold further complains that the trial court erred in granting summary judgment by ruling that he was not entitled to recover exemplary damages and mental anguish damages. It is clear from the record that the summary judgment does not specifically address the issue of damages and, of course, in the absence of a viable cause of action there would not be a damage recovery. However, we would point out that exemplary damages and mental anguish damages are recoverable for a breach of the duty of good faith and fair dealing under the same principles allowing recovery of those damages in other tort actions. *See, e.g., Trenholm v. Ratcliff,* 646 S.W.2d 927 (Tex.1983) and authorities cited therein; *Clements v. Withers,* 437 S.W.2d 818 (Tex.1969); *Ware v. Paxton,* 359 S.W.2d 897 (Tex.1962); *Bennett v. Howard,* 141 Tex. 101, 170 S.W.2d 709 (1943).

LIMITATIONS

The court of appeals held that all of Arnold's causes of action including his good faith and fair dealing claim were barred by both the two-year (tort) and four-year (contract) statutes of limitations. Tex.Rev.Civ.Stat.Ann. art. 5526 and art. 5527 (now Tex.Civ.Prac. & Rem.Code §§ 16.003 & 16.004). This was based on that court's reasoning that Arnold's rights were invaded at the time his claim was rejected.

[7][8] Arnold argues that as in "*Stowers* " cases the statute of limitations should not begin to run until judgment in the underlying cause becomes final. *See Linkenhoger v. American Fidelity & Casualty Company, Inc.,* 152 Tex. 534, 260 S.W.2d 884 (1953). We agree with the reasoning in *Linkenhoger* and hold that the statute of limitations does not begin to run on a good faith and fair dealing claim until the underlying insurance contract claims are finally resolved.[FN1] *See also Maryland American General Insurance Company v. Blackmon,* 639 S.W.2d 455 (Tex.1982). Thus, Arnold's cause of action for breach of the duty of good faith and fair dealing is not barred by the applicable two-year statute of limitations governing actions for personal injury. Tex.Rev.Civ.Stat.Ann. art. 5526 (now Tex.Civ.Prac. & Rem.Code § 16.003).

FN1. This does not mean that a contract claim and a claim for breach of the duty of good faith and fair dealing may not be tried together when possible.

The judgment of the court of appeals denying Arnold's statutory causes of action is affirmed. We reverse that part of the judgment denying the common law cause of action and remand the cause to the trial court for further proceedings consistent with this opinion.

GONZALEZ, J., concurs.

GONZALEZ, Justice, concurring.

I concur. I believe that the elements of this cause of action are: (1) a contract between the insurer and the insured; (2) the insurer denied the insured's claim or delayed in payment; and

(3)(a) the insurer knew that it had no reasonable basis for denying the claim or delaying in payment; or (b) the insurer failed to determine whether there was any reasonable basis for the denial or delay.

Tex.,1987.
Arnold v. National County Mut. Fire Ins. Co.
725 S.W.2d 165

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972 S.W.2d 738, 41 Tex. Sup. Ct. J. 1153
(Cite as: 972 S.W.2d 738)

Supreme Court of Texas.
Joe BALANDRAN and Dolores Balandran, Appellants,
v.
SAFECO INSURANCE COMPANY OF AMERICA, Appellee.

No. 97–1093.
Argued Feb. 4, 1998.
Decided July 3, 1998.

Insureds brought state-court action against homeowners' insurer to recover for damage to their home‘s foundation, as well as interior and exterior finishes, as result of broken sewer line. Insurer removed case. The United States District Court for the Western District of Texas, James R. Nowlin, J., granted insurer's motion for judgment as matter of law. Insureds appealed. The Court of Appeals, 129 F.3d 747, certified question. The Supreme Court, Phillips, C.J., held that exclusion in standard homeowners' insurance policy for loss to dwelling caused by settling, cracking, bulging, shrinkage, or expansion of foundations was inapplicable to structural damage from a plumbing leak.

Question answered.

Owen, dissented and filed opinion.

West Headnotes

[1] Insurance 217 ⚿2142(6)

217 Insurance
217XVI Coverage—Property Insurance
217XVI(A) In General
217k2139 Risks or Losses Covered and Exclusions
217k2142 Water Damage
217k2142(6) k. Sewers and drains; plumbing. Most Cited Cases

Insurance 217 ⚿2144(1)

217 Insurance
217XVI Coverage—Property Insurance
217XVI(A) In General
217k2139 Risks or Losses Covered and Exclusions
217k2144 Movement of Earth or Structure
217k2144(1) k. In general. Most Cited Cases

Exclusion in standard homeowners' insurance policy for loss to dwelling caused by settling, cracking, bulging, shrinkage, or expansion of foundations was inapplicable to structural damage from a plumbing leak; even though the policy stated in section for personal

property coverage that the exclusion did not apply to loss caused by accidental discharge, leakage, or overflow of water or steam, this exclusion repeal provision was ambiguous, was thus not limited to personal property coverage, and applied to the dwelling coverage.

[2] Insurance 217 ⚿1806

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1806 k. Application of rules of contract construction. Most Cited Cases

Insurance contracts are subject to the same rules of construction as other contracts.

[3] Insurance 217 ⚿1813

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1811 Intention
217k1813 k. Language of policies. Most Cited Cases

Primary goal in interpreting insurance policy is to give effect to the written expression of the parties' intent.

[4] Insurance 217 ⚿1810

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1810 k. Construction as a whole. Most Cited Cases

Supreme Court interpreting insurance policy must read all parts of the contract together, striving to give meaning to every sentence, clause, and word to avoid rendering any portion inoperative.

[5] Insurance 217 ⚿1808

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1808 k. Ambiguity in general. Most Cited Cases

While parol evidence of the parties' intent is not admissible to create an ambiguity, an insurance contract may be read in light of the surrounding circumstances to determine whether an ambiguity exists.

[6] Insurance 217 ⚿1808

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1808 k. Ambiguity in general. Most Cited Cases

Insurance policy is ambiguous, if, after rules of construction are applied, the contract is subject to two or more reasonable interpretations.

[7] Insurance 217 ⚿1835(2)

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1835 Particular Portions or Provisions of Policies
217k1835(2) k. Exclusions, exceptions or limitations. Most Cited Cases

Where an ambiguity involves an exclusionary provision of an insurance policy, Supreme Court must adopt the construction urged by the insured as long as that construction is not unreasonable, even if the construction urged by the insurer appears to be more reasonable or a more accurate reflection of the parties' intent.

***739** John R. Harrison, San Antonio, for Appellants.

Brian Blakeley, San Antonio, Dan Morales, Austin, for Appellee.

PHILLIPS, Chief Justice delivered the opinion of the Court, in which GONZALEZ, ENOCH, SPECTOR, BAKER, ABBOTT and HANKINSON, Justices join.

This case comes to us on a certified question from the United States Court of Appeals for the Fifth Circuit. The issue certified is whether the 1991 Texas Standard Homeowner's Policy—Form B covers damage to the insured's dwelling from foundation movement caused by an underground plumbing leak. We hold that the policy provides this coverage.

I

Safeco Insurance Company of America insured the home of Joe and Dolores Balandran. The form of the policy was the 1991 Texas Standard Homeowner's Policy—Form B. In September 1993, the Balandrans filed a claim against Safeco for damage to their home caused by an underground plumbing leak. The leak caused the soil to expand, damaging the home's foundation as well as its interior and exterior finishes. When Safeco denied the claim, the Balandrans sued the company in state district court. Safeco removed the case to federal court on diversity jurisdiction.

At trial, the jury found that the structural damage was caused by the plumbing leak and awarded the Balandrans $66,500. Safeco, however, moved for judgment as a matter of law, contending that the Balandrans' policy excluded this structural damage regardless of the underlying cause. The trial court granted this motion, rendering a take-nothing judgment for

Safeco.

The Balandrans appealed to the Fifth Circuit Court of Appeals. While their appeal was pending, a separate Fifth Circuit panel considered this issue, holding that an identical policy did not provide coverage for foundation damage from a plumbing leak. *See Sharp v. State Farm Fire & Cas. Ins. Co.*, 115 F.3d 1258 (5th Cir.1997). Subsequently, however, the Texas Commissioner of Insurance issued a bulletin vigorously disagreeing with the *Sharp* decision. *See* TEX. DEP'T OF INS. BULLETIN B–0032–97 (Aug. 22, 1997). In light of these developments, the panel hearing the Balandrans' appeal certified to us the controlling question regarding policy coverage.

II

[1] The Balandrans' policy provides two types of coverage. “Coverage A” insures the dwelling itself, while “Coverage B” insures personal property. Coverage A provides the following protection:

> We insure against all risks of physical loss to the [dwelling] unless the loss is excluded in Section I Exclusions.

The exclusion relevant to this case is 1(h), which provides:

> We do not cover loss under Coverage A (Dwelling) caused by settling, cracking, bulging, shrinkage, or expansion of foundations, walls, floors, ceilings, roof structures, walks, drives, curbs, fences, retaining walls or swimming pools.
>
> We do cover ensuing loss caused by collapse of building or any part of the building, water damage or breakage of glass which is part of the building if the loss would otherwise be covered under this policy.

Safeco argues that the damage to the Balandrans' home clearly falls under this exclusion. ***740** The Balandrans apparently concede that, if the exclusion applies, it excludes their claim. However, they present three arguments about why the exclusion does not apply. First, they contend that language in Coverage B (the personal property section of the policy) creates an exception to exclusion 1(h) when the structural damage results from a plumbing leak. Second, they argue that exclusion 1(h) does not apply to structural damage resulting from an underlying cause—in this case a plumbing leak—which itself is not an excluded peril under the policy. Finally, the Balandrans argue that the last sentence of exclusion 1(h) (the “ensuing loss” provision) creates an exception to exclusion 1(h) under the present circumstances. Because we conclude that the Balandrans are entitled to prevail on their first argument, we do not reach the other two.

III

A

Unlike Coverage A, which insures the dwelling against “all risks,” Coverage B insures personal property only against twelve enumerated perils. The ninth of these twelve perils is:

> **Accidental Discharge, Leakage or Overflow of Water or Steam** from within a plumbing, heating or air conditioning system or household appliance.

> A loss resulting from this peril includes the cost of tearing out and replacing any part of the building necessary to repair or replace the system or appliance. But this does not include loss to the system or appliance from which the water or steam escaped.
>
> *Exclusions 1.a through 1.h under Section I Exclusions do not apply to loss caused by this peril.*

(bold in original, italics added). Even though Coverage B deals with personal property loss, which the Balandrans did not suffer, the Balandrans rely heavily on the last sentence quoted above. They argue that this provision (the "exclusion repeal provision") means exactly what it says: Exclusions 1(a) through 1(h) do not apply to a loss caused by a plumbing leak. Because exclusion 1(h) does not apply to the Balandrans' loss, it is covered under Coverage A, which insures against any risk to the dwelling. In other words, the exclusion repeal provision, on its face, applies to any "loss," not just personal property losses.

Safeco, relying on the structure of the policy, argues that the exclusion repeal provision applies only to personal property losses resulting from a plumbing leak. Because Coverage B deals with personal property coverage, Safeco contends that the exclusion repeal provision should be similarly limited. Safeco argues that we may not construe this sentence without considering its context within the policy. *See State Farm Life Ins. Co. v. Beaston,* 907 S.W.2d 430, 433 (Tex.1995) ("[C]ourts must be particularly wary of isolating from its surroundings or considering apart from other provisions a single phrase, sentence, or section of a contract.").

As we have already noted, one Fifth Circuit panel has adopted Safeco's approach. *See Sharp v. State Farm Fire & Cas. Ins. Co.,* 115 F.3d 1258 (5th Cir.1997). Under identical facts, the court held that the damage to the dwelling was excluded under exclusion 1(h), and that the exclusion repeal provision applied only to personal property losses:

> We are sympathetic to the Sharps' situation, but we cannot agree that text specifically included in Coverage B, which applies only to personal property, may be imported into Coverage A, which applies to the dwelling or house, in order to create coverage for a loss that does not involve personal property damage. The Sharps' policy clearly and unambiguously divides dwelling losses and personal property losses into two separate "coverages." It therefore would appear to be nonsensical, and a rejection of the obvious structure of the policy, to reach into text that applies solely to Coverage B (Personal Property) to determine the extent of coverage provided under Coverage A (Dwelling).
>
> 115 F.3d at 1262.

B

[2][3][4][5] Several rules of construction guide our consideration of this issue. First, insurance***741** contracts are subject to the same rules of construction as other contracts. *See Beaston,* 907 S.W.2d at 433; *National Union Fire Ins. Co. v. CBI Indus.,* 907 S.W.2d 517, 520 (Tex.1995); *Forbau v. Aetna Life Ins. Co.,* 876 S.W.2d 132, 133 (Tex.1994). Our primary goal, therefore, is to give effect to the written expression of the parties' intent. *See Beaston,* 907 S.W.2d at 433; *Forbau,* 876 S.W.2d at 133. We must read all parts of the contract together, *see Beaston,* 907 S.W.2d at 433, striving to give meaning to every sentence, clause,

and word to avoid rendering any portion inoperative. *See United Serv. Auto. Ass'n v. Miles,* 139 Tex. 138, 161 S.W.2d 1048, 1050 (1942). While parol evidence of the parties' intent is not admissible to create an ambiguity, *see National Union,* 907 S.W.2d at 520, the contract may be read in light of the surrounding circumstances to determine whether an ambiguity exists. *See Columbia Gas Transmission Corp. v. New Ulm Gas, Ltd.,* 940 S.W.2d 587, 589 (Tex.1996); *National Union,* 907 S.W.2d at 520.

[6][7] If, after applying these rules, a contract is subject to two or more reasonable interpretations, it is ambiguous. *See National Union,* 907 S.W.2d at 520. Where an ambiguity involves an exclusionary provision of an insurance policy, we "must adopt the construction ... urged by the insured as long as that construction is not unreasonable, even if the construction urged by the insurer appears to be more reasonable or a more accurate reflection of the parties' intent." *National Union Fire Ins. Co. v. Hudson Energy Co.,* 811 S.W.2d 552, 555 (Tex.1991); *see also Glover v. National Ins. Underwriters,* 545 S.W.2d 755, 761 (Tex.1977). FN1

FN1. This widely followed rule is an outgrowth of the general principle that uncertain contractual language is construed against the party selecting that language. *See* SEGALLA, 2 COUCH ON INSURANCE § 22.14 (3d ed.1997). It is also justified by the special relationship between insurers and insureds arising from the parties' unequal bargaining power. *See Arnold v. National County Mut. Fire Ins. Co.,* 725 S.W.2d 165, 167 (Tex.1987).

Applying these rules, we conclude that the exclusion repeal provision is subject to two reasonable interpretations, and is therefore ambiguous. We are mindful of the Fifth Circuit's reasoning in *Sharp,* and we agree that it reflects one reasonable interpretation of the policy language. However, the Balandrans' interpretation is also reasonable. First, the policy on its face states that exclusion 1(h) does not apply to "loss" caused by a plumbing leak; this repeal of exclusion 1(h) is not expressly limited to "personal property loss." That the exclusion repeal provision is contained in Coverage B does not necessarily dictate Safeco's narrow reading. Instead, the exclusion repeal provision could be located under Coverage B simply because that is the only place in the policy that the "accidental discharge" risk is specifically described. Because the exclusion repeal provision applies solely to that risk, it is logical for it to be adjacent to the policy's description of the risk.

Further, Safeco's construction of the policy renders a part of the policy language meaningless. The exclusion repeal provision applies to "[e]xclusions 1.a. through 1.h." Under Safeco's reading, of course, exclusions 1(a) through 1(h) are repealed only for personal property losses caused by a plumbing leak. However, exclusion 1(h) on its face applies only to damage to the dwelling. Thus, if Safeco's reading is correct, it would have been unnecessary to extend the exclusion repeal provision to exclusion 1(h), because that exclusion can never affect personal property losses. Under Safeco's approach, therefore, the part of the exclusion repeal provision referring to exclusion 1(h) is without any effect.

The Balandrans' interpretation becomes even more reasonable when we consider the circumstances surrounding the promulgation of this policy form. Article 5.35 of the Texas

Insurance Code, subject to certain exceptions not relevant here, requires insurers to use policy forms adopted or approved by the Commissioner of Insurance. The policy at issue here was promulgated in 1990 by an advisory committee appointed by the Board of Insurance, the Commissioner's statutory predecessor. The Board directed this committee, which consisted of insurance industry representatives and consumer representatives, "to assist the Board with conversion of the Texas Standard Homeowners Policies ***742** into a simplified, easy-to-read form for use in the State of Texas." *See* RECORD OF OFFICIAL ACTION OF THE STATE BD. OF INS. no. 54929 (July 18, 1989). The Board expressly instructed the committee "that such conversion process shall not in any manner restrict coverages currently available to the insured under a homeowners policy." *Id.*

The policy in effect when the committee started its work unambiguously covered foundation damage resulting from a plumbing leak. Effective since 1978, that policy contained exclusion repeal language similar to that at issue here, but it was located in the *exclusions* section. Thus, one could not argue that the exclusion repeal provision applied only to personal property loss. *See State Farm Lloyds v. Nicolau,* 951 S.W.2d 444, 446 (Tex.1997) ("Under an express exception, however, these exclusions [referring to, among others, the foundation-damage exclusion] do not apply to losses caused by an 'accidental discharge, leakage or overflow of water' from within a plumbing system."). FN2 The 1978 policy, like the present one, also recited the "accidental discharge" language in the Coverage B (personal property) section. The committee, in promulgating its "easy-to-read" policy, moved the exclusion repeal language to section B, adjacent to the "accidental discharge" language there, thus eliminating the need to restate this language. The Board subsequently adopted the committee's form after being assured by the committee's chairman, Don Olsen (a representative of State Farm Fire & Casualty Insurance Company), that the revisions were "accomplished in line with [the Board's] charge of making sure that there is no restriction in coverage available to any insured under an existing homeowner policy in Texas." *See* FEBRUARY 14, 1990, HEARING ON PROPERTY INS. RULES CONCERNING TEXAS HOMEOWNERS POLICY AND RELATED MATTERS at 5. The circumstances surrounding the drafting of this policy thus support the Balandrans' theory that the exclusion repeal provision is located within Coverage B merely to simplify the policy, not to restrict the scope of the exclusion repeal.FN3

FN2. The relevant language from the 1978 policy was as follows:

> EXCLUSIONS (Applicable to Property Insured under Coverages A and B and Perils Insured Against)—This insurance does not cover:
>
> ...
>
> k. Loss under Coverage A caused by settling, cracking, bulging, shrinkage, or expansion of foundations, walls, floors, ceilings, roof structures, walks, drives, curbs, fences, retaining walls or swimming pools.
>
> The foregoing Exclusions a, b, c, f, h, i, j and k shall not apply to Accidental discharge, leakage or overflow of water or steam from within a plumbing, heating or air conditioning system or a domestic appliance (including necessary tearing out and

replacing any part of the building covered).

FN3. Contrary to the dissenting justices' contention, we are not considering this evidence for the purpose of creating an ambiguity. Because the Balandrans' interpretation of the contract language is reasonable, an ambiguity exists on the face of the policy. We merely highlight this evidence because it further supports the result we reach.

Safeco cites several cases for the proposition that exclusion 1(h) excludes damage to foundations, regardless of the underlying cause. *See, e.g., General Ins. Co. of America v. Hallmark,* 575 S.W.2d 134, 136 (Tex.Civ.App.—Eastland 1978, writ ref'd n.r.e.); *Lambros v. Standard Fire Ins. Co.,* 530 S.W.2d 138, 140 (Tex.Civ.App.—San Antonio 1975, writ ref'd); *Bentley v. National Standard Ins. Co.,* 507 S.W.2d 652, 654 (Tex.Civ.App.—Waco 1974, writ ref'd n.r.e.). These cases construe the standard homeowner's policy in effect before 1978, which contained no exclusion repeal provision for accidental discharge of water from a plumbing unit. These cases do not apply to the issue before us.

In sum, we conclude that the Balandrans' interpretation of the exclusion repeal provision is not unreasonable. Because the Balandrans are the insureds, we adopt their interpretation as the proper construction of the policy.

* * *

Accordingly, we hold that exclusion 1(h) in the 1991 Texas Standard Homeowner's Policy—Form B does not apply to loss caused by the accidental discharge, leakage or overflow of water or steam from within a plumbing, heating or air conditioning system or household appliance.

***743** OWEN, Justice, filed a dissenting opinion, in which HECHT, Justice, joins.

I am sympathetic to the Balandrans' plight. But, for the reasons expressed by the Fifth Circuit in *Sharp v. State Farm Fire & Casualty Insurance Co.,* 115 F.3d 1258 (5th Cir.1997), the Texas Standard Homeowner's Policy unambiguously excludes damage to a foundation caused by a plumbing leak. In finding an ambiguity, the Court ignores the structure of the policy. The Court is also unduly swayed by the arguments of the Commissioner of Insurance that the policy provides coverage. I respectfully dissent.

I

There is one matter on which all can agree. The so-called “easy-to-read” standard-form policy is very poorly drafted. As will be considered in more detail below, one of the provisions on which the Court relies is inoperative and meaningless in several respects. Nevertheless, the shortcomings of the drafting in some areas do not render the sections of the policy that govern the particular coverage question before us ambiguous.

The issue is whether the 1991 Texas Standard Homeowner's Policy (Form B) provides coverage for dwelling damage from foundation movement caused by an underground plumbing leak. The policy divides property coverage into two sections: “Coverage A,” for the dwelling, and “Coverage B,” for personal property. The policy maintains this division both in describing the property that is insured and in describing the risks that are insured against. The

pertinent provisions of the policy are contained in Appendix A.

The policy provides in straightforward language that it does not cover loss under Coverage A (Dwelling) "caused by settling, cracking, bulging, shrinkage, or expansion of foundations, walls, floors, ceilings...." App. A, para. 1(h) of Sec. I (exclusions). Thus, under exclusion h, settling, cracking, bulging, shrinkage, or expansion of foundations, walls, floors, and ceilings is excluded from coverage regardless of the cause of the settlement, cracking, bulging, shrinking, or expansion.

The Court, however, reaches into Coverage B, the personal property section of the policy, to find language that it says negates exclusion h. But the provision cited by the Court applies only to personal property losses. Under Coverage B, Safeco insured personal property against twelve enumerated perils, one of which is a plumbing leak:

> Accidental Discharge, Leakage or Overflow of Water or Steam from within a plumbing, heating or air conditioning system or household appliance.
>
> A loss resulting from this peril includes the cost of tearing out and replacing any part of the building necessary to repair or replace the system or appliance. But this does not include loss to the system or appliance from which the water or steam escaped.
>
> Exclusions 1.a though 1.h under Section I Exclusions do not apply to loss caused by this peril.
>
> App. A, para. 9 of Coverage B.

Nothing in this or any other part of Coverage B even remotely suggests that settling, cracking, or expansion of foundations, walls, floors, or ceilings is covered, even if the ultimate cause in fact of the settlement or cracking is a plumbing leak. The only part of Coverage B that relates to the dwelling is a limited provision that covers the cost of tearing out and replacing the part of the dwelling necessary to repair a plumbing system. By no stretch of the imagination does this extend coverage to settlement or cracking of the foundation.

The Court, however, relies on the last sentence of this limited provision, which it refers to as the "exclusion repeal provision" and which provides: "Exclusions 1.a. through 1.h. under Section I Exclusions do not apply to loss caused by this peril." App. A, para. 9 of Coverage B. The Court concludes that, because the word "loss" in this provision is not expressly limited to personal property losses, it must apply to any loss, including damage to the dwelling. Thus, the Court concludes, exclusions 1(a) through 1(h) do not apply to structural damage caused by a plumbing leak. *See* 972 S.W.2d at 740.

***744** This interpretation, in both my view and that of the United States Court of Appeals for the Fifth Circuit, is unreasonable. *See Sharp,* 115 F.3d at 1263; *see also Jimenez v. State Farm Lloyds,* 968 F.Supp. 330, 333 (W.D.Tex.1997). The exclusion repeal provision is located in the section of the policy dealing with personal property losses. While the one sentence on which the Court focuses may not contain the words "personal property," such a

limitation is unnecessary given its location. The word "loss" in the exclusion repeal provision can reasonably refer only to the type of loss at issue in Coverage B, which is personal property loss.

This Court has warned against reading policy language out of context:

> To [effectuate the parties' intent, courts] must read all parts of a contract together. Indeed, courts must be particularly wary of isolating from its surroundings or considering apart from other provisions a single phrase, sentence, or section of a contract.

State Farm Life Ins. Co. v. Beaston, 907 S.W.2d 430, 433 (Tex.1995) (citations omitted). Completely ignoring its own admonition, the Court seizes on one sentence without regard for its location in the policy.

The Fifth Circuit, considering this precise issue in *Sharp*, got it exactly right:

> We are sympathetic to the Sharps' situation, but we cannot agree that text specifically included in Coverage B, which applies only to personal property, may be imported into Coverage A, which applies to the dwelling or house, in order to create coverage for a loss that does not involve personal property damage. The Sharps' policy clearly and unambiguously divides dwelling losses and personal property losses into two separate "coverages." It therefore would appear to be nonsensical, and a rejection of the obvious structure of the policy, to reach into text that applies solely to Coverage B (Personal Property) to determine the extent of coverage provided under Coverage A (Dwelling).

115 F.3d at 1262. In order to except plumbing-leak damage from exclusion h, the drafters should have placed such language in the Coverage A section dealing with damage to the dwelling or in exclusion h, as was the case in the post–1978 version of the policy.[FN1] They did not. (The post–1978 policy was at issue in *State Farm Lloyds v. Nicolau,* 951 S.W.2d 444 (Tex.1997), not the version at issue here, which reflects amendments made in 1990.)

FN1. The post–1978 policy provided as follows:

> EXCLUSIONS (Applicable to Property Insured under Coverages A and B and Perils Insured Against)—This insurance does not cover:
>
> ...
>
> k. Loss under Coverage A caused by settling, cracking, bulging, shrinkage, or expansion of foundations, walls, floors, ceilings, roof structures, walks, drives, curbs, fences, retaining walls or swimming pools.
>
> The foregoing Exclusions a, b, c, f, h, i, j and k shall not apply to Accidental discharge, leakage or overflow of water or steam from within a plumbing, heating or air conditioning system or a domestic appliance (including necessary tearing out and replacing any part of the building covered).

While it may be true that the drafters did not intend to change the substance of the post–1978 standard policy form when they promulgated the present form, the unambiguous

language they chose nevertheless effected a change. The policy at issue in this case is very similar to the pre–1978 policy form that unquestionably excluded foundation damage caused by a plumbing leak. *See General Ins. Co. v. Hallmark,* 575 S.W.2d 134, 136 (Tex.Civ.App.—Eastland 1978, writ ref'd n.r.e.) (holding that what is now exclusion h excluded "settling of the foundation and cracking of the walls brought about by a water leak" underneath the home); *Park v. Hanover Ins. Co.,* 443 S.W.2d 940, 942 (Tex.Civ.App.—Amarillo 1969, no writ) (holding that loss from accidental discharge of water from a plumbing system resulting in structural damage was excluded by what is now exclusion h), *abrogated on other grounds by National Surety Corp. v. Adrian Assocs.,* 650 S.W.2d 67 (Tex.1983); *see also Lambros v. Standard Fire Ins. Co.,* 530 S.W.2d 138, 141–42 (Tex.Civ.App.—San Antonio 1975, writ ref'd); *Bentley v. National Standard Ins. Co.,* 507 S.W.2d 652, 654 (Tex.Civ.App.—Waco 1974, writ ref'd n.r.e.).

***745** As an additional justification for its construction of what it calls the "exclusion repeal provision," the Court asserts that, if the repeal were only for personal property losses, the repeal would be "without any effect." 972 S.W.2d at 741–42. But the repeal is wholly without effect in other respects. The repeal extends to exclusion b, which excludes "loss caused by smog or by smoke from industrial or agricultural operations." App. A, para. 1(b) of Sec. I (exclusions). I respectfully submit that damage to personal property caused by smog or smoke from industrial or agricultural operations would never coincide with the accidental discharge peril. Nor would loss caused by windstorm, hurricane, or hail to the property enumerated (exclusion c) ever coincide with the accidental discharge peril in Coverage B. The same can be said of exclusion d, which excludes theft of personal property when it is located outside the insured residence. And when would the repeal of exclusion g, which excludes loss caused by animals or birds kept by the insured, have any meaning in conjunction with the accidental discharge peril?

Because the Court's interpretation of the policy is unreasonable, it does not create an ambiguity. *See National Union Fire Ins. Co. v. CBI Indus.,* 907 S.W.2d 517, 520 (Tex.1995) ("If ... the language of a policy or contract is subject to two or more *reasonable interpretations,* it is ambiguous." (emphasis added)).

II

The Court also resorts to inadmissible extrinsic evidence to find support for its construction of the policy. Because insurance policies are contracts, however, we must "ascertain the true intent of the parties *as expressed in the instrument." National Union,* 907 S.W.2d at 520 (emphasis added). When the policy is not ambiguous on its face, extrinsic evidence may not be used to create an ambiguity. *See id.*

Ignoring this rule of construction, the Court cites statements from the Board of Insurance and testimony from a Board hearing. While the Court suggests that it is merely examining the "circumstances surrounding the promulgation of this policy form," 972 S.W.2d at 741–42, the Court relies on parol evidence directly relating to the drafters' intent that conflicts with the language of the policy. If this is not inadmissible extrinsic evidence, what is? This case is notably similar to *National Union,* in which the parties disputed whether an insurance policy's "absolute pollution exclusion" applied to an acid spill at a construction site. 907 S.W.2d at

518. The insured sought discovery regarding the insurers' "understanding" of this provision, specifically that they " 'understood that the pollution exclusions would not exclude coverage in construction accident situations.' " 907 S.W.2d at 520–21. The Court rejected this request, concluding that the insured was simply seeking "an opportunity to discover parol evidence going to the parties' intentions in order to create a latent ambiguity." *Id.* at 521. The Court reiterated that "no issue regarding the parties' intentions is raised *unless* the policy is ambiguous—and evidence of those intentions cannot be used to create an ambiguity." *Id.* at 521 n. 5.

Addressing this same issue in *Sharp,* the Fifth Circuit correctly concluded that "the Sharps may not point to the revision process to create an ambiguity." 115 F.3d at 1262; *see also Jimenez,* 968 F.Supp. at 333. Ironically, the federal courts have correctly applied Texas law, while this Court has not.

III

The Balandrans present two other arguments why exclusion h does not apply, which the Court does not address. These arguments are likewise without merit.

A

The Balandrans first point to the "ensuing loss" language of exclusion h. Exclusion h provides in full:

> We do not cover loss under Coverage A (Dwelling) caused by settling, cracking, bulging, shrinkage, or expansion of foundations, walls, floors, ceilings, roof structures, walks, drives, curbs, fences, retaining walls or swimming pools.
>
> *We do cover ensuing loss caused by collapse of building or any part of the building,* ****746*** *water damage or breakage of glass which is part of the building if the loss would otherwise be covered under this policy.*

App. A., para. 1(h) of Sec. I (exclusions) (emphasis added). The Balandrans argue that, under the italicized portion (the "ensuing loss" provision), exclusion 1(h) does not apply to loss from "water damage" if the loss is otherwise covered under the policy. Because their loss was caused by a plumbing leak, and would otherwise be covered under the "all risks" protection of Coverage A, the Balandrans argue that their loss falls under the ensuing loss provision.

This argument ignores the word "ensuing." We have held that this provision covers only loss *resulting from* the type of damage excluded under h. *See Lambros,* 530 S.W.2d at 141–42 ("Again, the plain language of the exception compels the conclusion that the water damage must be a consequence, i.e., follow from or be the result of the types of damage enumerated in exception [1(h)]."); *see also Park,* 443 S.W.2d at 942 (holding that accidental discharge of water from a plumbing system that resulted in structural damage was not covered and that loss did not result form "ensuing water damage"). In other words, if the shifting foundation were to cause a plumbing leak that further damaged the walls of the house, the further damage to the walls would be covered. As we held in *Lambros,* because the "water damage was the cause, rather than the consequence, of settling, etc., exclusion [h] is applicable." *Id.* In this

case, the plumbing leak was the cause of the foundation damage rather than a result of it. Therefore, the ensuing loss provision does not provide coverage.

B

The Balandrans, supported by amicus curiae Texas Department of Insurance (TDI), also argue that exclusion h does not exclude foundation damage unless the underlying cause of the damage—in this case a plumbing leak—is also an excluded peril. TDI offers hypotheticals of what might happen if the Court did not adopt this approach. For example, it posits that there would be no coverage if a tree falls on a house and cracks the roof, since exclusion h applies to "cracking ... of ... roof structures." Similarly, there would be no coverage if a car careens into a house and cracks a wall, since exclusion h applies to "cracking ... of ... walls."

This construction of the policy cannot be squared with our holding in *Lambros,* 530 S.W.2d at 140. In *Lambros,* the insured, by paying an additional premium, had an "underground water" exclusion omitted from his policy. The policy, however, still contained a foundation damage exclusion similar to that at issue here. When the insured subsequently suffered foundation damage from underground water, he argued that the foundation damage exclusion did not apply because underground water was a covered peril. This Court (by refusing the application for writ of error) rejected the insured's argument:

> Even after this plaintiff-oriented rewriting, it is clear that loss caused by settling, etc. is not covered. The cause of the settling is irrelevant, unless exclusion k [the foundation-damage exclusion] is also rewritten to limit it to settling, etc., not caused by underground water. We conclude that the deletion of the subsurface water exclusion did not eliminate exclusion k or limit it to settling not caused by underground water.

Id. Thus, exclusion h in the Balandrans' policy excludes loss from an expanding foundation, regardless of the underlying cause. TDI's hypotheticals are simply inapposite because exclusion h was never intended to cover the type of sudden structural damage resulting from a falling tree or an out-of-control car.

* * * * *

I would hold that the policy unambiguously excludes coverage for damage to a dwelling caused by an expanding foundation, even when the underlying cause is a plumbing leak.

APPENDIX A
SECTION I —PERILS INSURED AGAINST
COVERAGE A (DWELLING)

***747** We insure against all risks of physical loss to the property described in Section I Property Coverage, Coverage A (Dwelling) unless the loss is excluded in Section I Exclusions.

COVERAGE B (PERSONAL PROPERTY)

We insure against physical loss to the property described in Section I Property Coverage, Coverage B (Personal Property) caused by a peril listed below, unless the loss is excluded in

Section I Exclusions.

1. Fire and Lightning.

2. Sudden and Accidental Damage from Smoke.

3. Windstorm, Hurricane and Hail.

4. Explosion.

5. Aircraft and Vehicles.

6. Vandalism and Malicious Mischief.

7. Riot and Civil Commotion.

8. Collapse of Building or any part of the building.

9. Accidental Discharge, Leakage or Overflow of Water or Steam from within a plumbing, heating or air conditioning system or household appliance.

A loss resulting from this peril includes the cost of tearing out and replacing any part of the building necessary to repair or replace the system or appliance. But this does not include loss to the system or appliance from which the water or steam escaped.

Exclusions 1.a through 1.h under Section I Exclusions do not apply to loss caused by this peril.

10. Falling Objects.

This peril does not include loss to property contained in a building unless the roof or outside wall of the building is first damaged by the falling object.

11. Freezing of household appliances.

12. Theft, including attempted theft and loss of property from a known place when it is likely that the property has been stolen.

SECTION I—EXCLUSIONS

1. The following exclusions apply to loss to property described under Coverage A (Dwelling) or Coverage B (Personal Property), but they do not apply to an ensuing loss caused by fire, smoke or explosion.

a. We do not cover loss to electrical devices or wiring caused by electricity other than lightning.

b. We do not cover loss caused by smog or by smoke from industrial or agricultural operations.

c. We do not cover loss caused by windstorm, hurricane or hail to:

(1) cloth awnings, greenhouses and their contents, buildings or structures located wholly or partially over water and their contents.

(2) radio and television towers, outside satellite dishes, masts and antennas, including lead-in wiring, windchargers and windmills.

(3) personal property contained in a building unless direct force of wind or hail makes an opening in a roof or wall and rain, snow, sand or dust enters through this opening and causes the damage.

d. We do not cover loss of the following property by theft, including attempted theft and loss of property from a known place when it is likely that the property has been stolen.

(1) personal property while away from the **residence premises** at any other residence owned by, rented to or occupied by an **insured**, except while an **insured** is temporarily living there.

(2) building materials and supplies not on the **residence premises**.

e. We do not cover loss to machinery, appliances and mechanical devices caused by mechanical breakdown.

f. We do not cover loss caused by:

(1) inherent vice, wear and tear or deterioration.

(2) rust, rot, mold or other fungi.

***748** (3) dampness of atmosphere, extremes of temperature.

(4) contamination.

(5) vermin, termites, moths or other insects.

We do cover ensuing loss caused by collapse of building or any part of the building, water damage or breakage of glass which is part of the building if the loss would otherwise be covered under this policy.

g. We do not cover loss caused by animals or birds owned or kept by an **insured** or occupant of the **residence premises**.

We do cover ensuing loss caused by collapse of building or any part of the building, water damage or breakage of glass which is part of the building if the loss would otherwise be covered under this policy.

h. We do not cover loss under Coverage A (Dwelling) caused by settling, cracking, bulging, shrinkage, or expansion of foundations, walls, floors, ceilings, roof structures, walks, drives, curbs, fences, retaining walls or swimming pools.

We do cover ensuing loss caused by collapse of building or any part of the building, water damage or breakage of glass which is part of the building if the loss would otherwise be covered under this policy.

i. We do not cover loss caused by or resulting from flood, surface water, waves, tidal water or tidal waves, overflow of streams or other bodies of water or spray from any of these whether or not driven by wind.

We do cover an ensuing loss by theft or attempted theft or any act or attempted act of stealing.

j. We do not cover loss caused by or resulting from freezing while the building is unoccupied unless you have used reasonable care to:

(1) maintain heat in the building; or

(2) shut off the water supply and drain plumbing, heating and air conditioning systems of water.

k. We do not cover loss caused by earthquake, landslide or earth movement.

2. GOVERNMENTAL ACTION.

We do not cover loss caused by the destruction of property by order of governmental authority.

But we do cover loss caused by acts of destruction ordered by governmental authority taken at the time of a fire to prevent its spread, if the fire would be covered under this policy.

3. BUILDING LAWS.

We do not cover loss caused by or resulting from the enforcement of any ordinance or law regulating the construction, repair or demolition of a building or structure.

4. WAR DAMAGE.

We do not cover loss resulting directly or indirectly from war. This includes undeclared war, civil war, insurrection, rebellion, revolution, warlike act by military personnel, destruction or seizure or use for a military purpose, and any consequence of these. Discharge of a nuclear weapon will be deemed a warlike act even if accidental.

5. NUCLEAR DAMAGE.

We do not cover loss resulting directly or indirectly from nuclear reaction, radiation or radioactive contamination, all whether controlled or uncontrolled or however caused. We cover direct loss by fire resulting from nuclear reaction, radiation or radioactive contamination.

Tex.,1998.
Balandran v. Safeco Ins. Co. of America
972 S.W.2d 738, 41 Tex. Sup. Ct. J. 1153

END OF DOCUMENT

409 S.W.3d 181
(Cite as: 409 S.W.3d 181)

Court of Appeals of Texas,
Dallas.
BOB MONTGOMERY CHEVROLET, INC. d/b/a Bob Montgomery Collision, Appellant
v.
DENT ZONE COMPANIES, Appellee.

No. 05–13–00197–CV.
Aug. 5, 2013.

Background: Dent repairer sued Kentucky automobile dealership for breach of a contract for dealership to be a certified repair center in repairer's service program. Dealership filed a special appearance. After a hearing, the 95th Judicial District Court, Dallas County, Ken Molberg, J., 2013 WL 4771821, denied the special appearance. Dealership appealed.

Holdings: The Court of Appeals, Myers, J., held that:
(1) as a matter of apparent first impression, language in a signed application that referred to an Internet document that contained a forum-selection clause did not show that the parties intended the terms and conditions in the Internet document to be a part of the contract;
(2) parol evidence would not be considered when determining whether the Internet document was incorporated by reference;
(3) doctrine of ratification did not apply; and
(4) trial court's conclusions that was estopped, quasi-estopped, and equitably estopped from denying the applicability of the Internet document's terms and conditions were erroneous as a matter of law.

Reversed and rendered.

West Headnotes

[1] Courts 106 ⚿39

106 Courts
106I Nature, Extent, and Exercise of Jurisdiction in General
106I(A) In General
106k39 k. Determination of questions of jurisdiction in general. Most Cited Cases

Whether a trial court has personal jurisdiction over a nonresident defendant is a question of law.

[2] Appeal and Error 30 ⚿893(1)

30 Appeal and Error
30XVI Review
30XVI(F) Trial De Novo
30k892 Trial De Novo
30k893 Cases Triable in Appellate Court
30k893(1) k. In general. Most Cited Cases

Because a trial court's exercise of personal jurisdiction over a nonresident defendant is one of law, an appellate court reviews the trial court's determination of a special appearance de novo.

[3] Courts 106 ⚿32.5(2)

106 Courts
106I Nature, Extent, and Exercise of Jurisdiction in General
106I(A) In General
106k31 Jurisdiction to Be Shown by Record
106k32.5 Jurisdiction of the Person
106k32.5(2) k. Allegations, pleadings, and affidavits. Most Cited Cases

Courts 106 ⚿35

106 Courts
106I Nature, Extent, and Exercise of Jurisdiction in General
106I(A) In General
106k34 Presumptions and Burden of Proof as to Jurisdiction
106k35 k. In general. Most Cited Cases

A plaintiff bears the initial burden of pleading sufficient allegations to bring a nonresident defendant within the provisions of the Texas long-arm statute; the nonresident defendant then has the burden of negating all bases of jurisdiction alleged in the plaintiff's petition. V.T.C.A., Civil Practice & Remedies Code § 17.042.

[4] Courts 106 ⚿13.2

106 Courts
106I Nature, Extent, and Exercise of Jurisdiction in General
106I(A) In General
106k13.1 Actions by or Against Nonresidents, Personal Jurisdiction In; “Long-Arm” Jurisdiction
106k13.2 k. In general. Most Cited Cases

Broad language of the Texas long-arm statute extends Texas courts' personal jurisdiction over a nonresident defendant as far as the federal constitutional requirements of due process will permit. U.S.C.A. Const.Amend. 14; V.T.C.A., Civil Practice & Remedies Code § 17.042.

[5] Constitutional Law 92 ⚿3964

92 Constitutional Law
92XXVII Due Process
92XXVII(E) Civil Actions and Proceedings
92k3961 Jurisdiction and Venue
92k3964 k. Non-residents in general. Most Cited Cases

Due Process Clause operates to limit the power of a state to assert personal jurisdiction over a nonresident defendant. U.S.C.A. Const.Amend. 14.

[6] Constitutional Law 92 ⚿3964

92 Constitutional Law
92XXVII Due Process
92XXVII(E) Civil Actions and Proceedings
92k3961 Jurisdiction and Venue
92k3964 k. Non-residents in general. Most Cited Cases

Due Process Clause protects an individual's liberty interest in not being subject to the binding judgments of a forum with which he has established no meaningful contacts, ties, or relations. U.S.C.A. Const.Amend. 14.

[7] Constitutional Law 92 ⚿3964

92 Constitutional Law
92XXVII Due Process
92XXVII(E) Civil Actions and Proceedings
92k3961 Jurisdiction and Venue
92k3964 k. Non-residents in general. Most Cited Cases

Under the Due Process Clause, personal jurisdiction over a nonresident defendant is constitutional when the nonresident defendant has established minimum contacts with the forum state and the exercise of jurisdiction comports with traditional notions of fair play and substantial justice; personal jurisdiction is a waivable right, however, and a party may agree to a forum's jurisdiction. U.S.C.A. Const.Amend. 14.

[8] Contracts 95 ⚿206

95 Contracts
95II Construction and Operation
95II(C) Subject-Matter
95k206 k. Legal remedies and proceedings. Most Cited Cases

Courts 106 ⚿23

106 Courts
106I Nature, Extent, and Exercise of Jurisdiction in General
106I(A) In General
106k22 Consent of Parties as to Jurisdiction
106k23 k. In general. Most Cited Cases

Language in application signed by automobile dealership for dealership to be a certified repair center in dent repairer's service program, referring to an Internet document that contained a forum-selection clause, did not show that parties intended for the terms and conditions in the Internet document to be part of agreement, supporting conclusion that dealership, which was in Kentucky, did not consent to the jurisdiction of Texas courts; the language, which stated that additional benefits, qualifications, and details of the service program were available for dealership's review at a certain

website address, indicated that the Internet document contained only informative material. V.T.C.A., Civil Practice & Remedies Code § 17.042.

[9] Appeal and Error 30 ⚿185(1)

30 Appeal and Error
30V Presentation and Reservation in Lower Court of Grounds of Review
30V(B) Objections and Motions, and Rulings Thereon
30k185 Organization and Jurisdiction of Lower Court
30k185(1) k. In general. Most Cited Cases

Appeal and Error 30 ⚿1079

30 Appeal and Error
30XVI Review
30XVI(K) Error Waived in Appellate Court
30k1079 k. Insufficient discussion of objections. Most Cited Cases

Automobile dealership waived its argument for application of Kentucky law, not Texas law, to a determination of whether an Internet document with a forum-selection clause was incorporated by reference into a contract with a dent repairer, for the purpose of determining whether Texas courts had personal jurisdiction over dealership, where dealership, in trial court, did not assert Kentucky law as the appropriate choice of law, did not object to repairer's arguments applying Texas law to the incorporation-by-reference issue, and cited only Texas law on the issue.

[10] Contracts 95 ⚿147(2)

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k147 Intention of Parties
95k147(2) k. Language of contract. Most Cited Cases

When construing a contract, a court's primary goal is to determine the parties' intent as expressed in the terms of the contract.

[11] Contracts 95 ⚿166

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k166 k. Matters annexed or referred to as part of contract. Most Cited Cases

An unsigned document may be incorporated into a contract by referring in the signed document to the unsigned document; the language used to refer to the unsigned document is not important as long as the signed document plainly refers to the unsigned document.

[12] Contracts 95 ⚿166

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k166 k. Matters annexed or referred to as part of contract. Most Cited Cases

When a document is incorporated into another by reference, both instruments must be read and construed together.

[13] Contracts 95 ⚿166

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k166 k. Matters annexed or referred to as part of contract. Most Cited Cases

Plainly referring to a document in a signed document requires more than merely mentioning the document; the language of the signed document must show that the parties intended for the other document to become part of the agreement.

[14] Contracts 95 ⚿166

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k166 k. Matters annexed or referred to as part of contract. Most Cited Cases

Language in an original document that refers to another document must demonstrate that the parties intended to incorporate all or part of the referenced document.

[15] Evidence 157 ⚿450(5)

157 Evidence
157XI Parol or Extrinsic Evidence Affecting Writings
157XI(D) Construction or Application of Language of Written Instrument
157k449 Nature of Ambiguity or Uncertainty in Instrument
157k450 In General
157k450(5) k. Contracts in general. Most Cited Cases

Appellate court would not consider parol evidence when determining whether an Internet document with a forum-selection clause was incorporated by reference in a signed application for automobile dealership to be a certified repair center in dent repairer's service program; the language in the application that referred to the Internet document did not show any intent by the parties for the Internet document to be a part of their written contract, such that there was no ambiguity as to the parties' intent.

[16] Contracts 95 ⚿147(2)

95 Contracts

95II Construction and Operation
95II(A) General Rules of Construction
95k147 Intention of Parties
95k147(2) k. Language of contract. Most Cited Cases

Evidence 157 ⚿448

157 Evidence
157XI Parol or Extrinsic Evidence Affecting Writings
157XI(D) Construction or Application of Language of Written Instrument
157k448 k. Grounds for admission of extrinsic evidence. Most Cited Cases

When a written contract is unambiguous, a court determine the parties' intent from the terms of the contract, not from parol evidence.

[17] Contracts 95 ⚿97(1)

95 Contracts
95I Requisites and Validity
95I(E) Validity of Assent
95k97 Estoppel and Ratification
95k97(1) k. In general. Most Cited Cases

Contracts 95 ⚿206

95 Contracts
95II Construction and Operation
95II(C) Subject-Matter
95k206 k. Legal remedies and proceedings. Most Cited Cases

Doctrine of ratification did not apply on automobile dealership's appeal from a denial of its special appearance in dent repairer's action against it for breach of contract; the issue was whether an Internet document with a forum-selection clause was incorporated by reference in a signed application for dealership to be a certified repair center in repairer's service program, which in turn went to whether dealership, which was in Kentucky, consented to the jurisdiction of Texas courts, and dealership did not dispute on appeal that the parties had a legally binding contract or argue that any contract was voidable.

[18] Estoppel 156 ⚿90(1)

156 Estoppel
156III Equitable Estoppel
156III(B) Grounds of Estoppel
156k89 Acquiescence
156k90 Assent to or Ratification of Acts of Others in General
156k90(1) k. In general. Most Cited Cases

“Ratification” is the adoption or confirmation, by one with knowledge of all material facts, of a

prior act that did not then legally bind that person and which that person had a right to repudiate.

[19] Contracts 95 ⚿97(2)

95 Contracts
95I Requisites and Validity
95I(E) Validity of Assent
95k97 Estoppel and Ratification
95k97(2) k. What constitutes ratification. Most Cited Cases

Ratification of a contract occurs when a party recognizes the validity of a contract by acting under, performing under it, or affirmatively acknowledging it.

[20] Contracts 95 ⚿97(2)

95 Contracts
95I Requisites and Validity
95I(E) Validity of Assent
95k97 Estoppel and Ratification
95k97(2) k. What constitutes ratification. Most Cited Cases

A party ratifies a contract by conduct recognizing the contract as valid with knowledge of all relevant facts.

[21] Contracts 95 ⚿97(2)

95 Contracts
95I Requisites and Validity
95I(E) Validity of Assent
95k97 Estoppel and Ratification
95k97(2) k. What constitutes ratification. Most Cited Cases

Any act inconsistent with an intent to avoid a contract has the effect of ratifying the contract.

[22] Contracts 95 ⚿100

95 Contracts
95I Requisites and Validity
95I(E) Validity of Assent
95k100 k. Questions for jury. Most Cited Cases

Whether a party has ratified a contract may be determined as a matter of law if the evidence is not controverted or is incontrovertible.

[23] Estoppel 156 ⚿121

156 Estoppel
156III Equitable Estoppel

156III(G) Trial
156k121 k. Verdict, findings, and judgment. Most Cited Cases

Conclusions of trial court that automobile dealership was estopped, quasi-estopped, and equitably estopped from denying the applicability of the terms and conditions of an Internet document to a contract between dealership and dent repairer for dealership to be a certified repair center for repairer's service program were erroneous as a matter of law; the factual findings supporting the conclusions were not supported by any evidence.

***184** Alexander N. Beard, Saunders, Walsh & Beard, McKinney, for Appellant.

Gino J. Rossini, Hernes Sargent Bates, LLP, Thomas C. Clark, Dealy, Zimmermann, Clark, Malout & Blend, P.C., Dallas, for Appellee.

Before Justices MOSELEY, FILLMORE, and MYERS.

OPINION

Opinion by Justice MYERS.

Bob Montgomery Chevrolet, Inc. d/b/a Bob Montgomery Collision appeals the trial court's denial of its special appearance in this suit brought by Dent Zone Companies. *See* TEX. CIV. PRAC. & REM.CODE ANN. § 51.014(a)(7) (West Supp.2012). Montgomery brings five issues asserting the trial court erred by denying its special appearance. The parties' arguments include whether a written contract incorporated by reference terms and conditions, including a forum-selection clause, listed on an internet web site. We conclude the forum-selection clause was not incorporated by reference and the trial court erred by denying Montgomery's special appearance. We render judgment dismissing the cause against Montgomery for want of personal jurisdiction.

BACKGROUND

Montgomery is an automobile dealership in Louisville, Kentucky. The company does not sell any cars in Texas, advertise or solicit in Texas, or otherwise overtly conduct business in Texas. The company has a "collision center" that repairs vehicles. Dent Zone is a company providing "paintless dent repair" service.

In April 2012, a hailstorm struck Louisville, damaging many vehicles in the area. Duane Geise, a representative of Dent Zone, approached Anthony Rich, the manager of Montgomery's collision center, about making Montgomery a certified repair center in Dent Zone's "PDR Linx Service Program." If Montgomery became a certified repair center, Dent Zone would send its technicians to Montgomery's premises to perform paintless dent repairs, Dent Zone and insurance companies would direct their customers with hail damage to Montgomery's location to have dent repair performed, and Montgomery would receive a percentage of the payments for dent repair. Geise showed Rich Dent Zone's one-page application to become a certified repair center for Dent Zone.[FN1] After some negotiating, Rich and Geise agreed on Montgomery receiving twenty-five percent of the payments for ***185** dent repair. The application also stated, "Additional benefits, qualifications and details of the PDR LINX Service Program are available for your review at our website: http: //www. linx manager. com/ pdf/ CRC Terms Conditions. pdf." The website consisted of a two-page document (the internet

document) listing terms and conditions for the PDR Linx Service Program agreement, including what Dent Zone asserted was a minimum six-month contractual term, a choice-of-law provision making Texas law applicable to the agreement, and a forum-selection clause stating that any suit between the parties would be heard in Dallas County, Texas.[FN2] Geise did not tell Rich about the forum-selection clause, and he told Rich only about the benefits of the program. Geise testified he told Rich that "the terms and conditions and additional information" about the program were listed at the internet link in the middle of the page, and he told Rich to go to the website and look at them. Rich told Geise he needed to take the information to Steven Montgomery, the dealership's general manager, and discuss it with him, and he told Geise to come back the next day. When Geise returned, Rich told him "Mr. Montgomery and the powers that be" had approved the contract, and Rich signed the application.

FN1. The one-page application, as relevant to this opinion, provided:

> We are pleased that you are joining our team of Certified Repair Centers. "We" and "Our" will refer to PDR LINX (**PDR LINX**SM) and "You" will refer to you, the Certified Repair Center.
>
> **PDR LINX SERVICE PROGRAM**
>
> We have developed a network of Certified Technicians who perform paintless dent repair ("PDR") in accordance with Our standards. If there is a hail event in your area, Our Certified Technicians will perform PDR services at our Certified Repair Centers, including all of Your customers, all referrals to You from insurance Companies, and any vehicles directed to Your location by Us. Additional benefits, qualifications and details of the PDR LINX Service Program are available for your review at our website: http:// www. linx manager. com/ pdf/ CRC Terms Conditions. pdf
>
> **YOUR COMMISSION WILL BE 25% OF GROSS PDR SERVICES AND R & I SERVICES FOR EACH INVOICE GENERATED BY THE CRC.**
>
> We provide a Lifetime Limited Warranty for all PDR services. You will be an independent contractor working within the PDR LINX Service Program. You are free to perform non-PDR repairs. Most importantly, You will enjoy the benefits of Our network of nationally recognized companies who use and trust the **PDR LINX**SM name.
>
> You will become a "Certified Repair Center" as detailed in our PDR LINX Service Program after your signed application is accepted by us. Start enjoying the benefits of PDR LINX today!
>
> Prior to acceptance as a CRC, PDR LINX may check your credit.

APPLICANT:	ACCEPTED:
By: /T.Rich/	By: /[illegible]/
Certified Repair Center Representative	PDR LINX (a division of Dent Zone Companies, Inc.)

FN2. The internet document included the following:

> **CERTIFIED REPAIR PROGRAM**
>
> **PDR LINX PROGRAM**
>
> We are pleased that you are considering our invitation to become part of our team of Certified Repair Centers ("CRC") under our PDR LINX program. To help you evaluate what will be expected of you, and what you can expect from us, we have put together this site to set forth, in detail the terms and conditions of the Program. By signing the application to become a CRC, you are agreeing to the terms and conditions of this Program as outlined herein, or as amended from time to time.
>
> ....
>
> ADDITIONAL TERMS AND CONDITIONS
>
> ....
>
> The term of this Agreement shall be six (6) months or for the length of the storm from the Effective Date, unless terminated with 30 days advance written notice provided by either party....
>
> This Agreement shall be construed under and in accordance with the laws of the State of Texas. You hereby submit to the jurisdiction of the courts of the State of Texas which shall be the sole and exclusive jurisdiction for any legal dispute between us. Venue for any legal dispute shall be in Dallas County in the State of Texas, and both parties waive their right to a jury trial. This Agreement constitutes the final and complete agreement of the parties. The Agent of Record is 'independent' and has NO authority to modify, change or add to this Agreement or Our obligations or make any representations on Our behalf without prior written Corporate Approval. Aside from this Agreement, there exists no other agreement or understandings, whether orally, or in writing between the parties relating to the legal relationship set forth herein.
>
> The internet document also included a limited warranty, indemnity, and details regarding division of collected funds.

Dent Zone's technicians came to Montgomery's location, and Montgomery provided space for them to perform the paintless dent repairs. For a few weeks, the parties operated amicably: automobile insurers directed their customers with hail damage to Montgomery for dent repair, ***186** they paid Montgomery for the repairs, and Montgomery remitted three-fourths of the payments to Dent Zone and kept one-fourth, over $30,000, for itself. After a few weeks, problems arose, and Rich told Geise that Montgomery was canceling the contract with Dent Zone. Geise told Rich that the terms and conditions for the contract listed on the website included a minimum six-month term, but Rich required Dent Zone to leave Montgomery's premises. Geise asked if Dent Zone could continue its work through the weekend to finish the cars whose dent repairs were not completed, and Rich agreed. At the end of the weekend, Dent Zone left the premises. Geise testified that Montgomery never sent Dent Zone its share of the funds Montgomery collected for Dent Zone's work over that weekend.

Dent Zone brought suit against Montgomery in Dallas for breach of contract, alleging Montgomery "has consented to suit in Texas by the terms of the contract." Montgomery filed a special appearance. At the hearing on the special appearance, the evidence presented was Geise's testimony in court, the affidavits of Anthony Rich and Steven Montgomery, and various documents including the application, a printout of the internet document, checks from Montgomery to Dent Zone, and invoices and other records. The trial court denied the special appearance and made findings of fact and conclusions of law in support of its decision.

SPECIAL APPEARANCE

In its first four issues, Montgomery contends (1) the trial court erred by denying Montgomery's special appearance, (2) Montgomery sustained its burden of negating all bases of jurisdiction pleaded by Dent Zone, (3) the trial court erred by concluding Montgomery waived and consented to jurisdiction, and (4) there was legally and factually insufficient evidence to support the trial court's findings of fact and conclusions of law that Montgomery had knowledge of and agreed to the forum-selection clause in the internet document.

Standard of Review

[1][2] Whether a trial court has personal jurisdiction over a nonresident defendant is a question of law. *Michiana Easy Livin' Country, Inc. v. Holten,* 168 S.W.3d 777, 790–91 (Tex.2005); *BMC Software Belgium, N.V. v. Marchand,* 83 S.W.3d 789, 794 (Tex.2002). Because the trial court's exercise of personal jurisdiction over a nonresident defendant is one of law, an appellate court reviews the trial court's determination of a special appearance de novo. *Moki Mac River Expeditions v. Drugg,* 221 S.W.3d 569, 574 (Tex.2007); *BMC Software,* 83 S.W.3d at 794. However, the trial court must frequently resolve fact questions before deciding the jurisdictional question. *BMC Software,* 83 S.W.3d at 794; *Capital Tech. Info. Servs., Inc. v. Arias & Arias, Consultores,* 270 S.W.3d 741, 748 (Tex.App.-Dallas 2008, pet. denied) (en banc).

[3] The plaintiff bears the initial burden of pleading sufficient allegations to bring a nonresident defendant within the provisions of the Texas long-arm statute. *Moki Mac,* 221 S.W.3d at 574; *BMC Software,* 83 S.W.3d at 793. The nonresident defendant then has the burden of negating all bases of jurisdiction alleged in the plaintiff's petition. *Moki Mac,* 221 S.W.3d at 574; *BMC Software,* 83 S.W.3d at 793.

Findings of Fact and Conclusions of Law

A trial court's findings of fact in a nonjury trial carry the same force and dignity as a jury's verdict on jury questions. *Anderson v. City of Seven Points,* 806 S.W.2d 791, 794 (Tex.1991); *Kahn v. Imperial****187*** *Airport, L.P.,* 308 S.W.3d 432, 436–37 (Tex.App.-Dallas 2010, no pet.). When we review a trial court's findings of fact for legal and factual sufficiency, we use the same standards of review we use when determining if sufficient evidence exists to support a jury's answers. *Catalina v. Blasdel,* 881 S.W.2d 295, 297 (Tex.1994); *Thornton v. Dobbs,* 355 S.W.3d 312, 315 (Tex.App.-Dallas 2011, no pet.). When a trial court enters findings of fact and conclusions of law, we "indulge every reasonable presumption in favor of the findings and judgment of the trial court, and no presumption will be indulged against the validity of the judgment." *Vickery v. Comm'n for Lawyer Discipline,* 5 S.W.3d 241, 252 (Tex.App.-Houston [14th Dist.] 1999, pet. denied). In a bench trial, the trial court judges the credibility of the witnesses, determines the weight of testimony, and resolves conflicts and inconsistencies in the testimony. *See Sw. Bell Media, Inc. v. Lyles,* 825 S.W.2d 488, 493

(Tex.App.-Houston [1st Dist.] 1992, writ denied). As long as the evidence falls "within the zone of reasonable disagreement," we will not substitute our judgment for that of the fact-finder. *See City of Keller v. Wilson,* 168 S.W.3d 802, 822 (Tex.2005).

In a legal sufficiency review, we view the evidence in the light most favorable to the fact-finding, credit favorable evidence if a reasonable fact-finder could do so, and disregard contrary evidence unless a reasonable fact-finder could not. *See id.* at 827. "[F]indings of fact bind an appellate court only if the findings are supported by evidence of probative force." *Thomas v. Casale,* 924 S.W.2d 433, 437 (Tex.App.-Fort Worth 1996, writ denied). Unchallenged findings of fact are binding on the appellate court "unless the contrary is established as a matter of law, or if there is no evidence to support the finding." *Id.* (quoting *McGalliard v. Kuhlmann,* 722 S.W.2d 694, 696 (Tex.1986)). Anything more than a scintilla of evidence is legally sufficient to support the finding. *Formosa Plastics Corp. USA v. Presidio Eng'rs & Contractors, Inc.,* 960 S.W.2d 41, 48 (Tex.1998). In a factual sufficiency review, we view all the evidence in a neutral light and set aside the finding only if the finding is so contrary to the overwhelming weight of the evidence such that the finding is clearly wrong and unjust. *Cain v. Bain,* 709 S.W.2d 175, 176 (Tex.1986) (per curiam); *Morris v. Wells Fargo Bank, N.A.,* 334 S.W.3d 838, 842 (Tex.App.-Dallas 2011, no pet.).

We review de novo a trial court's conclusions of law. *See BMC Software Belg., N.V. v. Marchand,* 83 S.W.3d 789, 794 (Tex.2002). A conclusion of law is erroneous as a matter of law if the factual findings supporting the conclusion are not supported by any evidence. *Wright Group Architects–Planners, P.L.L.C. v. Pierce,* 343 S.W.3d 196, 205 (Tex.App.-Dallas 2011, no pet.). If we determine that the trial court made an erroneous conclusion of law, we will not reverse if the trial court rendered the proper judgment. *See BMC Software,* 83 S.W.3d at 794. We uphold conclusions of law if the judgment can be sustained on any legal theory supported by the evidence. *Adams v. H & H Meat Prods., Inc.,* 41 S.W.3d 762, 769 (Tex.App.-Corpus Christi 2001, no pet.).

Personal Jurisdiction

[4] The Texas long-arm statute permits Texas courts to exercise jurisdiction over nonresident defendants that do business in Texas. *See* TEX. CIV. PRAC. & REM.CODE ANN. §§ 17.041–045 (Vernon 2008); *PHC–Minden, L.P. v. Kimberly–Clark Corp.,* 235 S.W.3d 163, 166 (Tex.2007); *BMC Software,* 83 S.W.3d at 795. Under the statute, a nonresident does business in Texas if he: (1) contracts by mail or otherwise***188** with a Texas resident and either party is to perform the contract in whole or in part in this state; (2) commits a tort in whole or in part in this state; or (3) recruits Texas residents, directly or through an intermediary located in this state, for employment inside or outside this state. TEX. CIV. PRAC. & REM.CODE ANN. § 17.042. The broad language of section 17.042 extends Texas courts' personal jurisdiction "as far as the federal constitutional requirements of due process will permit." *PHC–Minden,* 235 S.W.3d at 166 (quoting *U–Anchor Adver., Inc. v. Burt,* 553 S.W.2d 760, 762 (Tex.1977)).

[5][6][7] The Due Process Clause of the Fourteenth Amendment operates to limit the power of a state to assert personal jurisdiction over a nonresident defendant. *Asahi Metal Indus. Co., Ltd. v. Superior Court of Cal., Solano Cnty.,* 480 U.S. 102, 108, 107 S.Ct. 1026, 94 L.Ed.2d 92 (1987); *Helicopteros Nacionales de Colom., S.A. v. Hall,* 466 U.S. 408, 413–14, 104 S.Ct. 1868, 80 L.Ed.2d 404 (1984). The Due Process Clause protects an individual's liberty interest in not being subject to the binding judgments of a forum with which he has established no meaningful contacts, ties, or

relations. *Burger King Corp. v. Rudzewicz,* 471 U.S. 462, 471–72, 105 S.Ct. 2174, 85 L.Ed.2d 528 (1985); *World–Wide Volkswagen Corp. v. Woodson,* 444 U.S. 286, 294, 100 S.Ct. 559, 62 L.Ed.2d 490 (1980); *Int'l Shoe Co. v. Washington,* 326 U.S. 310, 319, 66 S.Ct. 154, 90 L.Ed. 95 (1945). Under the Due Process Clause, personal jurisdiction over a nonresident defendant is constitutional when the nonresident defendant has established minimum contacts with the forum state and the exercise of jurisdiction comports with traditional notions of fair play and substantial justice. *Burger King,* 471 U.S. at 476, 105 S.Ct. 2174; *Int'l Shoe,* 326 U.S. at 320, 66 S.Ct. 154. However, personal jurisdiction is a waivable right, and a party may agree to a forum's jurisdiction. *Burger King,* 471 U.S. at 472 n. 14, 105 S.Ct. 2174.

In this case, the only basis for personal jurisdiction Dent Zone alleged was that Montgomery "has consented to jurisdiction in Texas by the terms of the contract."

Consent to Jurisdiction

Montgomery contends the trial court erred by concluding Montgomery consented to jurisdiction through the forum-selection clause in the internet document. Montgomery asserts the forum-selection clause was not incorporated by reference into the parties' contract, and that the court erred by concluding Montgomery had knowledge of and agreed to the clause.

Incorporation by Reference

[8][9] Dent Zone alleged Montgomery consented to the jurisdiction of the Texas courts by agreeing in the internet document "to submit to the jurisdiction of the courts of the State of Texas which shall be the sole and exclusive jurisdiction for any legal dispute between us." Montgomery asserts the internet document was not part of the contract; [FN3] Dent Zone contends the ***189** internet document was incorporated by reference into the contract.

> FN3. Montgomery argues we should apply Kentucky law to the determination of whether the internet document with the forum-selection clause was incorporated by reference into the contract. In the trial court, Montgomery did not assert Kentucky as the appropriate choice of law, did not object to Dent Zone's arguments applying Texas law to the incorporation-by-reference issue, and Montgomery cited only Texas law on the issue. By failing to urge application of Kentucky law in the trial court and by failing to object to Dent Zone's argument applying Texas law, Montgomery waived its choice-of-law argument. *See Gen. Chem. Corp. v. De La Lastra,* 852 S.W.2d 916, 920 (Tex.1993); *Daimler–Chrysler Motors Co., LLC v. Manuel,* 362 S.W.3d 160, 196–97 (Tex.App.-Fort Worth 2012, no pet.). Accordingly, we apply Texas law to the determination of whether the internet document was incorporated by reference.

[10][11][12] When construing a contract, our primary goal is to determine the parties' intent as expressed in the terms of the contract. *Chrysler Ins. Co. v. Greenspoint Dodge of Hous., Inc.,* 297 S.W.3d 248, 252 (Tex.2009); *Coker v. Coker,* 650 S.W.2d 391, 393 (Tex.1983). Unsigned documents may be incorporated into the parties' contract by referring in the signed document to the unsigned document. *Owen v. Hendricks,* 433 S.W.2d 164, 167 (Tex.1968). The language used to refer to the incorporated document is not important as long as the signed document "plainly refers" to the incorporated document. *Id.; In re C & H News Co.,* 133 S.W.3d 642, 645 (Tex.App.-Corpus Christi 2003, orig. proceeding). Documents incorporated into a contract by reference become part of that

contract. *In re 24R, Inc.,* 324 S.W.3d 564, 567 (Tex.2010) (orig. proceeding) (per curiam). When a document is incorporated into another by reference, both instruments must be read and construed together. *In re C & H News Co.,* 133 S.W.3d at 645–46.

[13] Plainly referring to a document requires more than merely mentioning the document. *See Trico Marine Servs., Inc. v. Stewart & Stevenson Technical Servs., Inc.,* 73 S.W.3d 545, 549–50 (Tex.App.-Houston [1st Dist.] 2002, mandamus denied). The language in the signed document must show the parties intended for the other document to become part of the agreement. *See One Beacon Ins. Co. v. Crowley Marine Servs., Inc.,* 648 F.3d 258, 267 (5th Cir.2011) (citing 11 SAMUEL WILLISTON & RICHARD A. LORD, A TREATISE ON THE LAW OF CONTRACTS § 30:25, at 234 (4th ed. 1999) ("in order to uphold the validity of terms incorporated by reference, it must be clear that the parties to the agreement had knowledge of and assented to the incorporated terms")); 17A C.J.S. *Contracts* § 402 (2011) ("For an incorporation by reference to be effective, it must be clear that the parties to the agreement had knowledge of and assented to the incorporated terms.").

[14] No Texas case has expressly held that the complete incorporation by reference of another document requires the original document show the parties intended for the referenced document to become part of the contract. However, the requirement for such a showing is supported by the general principle of contract law that reference to a document for a particular purpose incorporates that document only for the specified purpose. *See, e.g.,* 17A C.J.S. *Contracts* § 402 (2011). In *Valero Marketing & Supply Co. v. Baldwin Contracting Co.,* No. H–09–2957, 2010 WL 1068105 (S.D.Tex. Mar. 19, 2010), the issue was whether a forum-selection clause was incorporated by reference. In that case, the defendant purchased asphalt from the plaintiff, and the parties' signed contract stated, "All prices quoted above are subject to Valero's General Terms and Conditions for Petroleum Product Purchases/Sales." *Id.* at *1, 3. The General Terms and Conditions included a forum-selection clause. *Id.* at *3. The district court concluded the incorporation of the General Terms and Conditions did not extend to the forum-selection clause because it was not relevant to the quotation of prices, *see id.* at *5, and the incorporating language did not "suggest that Defendant is bound by all of the General Terms and Conditions." *Id.* (emphasis omitted); *see* ****190*** *also LeBlanc, Inc. v. Gulf Bitulithic Co.,* 412 S.W.2d 86, 93 (Tex.Civ.App.-Tyler 1967, writ ref'd n.r.e.) (general contract stated subcontract incorporated terms of general contract "only insofar as they are applicable to this Sub–Contractor," which showed parties did not intend for subcontract to incorporate by reference all the terms of the general contract). In other words, the referring language in the original document must demonstrate the parties intended to incorporate all or part of the referenced document.

In this case, the signed application stated Montgomery would "become a 'Certified Repair Center' as detailed in our PDR LINX Service Program," and would "be an independent contractor working within the PDR LINX Service Program." The application also stated, "Additional benefits, qualifications and details of the PDR LINX Service Program are available for your review at our website: http:// www. linx manager. com/ pdf/ CRC Terms Conditions. pdf." The question is whether this last-quoted sentence incorporated the internet document by reference.

The language, "Additional benefits, qualifications and details of the PDR LINX Service program are available for your review at our website: http:// www. linx manager. com/ pdf/ CRC Terms Conditions. pdf" does not state the internet document is incorporated by reference into the parties' agreement, does not plainly refer to additional terms and conditions in the internet document as

becoming part of the parties' agreement, and does not otherwise suggest that the parties intended for the internet document to become part of their agreement. Instead, this language indicates that the internet document contained informative material only, not binding terms and conditions intended to be part of the parties' contract.

None of the cases Dent Zone cites involved the type of language in this case. Instead, in all the cases except one where the courts found incorporation by reference, the referring language made clear that the parties intended for the outside material to become part of the contract.[FN4]

> FN4. The exception was *Westland Oil Development Corp. v. Gulf Oil Corp.*, 637 S.W.2d 903, 908 (Tex.1982), which concerned notice of documents referred to in the chain of title, and it is not relevant under the facts of this case.

In *In re International Profit Associates, Inc.*, 286 S.W.3d 921 (Tex.2009) (orig. proceeding) (per curiam), the forum-selection clause the defendant sought to enforce was contained on the first page of the parties' agreement, which was missing from the copy the plaintiff signed. *Id.* at 923. The court held the plaintiff should have realized a page of the contract was missing because he signed pages stating "2 of 4," "3 of 4," and "4 of 4" and a clause on one of the pages he signed stated, "This document, *4 pages in total*, constitutes the entire agreement for services ...." *Id.* This language clearly indicated there was a page "1 of 4" missing from the plaintiff's copy of the contract that was intended to be part of the contract.

In *In re Boulder Crossroads, LLC*, 2012 WL 1066482 (Bankr.W.D.Tex. Mar. 28, 2012), the parties' first agreement had attached to it a document titled, "April 2001 Terms and Conditions," which contained a limitation-of-liability provision. *Id.* at *1. The second agreement may not have had the "April 2001 Terms and Conditions" attached, but the last paragraph of the second agreement stated, "Terms and Conditions dated April 2001 (see attached) are hereby incorporated into and made part of this Work Authorization." *Id.* at *2. The court concluded that the "April 2001 Terms and Conditions" were incorporated***191** by reference into the second agreement. *Id.* at *8. The incorporating language in that case made clear that the "April 2001 Terms and Conditions" were intended to become part of the second agreement.

Owen v. Hendricks, 433 S.W.2d 164 (Tex.1968), involved two letters that did not refer to each other but involved the same transaction. *Id.* at 165–67. The Texas Supreme Court concluded that the letters did not incorporate one another by reference. *Id.* at 167. The court stated, "It is uniformly held that an unsigned paper may be incorporated by reference in the paper signed by the person sought to be charged. The language used is not important provided the document signed by the defendant plainly refers to another writing." *Id.* at 166. Because the documents did not reference each other, the court did not have before it whether the signed contract must show the parties intended for the referenced document to become part of the contract.

In re Prudential Insurance Co. of America, 148 S.W.3d 124 (Tex.2004) (orig. proceeding), involved incorporation of terms in a lease into a signed personal guaranty of the lease. The lease, which was between a corporate landlord and limited-partnership tenant, stated that in the event of litigation, the parties to the lease waived their right to a jury trial. *Id.* at 127–28. The principals of the tenant's limited partner also signed a personal guaranty stating they promised "to 'faithfully perform

and fulfill all of [the] terms, covenants, conditions, provisions, and agreements' of the lease in the event of the partnership's default." *Id.* at 135. The supreme court concluded this language incorporated the terms of the lease, including the jury waiver, into the guaranty agreement because the guaranty plainly referred to the lease's terms and because "documents executed at the same time, with the same purpose, and as part of the same transaction, are construed together." *Id.* The language in the guaranty incorporating by reference the terms of the lease made clear that the parties intended for all the agreements in the lease to become binding on the guarantors when the partnership defaulted.

In *Gray & Co. Realtors, Inc. v. Atlantic Housing Foundation, Inc.*, 228 S.W.3d 431 (Tex.App.-Dallas 2007, no pet.), a seller and purchaser of real estate entered into a real estate contract. *Id.* at 432. In a separate written agreement, the purchaser promised to pay a commission to a broker if the transaction was closed or consummated. *Id.* at 432–33. Nominal title was passed to the purchaser for tax purposes, but the purchaser never paid the purchase price, and it later returned the title to the seller. *Id.* at 433. The broker sued for its commission, and one of the issues was whether the terms of the real estate contract were incorporated by reference into the broker's representation agreement. *Id.* This Court concluded the real estate contract was incorporated by reference because it was mentioned six times in the representation agreement and because the representation agreement had no purpose without the real estate contract. *Id.* at 436. Thus, the parties did not merely mention the real estate contract but intended for its terms to be included in the representation agreement.

Castroville Airport, Inc. v. City of Castroville, 974 S.W.2d 207 (Tex.App.-San Antonio 1998, no pet.), involved a dispute over a city's lease of an airport. The parties entered into a settlement memorandum, and the city drafted a new lease. *Id.* at 209. The lessee rejected the new lease, and the city sued the lessee for breach of the settlement memorandum and the original lease. *Id.* The lessee argued the settlement***192** memorandum was not sufficiently definite to be enforceable. *Id.* at 211. The court of appeals set forth the required elements for an enforceable lease and observed that these terms were contained in Exhibit A and Exhibit B of the settlement memorandum. *Id.* at 212. The lessee asserted that the exhibits were not attached to the settlement memorandum, but the court of appeals concluded they were incorporated by reference. The court stated,

> Contracting parties are obligated to protect themselves by reading what they sign and are presumed, as a matter of law, to know the contract's terms.
>
> The Settlement Memorandum plainly referred to the description of the leased premises on the attached Exhibit A and the sample FBO lease agreement as Exhibit B. Under the doctrine of incorporation by reference, the property description and the sample FBO lease became a part of the Settlement Memorandum. Therefore, [lessee and its guarantor] were obligated to protect themselves by reading the exhibits and are presumed to know their terms.

Id. at 211–12 (citations omitted). The court then set forth the requirements for an enforceable lease and stated, "The Settlement Memorandum contains each of these terms." *Id.* at 212. Although the court did not quote the language referring to the exhibits, the court's description of the language shows the parties intended for the exhibits to become part of their contract.

Dent Zone also cited *Westland Oil Development Corp. v. Gulf Oil Corp.*, 637 S.W.2d 903

(Tex.1982). Dent Zone quotes the opinion in its brief as stating, " 'any description, recital of fact, or reference to other documents puts the purchaser upon inquiry, and he is bound to follow up this inquiry, step by step, from one discovery to another and from one instrument to another,' until he obtains 'complete knowledge' of all of the matters referred to." (Quoting *Westland,* 637 S.W.2d at 908.) That case involved title to oil and gas leases and whether one party was put on notice of another party's equitable title from a reference to a letter agreement contained in an operating agreement that was part of the party's chain of title. The supreme court stated that in matters of chain of title, "[i]t is well settled that 'a purchaser is bound by *every* recital, reference and reservation contained in or fairly disclosed by any instrument which forms an essential link in the chain of title under which he claims.' " *Id.* at 908 (quoting *Wessels v. Rio Bravo Oil Co.,* 250 S.W.2d 668, 670 (Tex.Civ.App.-Eastland 1952, writ ref'd)). The court then set forth the language quoted by Dent Zone.[FN5] The court concluded that because the party had the duty to investigate the operating agreement, it was charged with notice of the contents of the operating agreement. *Id.* And, because the operating agreement made a clear reference to the letter agreement, the party had the duty to inspect that document. *Id.* This level of notice and incorporation goes beyond that of incorporation by reference in contracts. Because this case does not involve documents ***193** in a chain of title to real estate, *Westland Oil* is not relevant.

FN5. The court stated,

> The rationale of the rule is that *any* description, recital of fact, or reference to other documents puts the purchaser upon inquiry, and he is bound to follow up this inquiry, step by step, from one discovery to another and from one instrument to another, until the whole series of title deeds is exhausted and a complete knowledge of *all the matters referred* to and affecting the estate is obtained.
>
> *Westland Oil,* 637 S.W.2d at 908 (quoting *Loomis v. Cobb,* 159 S.W. 305, 307 (Tex.Civ.App.-El Paso 1913, writ ref'd)).

The parties cite one case involving incorporation by reference of terms and conditions found on an internet site, *One Beacon Insurance Co. v. Crowley Marine Services, Inc.,* 648 F.3d 258 (5th Cir.2011).[FN6] *One Beacon* involved maritime law, not Texas law, but purported to apply general contract principles. *Id.* at 267. In that case, a contractor was repairing a barge owned by Crowley Marine Services when one of the contractor's employees was injured. *Id.* at 261. The employee sued Crowley and the contractor. *Id.* Crowley sought indemnity from the contractor and its insurance company based on the terms and conditions incorporated by reference into Crowley's repair service order that were listed on a website. The referring language in that case stated, in all capital letters, "THIS RSO [repair service order] IS ISSUED IN ACCORDANCE WITH THE PURCHASE ORDER TERMS & CONDITIONS ON WWW. CROWLEY. COM / DOCUMENTS & FORMS, UNLESS OTHERWISE AGREED TO IN WRITING." *Id.* at 263. This language made clear the parties' intent to incorporate the terms and conditions on the website into their agreement.

FN6. No Texas court appears to have addressed incorporation by reference into a contract of material at a website. However, as the Fifth Circuit stated,

> We see no reason to differ from these principles [of incorporation by reference] where, as

> here, the terms to be incorporated are contained on a party's website. We note that contracts formed in whole or in part over the internet present relatively new considerations for the courts, and will continue to challenge the courts as the internet plays an increasingly important role in commerce. However, "[w]hile new commerce on the Internet has exposed courts to many new situations, it has not fundamentally changed the principles of contract."
>
> *One Beacon,* 648 F.3d at 268 (quoting *Register.com, Inc. v. Verio, Inc.,* 356 F.3d 393, 403 (2nd Cir.2004)).

We conclude the referring language in this case, "Additional benefits, qualifications and details of the PDR LINX Service Program are available for your review at our website: http:// www. linx manager. com/ pdf/ CRC Terms Conditions. pdf," does not indicate the parties intended to incorporate the internet document. Instead, the language indicates the internet document contained informative but noncontractual material about the PDR LINX Service Program.

[15][16] Dent Zone also asserts incorporation by reference occurred through Geise's telling Rich before he signed the application that the website contained terms and conditions applicable to the program. The trial court made findings of fact and conclusions of law in support of this incorporation theory. However, when a contract is unambiguous, we determine the parties' intent from the terms of the written contract, not from parol evidence. *David J. Sacks, P.C. v. Haden,* 266 S.W.3d 447, 450 (Tex.2008) ("An unambiguous contract will be enforced as written, and parol evidence will not be received for the purpose of creating an ambiguity or to give the contract a meaning different from that which its language imports."). In this case, the language referring to the internet document does not show any intent by the parties that the internet document would become part of their written contract. There is no ambiguity concerning the parties' intent to incorporate the internet document, and we do not consider any parol evidence. We conclude the trial court erred by determining the internet document was incorporated by reference into the parties' contract.

Ratification

[17] Montgomery challenged the sufficiency of the evidence supporting the trial ***194** court's findings of fact and conclusions of law that Montgomery ratified the terms and conditions of the internet document. The trial court found and concluded:

> [Finding of Fact] 1.22 Bob Montgomery Chevrolet accepted the benefits of the contract, and continued to accept the benefits of services and profit, after admitting knowledge that the terms and conditions set forth in Plaintiff's Exhibit 2 [the internet document] applied to the contract.
>
> ....
>
> [Finding of Fact] 1.25 After Defendant admitted knowing about the terms and conditions, Defendant requested that Plaintiff continue its work in progress to completion, which was a benefit to Defendant, and Defendant kept all the proceeds (not just the 25%) of the work performed by Plaintiff after this admission.
>
> ....
>
> [Conclusion of Law] 2.19 Defendant ratified the contract, including the terms and conditions, by

continuing to accept and insist on performance after admitting knowledge of all terms and conditions, and keeping and retaining the benefits of such performance, including the amounts that were due and payable to Plaintiff.

The challenged findings and conclusion are based on Montgomery's admitting knowledge of all the terms and conditions and admitting they applied to the contract. There is no evidence that Montgomery admitted knowledge of the terms and conditions in the internet document or that Montgomery admitted those terms and conditions applied to the contract. Instead, the evidence shows Montgomery never agreed that the internet document was part of the contract, and no evidence shows Montgomery had knowledge of the terms and conditions.

Geise testified that when Rich told him Dent Zone would have to leave, Geise told Rich they had a contract and that Rich should be prepared for someone to contact him about the contract. Geise testified about what happened next:

Q. And what did he say in response to that?

A. He kind of laughed. And he said, first of all, I wouldn't hold anything against you, he said, but I have signed many contracts in my life, and this is merely an agreement, basically this—this—

Q. You can use the word—

A.—crap.... I said, sir, I don't understand why you would say that. I explained our process to you very clearly. Our terms and conditions I think are very clearly marked in the middle of our page underlined. We're not trying to hide it.

He made the comment, Judge, that any time you sign something that has this small print and makes me go somewhere else, I—that's crap. He said, I've signed many of these. This is merely an agreement. You go ahead and tell the powers that be that if they need to contact me, feel free to contact me....

Q. In other words, he admitted he saw the reference in the middle of the page because you weren't sitting there analyzing it? [sic]

A. Correct. Correct.

Q. He knew—he referenced—he said he knew he'd seen it?

A. And it was—and it was reviewed by himself and Mr. Montgomery overnight on the 30th as well, so they had time to look at the link, print the link, whatever they may need to do. So I try to make this as very clear there's nothing—we're not hiding anything. We actually have terms and conditions written right there ***195** in the—in the link. So it's not—he did—yes, he did.

Q. Did he say that he had seen it but not read it—

A. He—

Q.—seen the provision in the contract?

A.—he said whenever you put small print like this and make me go to a website, you know, to see something, it's crap. So that's acknowledgment to me that he saw the terms and conditions link. Whether or not he said I went there, I—I can't—I can't say that he—he said he personally went there. I know that it was reviewed.

Q. Okay. And then—so you specifically discussed these provisions, and yet he allowed you to continue working over the weekend, right?

A. Of course, yes.

This testimony shows Rich admitted being aware of the website address printed on the application he signed, but the testimony does not contain evidence that Rich admitted knowledge of the actual terms and conditions or that he admitted the terms and conditions listed on the website applied to their agreement. Instead, the record shows Geise did not know whether Rich or anyone else at Montgomery ever looked at the internet document, and Geise's testimony shows Rich rejected Geise's statement that the terms and conditions in the internet document were part of their agreement. We conclude that no evidence supports the trial court's findings and conclusions that Montgomery admitted knowledge of the terms and conditions on the website and that the dealership admitted those terms and conditions applied to the contract.

We next consider whether the record supports the trial court's conclusion of law that Montgomery ratified the terms and conditions in the internet document by accepting the benefits of the contract after Geise told Rich that the internet document applied to the contract. We conclude no ratification occurred.

[18][19][20][21][22] Ratification is the adoption or confirmation, by one with knowledge of all material facts, of a prior act that did not then legally bind that person and which that person had a right to repudiate. *Thomson Oil Royalty, LLC v. Graham,* 351 S.W.3d 162, 165 (Tex.App.-Tyler 2011, no pet.). Ratification of a contract occurs when a party recognizes the validity of a contract by acting under, performing under it, or affirmatively acknowledging it. *Barrand, Inc. v. Whataburger, Inc.,* 214 S.W.3d 122, 146 (Tex.App.-Corpus Christi 2006, pet. denied); *Mo. Pac. Ry. Co. v. Lely Dev. Corp.,* 86 S.W.3d 787, 792 (Tex.App.-Austin 2002, pet. dism'd). In other words, a party ratifies a contract by conduct recognizing the contract as valid with knowledge of all relevant facts. *Barrand,* 214 S.W.3d at 146. Any act inconsistent with an intent to avoid a contract has the effect of ratifying the contract. *Id.; Barker v. Roelke,* 105 S.W.3d 75, 85 (Tex.App.-Eastland 2003, pet. denied). Whether a party has ratified a contract may be determined as a matter of law if the evidence is not controverted or is incontrovertible. *Barrand,* 214 S.W.3d at 146; *Barker,* 105 S.W.3d at 85.

The doctrine of ratification is not applicable in this appeal. Montgomery does not dispute on appeal that the parties had a legally binding contract or argue that any contract was voidable.[FN7] *See Thomson Oil Royalty,* 351 S.W.3d at 165. Instead, the issue is whether the internet document was part of the contract. As discussed ***196** above, the internet document was not incorporated by reference. We conclude the doctrine of ratification does not apply.[FN8] *See Barrand,* 214 S.W.3d at 146.

FN7. In the trial court, Montgomery argued there was no contract because Rich lacked authority to sign contracts on behalf of Montgomery and because Rich thought he was signing a credit application, not a contract. The trial court found Montgomery's evidence on these

matters was not credible and found Rich had authority to sign the application at the time he signed it. Montgomery does not challenge these findings in this appeal.

FN8. The court of appeals stated in *Barrand, Inc.:*

> There is no dispute in this case regarding the validity of the Settlement Agreement and the Modified Franchise Agreement, the only contracts at issue between Whataburger and BurgerWorks. Although Whataburger has maintained that the Settlement Agreement is terminable at-will, we do not view that argument as casting a cloud on the validity of the contract. To the contrary, Whataburger's position recognizes the existence of a valid contract and then suggests that the contract may be terminated at-will. This, in our view, is different from a claim that there is no contract or that the contract relied upon is invalid. In fact, Whataburger's entire suit for declaratory judgment is, in essence, a request for the trial court to review the parties' written agreements and to declare their respective rights and obligations under those agreements, not to declare them invalid. Accordingly, there is no reason for us to conclude, as urged by BurgerWorks, that the affirmative defense of ratification presents fact issues precluding summary judgment for Whataburger.
>
> *Barrand, Inc.*, 214 S.W.3d at 146 (citation omitted).

Estoppel

[23] The trial court entered conclusions of law that Montgomery was estopped, quasi-estopped, and equitably estopped from denying applicability of the terms and conditions of the internet document to the parties contract: FN9

> FN9. On appeal, Dent Zone asserts, “There is no challenge to the finding that BMC [Montgomery] is estopped to deny that the Terms and Conditions were incorporated into the contract.” Dent Zone does not identify which of the court's findings of fact found Montgomery was estopped. None of the findings of fact mention “estoppel.” On appeal, Montgomery challenges all of the trial court's conclusions of law that Montgomery was estopped.

2.15 Defendant is estopped to deny the existence of the contract (Plaintiff's Exhibit 1 [the one page application] and 2 [the internet document]) by accepting and retaining the benefits of the contract after obtaining knowledge of all of the terms.

2.16 Defendant is estopped from claiming that the terms and conditions of Plaintiff's Exhibit 2 are not binding on Defendant because Defendant accepted and retained the benefits of the contract after acquiring knowledge that the terms and conditions in Plaintiff's Exhibit 2 were part of the Program that Defendant joined.

2.17 Defendant is quasi estopped from claiming that the terms and conditions of Plaintiff's Exhibit 2 are not binding on Defendant because Defendant accepted and retained the benefits of the contract after acquiring knowledge that the terms and conditions in Plaintiff's Exhibit 2 were part of the Program that Defendant joined.

2.18 Defendant is equitably estopped from claiming that the terms and conditions of Plaintiff's

Exhibit 2 are not binding on Defendant because Defendant accepted and retained the benefits of the contract after acquiring knowledge that the terms and conditions in Plaintiff's Exhibit 2 were part of the Program that Defendant joined.

All of these conclusions are based on the court's findings that the terms and conditions in the internet document were terms of the parties' contract and that Montgomery agreed that the terms in the internet document were part of the contract. As discussed above, the contents of the internet document did not become part of the parties' agreement because the document ***197** was not signed by Montgomery, the document was not incorporated by reference, and no evidence supports a finding that Montgomery agreed that the contents of the internet document were part of the parties' agreement. FN10 Because the factual findings supporting the court's conclusions of law concerning estoppel are not supported by any evidence, those conclusions are erroneous as a matter of law. *See Wright Group Architects–Planners, P.L.L.C. v. Pierce,* 343 S.W.3d 196, 205 (Tex.App.-Dallas 2011, no pet.).

FN10. In its appellee's brief, Dent Zone asserts that Montgomery did not challenge "the finding that BMC [Montgomery] is estopped to deny that the Terms and Conditions were incorporated into the contract." The court's findings of fact do not mention "estoppel," and the court's conclusions of law about estoppel do not mention incorporation of the internet document into the parties' contract by reference.

CONCLUSION

Having determined (1) the internet document was not incorporated by reference into the parties' contract, (2) Montgomery did not ratify the internet document, and (3) the evidence does not support the trial court's conclusions of law that Montgomery was estopped from denying the terms and conditions in the internet document applied to the contract, we conclude the forum-selection clause was not a part of the parties' contract. Accordingly, the trial court erred by concluding Montgomery consented to jurisdiction in Texas. We sustain Montgomery's first four issues. FN11

FN11. Because of our disposition of the first four issues, we do not reach Montgomery's fifth issue asserting the evidence was legally and factually insufficient to support the trial court's finding and conclusion that the forum-selection clause was not the result of overreaching by Dent Zone.

We reverse the trial court's order denying Montgomery's special appearance, and we render judgment granting the special appearance and dismissing the cause for want of personal jurisdiction.

Tex.App.–Dallas,2013.
Bob Montgomery Chevrolet, Inc. v. Dent Zone Companies
409 S.W.3d 181

END OF DOCUMENT

Supreme Court of Washington,
En Banc.

Certification from the United States District Court for the Western District of Washington in
The BOEING COMPANY, Plaintiff,
v.
AETNA CASUALTY AND SURETY COMPANY; et al., Defendants.
NORTHWEST STEEL ROLLING MILLS, INC., a Washington corporation, Plaintiff,
v.
FIREMAN'S FUND INSURANCE COMPANY, a foreign insurance company; et al., Defendants.
RSR CORPORATION, Plaintiff,
v.
GRANITE STATE INSURANCE COMPANY, and American Centennial Insurance Company, Defendants.
JOHN FLUKE MANUFACTURING COMPANY, INC., Plaintiff,
v.
HARTFORD ACCIDENT & INDEMNITY COMPANY; et al., Defendants.
HARTFORD ACCIDENT & INDEMNITY COMPANY, Plaintiff,
v.
JOHN FLUKE MANUFACTURING COMPANY, INC.; et al., Defendants.
DAVIS WALKER CORPORATION, a California corporation, Plaintiff,
v.
AETNA CASUALTY & SURETY COMPANY, a Connecticut corporation, Defendant.

No. 55700–4.
Jan. 4, 1990.

Insureds held liable for response costs under CERCLA for contamination of groundwater and real property with hazardous waste brought suit against insurers for indemnification. The United States District Court for the Western District of Washington certified question of state law. The Washington Supreme Court, Dore, J., held that environmental response costs to be paid by insureds under CERCLA for clean up of hazardous waste sites were “damages” covered by comprehensive general liability policies issued by insurers.

Question answered.

Callow, C.J., filed dissenting opinion with which Dolliver, J., concurred.

West Headnotes

[1] Insurance 217 2269

217 Insurance

217XVII Coverage—Liability Insurance
217XVII(A) In General
217k2267 Insurer's Duty to Indemnify in General
217k2269 k. Insured's Liability for Damages. Most Cited Cases
(Formerly 217k512(1))

Environmental response costs to be paid by insureds under CERCLA for clean up of hazardous waste sites were "damages" covered by comprehensive general liability policies issued by insurers, where substance of claim concerned compensation for restoration of water and real property contaminated by hazardous waste. Comprehensive Environmental Response, Compensation and Liability Act of 1980, §§ 101(25), 107(a)(4)(A), as amended, 42 U.S.C.A. §§ 9601(25), 9607(a)(4)(A).

[2] Insurance 217 ⚿1810

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1810 k. Construction as a Whole. Most Cited Cases
(Formerly 217k146.2)

In construing language of insurance policy, entire content must be construed together so as to give force and effect to each clause.

[3] Insurance 217 ⚿1822

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1822 k. Plain, Ordinary or Popular Sense of Language. Most Cited Cases
(Formerly 217k146.5(2))

Undefined terms in insurance contract must be given their plain, ordinary, and popular meaning.

[4] Insurance 217 ⚿1855

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1855 k. Dictionaries. Most Cited Cases
(Formerly 217k146.5(2))

To determine ordinary meaning of undefined term in insurance contract, court looks to standard English language dictionaries.

[5] Insurance 217 ⚿2269

217 Insurance
217XVII Coverage—Liability Insurance
217XVII(A) In General
217k2267 Insurer's Duty to Indemnify in General
217k2269 k. Insured's Liability for Damages. Most Cited Cases
(Formerly 217k512(1), 217k434(1))

Provision in comprehensive general liability policy providing coverage for "damages" paid as consequence of property damage is not limited to sums imposed pursuant to "legal," as opposed to "equitable," basis for liability.

[6] Insurance 217 ⚿1822

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1822 k. Plain, Ordinary or Popular Sense of Language. Most Cited Cases
(Formerly 217k146.5(2))

Before insurance company can avail itself of legal technical meaning of word or words in policy, it must be clear to both parties to contract intended that language had legal technical meaning; otherwise, words will be given their plain, ordinary meaning.

[7] Insurance 217 ⚿1833

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1833 k. Status or Bargaining Power of Insureds. Most Cited Cases
(Formerly 217k146)

Court does not apply different rule of construction to policy based on fact that policy has been issued to corporate giant rather than individual; once court construes standard form coverage clause as matter of law, court's construction will bind policyholders throughout state regardless of size of their business.

[8] Insurance 217 ⚿2269

217 Insurance
217XVII Coverage—Liability Insurance
217XVII(A) In General
217k2267 Insurer's Duty to Indemnify in General
217k2269 k. Insured's Liability for Damages. Most Cited Cases
(Formerly 217k512(1))

Response costs incurred by insured under CERCLA are "damages" to extent that costs are

incurred "because of" property damage within meaning of comprehensive general liability policy coverage clause; however, "damages" do not include safety measures or other preventive costs incurred in advance of any damage to property.

****508 *871** Perkins, Coie, Stone, Olsen & Williams, Charles C. Gordon, William A. Gould, Nicholas P. Gellert, Paul R. Carlson, Seattle, and Covington & Burlington, Robert N. Sayler, James R. Murray, and Eric C. Bosset, Washington, D.C., for plaintiff, Boeing Co.

Sylvester, Ruud, Petrie & Cruzen, John T. Petrie and Robert W. Bryan, Seattle, Wash., for plaintiff, Northwest Steel.

Don M. Gulliford, Robert R. Cole, Bellevue, and Whiteman, Osterman & Hanna, Philip H. Gitlen and Jonathan P. Nye, Albany, N.Y., for plaintiff, RSR.

Stoel, Rives, Boley, Jones & Grey, Stevan D. Phillips, Seattle, and Phillips, Nizer, Benjamin, Krim & Ballon, Judith S. Roth and George Berger, New York City, for plaintiff, John Fluke Mfg.

Bogle & Gates, Jeffrey W. Leppo and Ruth Piekarska, Seattle, for plaintiff, Davis Walker Corp.

Williams, Kastner & Gibbs, Jerry B. Edmonds, Patrick M. O'Loughlin, Roy Umlauf, Frankie A. Crain, Coleen Cook, Merrick, Hofstedt & Linsey, Sidney R. ***872** Snyder, Jr., Ronald Dinning, Wilson, Smith, Cochran & Dickerson, Dennis Smith, David M. Jacobi, Hallmark, Keating & Abbott, William Fitzharris, Jr., Pamela Lang, Carney, Stephenson, Badley, Smith, Mueller & Spellman, Sylvia Luppert, Seattle, Carr, Goodson, Lee & Foret, Michael Hooks, Margaret Warner, Washington, D.C., Thorsrud, Cane & Paulich, Mark Thorsrud, Patrick M. Paulich, Dunlap & Soderland, David Soderland, Seattle, and Sedgwick, Detert, Moran & Arnold, Mark C. Raskoff, Los Angeles, Cal., for defendants, insurers.

Bassett & Morrison, W. George Bassett, Philip R. Croessmann, and Margaret A. Morgan, Seattle, for defendant, Granite State Ins.

Betts, Patterson & Mines, Jeffrey C. Grant and Margaret E. Wetherald, Seattle, for defendant, Highlands Ins.

Lane, Powell, Moss & Miller, David Schoeggl, Robert Israel, and Douglas J. Ende, Seattle, for defendants, London Underwriters, et al.

Rivkin, Radler, Dunne & Bayn, Jeffrey Silberfeld, Richard S. Feldman, and Steven Brock, Uniondale, N.Y. and Bradbury, Bliss & Riodan, John H. Bradbury and Carl E. Forsberg, Seattle, for defendant, Hartford.

David M. Brenner, Seattle, Peter J. Kalis, Thomas M. Reiter, James R. Segerdahl, Pittsburgh, Pa., Carol A. Wardell, Wenatchee, Douglas N. Jewett, Seattle City Atty., Terrence J. Cullen, Asst. City Atty., Seattle, William J. Barker, Tacoma City Atty., G. Stephen Karavitis, Asst. City Atty., Tacoma, Robert F. Hauth, Kenneth Eikenberry, Atty. Gen., Jerry Ackerman, Lee Rees, Asst. Attys. Gen., Ecology Div., Olympia, George E. Greer, Linda R. Larson, Molly B.

Burke, Mark S. Parris, Norm Maleng, King County Prosecutor, and ****509** James L. Brewer, Deputy County Prosecutor, Seattle, amicus curiae for plaintiffs on behalf of Washington State Ass'n of Mun. Attys.

***873** William R. Hickman, Seattle, Frederick S. Ansell, Washington, D.C., Thomas S. James, P. Cameron Devore, and Donald S. Kunze, Seattle, amicus curiae for defendants on behalf of Ins. Environmental Litigation Ass'n.

DORE, Judge.

The United States District Court for the Western District of Washington has certified the following question of state law to this court:

> Whether, under Washington law, the environmental response costs paid or to be paid by the insureds, as the result of action taken by the United States and the State of Washington under CERCLA, 42 U.S.C. § 9601 *et seq.*, constitute "damages" within the meaning of the comprehensive general liability policies issued by the insurers.

ANSWER: Yes.

FACTS

In 1983, the United States Environmental Protection Agency designated the Western Processing hazardous waste facility at Kent, Washington, as one of 400 hazardous waste sites requiring cleanup. On February 25, 1983, the EPA filed a complaint against Western Processing and its owners in the United States District Court for the Western District of Washington. In May 1983, pursuant to the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), 42 U.S.C. § 9601 *et seq.*, the EPA notified the appellants (hereinafter policyholders) that they were generators of hazardous waste at the Western Processing site and were responsible parties for the "response costs" at this site. On July 17, 1984, the EPA and the State of Washington, as an additional plaintiff, named the policyholders in a "Second Amended Complaint" as " 'generator and transporter defendants' facing potential liability for all monies expended by the government at the Western Processing site.' " Certification order app., at 141. On August 28, 1984, the Court entered a "Partial Consent Decree" between the EPA and the policyholders for the cleanup of the surface of the Western Processing site. On April 13, 1987, the ***874** Court entered a "Consent Decree" between EPA and policyholders for the cleanup of hazardous waste contamination of the subsurface of the Western Processing site.

EPA, in its complaint, alleged that the policyholders generated or transported hazardous substances found at the site. Further, that the migration of such wastes has contaminated the groundwater, aquifer (water bearing geological zone), commercial and agricultural property adjoining the site, and nearby surface waters. Certification order app., at 324–73, "Third Amended Complaint" filed by United States Attorneys in *United States v. Western Processing Co.* It further alleged that the United States, in order to combat the effects of contaminated groundwater, aquifer and property adjoining the site, had incurred and was incurring "response costs" as defined by CERCLA for which policyholders were liable. CERCLA defines the costs of "response" to include costs of removal of hazardous substances from the

environment and the costs of other remedial work. 42 U.S.C. § 9601(25). CERCLA provides that any person or business entity responsible for a release or threatened release of hazardous substances "shall be liable for ... all costs of removal or remedial action incurred by the United States Government or a State ..." 42 U.S.C. § 9607(a)(4)(A). Pursuant to the action by EPA, the policyholders have paid and will continue to pay environmental response costs relating to the Western Processing hazardous waste facility.

During the period of time that the policyholders generated and transported hazardous wastes to Western Processing, they carried Comprehensive General Liability (CGL) insurance purchased from the respondents (hereinafter insurers). The operative coverage provision of four of the policies provide that the insurer " 'will pay on behalf of the insured all sums which the ****510** insured shall become obligated to pay *as damages* because of bodily injury or property damage to which this policy applies, caused by an occurrence....' " Certification order, at 3. In one case, the policy provides indemnification " 'for all sums which the ***875** Assured shall be obligated to pay ... *for damages* ... all as more fully defined by the term "ultimate net loss" on account of: (i) Personal injuries ... [or] (ii) Property Damage ...' ", and goes on to define "ultimate net loss" as " 'the total sum which the Assured, or any company as his insurer, or both, become obligated to pay by reason of ... property damage ... either through adjudication or compromise ...' " Certification order, at 3. The policies do not specifically define "damages."

The policyholders sued the insurers for indemnification for the "response costs" they incurred relating to the Western Processing facility. In each case, motions for summary judgment were filed in the United States District Court. Since the motions raised a determinative question of state law, the question of whether "response costs" constitute "damages" within the CGL policies issued by insurers, this question was certified to this court. No extrinsic evidence touching upon the parties' interpretation of the coverage clause was provided in this certification. It was the intent of the district court that extrinsic evidence not be considered by this court, since the certification procedure is authorized to obtain answers to questions of law, not questions of fact.

ANALYSIS

[1] Under CERCLA any person responsible for an "actual release" or "threatened release" of hazardous substances is liable for response costs. The response costs paid by the insureds in the case before us concern responses to an "actual release" of hazardous substances which have already contaminated the groundwater and real property surrounding the Western Processing site. The question before us is whether these response costs to remedy an actual release of hazardous substances constitute damages within the meaning of the insureds' comprehensive general liability policies issued by insurers. In order for the policyholders to be indemnified, the plain meaning of the contract must provide coverage for the subject "response ***876** costs." [FN1] Alternatively, before the insurers can avoid indemnifying the policyholders, this court must be satisfied that the plain meaning of "damages", as it would be understood by the average lay person, unmistakably precludes coverage for response costs, and any ambiguity is to be construed against the insurer.

FN1. It is important to note the absence of public policy in the construction of

> insurance contracts. While this case implicitly presents a grave question of policy, namely who should bear the cost of polluting our environment, the task presently before this court only requires us to construe the terms of the policies under Washington law. Washington courts rarely invoke public policy to override express terms of an insurance policy. *State Farm Gen. Ins. Co. v. Emerson,* 102 Wash.2d 477, 481–83, 687 P.2d 1139 (1984); *Progressive Cas. Ins. Co. v. Cameron,* 45 Wash.App. 272, 282, 724 P.2d 1096 (1986).

The insurers have attempted to meet this burden by drawing lines, increasingly limited, around the word "damages." First, insurers draw a bright line between law remedies and equity remedies under common law. They assert that the legal technical meaning of "damages" includes monetary compensation for injury but not monetary equitable remedies such as sums paid to comply with an injunction or restitution. The insurers conclude that costs incurred under CERCLA are like injunction and restitution costs; therefore, they are equitable rather than legal and they are not "damages" within the policy language because equity does not award damages. The linchpin to insurers' argument is that "damages" should be given its legal technical meaning. Next, they draw a line between law remedies, excluding restitution-type law damages, such as remedies like CERCLA. Finally, they draw a line through the available common law damages and exclude everything except the tort-type damages.

The court is not persuaded that, under the rules of insurance contract analysis in ****511** Washington, the words "as damages" communicate these restrictions.

[2] In construing the language of an insurance policy, the entire contract must be construed together so as to give force and effect to each clause. *Transcontinental Ins. Co. v. ***877** Washington Public Utils. Districts' Util. Sys.,* 111 Wash.2d 452, 456, 760 P.2d 337 (1988). Here, the structure of the subject contracts defeats insurers' argument that "as damages" precludes coverage for cleanup costs. The subject clause, "as damages", is sandwiched into the general coverage provisions of policyholders' insurance contracts. This is an odd place to look for exclusions of coverage. *See Dairyland Ins. Co. v. Ward,* 83 Wash.2d 353, 358–59, 517 P.2d 966 (1974). Furthermore, there is nothing more in the contracts. Under the title "Exclusions", there is nothing in the enumerated exclusionary provision about "damages." Finally, there are long sections of the contracts defining all the key terms. However, there are no defining words about damages.

[3][4] Undefined terms in an insurance contract must be given their "plain, ordinary, and popular" meaning. *Farmers Ins. Co. v. Miller,* 87 Wash.2d 70, 73, 549 P.2d 9 (1976); *Prudential Property & Cas. Ins. Co. v. Lawrence,* 45 Wash.App. 111, 724 P.2d 418 (1986). To determine the ordinary meaning of an undefined term, our courts look to standard English language dictionaries. *See, e.g., Safeco Ins. Co. of Am. v. Davis,* 44 Wash.App. 161, 165, 721 P.2d 550 (1986) (entitle); *Transport Indem. Co. v. Sky–Kraft, Inc.,* 48 Wash.App. 471, 487, 740 P.2d 319, 328 (1987) (performance); *Miebach v. Safeco Title Ins. Co.,* 49 Wash.App. 451, 454 n. 1, 743 P.2d 845 (1987), (actual) *review denied,* 110 Wash.2d 1005 (1988); *Sperry v. Maki,* 48 Wash.App. 599, 602, 740 P.2d 342 (motor vehicle) *review denied,* 109 Wash.2d 1014 (1987).

The plain, ordinary meaning of damages as defined by the dictionary defeats insurers' argument. Standard dictionaries uniformly define the word "damages" inclusively, without making any distinction between sums awarded on a "legal" or "equitable" claim. For example, *Webster's Third New International Dictionary* 571 (1971) defines "damages" as "the estimated reparation in money for detriment or injury sustained". See also *The Random House Dictionary of the English Language* 504 (2d ed. 1987) (cost or expense). Indeed, even the insurers' own dictionaries define ***878** "damages" in accordance with the ordinary, popular, lay understanding: "Damages. *Legal.* The amount required to pay for a loss." Merit, *Glossary of Insurance Terms* 47 (1980); see also Rubin, *Barrons Dictionary of Insurance Terms* 71 (1987). Even a policyholder with an insurance dictionary at hand would not learn about the coverage-restricting connotation to "damages" that the insurers argue is obvious.

Numerous federal and sister-state decisions (counsel at oral argument stated over 56 judges across the country) agree that "damages" include cleanup costs. *See Intel Corp. v. Hartford Accident & Indem. Co.,* 692 F.Supp. 1171, 1186–87 (N.D.Cal.1988); *Aerojet–General Corp. v. San Mateo Cy. Superior Court,* 211 Cal.App.3d 216, 257 Cal.Rptr. 621, 631, 258 Cal.Rptr. 684 (1989) ("the great weight of authority is consistent with [Policyholder's position]"). This persuasive authority includes federal district courts in California, Colorado, Michigan, Pennsylvania, New Jersey, Missouri, Massachusetts, New York, Texas, and Delaware and state appellate courts in Wyoming, New Jersey, North Carolina, Michigan and Wisconsin. *Intel Corp.,* 692 F.Supp. at 1188 n. 24.

These cases have found that cleanup costs are essentially compensatory damages for injury to property, even though these costs may be characterized as seeking "equitable relief." *United States Fid. & Guar. Co. v. Thomas Solvent Co.,* 683 F.Supp. 1139, 1168 (W.D.Mich.1988); *CPS Chem. Co. v. Continental Ins. Co.,* 222 N.J.Super. 175, 536 A.2d 311, 316 (1988); *Intel Corp. v. Hartford Accident & Indem. Co.,* 692 F.Supp. 1171, 1186–87 (N.D.Cal.1988). Or put another way, "coverage does not hinge on the form of action taken or the nature of relief sought, but on an actual or threatened use of legal process to coerce payment or conduct by a policyholder."****512** *Fireman's Fund Ins. Cos. v. Ex–Cell–O Corp.,* 662 F.Supp. 71, 75 (E.D.Mich.1987). In *United States Fidelity & Guar. Co.,* the court found that once property damage is found as a result of environmental contamination, cleanup costs should be recoverable as sums ***879** that the insured was liable to pay. According to an earlier case, *United States Aviex Co. v. Travelers Ins. Co.,* 125 Mich.App. 579, 589–90, 336 N.W.2d 838 (1983), the environmental cleanup costs are covered because they are equivalent to "damages" under state law:

> If the state were to sue in court to recover in traditional "damages", including the state's costs incurred in cleaning up the contamination, for the injury to the ground water, defendant's obligation to defend against the lawsuit and to pay damages would be clear. It is merely fortuitous from the standpoint of either plaintiff or defendant that the state has chosen to have plaintiff remedy the contamination problem, rather than choosing to incur the costs of clean-up itself and then suing plaintiff to recover those costs. The damage to the natural resources is simply measured in the cost to restore the water to its original state.

Courts consistently agree that the "common-sense" understanding of damages within the

meaning of the policy "includes a claim which results in causing [the policyholder] to pay sums of money because his acts or omissions affected adversely the rights of third parties ... [*i.e.*, the public.]" *United States Fid. & Guar. Co. v. Thomas Solvent Co.*, 683 F.Supp. 1139, 1168 (W.D.Mich.1988). Even our own state trial courts have rejected the insurers' "damages" argument.[FN2]

FN2. *See, e.g., Queen City Farms, Inc. v. Aetna Cas. & Sur. Co.*, No. 86–2–06236–0 (Wash.Super.Ct.King Cy. Sept. 4, 1987) (order denying defendants' motion: re: "Damages"), *reported in* Mealey's Litigation Reports—Insurance (Nov. 24, 1987); *Isaacson Corp. v. Holland–America Ins. Co.*, No. 85–2–12843–5, slip op. at 17–18 (Wash.Super.Ct.King Cy. Dec. 22, 1987).

> In the *Queen City Farms* order at page 7, Judge Shellan rejected the insurers' argument: "[t]he average purchaser of insurance would understand the term 'damages', as used in the defendants' insurance policies, to include monies paid to clean up and remediate damage to the groundwater or other pollution damage affecting the rights of third parties ..."

In contrast to the plain ordinary meaning accorded to damages by courts across the country, insurers insist upon an accepted technical and legal meaning of damages. Insurers rely primarily on *Travelers Ins. Co. v. Ross Elec. of Wash., Inc.*, 685 F.Supp. 742 (W.D.Wash.1988); *Continental Ins. Cos. v. Northeastern Pharmaceutical & Chem.* ****880*** *Co.*, 842 F.2d 977 (8th Cir.1988), and *Maryland Cas. Co. v. Armco, Inc.*, 822 F.2d 1348 (4th Cir.1987), *cert. denied*, 484 U.S. 1008, 108 S.Ct. 703, 98 L.Ed.2d 654 (1988).

The definition of damages used by *Armco* was taken from *Aetna Cas. & Sur. Co. v. Hanna*, 224 F.2d 499, 503 (5th Cir.1955) (damages include "only payments to third persons when those persons have a legal claim for damages."). As a very recent case stated "[i]t is not clear why the *Armco* court turned to a 30–year–old case for a definition of 'damages,' a definition which is essentially a tautology defining damages as payment to a person who has 'a legal claim for damages.' " *Aerojet–General Corp.*, 257 Cal.Rptr. at 631. The *Armco* court did express the opinion that it is a "dangerous step" for courts to construe insurance policies to cover "essentially prophylactic" or "harm avoidance" costs. *Armco*, at 1353. However, a construction of "damages" which includes equitable relief "is not a boundless universe—such 'damages' still must be 'because of' property damage. Thus *Armco* 's conclusion that an insurer would be held liable for prophylactic safety measures, taken in advance of any damage to property, is not applicable to the policies under review." *Aerojet–General Corp.*, 257 Cal.Rptr. at 632.

[5] In *Northeastern Pharmaceutical*, the Eighth Circuit in a sharply divided en banc decision reached a similar result as in *Armco*. The majority relied primarily on the narrow, technical decision espoused in *Armco* and *Hanna*. As with the *Armco* court, the *Continental* majority was concerned that absent a limited definition of damages, " 'all sums which the insured ****513** shall become legally obligated to pay *as damages* ' " would be reduced to " '*all sums* which the insured shall become legally obligated to pay.' " *Northeastern Pharmaceutical*, at 986. However, both *Armco* and *Northeastern Pharmaceutical* effectively

sever "damages" from the additional restrictive phrase "because of property damage." *Northeastern Pharmaceutical, Armco* and insurers are in effect trying to write out of the CGL policy a concept that is expressly stated—that damages paid as a ***881** consequence of property damage caused by an occurrence are covered by the policy—and to write into the policy a condition that is not there—that such sums are covered only if they have been imposed pursuant to a "legal", as opposed to an "equitable" basis for liability. The court cannot ignore the operative language of the clause itself. Our responsibility is to interpret the coverage clause as a whole. *Transcontinental Ins. Co. v. Washington Public Utils. Districts' Util. Sys.,* 111 Wash.2d 452, 456, 760 P.2d 337 (1988).

Even *Northeastern Pharmaceutical* and *Armco,* which found that "damages" do not include cleanup costs, support the policyholders' position. The reason is that these cases admit that the common meaning of the word "damages" is broad and all inclusive. In *Northeastern Pharmaceutical,* at page 985, the majority conceded that:

> The dictionary definition does not distinguish between legal damages and equitable monetary relief. Thus, from the viewpoint of the lay insured, the term "damages" could reasonably include all monetary claims, whether such claims are described as damages, expenses, costs, or losses.

(Citation omitted.) *See Armco,* 822 F.2d at 1352 (limiting "the breadth of the definition of 'damages' somewhat more narrowly" than its "ordinary meaning.").

Furthermore, these cases are not helpful to the insurers' position because they are inconsistent with Washington law. In this state, legal technical meanings have never trumped the common perception of the common man. "[T]he proper inquiry is not whether a learned judge or scholar can, with study, comprehend the meaning of an insurance contract" but instead "whether the insurance policy contract would be meaningful to the layman ..." *Dairyland Ins. Co. v. Ward,* 83 Wash.2d 353, 358, 517 P.2d 966 (1974). "The language of insurance policies is to be interpreted in accordance with the way it would be understood by the average man, rather than in a technical sense."

[6] Insurers, perhaps in realizing the infirmities of *Northeastern Pharmaceutical* and *Armco,* try to argue that when legal words are used in a document, this court applies ***882** their usual legal interpretations. [FN3] *See R.A. Hanson Co. v. Aetna Ins. Co.,* 26 Wash.App. 290, 612 P.2d 456 (1980). However, before an insurance company can avail itself of a legal technical meaning of a word or words, it must be clear that *both* parties to the contract intended that the language have a legal technical meaning. *Thompson v. Ezzell,* 61 Wash.2d 685, 688, 379 P.2d 983 (1963). Otherwise the words will be given their plain, ordinary meaning. *Farmers Ins. Co. v. Miller,* 87 Wash.2d 70, 73, 549 P.2d 9 (1976).

> FN3. Carriers in their oral arguments also relied on *Detweiler v. J.C. Penney Cas. Ins. Co.,* 110 Wash.2d 99, 104, 751 P.2d 282 (1988), for the proposition of applying a legal technical definition. In *Detweiler,* the court stated "[w]here, as here, the word 'accident' is not otherwise defined in a policy, we look to our common law for definition." (Footnote omitted.) While the court said we look to the common law, the

> cases interpreting accident employed the popular ordinary meaning of accident as defined in the dictionaries. *See Evans v. Metropolitan Life Ins. Co.,* 26 Wash.2d 594, 605, 174 P.2d 961 (1946). Thus *Detweiler,* does not support carriers' proposition that when this court is faced with a legal term, we employ the technical legal meaning of the word.

Here, there is nothing about the language from the subject standard form policies that indicates the parties intended a legal meaning to apply to the disputed term. Therefore, the words "as damages" should be interpreted in accordance with its plain, ordinary meaning, as dictated by the ****514** well established rules of construction under Washington law.

Insurers also try to argue that this court, when it is dealing with corporations, analyzes the contract language and determines its meaning without reference to what the average lay person might understand. *See Transcontinental Ins. Co.; Continental Ins. Co. v. Paccar, Inc.,* 96 Wash.2d 160, 634 P.2d 291 (1981). While *Transcontinental Ins. Co.* and *Paccar* did not talk about the average lay person, these decisions did not hold that a different rule should apply when corporations are involved. Furthermore, this court has applied the "layman" rule when dealing with corporations. *See, e.g., Phil Schroeder, Inc. v. Royal Globe Ins. ***883** Co.,* 99 Wash.2d 65, 659 P.2d 509 (1983) (carpet cleaning company), *modified,* 101 Wash.2d 830, 683 P.2d 186 (1984); *McDonald Indus., Inc. v. Rollins Leasing Corp.,* 95 Wash.2d 909, 631 P.2d 947 (1981) (crane company).

[7] In any event, on the facts of this case, it is questionable whether these standard rules of construction are no less applicable merely because the insured is itself a corporate giant. The critical fact remains that the policy in question is a standard form policy prepared by the company's experts, with language selected by the insurer. The specific language in question was not negotiated, therefore, it is irrelevant that some corporations have company counsel. Additionally, this standard form policy has been issued to big and small businesses throughout the state. Therefore it would be incongruous for the court to apply different rules of construction based on the policyholder because once the court construes the standard form coverage clause as a matter of law, the court's construction will bind policyholders throughout the state regardless of the size of their business.

Insurers attempt to save themselves from these rules of construction by arguing that, in any event, criticism of *Travelers Ins. Co. v. Ross Elec. of Wash., Inc.,* 685 F.Supp. 742 (W.D.Wash.1988) fails since it relies heavily on Washington law. In *Ross,* the matter came before the court on the insurer's motion for partial summary judgment concerning response costs. In granting the motion, the court relied on *Armco, Northeastern Pharmaceutical,* and *Seaboard Sur. Co. v. Ralph Williams' Northwest Chrysler Plymouth, Inc.,* 81 Wash.2d 740, 504 P.2d 1139 (1973).

The *Ross* court and the insurers rely on *Seaboard* for the proposition that any lawsuit that could be characterized as a claim for equitable relief cannot constitute a claim for "damages." However, *Seaboard* does not stand for this proposition; indeed, the court's analysis supports the policyholders' position.

***884** In *Seaboard,* the State Attorney General sought a judgment for statutory penalties and to enjoin the insured automobile dealer from "unfair methods of competition." The Attorney General also alleged that the dealer had gained possession of, and unlawfully withheld, property of members of the public, and accordingly sought "such additional orders or judgments as may be necessary to restore to any person in interest any monies or property which may have been acquired by means of an act or conduct of [defendants] found to be in violation of RCW 19.86.020." 81 Wash.2d at 742, 504 P.2d 1139. However, the Attorney General had no authority to recover damages, only statutory penalties. 81 Wash.2d at 741, 504 P.2d 1139.

The dealer's insurer, Seaboard Surety, sought a judicial determination that it had no duty to defend the suit because its policy required Seaboard to pay "sums which the Insured shall become obligated to pay ... as the result of any final judgment for *money damages resulting from ... unfair competition* ". (Italics ours.) 81 Wash.2d at 741, 504 P.2d 1139. In denying coverage, the *Seaboard* court did not rule that "damages" cannot include sums paid in restitution; instead, the court looked to the substance of the damage claim to determine whether it constituted one *for unfair competition* as ordinarily understood. The court concluded that damages for unfair competition can only be recovered by a competitor, and that a suit brought by the State to require the return of property ****515** wrongfully withheld from *customers* did not constitute such a claim.

In contrast, the substance of the claim for response costs in the present case concerns compensation for restoration of contaminated water and real property. The cost of repairing and restoring property to its original condition has long been considered proper measure of damages for property damage. *Koch v. Sachman–Phillips Inv. Co.,* 9 Wash. 405, 37 P. 703 (1894); *Olson v. King Cy.,* 71 Wash.2d 279, 428 P.2d 562, 24 A.L.R.3d 950 (1967). Consequently, the substance of the claim for response costs constitutes a claim for property damage and falls within the scope of ***885** coverage afforded by a CGL policy. Thus *Ross* incorrectly applied the Washington law it relied on. FN4

> FN4. The carriers also cite *Felice v. St. Paul Fire & Marine Ins. Co.,* 42 Wash.App. 352, 711 P.2d 1066 (1985), *review denied,* 105 Wash.2d 1014 (1986). In *Felice,* an attorney failed to remove himself as guardian of a elderly lady and paid himself attorney fees not owing to him. Therefore, the proceeding was an action to remove the guardian, not a proceeding to recover damages. Like *Seaboard, Felice* is not applicable to the issue of whether sums paid by a policyholder to clean up or to restore property damage are "damages" within the meaning of the subject CGL policy.

Furthermore, when Ross Electric's counsel became aware of two superior court cases FN5 that had addressed the same issue before the court, they moved for reconsideration of the damages ruling on the basis of these decisions. Judge Bryan then wrote counsel for additional briefing on whether these superior court decisions were binding or if they required certification to the State Supreme Court. Soon thereafter, the insurers settled with Ross Electric. Thus the *Ross* opinion was decided without the benefit of the reasoning of the only Washington court to have addressed the issue.

FN5. *Queen City Farms, Inc. v. Aetna Cas. & Sur. Co.,* No. 86–2–06236–0 (Wash.Super.Ct.King Cy. Sept. 4, 1987) (order denying defendants' motion: re: "Damages"), *reported in* Mealey's Litigation Reports—Insurance (Nov. 24, 1987); *Isaacson Corp. v. Holland–America Ins. Co.,* No. 85–2–12843–5, slip op. at 17–18 (Wash.Super.Ct.King Cy. Dec. 22, 1987).

We are not persuaded with the cases relied on by the insurers. The *Ross* court relied almost exclusively on the logic of *Northeastern Pharmaceutical,* and *Armco* which we find faulty and it misconstrued *Seaboard.* Instead, we agree with the majority of cases across the country that the plain meaning of damages does not distinguish between sums awarded on a "legal" or "equitable" basis and that the plain meaning of damages may include cleanup costs to the extent that these costs are incurred because of property damage.

The policy defines property damage as "physical injury to or destruction of tangible property, which occurs during the policy period ..." Certification order app., at ***886** 412. "Property damage" includes discharge of hazardous waste into the water. In *Port of Portland v. Water Quality Ins. Syndicate,* 796 F.2d 1188, 1196 (9th Cir.1986), the court held that the discharge of pollution into water caused "damage to tangible property," within the meaning of the policy defining property damage as physical injury to or destruction of tangible property. In *Broadwell Realty Servs., Inc. v. Fidelity & Cas. Co.,* 218 N.J.Super. 516, 528 A.2d 76, 81 (1987), the court held the insurer was liable to pay as damages government mandated cleanup costs, on the ground that the costs represented a legal obligation owing because of property damage.

The issue of when costs are or are not incurred "because of" property damage is illustrated in *Aerojet,* 257 Cal.Rptr. at page 635 by the following hypothetical:

> Petitioners have two underground storage tanks for toxic waste. Tank # 1 has leaked wastes into the soil which have migrated to the groundwater or otherwise polluted the environment. Tank # 2 has not leaked, but government inspectors discover that it does not comply with regulatory requirements, and could eventually leak unless corrective measures are taken. Response costs associated with Tank # 1 will be covered as damages, because pollution has occurred. Tank # 2 would not be covered. Likewise,****516** the expense of capital improvements to prevent pollution in an area of a facility where there is none, or improvements or safety paraphernalia required by government regulation and not causally related to property damage, would not be covered as "damages."

Aerojet–General Corp. v. San Mateo Cy. Superior Court, 211 Cal.App.3d 216, 257 Cal.Rptr 621, 635, 258 Cal.Rptr. 684 (1989). Thus, costs owing because of property damages are remedial measures taken after pollution has occurred, but preventive measures taken before pollution has occurred are not costs incurred because of property damage.

The occurrence of the hazardous wastes leaking into the ground contaminating the groundwater, aquifer and adjoining property constituted "property damage" and thus triggered the "damages" provision of the policies carried by the policyholders. The costs assessed against the policyholders ***887** by the underlying lawsuits are covered by the subject policies

to the extent that these costs are because of property damage. This duty to pay money is no different from the legal obligation that burdens a party who has been held liable to restore property to the condition it was in prior to the occurrence of the tortfeasor's conduct or damages consisting of amounts necessary to restore property to its status quo. *See CPS Chem. Co. v. Continental Ins. Co.,* 222 N.J.Super. 175, 536 A.2d 311, 316 (1988).

CONCLUSION

[8] Response costs in response to actual releases of hazardous wastes are "damages" within the meaning of CGL coverage clauses at issue. The term "damages" does not cover safety measures or other preventive costs taken in advance of any damage to property. Consequently, we concur with the great majority of judges across the country that response costs incurred under CERCLA are "damages" to the extent that these costs are incurred "because of" property damage within the meaning of the CGL coverage clauses at issue. The reported decisions across the country, the lay dictionary, the insurance dictionary, the failure of the insurance industry to write down what it meant, each of these facts lays waste to insurers' argument. For us to read the words "as damages" to exclude coverage for cleanup costs, would require this court to rewrite the principles of insurance contract analysis in Washington, and then to retroactively apply these rewritten principles to the policyholders that bought their policies decades ago. However, we decline to do this. The industry knows how to protect itself and it knows how to write exclusions and conditions. The words "as damages" do not stand exclusionary guard for the industry and represent a vast exclusion from coverage. The term "damages" is to be given its plain, ordinary meaning and not the technical meaning advocated by insurers.

***888** The question certified by the District Court asks

> [w]hether, under Washington law, the environmental response costs paid or to be paid by the insureds, as the result of action taken by the United States and the State of Washington under CERCLA, 42 U.S.C. § 9601 *et seq.*, constitute "damages" within the meaning of the comprehensive general liability policies issued by the insurers.

In answer to this question, on the facts submitted to us, we conclude that under Washington law, "response costs" incurred under CERCLA are "damages" to the extent that these costs are incurred "because of" property damage and therefore fall within the meaning of the CGL policies issued by insurers.

We answer: Yes.

UTTER, BRACHTENBACH, DURHAM, ANDERSEN and SMITH, JJ., and PEARSON, J. Pro Tem., concur.

CALLOW, Chief Justice (dissenting)

We are asked in this case to determine whether an insured's liability to pay CERCLA response costs constitute "sums which the insured [has] become legally obligated to pay *as damages* " within the meaning of ****517** a standard comprehensive general liability insurance policy. As the majority opinion itself acknowledges, the plain, ordinary, and popular meaning of the word damages is "reparation for detriment or injury sustained." Because CERCLA

response costs are not "reparation for detriment or injury sustained," CERCLA response costs are not payable "as damages" within the plain meaning of the policies at issue. The majority's contrary holding upsets settled rules of insurance construction, violates controlling precedent, and contravenes public policy.

I

CERCLA Response Costs Are a Restitutionary, Not a Damage Remedy

A. Damage remedies are compensatory; equitable remedies are coercive or restitutionary.

***889** Washington law defines damages as:

> [T]he sum of money which the law imposes or awards as compensation, or recompense, or in satisfaction for an injury done, or a wrong sustained as a consequence, *either* of a breach of a contractual obligation or a tortious act or omission.

Puget Constr. Co. v. Pierce Cy., 64 Wash.2d 453, 392 P.2d 227 (1964) (citing 15 Am.Jur. *Damages* § 2). *See also* D. Dobbs, *Remedies* § 1.2, at 3 (1973).

Damages for injury to property are measured in terms of the amount necessary to compensate for the injury to the property interest. D. Dobbs, § 5.1, at 311. Therefore, damages for injury to property are limited under Washington law to *the lesser of* diminution in value of the property or the cost to restore or replace the property. *Koch v. Sackman–Phillips Inv. Co.,* 9 Wash. 405, 37 P. 703 (1894); *Burr v. Clark,* 30 Wash.2d 149, 158, 190 P.2d 769 (1948); *Hogland v. Klein,* 49 Wash.2d 216, 220, 298 P.2d 1099 (1956); *Grant v. Leith,* 67 Wash.2d 234, 235, 407 P.2d 157 (1965); *Falcone v. Perry,* 68 Wash.2d 909, 913, 416 P.2d 690 (1966); *Butler v. Anderson,* 71 Wash.2d 60, 426 P.2d 467 (1967), *overruled on other grounds in Chaplin v. Sanders,* 100 Wash.2d 853, 676 P.2d 431 (1984). *See also* D. Dobbs, *Remedies* § 1.2, at 3, § 3.1, at 135–36. Damages compensate for the injury party's loss.

Restitution stands "in bold contrast" to damages, because it is based upon a benefited party's gain. D. Dobbs, *Remedies* § 3.1, at 137. Restitutionary recovery is appropriate when the defendant has received a benefit under circumstances which make it unjust for him to retain it. *Chandler v. Washington Toll Bridge Auth.,* 17 Wash.2d 591, 601, 137 P.2d 97 (1943).

> "A person confers a benefit upon another if he gives to the other possession of or some other interest in money, land, chattels, or choses in action, *performs services beneficial to or at the request of the other,* satisfies a debt or a duty of the other, or in any way adds to the other's security or advantage. He confers a benefit not only where he adds to the property of another, *but also where he saves the other from expense or loss.* The word 'benefit,' therefore, denotes any form of advantage."

***890** (Italics mine.) *Chandler,* 17 Wash.2d at 602–03, 137 P.2d 97 (quoting Restatement of Restitution, § 1(b), at 12 (1937). The measure of recovery is the reasonable value of the benefit received by the defendant. *Noel v. Cole,* 98 Wash.2d 375, 383, 655 P.2d 245 (1982). Unlike compensatory damages, the amount of a restitutionary recovery can therefore greatly exceed the value of any property harmed. *Olwell v. Nye & Nissen Co.,* 26 Wash.2d 282, 285, 173 P.2d 652, 169 A.L.R. 139 (1946).

B. CERCLA response costs are restitutionary.

CERCLA authorizes the President, acting through the Environmental Protection Agency (EPA), to respond to the release or the substantial threat of a release of any hazardous substance or any pollutant or contaminant which may present an imminent and substantial danger to public health or welfare. 42 U.S.C. § 9604(a)(1); Exec. Order No. 12, 316, 46 Fed.Reg. 42,237 (1981). The EPA has broad authority to take whatever response measures it deems necessary to remove or neutralize ****518** hazardous waste. 42 U.S.C. § 9604; 42 U.S.C. § 9621(a). Alternatively, the EPA may seek injunctive relief to compel "responsible parties" to take necessary response action. 42 U.S.C. § 9606(a). Private citizens also have standing to sue to force compliance with CERCLA. 42 U.S.C. § 9659(a)(1).

CERCLA permits certain governmental bodies (but not private citizens) to recover "damages for injury to, destruction of, or loss of natural resources." 42 U.S.C. § 9607(a)(4)(C). CERCLA does *not* provide for compensation to private individuals for personal injury, property damages and economic losses resulting from releases of hazardous substances. *See* section 4(a) of S. 1480, 96th Cong., 1st Sess., 125 Cong.Rec. 17,991 (1979) (providing for such liability, but eliminated from CERCLA as ultimately passed), *cited in* Brett, *Insuring Against the Innovative Liabilities and Remedies Created by Superfund,* 6 J.Envtl.L. 1, 18 & n. 95 (1986).

***891** Natural resource damages are essentially a compensatory remedy. The measure of natural resource damages is "*the lesser of:* restoration or replacement costs or diminution of use values". (Italics mine.) 43 C.F.R. § 11.35(b)(2). Natural resource damages must be based on actual injury or loss. 42 U.S.C. § 9601(6). They are available only to governmental bodies "act[ing] on behalf of the public as trustee" of the natural resources. 42 U.S.C. § 9607(f)(1). *Artesian Water Co. v. New Castle Cy.,* 851 F.2d 643 (3d Cir.1988). Total liability is limited to the value of the injured property. 42 U.S.C. § 9651(c); 43 C.F.R. § 11.35(b)(2).

In addition to natural resource damages, CERCLA permits both the EPA and other parties to recover costs which they have incurred as a result of a response action from "responsible parties". 42 U.S.C. § 9607(a)(4)(A), (B). Responsible parties include hazardous waste generators, hazardous waste transporters, and hazardous waste disposal facility owners and operators. 42 U.S.C. § 9607(a).

CERCLA defines the term "response" to mean "removal ... and remedial action ... includ[ing] enforcement activities related thereto." 42 U.S.C. § 9601(25). Among the many safety measures identified as potential response actions are monitoring, security fencing, dikes, on-site treatment or incineration, recycling, provision of alternative water supplies, and related enforcement activities. 42 U.S.C. § 9601(23), (24).

CERCLA response cost liability is essentially restitutional:

> When a party, governmental or nongovernmental, incurs response costs it is performing the duty of the responsible party. In seeking recovery of those costs under section 107(a) [42 U.S.C. 9607(a)], that party is asking for the return of money spent on behalf of the responsible party to safeguard public health. Thus, response cost recovery restores the status

> quo by returning to the plaintiff what rightfully belongs to it, rather than compensating the plaintiff for loss sustained to its interest as a result of the responsible parties' wrongful conduct, and is a classic example of equitable restitution.

***892** (Footnotes omitted.) Brett, *Insuring Against the Innovative Liabilities and Remedies Created by Superfund,* 6 J.Envtl.L. 1, 35 (1986).

The contrast between natural resource damage liability and response cost liability further indicates that CERCLA response costs are a restitutionary remedy. First, a responsible party can be held liable for response costs even though there is no property damage to compensate, because no actual release has yet occurred. 42 U.S.C. § 9604. Second, parties without an economic interest in the affected property can maintain an action for response costs. 42 U.S.C. §§ 9607(a)(4)(B), 9659(a). Finally, liability for response costs can greatly exceed the economic value of the affected property. *See* Abraham, *Environmental Liability and the Limits of Insurance,* 88 Colum.L.Rev. 942, 969 (1988).

The contrast between response costs and natural resource damages makes clear that response costs are an equitable restitutionary remedy, not a compensatory damage remedy. *Verlan, Ltd. v. John L. Armitage & Co.,* 695 F.Supp. 950 (N.D.Ill.1988). ****519** Every court that has examined the nature of Superfund response costs liability outside of the insurance context has held that such costs are a form of equitable restitution. *See, e.g., United States v. Northernaire Plating Co.,* 685 F.Supp. 1410 (W.D.Mich.1988) (no right to jury trial); *Wehner v. Syntex Corp.,* 682 F.Supp. 39 (N.D.Cal.1987) (idem); *United States v. Dickerson,* 640 F.Supp. 448 (D.Md.1986) (idem); *United States v. Conservation Chem. Co.,* 619 F.Supp. 162, 206 (W.D.Mo.1985) (permitting assertion of equitable defenses); *Mardan Corp. v. C.G.C. Music, Ltd.,* 600 F.Supp. 1049 (D.Ariz.1984) (idem); *Penn Terra Ltd. v. Department of Envtl. Resources,* 733 F.2d 267, 278 (3d Cir.1984) (response action not automatically stayed under Bankruptcy Code). In fact, this authority is so overwhelming that *even the policyholders admit that "the governmental remedy under CERCLA is equitable."* Brief of Policyholders, at 37. Therefore, this court must also hold that CERCLA response costs are a restitutionary remedy.

***893** II

The Insurance Policies Do Not Cover Restitutionary Remedies

The insurance policies in this case provide that the insurer "will pay on behalf of the insured all sums which the insured shall become legally obligated to pay as damages ... because of ... property damage ..." Certification order, at 3.[FN1] This language unambiguously extends coverage only to compensatory "damages" liability, not claims for restitutionary CERCLA response cost liability.

> FN1. In fact, one of the insurance policies contains slightly different language, providing coverage "for all sums which the Assured shall be obligated to pay ... for damages ... on account of ... [p]roperty damage ..." Certification order, at 3. The majority does not separately address this language, implicitly holding that it has the same effect as that contained in the other policies. Because I agree with the conclusion, I do not separately address this language either.

The majority makes several arguments attempting to show that this language is ambiguous. First, the majority asserts that the language is ambiguous because the policyholders were not subjectively aware of its meaning. Majority, at 510–11, Second, because the phrase "as damages" is "sandwiched into the general coverage provisions", the majority implies that the contract is structurally ambiguous. Majority, at 511. Third, the majority asserts that the "plain, ordinary meaning" of damages can include the costs of complying with coercive and restitutionary remedies. Majority, at 511. Fourth, the majority argues that because "56 judges" have held that identical policy language cover CERCLA response costs, the policy language is ambiguous. Majority, at 511–14. Finally, the majority asserts that ambiguous policy language must be construed against the insurers because the "average lay person" rule of insurance interpretation applies equally to "corporate giant [s]." Majority, at 514.[FN2] I will address each argument in turn.

> FN2. The majority also improperly purports to determine whether CERCLA response cost liability arises "because of ... property damage" within the meaning of these policies. Majority, p. 516. This question was not certified to us by the federal court.

***894** A. The policyholders' subjective understanding of the meaning of the policies is irrelevant.

The majority argues that because these policyholders were subjectively unaware of the meaning of the policy's "as damages" clause, the policy language is unenforceable.[FN3] This argument was not advanced by the policyholders, and it flatly contradicts the law of this State.

> FN3. "Alternatively, before the insurers can avoid indemnifying the policyholders, this court must be satisfied that the plain meaning of "damages", as it would be understood by the average lay person, unmistakably precludes coverage for response costs, and any ambiguity is to be construed against the insurer." Majority, at 510.
>
> > "The court is not persuaded that, under the rules of insurance contract analysis in Washington, the words 'as damages' communicate these restrictions." Majority, at 510–11.

Settled law requires this court to enforce an insurance policy according to its clear meaning and purpose, regardless of the ****520** coverage the insured may have thought he had. *Nevers v. Aetna Ins. Co.,* 14 Wash.App. 906, 908, 546 P.2d 1240 (1976). This court has on several occasions specifically declined to adopt the doctrine of reasonable expectations, under which the insured's subjective expectation of coverage determines the insurer's liability. *Keenan v. Industrial Indem. Ins. Co. of the Northwest,* 108 Wash.2d 314, 322, 738 P.2d 270 (1987); *State Farm Gen. Ins. Co. v. Emerson,* 102 Wash.2d 477, 485, 687 P.2d 1139 (1984). The policyholder's subjective understanding of the "as damages" provision is therefore irrelevant.

B. The policies are not structurally ambiguous.

The majority next implies that because the "as damages" clause is not in an exclusionary provision, but instead "sandwiched into the general coverage provisions," these policies are structurally ambiguous.[FN4] This court has explicitly rejected the doctrine of structural

ambiguity. *State* ***895** *Farm Gen. Ins. Co. v. Emerson,* 102 Wash.2d 477, 484, 687 P.2d 1139 (1984). Moreover the general coverage provisions are exactly where one would expect to find language describing the basic coverage granted.

> FN4. "Here, *the structure of the subject contracts* defeats insurers' argument that 'as damages' precludes coverage for cleanup costs. The subject clause, 'as damages', is sandwiched into the general coverage provisions of policyholders' insurance contracts. This is an odd place to look for exclusions of coverage. Furthermore, there is noting more in the contracts. Under the title 'Exclusions', there is nothing in the enumerated exclusionary provision about 'damages'." (Citation omitted. Italics mine.) Majority, at 511.

The absence of an exclusionary provision, if anything strengthens the argument that "damages" do not encompass restitutionary liabilities like CERCLA response costs. Exclusions subtract from the coverage which an insurance policy would otherwise provide. *See Harrison Plumbing & Heating, Inc. v. New Hampshire Ins. Group,* 37 Wash.App. 621, 627, 681 P.2d 875 (1984). The general coverage provisions of these policies only extend coverage to sums which an insured is legally obligated to pay "as damages." Therefore, they do not provide coverage from which a "damages" exclusion could subtract. These policies are structurally consistent.

C. The phrase "as damages" plainly refers to compensation for injuries.

1. *The standard definition of the word "damages"—reparation for detriment or injury sustained—plainly distinguishes damages from restitution.*

The majority asserts that because standard dictionaries do not explicitly distinguish between "legal" and "equitable" claims, the "as damages" clause can reasonably be interpreted to provide coverage for CERCLA response costs. Standard dictionary definitions of "damages," *including the definition cited by the majority,*[FN5] ****521** in fact unambiguously distinguish damages from restitution. *"Damages" are compensatory* —reparation for detriment or ***896** injury sustained. *CERCLA response cost liability, in contrast, is restitutionary* —reimbursement of a benefit unjustly retained by a responsible party. See *supra.*

> FN5. "Standard dictionaries uniformly define the word 'damages' inclusively, without making any distinction between sums awarded on a 'legal' or 'equitable' claim. For example, *Webster's Third New International Dictionary* 571 (1971) defines 'damages' as 'the estimated reparation in money for detriment or injury sustained'." Majority, at 511.
>
> This dictionary's complete entry for "damages" is:
>
> 3 damages *pl* : the estimated reparation in money for detriment or injury sustained: compensation or satisfaction imposed by law for a wrong or injury caused by a violation of a legal right {bring a suit for s} {was awarded compensatory s of $4000}—compare DAMNUM ABSQUE INJURIA; see COMPENSATORY

> DAMAGES, GENERAL DAMAGES, NOMINAL DAMAGES, PUNITIVE DAMAGES, SPECIAL DAMAGES 4: EXPENSE, COST, CHARGE syn see INJURY
>
> *Webster's Third New International Dictionary* 571 (981).
>
> Numerous other dictionaries contain virtually identical definitions. *See The Random House Dictionary of the English Language* 504 (2d ed. 1987); *The American Heritage Illustrated Encyclopedic Dictionary* 431 (1987); *Collins Cobuild English Language Dictionary* 353–54 (1987); *The Penguin Wordmaster Dictionary* 174 (1987); *Webster's New Universal Unabridged Dictionary* 315 (1983); *The American Heritage Dictionary* 364 (2d College ed. 1982); *Oxford English Dictionary* 14 (1981); *Oxford American Dictionary* 159 (1980); *The Concise Oxford Dictionary* 256 (1976); *Oxford Advanced Learner's Dictionary of Current English* 219 (1974); *Collins English Dictionary* 248 (1972); *Webster's New World Dictionary of the American Language* 356 (2d College ed. 1972); *Cassell's English Dictionary* 282 (1962); *Thorndike–Barnhart Comprehensive Desk Dictionary* 215 (1962); *Oxford English Dictionary* 14 (1961); *Webster's New International Dictionary of the English Language* 664 (2d ed. 1960); *Swan's Anglo–American Dictionary* 435 (1952).

Of course, no dictionary explicitly defines damages as "not equitable relief." Dictionaries define what a word means, not everything a word does not mean. But standard dictionaries' definitions of "damages" do establish that the "plain, ordinary, and popular meaning" of "damages" *is* reparation for detriment or injury sustained. Because CERCLA response costs are not reparation for detriment or injury sustained, they do not fall within the "plain, ordinary and popular meaning" of damages.

2. *The alternative definition of "damages"—cost or expense—is both informal and makes no sense when placed into context in the policy as a whole.*

Unlike the majority, the policyholders recognized that if the word "damages" is given this plain, ordinary meaning, the insurance policies will not cover their CERCLA ***897** response cost liabilities. They therefore vigorously advocate an alternative "cost or expense" interpretation of the word "damages." See Brief of Policyholders, at 11 ("Here, the policyholders are 'legally obligated to pay' the ' *costs* ' of conducting a comprehensive cleanup program ...") (Italics mine.)

The majority does cite *The Random House Dictionary of the English Language* in an attempt to show that damages can also mean "cost or expense". Majority, at 8. The majority neglects to mention that this dictionary labels the "cost or expense" definition informal. The entire definition reads:

> 2. damages, law. the estimated money equivalent for detriment or injury sustained. 3. Often, damages. *Informal.* cost; expense; charge: *What are the damages for the lubrication job on my car?*
>
> *The Random House Dictionary of the English Language* 365 (1973).

This court should reject the "cost or expense" definition for several reasons. First, the phrase "legally obligated to pay as damages" lies at the heart of a legal document, insuring against legal liability. Every dictionary cited indicates that the "compensation" definition is appropriate to a legal context. In contract, every dictionary that evaluates usage describes "cost or expense" as informal, colloquial or slang.FN6

> FN6. Only *Webster's Third New International Dictionary* and the related *Webster's New Collegiate Dictionary* do not identify the "cost or expense" definition of damages as informal, colloquial, or slang. These dictionaries do not specially identify such usages. See E. Sheehy, *Guide to Reference Works* 148 (10th ed. 1986).

Second, the "compensation" definition gives meaning to the "as damages" clause while the "cost or expense" definition renders "as damages" redundant. The "as damages" clause qualifies the phrase "all sums which the insured shall become legally obligated to pay." Certification order, at 3. Amounts payable in reparation for detriment or injury sustained constitute a subset of the amounts an insured is ***898** "legally obligated to pay." The "compensation" definition therefore makes the "as damages" clause meaningfully qualify its referent.

In contrast, if interpreted to mean "cost or expense," the "as damages" clause redundantly repeats its referent. Because all sums which an insured is "legally obligated to pay" already constitute a "cost or expense" to the insured, the "as damages" clause becomes "mere surplusage, because any obligation to pay would be covered." *Maryland Cas. Co. v. Armco, Inc.*, 822 F.2d 1348, 1352 (4th Cir.1987), *cert. denied* 484 U.S. 1008, 108 S.Ct. 703, 98 L.Ed.2d 654 (1988).

****522** This court will give force and effect to each clause of the insurance policy. *Transcontinental Ins. Co. v. Washington Publ. Utils. Dists.' Util. Sys.*, 111 Wash.2d 452, 456, 760 P.2d 337 (1988). The court must therefore reject the "cost or expense" interpretation of damages.

D. Contrary results from other jurisdictions do not make the "as damages" language ambiguous under Washington law.

The majority next emphasizes that "56 judges" have held that "damages" can include CERCLA cleanup costs. Majority, at 511.FN7 While the judicial "head-count" is hardly dispositive, is not nearly as one-sided as the majority implies. In addition to the three cases discussed by the majority, the following reported cases also hold that CERCLA response costs are not covered "as damages": *Cincinnati Ins. Co. v. Milliken & Co.*, 857 F.2d 979 (4th Cir.1988) (applying South Carolina law); *Mraz v. Canadian Universal Ins. Co.*, 804 F.2d 1325 (4th Cir.1986) (applying Illinois law); *Hayes v. Maryland Cas. Co.*, 688 F.Supp.***899** 1513 (N.D.Fla.1988); *Verlan, Ltd. v. John L. Armitage & Co.*, 695 F.Supp. 950 (N.D.Ill.1988).

> FN7. Apparently included in this count are two Washington superior court decisions, as well as numerous unpublished foreign decisions. Neither has any precedential value under Washington law. *See* RAP 10.4(h); *Washington Banker's Ass'n v. Washington Mut. Sav. Bank*, 92 Wash.2d 453, 463, 598 P.2d 719 (1975); *State v. Ross*, 20

> Wash.App. 448, 455 n. 5, 580 P.2d 1110 (1978); *State v. Fitzpatrick*, 5 Wash.App. 661, 668, 491 P.2d 262 (1971).

Of course, the court must reject the policyholders' suggestion that the mere existence of these conflicting decisions establishes that "damages" is ambiguous. The fact that a term in an insurance policy has been construed differently in other jurisdictions does not mean that the term is ambiguous under Washington law. *Crunk v. State Farm Fire & Cas. Co.*, 106 Wash.2d 23, 29–30, 719 P.2d 1338 (1986) (Goodloe, J., concurring), 106 Wash.2d at 31–32, 719 P.2d 1338 (Dore, J. dissenting). The foreign cases discussed by the majority are ultimately important only for the persuasiveness of the reasoning they employ.

These cases are in fact not persuasively reasoned. For example, the stem case that sets out the rationale for holding that "damages" encompass CERCLA response costs is *United States Aviex Co. v. Travelers Ins. Co.*, 125 Mich.App. 579, 589–90, 336 N.W.2d 838 (1983) (quoted in majority, at 10). I disagree with its reasoning.

In *Aviex*, water used in putting out a fire at a chemical manufacturing facility caused toxic chemicals to seep into the ground contaminating the groundwater underneath the manufacturer's property. 336 N.W.2d at 840. The manufacturer brought a declaratory judgment action against its insurer seeking to establish its rights under a standard form liability policy which contained an "as damages" clause identical to those at issue in the present case. 336 N.W.2d at 841, 840.

The appeals court found "persuasive" the insurer's argument that "damages" do not include the costs incurred in complying with injunctive orders. 336 N.W.2d at 842. However, the court noted that under the state act, the State was empowered to file suit "to recover the full value of the injuries done to the natural resources of the state". 125 Mich.App. at 589, 336 N.W.2d at 842–43. Because the court felt it was fortuitous "that the state has chosen to have the plaintiff remedy the contamination problem, rather than choosing to incur the costs of clean-up itself ***900** and then suing plaintiff to recover those costs", the court held that the insurer was liable under the policy. 125 Mich.App. at 590, 336 N.W.2d at 843.

Aviex consists of two syllogisms that do not connect. The *Aviex* court correctly recognized that if the state had sought a compensatory remedy (as state law empowered it to do), the insurance policy would have provided coverage for any resulting liability. The *Aviex* court also correctly recognized that if the insurance policy covered one form of equitable recovery—reimbursement of the state's cleanup costs—it would have been pointless to condition coverage on the form of equitable remedy—injunction****523** or reimbursement—that the state chose to pursue.

Aviex errs by equating the compensatory damage remedy the state could have sought with the equitable remedies which the state in fact sought. The state's choice of remedy fundamentally affected the measure of recovery:

> [T]he distinction between recovery of cleanup costs and recovery of damages is not "merely fortuitous" to either the insured as a CERCLA and RCRA defendant or the insurer. The cost of cleaning up a hazardous waste site often exceeds its original value. On the other hand,

some natural resources are of exceptional value and their destruction could greatly exceed the cost of cleaning up any hazardous waste contamination.

Continental Ins. Cos. v. Northeastern Pharmaceutical & Chem. Co., 842 F.2d 977, 986–87 (8th Cir.1988) (applying Missouri law).

The other foreign cases cited in the majority opinion either depend on *Aviex* or do not involve CERCLA liability. *Aviex* was applied as controlling state law by two of the federal district court decisions the majority cites: *United States Fid. & Guar. Co. v. Thomas Solvent Co.,* 683 F.Supp. 1139, 1168 (W.D.Mich.1988) (cited in majority, at 9, 10) and *Fireman's Fund Ins. Cos. v. Ex–Cell–O Corp.,* 662 F.Supp. 71, 75 (E.D.Mich.1987) (cited in majority, at 511). A third case relies exclusively on *Aviex. Intel Corp. v. Hartford Accident & Indem. Co.,* 692 F.Supp. 1171, 1187 (N.D.Cal.1988) (cited in majority, at 511). Finally, *CPS Chem. Co. v. Continental Ins. Co.,* 222 N.J.Super. 175, 536 ***901** A.2d 311, 316 (1988) (cited in majority, at 511) dealt with an insurer's liability for cleanup costs under a state environmental law, not under CERCLA. Therefore, no foreign case cited by the majority persuasively supports its holding.

E. This court has squarely held that "damages" do not encompass restitutionary liabilities.

The majority's analysis also directly contradicts this court's holding in *Seaboard Sur. Co. v. Ralph Williams' Northwest Chrysler Plymouth, Inc.,* 81 Wash.2d 740, 504 P.2d 1139 (1973). *Seaboard* is virtually indistinguishable from the present case.

In *Seaboard,* the Attorney General brought suit to enjoin an automobile dealer for "unfair methods of competition and unfair or deceptive acts or practices", and for the restitution of property wrongfully withheld by the dealer. 81 Wash.2d at 741–42, 504 P.2d 1139. Like the underlying suit in this action, the underlying suit in *Seaboard* involved a public agency acting to protect the public interest. The court emphasized that the Consumer Protection Act specifically distinguished between injunctive, restitutionary, and damage remedies. 81 Wash.2d at 744–45, 504 P.2d 1139. CERCLA similarly distinguishes between injunctive, restitutionary, and damage remedies.

The insurance policy in *Seaboard* provided coverage for "all sums which the Insured shall become obligated to pay by reason of the liability imposed upon him by law ... for money damages resulting from ... unfair competition". 81 Wash.2d at 741, 504 P.2d 1139. Similarly, the present policies provide coverage for "sums payable as damages because of ... property damage."

In *Seaboard,* the court determined that in an action for damages for unfair competition, the measure of recovery is compensatory, not restitutionary. 81 Wash.2d at 743, 504 P.2d 1139. Because the Attorney General's action only sought injunctive and restitutionary relief, the court held that "the dealer is not faced with the prospect of a judgment *for damages* ..." (Italics mine.) 81 Wash.2d at 744, 504 P.2d 1139. Similarly, although CERCLA provides for compensatory recovery for damages ***902** to natural resources, in the underlying action the EPA has only sought reimbursement of its response costs, a restitutionary form of relief. Therefore, the court should hold that the policyholders are not faced with a judgment payable

"as damages."

According to the majority, *Seaboard* holds that the Attorney General's suit for restitution would result in judgment of "damages" however, the suit seeking such ****524** "damages" for *unfair methods of competition* could not result in a judgment for damages *for unfair competition.* Majority, at 514–15. Given the reasoning in the rest of the majority's opinion, this explanation is totally untenable. If the word "damages" includes restitution, certainly "unfair competition" includes unfair methods of competition.

The majority's reasoning thus completely contradicts both *Seaboard* 's rationale and result. *Seaboard* in fact requires this court to hold that these liability insurers are only required to indemnify their insured's compensatory liabilities, but not the cost of complying with equitable remedies.

The Court of Appeals has also squarely held that a liability insurer is not required to indemnify its insured's restitutionary liability. *Felice v. St. Paul Fire & Marine Ins. Co.,* 42 Wash.App. 352, 357, 711 P.2d 1066 (1985), *review denied,* 105 Wash.2d 1014 (1986).[FN8] Even the policyholders admit that *Felice* reached a proper result, conceding that the "as damages" clause "might also exclude sums paid in restitution of money had and received." Brief of Boeing Co., at 35. If "damages" does not encompass this form of restitution, it also does not encompass CERCLA response costs.

> FN8. The majority purports to distinguish *Felice* on the grounds that "the proceeding was an action to remove the guardian, not a proceeding to recover damages." Majority, at 515 n. 4. In fact, the complaint in *Felice* sought both Felice's removal as guardian, and restitution of attorney fees he had charged. 42 Wash.App. at 355, 711 P.2d 1066. *Felice,* therefore, did involve a proceeding to recover "damages," at least as the majority would interpret the term.

***903** In addition, numerous cases from other jurisdictions hold that liability insurers need not indemnify their insured's restitutionary liabilities, even if payable in money. *See, e.g., Thief River Falls v. United Fire & Cas. Co.,* 336 N.W.2d 274 (Minn.1983); *Ladd Constr. Co. v. Insurance Co. of N. Am.,* 73 Ill.App.3d 43, 29 Ill.Dec. 305, 391 N.E.2d 568 (1979); *Garden Sanctuary, Inc. v. Insurance Co. of N. Am.,* 292 So.2d 75 (Fla.Dist.Ct.App.1974); *Aetna Cas. & Sur. Co. v. Hanna,* 224 F.2d 499 (5th Cir.1955); *Desrochers v. New York Cas. Co.,* 99 N.H. 129, 106 A.2d 196 (1954). For example, in *Desrochers,* the insureds had been enjoined to remove a culvert placed upon their land. In holding the insurer not liable for the cost of complying with the injunction, the court stated:

> The cost of compliance with the mandatory injunction is not reasonably to be regarded as a sum payable "as damages." Damages are recompense for injuries sustained. Restatement, Torts, § 902. They are remedial rather than preventive, and in the usual sense are pecuniary in nature. 1 Sedgwick on Damages (9th ed.) §§ 2, 29. The expense of restoring the plaintiff's property to its former state will not remedy the injury previously done, nor will it be paid to the injured parties....
>
> . . . . .

> ... In short, the expense of complying with the order is neither a sum which the insured is obligated to pay as damages, nor is it in any real sense equivalent thereto. No equitable principle requires the [insurer] to pay it, and it is not within the scope of its undertaking as a reasonable man ... would interpret it.
>
> (Citations omitted.) 99 N.H. at 131–33, 106 A.2d 196.

F. The "average lay person" rule of insurance interpretation does not apply to corporations able to negotiate contract terms from a position of equal bargaining power.

The "as damages" clause in these policies unambiguously limits coverage to compensatory damage remedies, not restitutionary remedies like CERCLA response costs. However, even if the phrase "as damages" were ambiguous, this term should not automatically be construed against the ***904** insurer. The "average lay person" rule of insurance interpretation does not apply to corporate giants.

The principle that ambiguities in insurance policies must be strictly construed against the insurer derives from recognition of the typical relationship between the purchaser or an insurance contract and the ****525** insurance carrier. Ordinarily, the carrier unilaterally drafts the insurance contract and thus, for policy reasons, is held responsible for any ambiguity in the language. *See, e.g., Shell Oil Co. v. Accident & Cas. Ins. Co.,* at 14–15, No. 278953 (Calif.Sup.Ct., San Mateo Cy., July 13, 1988) as reprinted in Brief of Policyholders, Exhibit 2.

This court early on adopted the rule of strictly construing policy language against the insurer in response to this inequality of bargaining power.

> "The policy, although of the standard form, was prepared by insurers, who are presumed to have had their own interests primarily in view; and hence, when the meaning is doubtful, it should be construed most favorably to the insured, who had nothing to do with the preparation thereof."

Montana Stables v. Union Assur. Soc'y, 53 Wash. 274, 276–77, 101 P. 882 (1909) (quoting *Matthews v. American Cent. Ins. Co.,* 154 N.Y. 449, 48 N.E. 751 (1897)). Numerous subsequent cases have reaffirmed both this rule, and the underlying rationale. *See, e.g., Stusser v. Mutual Union Ins. Co.,* 127 Wash. 449, 455, 221 P. 331 (1923); *Guaranty Trust Co. v. Continental Life Ins. Co.,* 159 Wash. 683, 688, 294 P. 585 (1930); *Braley Motor Co. v. Northwest Cas. Co.,* 184 Wash. 47, 52–53, 49 P.2d 911 (1935); *Kane v. Order of United Comm'l Travelers of Am.,* 3 Wash.2d 355, 359–60, 100 P.2d 1036 (1940); *Zinn v. Equitable Life Ins. Co.,* 6 Wash.2d 379, 385, 107 P.2d 921 (1940); *Doke v. United Pac. Ins. Co.,* 15 Wash.2d 536, 544, 131 P.2d 436, 135 P.2d 71 (1942); *Johnson v. State Farm Mut. Auto Ins. Co.,* 70 Wash.2d 587, 590, 424 P.2d 648 (1967); *Safeco Ins. Co. of Am. v. McManemy;* 72 Wash.2d 211, 213, 432 P.2d 537 (1967); *Continental Ins. Co. v. Paccar, Inc.,* 96 Wash.2d 160, 167, 634 P.2d 291 (1981).

***905** The majority acknowledges that at least some of the policyholders in the present case are "corporate giant[s]. Majority, at 514. [FN9] Because these insureds *do* possess the ability and expertise to negotiate the language of the policy, the "average lay person" rule applicable to the typical consumer insurance contract should not extend to this case.

FN9. The majority asserts at page 514 that:

> the policy in question [was] ... prepared by the company's experts, with language selected by the insurer. The specific language in question was not negotiated.
>
> I note that nothing in the District Court's certification order substantiates this recitation of "facts."

In fact, this court has explicitly declined to apply these rules in a case involving a large corporate defendant:

> We are of the opinion that *the rule of construing the policy against the insurer does not fit the circumstances of this case.* Regardless of which party drafted the policy language, it is uncontested that neither party considered proration of the aggregate at the time they agreed on the unambiguous policy terms.

(Italics mine.) *Continental Ins. Co. v. Paccar, Inc.,* 96 Wash.2d 160, 167, 634 P.2d 291 (1981). *See also Transcontinental Ins. Co. v. Washington Pub. Utils. Dists. Util. Sys.,* 111 Wash.2d 452, 456, 760 P.2d 337 (1988). FN10 Indeed, application of such a rule might well unfairly benefit the corporate insured. *See Shell Oil,* at 18 (corporate insured intentionally left ambiguous language unclarified so that rule would apply).

FN10. The italicized language of this quotation simply belies the majority's assertion that *Paccar* "did not hold that a different rule should apply when corporations are involved." Majority, at 514.

III

The Majority's Holding Violates Public Policy

In addition to misapplying pertinent rules of construction, the majority opinion also ignores relevant public policy considerations. "[T]his case implicitly presents a grave question of policy, namely who should bear the cost of polluting our environment[.]" Majority, at 6 n. 1. In interpreting an insurance contract, the court will look to public policy expressed in a relevant legislative enactment. *State* ****526 *906** *Farm Gen. Ins. Co. v. Emerson,* 102 Wash.2d 477, 481, 483, 687 P.2d 1139 (1984). Nevertheless, the majority opines that "[i]t is important to note the absence of public policy in the construction of insurance contracts." Majority, at 510 n. 1. The majority's interpretation of these insurance policies ignores the public policy expressed by the United States Congress in enacting CERCLA.

A. Congressional intent

Congress enacted CERCLA's extraordinarily novel liability provisions in order to impose the cost of cleaning up hazardous waste on those who have "profited or otherwise benefited from commerce involving [hazardous] substances." S.Rep. No. 848, 96th Cong., 2d Sess. 98, reprinted in Senate Comm. on Env't & Pub. Works, *Legislative History of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 Public Law 96–510,* at 308, 320, 97th Cong., 2d Sess. (1980) (statement of EPA administrator Costle). Congress intended that those who financially benefited from polluting activity internalize the health and environmental costs of that activity into their cost of doing business. S.Rep. No. 848, at 34, 13

n. 2. This congressional intent is summarized in the slogan "make the polluter pay." *See* Developments in the Law, *Toxic Waste Litigation,* 99 Harv.L.Rev. 1458, 1477 (1986).

Congress clearly recognized that corporate polluters have reaped enormous benefits from their past inadequate waste disposal practices. These practices created significant short-term savings for polluters, resulting in higher profits for them, but caused enormous long-term harm in the form of environmental degradation. CERCLA response cost liability forces these polluters to disgorge these profits.

The insurers from whom these polluters now seek indemnification, in contrast, did not charge a premium to cover response cost liability. *See* Note, *CERCLA Cleanup Costs Under Comprehensive General Liability Insurance* ***907** *Policies: Property Damage or Economic Damage,* 56 Fordham L.Rev. 1169, 1176 (1988). As Congress itself has recognized CERCLA's innovative provisions were simply unforeseeable at the time these policies were issued. *See* Superfund Amendments and Reauthorization Act of 1986, H.R.Rep. No. 253(I), 99th Cong., 2d Sess., 1, 109, reprinted in 1986 U.S.Code Cong. & Ad.News 2835, 2891 (disapproving "judicial trends regarding policy interpretation that have called upon old policies to pay for claims that were not envisioned at the time the policies were written"). By requiring these insurers to indemnify the corporate polluters for the cost of cleanup, the majority permits the polluters to both reap the benefits and avoid the costs attributable to their pollution. This directly violates the congressional intent that polluters internalize their pollution costs. *See* Brett, *Insuring Against the Innovative Liabilities and Remedies Created by Superfund,* 6 J.Envtl.L. 1, 52 (1986).

B. CERCLA liability is fundamentally uninsurable

The majority holding also violates public policy because it requires insurers to insure liability which is fundamentally uninsurable. The innovative new features of CERCLA's liability scheme simply prevent insurers from calculating and charging premiums that bear any real relation to the risk of CERCLA liability.

CERCLA's liability provisions differ from ordinary tort liability in many important respects. First, CERCLA imposes an especially strict liability upon responsible parties. Liability attaches even to those who nonnegligently dispose of a hazardous substance using state of the art procedures. *See, e.g., United States v. Monsanto Co.,* 858 F.2d 160 (4th Cir.1988); *United States v. Price,* 577 F.Supp. 1103, 1114 (D.N.J.1983).

Second, CERCLA liability is retroactive. Responsible parties who disposed of hazardous waste in a completely legal, nonactionable manner before the enactment of CERCLA are now potentially liable for response costs. *See,* ***908** *e.g., United States v. Hooker Chems. & Plastics Corp.,* 680 F.Supp. 546 (W.D.N.Y.1988).

****527** Third, CERCLA regularly makes individuals liable for harms they did not cause. CERCLA imposes joint and several liability upon every responsible party connected with a hazardous waste site. 42 U.S.C. § 9607. Therefore, both the government and private parties may recover response costs from a "responsible party" with virtually no showing of causation. 1 C. Schraff & R. Steinberg, *RCRA and Superfund: A Practice Guide with Forms,* para.

2.05[3], at 2–26 (1989). *See also New York v. Shore Realty Corp.,* 759 F.2d 1032 (2d Cir.1985) (CERCLA requires no showing of causation).

Fourth, private citizens without any proprietary interest in the property harmed have standing to sue to enforce CERCLA. 42 U.S.C. §§ 9607(a)(4)(B), 9659(a). To recover response costs, a private party need only show an outlay of costs and that the costs were incurred consistently with the National Contingency Plan promulgated by the EPA. *See* Brett, *supra,* at 16 & n. 87.

Fifth, CERCLA authorizes the initiation of response action in response to the *threat* of a hazardous waste release. 42 U.S.C. § 9604. For example CERCLA authorizes the government to recoup the costs of health assessment and health effects studies. 42 U.S.C. § 9607(a)(4)(D). Therefore, responsible parties may be held liable for CERCLA response costs even in the absence of any actual harm to persons or property. *See, e.g., United States v. Northeastern Pharmaceutical & Chem. Co.,* 579 F.Supp. 823 (W.D.Mo.1984).

Sixth, CERCLA response cost liability is inevitable. Every hazardous waste containment system eventually will leak. Because CERCLA imposes liability even if hazardous waste is disposed of in a state of the art manner, every responsible party should expect eventually to be subject to CERCLA response liability.

Seventh, CERCLA response cost liability is essentially boundless, both in amount and duration. The EPA has an ***909** almost unfettered discretion to incur and recoup whatever response cost it believes are necessary to clean up a site. 42 U.S.C. §§ 9604 9621(a). Moreover, because the EPA currently refuses to grant settling parties releases from further litigation, a responsible party's liability exists indefinitely into the future regardless of how much it has paid to clean up a site. *See* Developments in the Law, *Toxic Waste Litigation,* 99 Harv.L.Rev. 1458, 1509 (1986). *But see* 42 U.S.C. § 9622(f) (providing EPA with discretion to enter into covenant not to sue).

CERCLA's broadly worded provisions mean that insurers have no way of predicting what insured conduct may lead to liability. For example, CERCLA defines “pollutant or contaminant” to include “any element, substance, compound, or mixture ... which after release into the environment ... will or may reasonably be anticipated to cause ... [a toxic effect]”. 42 U.S.C. § 9601(33). Because the toxic characteristics of any substance are dose dependent:

> [t]he application of the statute is highly dependent upon *ad hoc* and *post hoc* characterizations of a substance as a “pollutant or contaminant.” ... [Therefore], a party has literally no ability to conform his conduct to the requirements and prohibitions of the Act. A party also has little or no ability to avoid liability for the release of a pollutant or contaminant because he cannot know, in advance, whether any release will constitute actionable or prohibited conduct under CERCLA.

C. Schraff & R. Steinberg, *RCRA and Superfund: A Practice Guide with Forms* para. 1.02[5] at 1–11 (1989). CERCLA's other broadly defined terms create similar problems. *See, e.g., RCRA and Superfund,* para. 1.07.

CERCLA's conferral of standing upon parties who do not satisfy traditional requirements multiplies this uncertainty. "The broad liability provisions given enormous discretion to the responding party in deciding how to incur response costs with virtually no limit on the amounts recoverable." Brett, *supra* at 18.

CERCLA's retroactive strict liability provisions result in liability for the failure to reduce risks that cannot be discovered through the exercise of reasonable care. ****528** An insurer ***910** who undertakes to insure response cost liability will therefore be liable for risks that are undiscovered and largely undiscoverable at the time the actions are taken. "Because the magnitude of such risks is inestimable—they are unknowable when insured against—it is impossible confidently to set a price for insurance against them." Abraham,*Environmental Liability and the Limits of Insurance,* 88 Colum.L.Rev. 942, 957–58 (1988).

Another factor making response costs particularly difficult to insure is CERCLA's imposition of liability for harms a party did not cause. Such liability:

> creates special uncertainty, because the probability of liability—and of consequent loss for the insurer—is affected by the behavior of nonpolicyholders whom the insurer cannot necessarily identify in advance. When the scope of that liability is potentially very large, that uncertainty is magnified.
>
> . . . . .
>
> In order to insure against the threat, insurers would have to make nearly impossible calculations based on both the potential behavior of the other parties whose activities might combine with the insured's to cause damage, and on the probability that these parties would prove to be judgment proof.
>
> Abraham, at 959–60.

Finally, the inevitability of CERCLA response costs renders them totally uninsurable under traditional occurrence-type policies (such as the ones at issue in this case):

> [I]nsurance contracts do not ordinarily cover economic detriment of a type occurring so regularly in relation to an insured enterprise or activity that it is commonly regarded as a cost rather than a risk of that activity or enterprise. Second, insurance contracts do not cover economic detriment that is not fortuitous from the point of view of the person (usually the insured) whose detriment is asserted as the basis of the insurer's liability.
>
> (Footnote omitted.) R. Keeton, *Insurance Law* § 5.3(a), at 278–79 (1971).

For example, it is an "elemental proposition" under Washington law that insurance policies do not cover losses which are expected or intended from the standpoint of the insured, "this generally being ... against public policy to insure." *Detweiler v. J.C. Penney Cas. Ins. Co.*, 110 Wash.2d ***911** 99, 105, 751 P.2d 282 (1988). Thus, where an insured took a calculated business risk that pollution from a sewage plant would contaminate nearby property, we have held that the insured could not look to its insurer to indemnify it for its

liability resulting from its failure to prevent the event. *Tieton v. General Ins. Co. of Am.,* 61 Wash.2d 716, 722, 380 P.2d 127 (1963). Because no containment system can permanently prevent the escape of hazardous waste, polluters who dump their wastes at the very least take a calculated business risk of eventually incurring CERCLA response cost liability.

A congressionally authorized study group report on the availability of private insurance for CERCLA liability recognizes that CERCLA's radically unique approach to the imposition of response costs renders the insured's potential liability so limitless that such liability cannot be assessed by prospective insurers seeking to set premium levels. *See* U.S. Dep't of Treasury, *Adequacy of Private Insurance Protection under Section 107 of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980: A Report in Compliance With Section 301(b) of P.L. 96–105,* at 83–87 & 94–95 (June 1983). In fact, since the enactment of CERCLA, pollution insurance has become unavailable in any insurance market. *E.g.,* Brett, at 44; Smith, Weishaar, Ledbetter & Light, *Hurricane SARA: An Introduction to the 1986 Superfund Amendments,* Toxics L.Rep. 1104, 1110 (1987). The fact that insurers are unable to provide coverage for response cost liability even today highlights the fundamental unfairness of finding such coverage in policies written years before CERCLA's radical new liabilities could possibly have been anticipated.

IV

Conclusion

Congress enacted CERCLA's innovative response cost liability provisions in order to ****529** properly address the threat posed by inadequate past hazardous waste disposal practices. CERCLA liability accordingly differs substantially ***912** from ordinary tort liability. Normal tort liability results in a compensatory "damages" remedy. CERCLA response cost liability, in contrast, results in a restitutionary remedy.

The insurance policies at issue in this case require the insurer to indemnify the insureds for "all sums which the insured shall be legally obligated to pay as damages ..." The plain, ordinary and popular meaning of damages, as recognized by the majority, is "reparation for detriment or injury sustained." Because CERCLA response costs do not constitute reparation for detriment or injury sustained, they do not constitute "damages" within the meaning of these policies. On-point mandatory precedent, the better reasoned foreign cases, and public policy all support this result.

I respectfully dissent.

DOLLIVER, J., concurs.

Wash.,1990.
Boeing Co. v. Aetna Cas. and Sur. Co.
113 Wash.2d 869, 784 P.2d 507, 30 ERC 2001, 87 A.L.R.4th 405, 58 USLW 2447, 20 Envtl. L. Rep. 20,362

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40 Conn. 575, 1874 WL 3166 (Conn.)
(Cite as: 40 Conn. 575, 1874 WL 3166 (Conn.))

Supreme Court of Errors of Connecticut.
William C. Boon and others
v.
The Ætna Insurance Company.

November Term, 1873.

***1** A policy of insurance, made by the defendants against loss by fire, of goods of the plaintiffs, in their store in the city of Glasgow, Missouri, contained the usual proviso in such policies, that "the company shall not be liable to make good any loss or damage by fire, which may happen or take place by means of any invasion, insurrection, riot or civil commotion, or of any military or usurped power." At the time of the insurance Glasgow was a military post, occupied by the forces of the United States engaged in the war of the rebellion, and was a depot for military stores, which were deposited in the city hall. In consequence of an attack made by a superior rebel force, the United States military commander, finding that the city could not be successfully defended, and to prevent the stores from falling into the hands of the rebels, ordered their destruction, and, as the only means of effecting it, the city hall was set on fire; whence the fire spread through three intermediate buildings to the store of the plaintiffs, and burned the insured goods. It was conceded that such setting on fire of the city hall by the military power of the United States was the proximate cause of the fire which destroyed the plaintiffs' goods, unless the attack by the rebels was to be so regarded: and that such firing of the city hall was a lawful act and justified by the exigency and the motive for which it was done. Held-1. That the fire which destroyed the plaintiffs' goods did not happen or take place by means of the attack by the rebels on the city, nor by means of invasion or insurrection, riot, or civil commotion, within the meaning of the proviso in the policy. The attack by the rebels furnished a motive to the setting on fire of the city hall, but was not the proximate cause of the fire. 2. That the terms "military or usurped power," in the proviso, do not include the lawful acts of the military authorities of the government; but relate to organized unlawful force, acting in hostility to the government or in subversion thereof. A fire caused by the lawful orders of the officer in command of the military forces of the United States would not therefore be within the exception. 3. That the defendants were liable for the loss.

In determining the meaning of one of several terms that are associated in a contract, the maxim "noscitur a sociis" is not conclusive; but, in a case of doubt, and where a like meaning will satisfy the requirements of the general purpose, where there is no other clause or expression hostile to the like interpretation, and especially where other considerations tend to support it, the maxim has especial force and significance.

Where there is an excepting clause in a general and positive agreement, the latter should have effect unless the exception clearly withdraws the case from its operation.

It is the duty of an insurance company seeking to limit the operation of its contract of insurance by special provisos or exceptions, to make such limitations in clear terms and not leave the insured in a condition to be misled. The insured may reasonably be held entitled to

rely on a construction favorable to himself where the terms will rationally permit it.

***2** Assumpsit on a policy of fire insurance, brought to the Circuit Court of the United States for the District of Connecticut, and tried, on an issue closed to the court, before *Woodruff*, Circuit Judge, and *Shipman*, District Judge, at the April term, 1874. The facts are sufficiently stated in the opinion.

West Headnotes

Insurance 217 ⚿1823

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1823 k. Exceptions, Exclusions or Limitations. Most Cited Cases
(Formerly 217k146.5(4))

Insurance 217 ⚿1835(2)

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1835 Particular Portions or Provisions of Policies
217k1835(2) k. Exclusions, Exceptions or Limitations. Most Cited Cases
(Formerly 217k146.5(4))

It is the duty of an insurance company, seeking to limit the operation of its contract of insurance by special provisos or exceptions, to make such limitations in clear terms, and not to leave the insured in a condition to be misled; and the insured may reasonably be held entitled to rely on a construction favorable to himself where the terms will rationally permit it.

Insurance 217 ⚿2159

217 Insurance
217XVI Coverage--Property Insurance
217XVI(A) In General
217k2139 Risks or Losses Covered and Exclusions
217k2159 k. War or Civil Commotion; Riot. Most Cited Cases
(Formerly 217k421(3))

A fire policy on merchandise provided that the insurers should not be liable for any loss happening by means of invasion, insurrection, riot, or civil commotion, or of any military or usurped power. In consequence of an attack made on the town by a force of the Confederate army, the United States military commander ordered the destruction of certain stores, in pursuance of which order the city hall was set on fire, from which the fire spread to intermediate buildings and burned the insured merchandise. Held, that the loss was not

occasioned by means of invasion, insurrection, riot, or civil commotion, or by military or usurped power, as the latter terms do not include the lawful acts of the military authorities of the government, but relate only to organized unlawful forces acting in hostility thereto.

Insurance 217 ⚿2165(2)

217 Insurance
217XVI Coverage--Property Insurance
217XVI(A) In General
217k2139 Risks or Losses Covered and Exclusions
217k2165 Proximate Cause
217k2165(2) k. Combined or Concurrent Causes. Most Cited Cases
(Formerly 217k427)

A fire policy on merchandise provided that the insurer should not be liable for any loss happening by means of invasion, insurrection, riot, or civil commotion, or of any military or usurped power. In consequence of an attack made on the town by a force of the Confederate army, the United States military commander ordered the destruction of certain stores, in pursuance of which order the city hall was set on fire, from which the fire spread to intermediate buildings and burned the insured merchandise. Held, that the fire did not happen or take place by means of the Confederate attack on the city, as that attack, though furnishing a motive for the firing of the city hall, was not the proximate cause of the loss.

Contracts 95 ⚿152

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k151 Language of Instrument
95k152 k. In General. Most Cited Cases

Maxim noscitur a sociis is not conclusive in determining the meaning of one of several terms that are associated in a contract.

Contracts 95 ⚿152

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k151 Language of Instrument
95k152 k. In General. Most Cited Cases

Maxim noscitur a sociis has special force and significance in case of doubt and where a like meaning will satisfy requirements of general purpose of contract and there is no other clause or expression hostile to like interpretation.

Contracts 95 ⚿174

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k174 k. Exceptions and Provisos. Most Cited Cases

General and positive agreement should have effect unless exception therein clearly withdraws case from its operation.

F. Fellowes, for the plaintiffs.

G. W. Parsons, for the defendants.

Woodruff, J.

***3** The facts in this case are not doubtful nor in dispute. The action is brought to recover from the defendant the amount of an insurance against loss by fire upon the goods of the plaintiffs in their store in Glasgow, Missouri, in the sum of six thousand dollars. It is founded on a policy executed by the defendant, dated September 2d, 1864, and the goods were destroyed by fire on the 15th day of October, 1864, within the term of the insurance. The loss was sufficiently great to entitle the plaintiffs to recover, if the defendant is liable at all, the whole sum insured. The plaintiffs have complied with all the terms and conditions of the policy, by the payment of premium, furnishing proper preliminary proofs, and compliance with all other requirements. The policy however contained the following express proviso, annexed to the agreement of insurance, and in the body of the policy, namely:

"Provided always and it is hereby declared, that the company shall not be liable to make good any loss or damage by fire which may happen or take place by means of any invasion, insurrection, riot, or civil commotion, or of any military or usurped power, or any loss by theft at or after a fire."

The defense herein rests solely on this proviso, and on the facts which are claimed to bring the plaintiffs' loss within its operation, so as to exempt the defendant from liability under the policy.

At and before the time of the fire in question the city of Glasgow, within which the said store of the plaintiffs was situated, was occupied as a military post by the military forces and portion of the army of the United States engaged in the civil war, then, and for more than three years theretofore, prevailing between the government and the citizens of several southern states, who were in rebellion and seeking to establish an independent government, under the name of "The Confederate States of America."

As such military post, the said city of Glasgow was made the place of deposit of military stores for the use of the army of the United States, which stores were in a building called the city hall of the said city of Glasgow, situated on the same street, and on the same side of the street, and about one hundred and fifty feet distant from the plaintiffs' store, three buildings being located in the intervening space, not however in actual contact with either.

Colonel Chester Harding, an officer of the United States government and in command of the military forces of the United States, held the possession of the city and had lawful charge and control of the military stores aforesaid.

On the said fifteenth of October, 1864, an armed force of the rebels, under military organization, surrounded and attacked the city, at an early hour in the morning, and threw shot and shell into the town, penetrating some buildings and killing soldiers and citizens. The city was defended by Colonel Harding and the military forces under his command, and battle between the loyal troops and the rebel forces continued for many hours. The citizens fled to places of security and no civil government prevailed in the city. The rebel forces were superior in numbers and, after a battle of several hours, drove the forces of the government from their position, compelled their surrender and entered and occupied the said city.

***4** During the battle and when the government troops had been driven from their exterior lines of defence, it became apparent to Colonel Harding that the city could not be successfully defended, and he thereupon, in order to prevent the said military stores from falling into the possession of the rebels, ordered Major Moore, one of the officers under his command, to destroy them. In obedience to that order to destroy the said stores and having no other means of doing so, Major Moore set fire to the city hall, and thereby the said building with its contents was consumed. Without other interference, agency or instrumentality, the fire spread along the line of the street aforesaid to the building next adjacent to the city hall and from building to building, through two other intermediate buildings, to the store of the plaintiffs, and destroyed the same, together with its contents, including the goods insured by the defendant's policy aforesaid.

During this time, and until after the fire had consumed such goods, the battle continued, and no surrender had taken place, nor had the forces of the rebels nor any part thereof obtained the possession of or entered the city.

Upon these facts, and in view of the before mentioned proviso in the policy of insurance, the question arises,-Is the defendant liable for the loss of the plaintiffs' goods, or does that proviso exempt the defendant from liability?

That question depends upon the answer to be given to some other questions, that is to say:

1. It is insisted that, within the just and proper meaning of the proviso, the fire happened by means of the unlawful and rebellious attack upon the city, by forces acting in assumption of usurped power, endeavoring to capture the forces of the United States, obtain possession of territory in the lawful possession and power of the United States, in aid of the usurped rebel government, and to forcibly accomplish its object and designs; that the fire and therefore the destruction of the goods were a military necessity created by such attack by an illegal armed force, and that so they happened by means of the rebellion and the employment of organized forces to effect the object thereof and the actual attempt of such forces to overcome the authority and government of the United States; that this was therefore the direct or proximate cause of the loss, or, in the words of the proviso, “the means” by which the fire, destroying the goods, “happened.”

We think that this reasoning cannot prevail. Fire destroyed the goods. The fire was not communicated to the goods, nor to the building from which it spread, by the rebel forces, nor by any one acting in co-operation with them; nor was it so communicated in any wise in furtherance of the rebellion, its purposes or objects. No act of the rebels, in any physical sense, caused the fire; there is nothing to justify the inference that the rebels would have destroyed the government stores found in the city hall, by fire or otherwise, nor to justify the inference that the destruction of the goods or any loss thereof would have happened to the plaintiffs by the capture and the occupation of the city by the rebels. As matter of fact there was no connection, direct or by necessary inference, between such destruction of the goods and the attack of the rebels, the capture of the United States forces and the occupation of the city.

***5** But it is said that such attack by a superior armed force created a military necessity that the government stores should be destroyed; which destruction, in the manner in which alone it could be done, involved the destruction of the plaintiffs' goods, and so that destruction was the necessary result of the attack; that the fire, being thus the necessary result of the attack, it ""happened by means thereof."

The fire was actually and voluntarily communicated to the city hall by the military authority of the United States. It is conceded on this trial that, in the exigency, it was a lawful exercise of such military authority. The power was discretionary, and, if the circumstances were such as made it discreet,-and no doubt they were,-such setting fire to the city hall may have been a duty. In saying that it was voluntary we only mean that it was not a physical necessity, nor the physical result of any agency or act of the rebels or of their unlawful or usurped power. It was physically independent of them, hostile to them, and an act which they not only did not commit but would not have committed, and would if possible have prevented.

What is called a military necessity was therefore nothing more than this; it constituted the motive, and no doubt the sufficient motive, to the burning of the city hall. This was not even an act of resistance to the attack upon the city; it was no part of the defence, nor a force employed in any wise in maintenance of the authority or possession of the government. It was done in the exercise of military discretion for the incidental purpose of preventing an accession to the means of the rebels for maintaining their rebellion. The importance of preventing such an accession to their means furnished a motive, and it may be conceded a controlling motive, to the burning of the city hall, but that did not make the fire happen *by means* of anything done by them. In a certain sense it may be true that the city hall was set on fire *by reason* of the attack upon the city by an armed force of rebels, but between that attack and the fire was interposed another actor who caused the fire, who set in operation the means by which it happened. An efficient and a sufficient cause of fire, and the means by which it happened, intervened between the acts of the rebels and the fire itself, and a cause or means without which, (notwithstanding the acts of the rebels,) the fire would not have happened at all.

In the language of Mr. Justice Miller, in the Supreme Court of the United States, in *Insurance Co. v. Tweed*, (7 Wallace, 52,) "If a new force or power has intervened, of itself sufficient to stand as the cause of the misfortune, the other must be considered as too remote."

That language was used in reference to a similar provision in a policy of insurance, and in aid of the enquiry by what "means" the fire happened. There, as in this case, there was, in some sense, another cause but for which the fire would not have happened at all. And the opinion shows that the existence of just such an influential cause is not enough to bring a case within the proviso. The facts here are much stronger than the reasoning there, in withdrawal of the case from the operation of the proviso, because, although the fire would not have happened but for the existence of such remote cause, (the attack by the rebels,) it is equally true that such remote cause would not have produced the fire at all.

***6** To apply the criterion suggested by Mr. Justice Miller, there was here the intervention of distinct, new, affirmative power and force, other than the acts of the rebels, not only sufficient but efficient as the cause of the fire in the city hall, and the actual means by which it happened.

We think therefore that it cannot be held that, within the meaning of the proviso in question, the fire which destroyed the plaintiffs' goods happened by means of the rebellion or of anything done by the rebel forces.

2. An obvious enquiry is suggested by the facts stated:-Whether the setting on fire of the city hall was the cause of the loss in such sense that, within the proviso, it was "the means" by which the fire happened? or whether that also was not the remote cause of the fire which destroyed the plaintiffs' goods.

In our preceding discussion we have assumed that the setting on fire of the city hall was the means of the fire to the plaintiffs' goods, within that proviso, unless the rebellion or the acts of the rebels should be held such means; that in this sense the acts of the lawful military authorities of the United States were the proximate and efficient cause and means by which the fire happened and of the destruction of those goods by fire.

We do not find it necessary to discuss the question, what was the proximate and what was the remote cause of such destruction, under this head. The suggestion that the setting on fire of the city hall was only the remote cause, while the casual and incidental communication of the fire to the plaintiffs' store from the burning building next adjacent thereto was the proximate cause of the fire and the means by which the fire happened, is not made by the counsel for either of the parties. The contrary is conceded, if not insisted upon, by both. The decision by the Supreme Court in *Insurance Co. v. Tweed*, was assumed by both to be decisive against such a suggestion. We are therefore not called upon to pursue that subject.

3. It remains to consider the claim of the defendant, that the fire happened by means which exempt the company from liability upon the ground that it was caused by "military power," and was therefore within the very words of the proviso.

It is insisted by the plaintiffs that the word "military," in the connection in which it is found in the proviso, does not mean the lawful military power of the government, acting lawfully, in the performance of the proper duty of the government forces, whether engaged in hostile contest with an invading army or in a forcible endeavor to suppress an internal rebellion.

For reasons which seem to us convincing we are of opinion that the word ""military," in the proviso in question, has no reference to the lawful acts of the military power of the government. Neither the reasons for the insertion of the proviso in policies of insurance against fire, nor the history of that insertion, nor any judicial decisions upon the meaning and purport of the proviso, nor the discussions had upon its construction, with especial reference to the meaning of other terms employed therein, sustain the interpretation for which the defendant contends. It is true that the precise question, what is the import and legal effect of the word "military," does not appear to have been decided in any case to which our attention is called. And had that proviso been now for the first time employed to exempt the defendant from a portion of the liability which the preceding general agreement for insurance imports, there would be much plausibility in the argument that the defendant intended not only to exclude liability for the consequences of an insurrection, invasion or rebellion, but for the possible consequences of those violent and forcible means which may be necessary to repel or suppress it. And yet, if this was the intent, it may be pertinently asked, why was the exemption limited to the employment of military force and not made to include the forcible or violent measures which municipal authorities or police organizations might find it necessary to employ to suppress a riot, insurrection, or civil commotion?

***7** The proviso containing the words "military or usurped power," was inserted in policies as early as 1720, and the history of the subject, as given in Ellis on Insurance, page 41, Park on Insurance, page 657, and Marshall on Insurance, page 791, shows that the occasion thereof was manifestly the liability to loss by fire caused by a foreign enemy and invasion. And the terms "military or usurped power" were used in reference to the existence of claims to the exercise of governmental authority, enforced within the kingdom and constituting rebellion against the recognized government. The clause originally embraced no other terms than were apt to indicate the violence of enemies from abroad, and of usurpation exercising governmental authority, or rebellion sustained by organized forces within the kingdom.

The exception as then introduced into policies read as follows: "No loss or damage by fire happening by any invasion, foreign enemy, or any military or usurped power whatsoever, will be made good by this company." The idea of interference with the peace and safety of the realm, by organized force from abroad or rebellion rising to the proportions of actual or at least formal usurpation of governmental authority, (whether more or less successful,) and manifestly hostile to the lawful government, is indicated by this language. The experience of the country, in those days of not infrequent invasion and rebellion, the result of disputes touching the right or the succession to the crown of England, gave occasion for the exception, and by suggesting its cause furnished also an explanation of its meaning. Foreign invading armies and the organized forces, rallied in whole or in part within the kingdom, to overturn the government or to enforce the alleged title of a claimant to the crown, usurping or endeavoring forcibly to usurp governmental authority, were in view. Reason for refusing to become liable for losses caused by these forces, in either form, is found, not only in helplessness and inability to resist them and the magnitude of the destruction they may affect, but in the want of recourse for indemnity to those who commit the violence.

It is well and pertinently suggested that, while on the one hand no one would think of obtaining insurance against the lawful acts of the government, so on the other an insurer

would not think of excepting such lawful acts as a cause of the fire against which he insured. The citizen without insurance and an insurer making insurance, if that contingency was contemplated, would regard his government as bound and presumptively always ready to indemnify against losses sustained by acts done in its own defense or in maintaining the authority of the laws.

The subsequent extension of the proviso to "riot, insurrection and civil commotion," rather confirms than impairs this view of the meaning and intent of the original proviso. And these were held to import occasional, local or temporary out-breaks or lawless violence, which, though temporarily destructive in their effects, did not rise to the proportions of organized rebellion against the government.

***8** The observations made by the court in the few early cases in which this proviso came under consideration, (although any possible separate meaning of the word "military" is not suggested), indicate that the clause has reference to acts done in disregard or in subversion of lawful authority, and includes only such affirmative acts. *Drinkwater v. London Assurance Corporation*, 2 Wilson, 363; *Langdale v. Mason*, referred to by the text writers above cited.

In the last named case Lord Mansfield uses this significant language:-"What is meant by military or usurped power? They are ambiguous and they seem to have been the subject of a question and determination. They must mean rebellion when the fire is made by authority; as in the year 1745, the rebels came to Derby, and, if *they* had ordered any part of the town or a single house to be set on fire, *that* would have been by authority of a rebellion. That is the only distinction in the case. It must be by rebellion got to such a head as to be under authority."

The term "military" is employed in the proviso in a meaning synonymous with the "usurped power" intended to be described, or as qualifying and explaning what was meant by "usurped power." It was in this view, and as a ground of distinguishing between the usurped power specified in the proviso and the power of a mob, that Mr. Justice Bathurst, in the case of *Drinkwater v. London Assurance Corporation*, construed usurped power to mean either an invasion by foreign enemies, to give laws and usurp the government thereof, or an internal force or rebellion, assuming the power of the government, by making laws and punishing for not obeying those laws.

An "invasion" necessarily supposed organization and military power or force; so of the words "foreign enemy;" and in the use of a phrase which should include also violence within the kingdom, viz: "military or usurped power," something in like manner hostile to or subversive of the laws and of lawful government was intended, as plainly as if the clause had been "or any other military or usurped power."

That the terms used in the proviso have express application to force illegally employed and adversely to the government, is indirectly but impliedly involved in the decision and opinion of the court in *the City Fire Ins. Co. v. Corlies*, 21 Wendell, 367. The court deemed the meaning of the words "usurped power" long settled. The property there in question was destroyed by order of the mayor of the city of New York, for the purpose of arresting a

conflagration. It was claimed that this was a usurpation of power and authority in disregard of the law. The court deemed that, if the mayor had no authority to do the act, the company were still liable, for that it was not a usurpation of the power of government, against which the defendants intended to protect themselves.

The case of *Sprull v. North Carolina Ins. Co.*, 1 Jones N. Car. Law R., 126, tends strongly in the same direction; and if an armed patrol may be deemed a ""military power," that case is especially pointed and significant.

***9** These considerations, and the significant fact that every other word used in this proviso to designate the means by which a fire may happen for which the company will not be liable, expresses clearly and unequivocally what is unlawful, employed in disregard or in subversion of the laws or the government, furnish a strong case for the application of the maxim relied upon by the plaintiffs, *noscitur a sociis*. This maxim is not conclusive, but, in a case of doubt, and where a like meaning will satisfy the provision, where there is no other clause or language hostile to the like interpretation, and especially when other considerations tend to support it, the maxim has especial force and significance.

We think it not too much to say that most, if not all, intelligent readers of the proviso in question, would at once declare that the word "military" therein was employed in a sense kindred to the other terms, and that it described an organization military in its form, but unlawful and hostile to the government in its character and purpose.

Again, it is a familiar rule in the construction of provisos and exceptions of this sort, made in qualification of the general positive agreement, that words susceptible of either construction should be taken most strongly against the speaker or party whose language is to be interpreted; and that the general and positive agreement should have effect unless the exception clearly withdraws the case from its operation. This has especial force when the other considerations pertaining to the subject tend to the same result.

To this should be added, that it is the duty of an insurance company seeking to limit the operation of its contract of insurance by special provisos or exceptions, to make such limitations in clear terms and not leave the insured in a condition to be misled. The uncertainties arising from provisos, exceptions, qualifications and special conditions in or endorsed upon policies, have been often condemned, and such special modifications are justly characterized as traps to deceive and catch the unwary. An insured may reasonably be held entitled to rely on a construction favorable to himself where the terms will rationally permit it. Where, as in this case, such construction gives a signification to a word *ejusdem generis* with all those with which it is found associated and in harmony with the general character and purpose of the provision in which they are found, he is clearly entitled to insist upon such construction.

Our conclusion is that the plaintiffs are entitled to judgment for the amount of the insurance, with interest thereon from the expiration of sixty days from the 2d day of May, 1865, on which day it is admitted the preliminary proofs of loss were furnished to the defendant and with costs.

Conn. 1873.
Boon v. Aetna Ins. Co.
40 Conn. 575, 1874 WL 3166 (Conn.)

END OF DOCUMENT

Supreme Court of Texas.
BROWN
v.
PALATINE INS. CO.

May 25, 1896.

Error to court of civil appeals of Fourth supreme judicial district.

Action by N. Brown against the Palatine Insurance Company to recover on a fire insurance policy. There was judgment for plaintiff, which was reversed by the court of civil appeals (34 S. W. 462), and plaintiff brings error. Reversed.

West Headnotes

Insurance 217 ⚿1813

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1811 Intention
217k1813 k. Language of policies. Most Cited Cases
(Formerly 217k146.3(2))

The language used in an insurance policy must be construed according to the evident intent of the parties, to be derived from the words used, the subject-matter to which they relate, and the matters naturally or usually incident thereto.

Insurance 217 ⚿1806

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1806 k. Application of rules of contract construction. Most Cited Cases
(Formerly 217k146.6)

Insurance 217 ⚿1829

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1829 k. Liberal or strict construction. Most Cited Cases
(Formerly 217k146.6)

In the construction of policies of insurance, the same rules of law will be applied as in the

construction of contracts made between individuals under like conditions, and no greater strictness is required in the performance of the one than the other.

Insurance 217 ⚿1831

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1831 k. In general. Most Cited Cases
(Formerly 217k146.7(1))

A contract of insurance prepared by an insurance company will be construed liberally as against the insured and strictly as against the company.

Insurance 217 ⚿1835(1)

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1835 Particular Portions or Provisions of Policies
217k1835(1) k. In general. Most Cited Cases
(Formerly 217k146.8)

All provisions tending to work a forfeiture should be construed most strongly against the insurer.

Insurance 217 ⚿3054(1)

217 Insurance
217XXV Forfeiture
217XXV(B) Particular Kinds of Insurance
217k3047 Property and Title Insurance
217k3054 Keeping Books, Papers, and Safe
217k3054(1) k. In general. Most Cited Cases
(Formerly 217k335(4))

Where it was the custom of the insured to enter the credit sales each day upon a blotter, entries being afterwards transferred to the regular books of account, the failure to produce a record of the credit sales of the day before the fire, because of the destruction of the blotter, which was not placed in the safe at night, is not a violation of the condition in a fire insurance policy providing that the insured shall keep a set of books, showing the cash and credit sales, in a fireproof safe, and that failure to produce such books shall avoid the policy.

***593 **1060** M. B. Templeton and Crawford & Crawford, for plaintiff in error.

Morgan & Thompson, for defendant in error.

***594** BROWN, J.

The Palatine Insurance Company, of Manchester, England, issued to N. Brown, on his stock of goods, an insurance policy for the sum of $1,500, which contained the following condition: 'The insured, under this policy, covenants and warrants to keep a set of books showing a record of business transacted, including all purchases and sales both for cash and credit, together with the last inventory of the stock insured, and further covenants and warrants to keep such books and inventory securely locked in a fireproof safe at night, and at all times when the store mentioned in the within policy is not actually open for business, or in some secure place not exposed to a fire which would destroy the house where such business is carried on; and in case of loss the assured warrants and covenants to produce such books and inventory, and in the event of a failure to produce the same this policy shall be deemed null and void, and no suit or action at law shall be maintained thereon for such loss.' The defendant insurance company pleaded that plaintiff had failed to keep and produce the set of books required by the terms of the policy, whereby the policy was forfeited. Plaintiff kept and produced a set of books which were in compliance with the requirements of the policy, except that the sales for the day on which the fire occurred were entered by the clerks on small books known as 'blotters,' as usual, which it was customary to transfer to books of more substantial character, but the blotters for that day were left out of the safe, and destroyed by the fire, and the sales had not been entered upon the journal. The books showed the sales on credit for the three preceding days to have been, respectively, $65, $70, and $76. The fire occurred without fault on the part of plaintiff, and he had on hand at the time goods to an amount sufficient to entitle him to recover the amount of the judgment of the district court, if the policy was not forfeited. Trial was had below before the judge, who found that the books kept by plaintiff complied with the requirements of the policy, and gave judgment for plaintiff for $1,353.12, which was reversed by the court of civil appeals, and judgment rendered in favor of defendant.

It the construction of policies of insurance, the same rules of law will be applied as in the construction of contracts made between individuals under like conditions, and no greater strictness is required in the performance of the one than the other. Hoose v. Insurance Co., 84 Mich. 317, 47 N. W. 587; Insurance Co. v. Cherry, 84 Va. 75, 3 S. E. 876. It is often said that a warranty in an insurance policy must be strictly complied with, and sometimes it is said that it must be literally fulfilled; but this is no more true of that character of contract than of others, and means no more than that when the language is clear it must be performed as expressed, ***595** which is equally true of all kinds of written undertakings. The same is true of such instrument when the language calls for construction; for when the meaning and intent are arrived at, whether it be explicitly expressed in the words, or derived from them and attending circumstances, that intention ****1061** must govern, in enforcing the contract. Goddard v. Insurance Co., 67 Tex. 71, 1 S. W. 906. It is, however, unnecessary for us to discuss the question as to whether the compliance must be strict, or may be substantial; for in the case now before us the real question is, what did the parties intend to prescribe as the measure of duty on the part of the insured in keeping the books? Did the insured undertake to keep a set of books absolutely correct, by the entry of every business transaction, and of the sale of each article of merchandise? It is not so written in the policy, and can only be claimed as the intention of the parties, to be ascertained from a construction of the language used. Since the

language calls for construction to determine what the parties intended, that construction must be governed by the following familiar rules of law: First. The language being selected and used by the insurer to express the terms and conditions upon which it issued, the policy will be strictly construed against it, and liberally in favor of the insured. If the words admit of two constructions, that one will be adopted most favorable to the insured. Wood, Ins. § 60; Bills v. Insurance Co., 87 Tex. 551, 29 S. W. 1063; Goddard v. Insurance Co., 67 Tex. 71, 1 S. W. 906; Insurance Co. v. Hazlewood, 75 Tex. 347, 12 S. W. 621. Second. The language used must be construed according to the evident intent of the parties, to be derived from the words used, the subject-matter to which they relate, and the matters naturally or usually incident thereto. Wood, Ins. §§ 182–187; Whitney v. Insurance Co., 72 N. Y. 117. Third. Forfeitures are not favored by the law, and if the language used is fairly susceptible of an interpretation which will prevent a forfeiture, it will be so construed. 1 Wood, Ins. § 181, p. 436.

The subject to which this warranty relates is the keeping of a set of books in a mercantile business, in which the sales were to be made and recorded by a number of clerks, and, when so made, to be transferred by other employés. In other words, it was a business to be transacted for the insured by employés. It is a matter of common knowledge that absolute accuracy in such business is unattainable, and it would be perhaps an impossible thing to find a set of books which would show the transactions of such business with the accuracy claimed by the insurance company. These things must have been in contemplation of the parties when the contract was made, and it will not be presumed that the parties intended to prescribe that which was practically impossible. A substantial performance of the contract would suffice, in such case; that is, the contract is to be construed as including no more than could be reasonably expected of the insured. Wood, Ins. §§ 187–189. The purpose of introducing the warranty into the policy should also ***596** be considered, in construing its language, and in determining whether or not the intent and meaning of the language had been complied with, in the manner of keeping the books. The evident object on the part of the insurance company was to require of the insured to preserve such evidence as would enable it, with reasonable certainty, to arrive at the amount of loss, in case the property should be destroyed by fire, and it should be called upon to perform its contract of insurance, and thereby to guard itself against fraudulent and wrongful claims. If the books kept and produced by the insured served the purpose in view, it should be held a compliance with the contract. Considering the language used, the character of the business, and the purposes to be served, we think that the insured had a right to understand that he was to use that care which a prudent man engaged in like business would use in keeping the set of books required by the warranty, and that he should keep such a record of his business as would reasonably afford the insurer evidence of the condition of that business, and the amount of the loss sustained by him. If the contention of the insurance company be sustained, it will lead to the result that if, in the course of the business, the clerks of the insured should omit the entry of a single sale, whether for cash or credit, during the time of the continuance of the policy, this omission would work an absolute forfeiture of the insurance. We do not think that a contract with reference to such a subject should be construed with that strictness, and under the general rules, well established, that forfeitures are not favored, and that the language employed will be so construed as to sustain the contract, rather than to destroy it, we feel constrained to hold that the contract in this case did not mean, and was not intended to mean, that by any slight and trivial error in keeping the

books of the business the insured should suffer a forfeiture, and the insurer be free from liability upon its contract.

Whether Brown complied with the warranty—that is, did those things which, by the true intent and meaning of the contract, he undertook to do—was a question of fact, and the judge before whom the case was tried without a jury found as a fact that he had complied with the terms of his contract. The court of civil appeals did not find the facts to be different from those found by the trial court, but held, as a matter of law, that the omission to enter the sales of one day upon the books of the business worked a forfeiture of the contract, and, upon this legal conclusion, reversed the judgment of the district court, and rendered judgment for the insurance company. Unless it can be said—which we think it cannot—that the language of the contract absolutely required that every sale should be entered, it cannot be held, as a matter of law, that the failure to enter the sales of one day works a forfeiture of the contract. It appears from the findings of fact by the trial court that the condition of the ****1062** books was such that the insurer could ascertain therefrom with reasonable certainty what the loss was that it was called upon to meet. The books showed the sales for each day preceding the fire, and especially for the few days next preceding, and it could well be presumed***597** that the sales were practically the same as upon the days immediately preceding the fire. The purpose, then, for which the warranty was made, was fully subserved by the construction that we place upon it, and the rights of the insurance company were fully protected and guarded by the rules laid down. It might be the case that the sales of one day might be so heavy, so unusual, that a jury or a court would find that the failure to enter them was a failure to comply with the true meaning of the contract, but the facts before us do not justify any such conclusion. We therefore hold that the court of civil appeals erred in reversing the judgment of the district court and in rendering judgment for the insurance company, and therefore reverse the judgment of the court of civil appeals, and affirm the judgment of the district court.

Tex. 1896
Brown v. Palatine Ins. Co.
89 Tex. 590, 35 S.W. 1060

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64 Ill. 265, 1872 WL 8304 (Ill.), 16 Am.Rep. 557
(Cite as: 64 Ill. 265, 1872 WL 8304 (Ill.))

Supreme Court of Illinois.
COMMERCIAL INSURANCE COMPANY
v.
ISAAC S. ROBINSON.

September Term, 1872.

West Headnotes

Insurance 217 ⚿2143(1)

217 Insurance
217XVI Coverage--Property Insurance
217XVI(A) In General
217k2139 Risks or Losses Covered and Exclusions
217k2143 Fire or Smoke
217k2143(1) k. In General. Most Cited Cases
(Formerly 217k421(3))

Insurance 217 ⚿2151

217 Insurance
217XVI Coverage--Property Insurance
217XVI(A) In General
217k2139 Risks or Losses Covered and Exclusions
217k2151 k. Explosion. Most Cited Cases
(Formerly 217k421(3))

Insurance 217 ⚿2165(2)

217 Insurance
217XVI Coverage--Property Insurance
217XVI(A) In General
217k2139 Risks or Losses Covered and Exclusions
217k2165 Proximate Cause
217k2165(2) k. Combined or Concurrent Causes. Most Cited Cases
(Formerly 217k421(3))

Under the rule that equivocal expressions in a policy, which would narrow the range of the company's obligations, must be construed most strongly against the company, a provision that the company should not be liable “for any loss by fire caused by means of an insurrection,” etc., “nor for any loss caused by explosion,” etc., “of any kind,” does not exempt the company from liability for loss by fire caused by an explosion, but only from liability for loss caused by explosion.

64 Ill. 265, 1872 WL 8304 (Ill.), 16 Am.Rep. 557
(Cite as: 64 Ill. 265, 1872 WL 8304 (Ill.))

Insurance 217 ⚿3256

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(B) Claim Procedures
217XXVII(B)6 Appraisal
217k3256 k. Appraisers. Most Cited Cases
(Formerly 217k568)

Where a fire insurance company objected to the inventory of loss furnished by the assured, but made no offer to have appraisers "mutually appointed," as provided in the policy, it was not incumbent on the assured to move further towards their appointment.

***1** APPEAL from the Superior Court of Chicago; the Hon. WILLIAM A. PORTER, Judge, presiding.

This was an action on a policy of insurance. The policy contained, among other provisions, the following: "When personal property is damaged, the assured shall forthwith cause it to be put in order, assorting and arranging the various articles according to their kinds, separating the damaged from the undamaged, and shall cause an inventory to be made, and furnished to the company, of the whole, naming the quantity, quality and cost of each article. The amount of sound value and of damage shall then be ascertained by appraisal of each article by competent persons (not interested in the loss as creditors or otherwise, nor related to the assured or sufferers), to be mutually appointed by the assured and the company; their report in writing to be made under oath before any magistrate or other properly commissioned person; one-half of the appraisers' fees to be paid by the assured. The company reserves the right to take the whole or any part of the articles at their appraised value; and until such proofs, declarations and certificates are produced, and examinations and appraisals to be permitted by the claimant, the loss shall not be payable."

A trial by jury in the circuit court resulted in a verdict and judgment for the plaintiff. The defendant appeals.
Mr. O. B. SANSUM, and Messrs. DENT & BLACK, for the appellant.

Messrs. E. & A. VANBUREN, for the appellee.

Mr. CHIEF JUSTICE LAWRENCE delivered the opinion of the Court:
The policy in this case provided that the company should not be liable "for any loss or damage by fire caused by means of an invasion, insurrection, riot, civil commotion or military or usurped power; * * * nor for any loss caused by the explosion of gunpowder, camphene, or any explosive substance, or explosion of any kind."

The main question is as to the construction to be given to this last clause. It is contended by counsel for the company that it protects the company from liability for any loss by fire where the fire has been produced by an explosion. It is insisted on the other hand, by counsel for appellee, that the clause protects the company only against losses occasioned directly by

an explosion, and not against losses from fire where the fire has been caused by an explosion.

Counsel for appellant, in support of their position, cite *St. John v. Am. Mut. Ins. Co.* 1 Kernan, 516; *Haynard v. Liverpool and London Ins. Co.* 7 Bosw. 385, and *Stanley v. West. Ins. Co.* 3 Exch. 71.

In the case in 1 Kernan, the court of appeals was divided. We have read the opinions of the majority and minority of the court, and consider the reasoning of the latter the more satisfactory. Even the majority of the court did not agree upon the grounds for affirming the judgment of the lower court. As pointed out in the dissenting opinion, the judgment was affirmed not merely upon different, but adverse reasons. The case is, therefore, worth little as authority. The case in 7 Bosw. is not correctly stated by counsel for appellant. In that case there were two clauses in the policy. Counsel gave but one. The other was explicit and, in terms, excluded liability for losses by fire arising from an explosion. The English case cited is in point for appellant.

***2** If this were a question as to an alleged rule or principle of the common law, with these authorities cited on the one side, and none upon the other, we might repose securely upon them, and hold them decisive of the case before us. But it is simply a question as to the interpretation of a few words in a written instrument which are susceptible of two different interpretations. We are to determine which is the more reasonable construction, and if our judgment is satisfied on this point, we must accept its conclusions, though differing from those of the courts to which reference has been made.

Let us remark, in the first place, that equivocal expressions in a policy of insurance, whereby it is sought to narrow the range of the obligations these companies profess to assume, are to be interpreted most strongly against the company. *Aurora Fire Ins. Co. v. Eddy*, 49 Ill. 106. The companies have the preparation of their own policies, the choice of language in which to express their obligations, and they show a studious solicitude to limit their liability. Their policies are prolix with provisions of this character, and the public must accept them or go without insurance. We have no right to censure the companies for this, and do not, but the reading of a policy furnishes a sufficient reason for the rule of interpretation formerly laid down by this court.

It will be observed that, in a clause of the policy preceding the one under consideration, the company stipulated that it should not be liable “for any loss or damage *by fire* caused by means of an invasion, insurrection,” etc. Here exemption is specially secured against liability for losses *by fire* caused in a certain manner. But the clause under consideration leaves out the words “by fire.” It secures exemption from liability for losses caused by explosion, but not from liability for losses *by fire* caused by explosion. The difference in phraseology between the two clauses is so marked, that, when we consider their connection with each other, we can not resist the conclusion that the difference was intended.

Whether the difference was intended or not, can not be certainly ascertained, but it is reasonable to resolve the doubt against the company. The object of the company's existence is to insure against fire. That is what it holds itself out to the public as able and willing to do.

When a person takes out a policy, and pays his premium, he takes it for granted, without reading his policy, that he can not be permitted to make the risk more hazardous to the company by storing highly inflammable materials upon his premises. He knows that would be acting in bad faith with the company, and that the policy has probably provided against it. But he would have no reason to suppose that, among the voluminous stipulations of the policy, there would be found one intended to deprive him of its benefit because a fire, which has destroyed his property, originated in another house a half mile distant, in the explosion of a camphene lamp. Most fires originate in acts of carelessness, and it is chiefly to guard themselves against the carelessnes of others that prudent persons insure. Yet the construction of this policy contended for by the company would make the assured assume the liability for the carelessness of others. He is thus deprived of the very protection he seeks by his insurance if, when his house burns up, he can be denied the payment of his policy because the fire was caused by an explosion upon the premises of others. The great fire of Chicago is supposed to have originated in the overturning and explosion of a lamp, but we are not aware that any of the insurance companies that suffered by that fire have sought to interpose this defense, although this clause is a very common one in insurance policies, and was probably contained in many that had been issued on the property then destroyed.

***3** Counsel for the company, feeling the unreasonable character of this condition, with their interpretation, in cases where the fire comes from an explosion on other premises, speak of it as if it referred only to explosions on the premises of the assured. But the policy will bear no such construction or limitation. We must either hold that the clause refers to loss by explosions simply, without reference to fire, or to losses by fire caused by explosion anywhere, whether on or remote from the premises. There is no middle term. It must receive one of these constructions or the other. One is consistent with the context, reasonable in itself, and just to both parties. The other requires the interpolation of two additional words in the policy, is inconsistent with the context, and in a large degree would make fire insurance a mere mockery. We can not hesitate which construction to choose.

But, say the counsel for appellant, this company does not profess to insure against losses by explosion, but only by fire, and the clause, construed as we construe it, is unmeaning, or at least useless. But not so. The clause was designed to apply to all cases where the explosion was the immediate cause of the loss. Suppose fire is carelessly applied to powder or other explosive substance. An explosion follows which rends furniture and building. This explosion is the result of the ignition of the explosive material, and it might be claimed that the loss caused thereby was a loss caused by fire. The courts might not so hold, independently of the clause in the policy, but we can well understand, when we examine these policies, that the insurers may have introduced this clause for the purpose of leaving no room for argument or doubt. Again, suppose a case where a fire is speedily subdued, but before it is, it has ignited powder, and an explosion has taken place which has caused much damage but has not extended the fire. In such a case, the company would claim they were protected by this clause from the liability for the consequences of the explosion.

It is not necessary, however, for us to show how the clause was designed to operate. It is sufficient to say that, in our judgment, it can not receive the construction claimed by the company.

It is urged that the stipulations of the policy were not complied with in regard to an appraisement. An inventory of the goods burned or injured was furnished to the company. They expressed their dissatisfaction with it, and might have insisted on the appointment of appraisers. They made no offer to have them appointed, and it was not incumbent on the appellee to move further in the matter. He did what the policy required him to do when he furnished the inventory.

The judgment of the court below is affirmed.

Judgment affirmed.

Ill. 1872.
Commercial Ins. Co. v. Robinson
64 Ill. 265, 1872 WL 8304 (Ill.), 16 Am.Rep. 557

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839 N.W.2d 749
(Cite as: 839 N.W.2d 749)

Court of Appeals of Minnesota.
ECONOMY PREMIER ASSURANCE COMPANY, Appellant,
v.
WESTERN NATIONAL MUTUAL INSURANCE COMPANY, Respondent.

No. A13–0621.
Nov. 25, 2013.

Background: Automobile insurer for driver's father whose truck driver was operating at time of accident brought action against mother's automobile insurer, in which policy driver was named insured, seeking declaratory judgment that mother's insurer was obligated to provide primary coverage for motorist's injuries in accident with driver. The District Court, Hennepin County, entered summary judgment in favor of mother's insurer, and father's insurer appealed.

Holdings: The Court of Appeals, Ross, J., held that:
(1) as matter of first impression, doctrine of contra proferentem, which required any ambiguity in insurance policy to be construed strictly against insurer and in favor of insured did not apply to dispute between two insurers regarding interpretation of policy to which father's insurer was not party, and
(2) truck insured under father's policy was not “temporary loaned vehicle” within meaning of mother's policy which stated that it would provide primary coverage for loss caused by insured in operation of temporary loaned vehicle.

Affirmed.

West Headnotes

[1] Insurance 217 2691

217 Insurance
217XXII Coverage—Automobile Insurance
217XXII(A) In General
217k2689 Evidence
217k2691 k. Presumptions. Most Cited Cases

There is a general presumption that automobile insurance typically follows the vehicle rather than the driver.

[2] Insurance 217 1806

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1806 k. Application of rules of contract construction. Most Cited Cases

Insurance 217 ⚿1813

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1811 Intention
217k1813 k. Language of policies. Most Cited Cases

Insurance 217 ⚿1822

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1822 k. Plain, ordinary or popular sense of language. Most Cited Cases

The court interpret insurances contracts under the general rules of contract law, giving terms their plain and ordinary meaning to honor the intent of the parties.

[3] Insurance 217 ⚿1810

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1810 k. Construction as a whole. Most Cited Cases

Insurance 217 ⚿1813

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1811 Intention
217k1813 k. Language of policies. Most Cited Cases

The court will construe insurance contract terms in light of the whole and will not read the policy language to negate a term if a viable alternate reading is consistent with the parties' general intent and would give meaning to every term.

[4] Insurance 217 ⚿1832(1)

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1832 Ambiguity, Uncertainty or Conflict
217k1832(1) k. In general. Most Cited Cases

Insurance 217 ⚿1833

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1833 k. Status or bargaining power of insureds. Most Cited Cases

In the typical coverage contest between an insurer and its insured, ambiguous terms in the insurance policy are construed in favor of the insured; this rule of construction recognizes the disparity in bargaining power that typically exists between an insurer and an insured, particularly since insurance contracts are often contracts of adhesion.

[5] Insurance 217 ⚿1836

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1836 k. Favoring coverage or indemnity; disfavoring forfeiture. Most Cited Cases

Undefined terms in an insurance policy subject to multiple interpretations are interpreted in favor of coverage.

[6] Insurance 217 ⚿1833

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1833 k. Status or bargaining power of insureds. Most Cited Cases

The rule requiring any ambiguity in an insurance policy to be construed strictly against the insurer protects the insured, who is usually at a disadvantage in terms of knowledge, expertise, and bargaining power relative to her insurer, but the rule applies even to disputes involving a sophisticated insured with equal bargaining power.

[7] Insurance 217 ⚿2652

217 Insurance
217XXII Coverage—Automobile Insurance
217XXII(A) In General
217k2651 Automobiles Covered
217k2652 k. In general. Most Cited Cases

Insurance 217 ⚿2658

217 Insurance
217XXII Coverage—Automobile Insurance
217XXII(A) In General

217k2651 Automobiles Covered
217k2658 k. Substitute automobiles. Most Cited Cases

Doctrine of contra proferentem, which required any ambiguity in insurance policy to be construed strictly against insurer and in favor of insured did not apply to determination whether vehicle that father had loaned to driver that driver was operating at time of accident, which was insured under father's policy, was "temporary substitute" vehicle or "temporary loaned vehicle" within meaning of mother's policy, for purposes of determining whether mother's insurer or father's insurer was primarily liable to provide coverage for injuries to other motorist, in action by father's insurer against mother's insurer for declaratory relief, where father's insurer was not party to contract between mother and mother's insurer.

[8] Automobiles 48A 389

48A Automobiles
48AVIII Garage Keepers, Repairmen, Auto Liverymen, and Filling Stations
48Ak386 Renting Out of Vehicle by Auto Liverymen
48Ak389 k. Liability of hirer in general. Most Cited Cases

Minnesota's No-Fault Act obligates the drivers of vehicles rented or on loan from a service center to maintain primary liability insurance to cover any collision they cause. M.S.A. § 65B.41 et seq.

[9] Insurance 217 2652

217 Insurance
217XXII Coverage—Automobile Insurance
217XXII(A) In General
217k2651 Automobiles Covered
217k2652 k. In general. Most Cited Cases

Truck insured under driver's father's policy that driver was operating at time of accident, which father had allowed driver to use while driver's vehicle was inoperable, was not "temporary loaned vehicle," within meaning of policy issued to driver's mother, in which driver was named insured, and which stated that it would provide primary coverage for loss caused by insured in operation of temporary loaned vehicle, thus, father's insurer was obligated to provide primarily liable for coverage for injuries sustained by motorist in accident; rather, under No Fault Act, "temporary loaned vehicle" applied to rental vehicles or vehicles temporarily loaned by garage or repair facility during repair of insured vehicle. M.S.A. § 65B.49(5a).

***751** *Syllabus by the Court*

The doctrine of *contra proferentem*, which ordinarily guides courts to interpret ambiguous insurance-contract language against the insurer-drafter and in favor of finding coverage for the insured policy holder, does not influence the interpretation of allegedly ambiguous language in an insurance policy that is the subject of a coverage suit between the drafting insurer and another insurance company.

William L. Davidson, Timothy J. O'Connor, Lind, Jensen, Sullivan & Peterson, P.A., Minneapolis, MN, for appellant.

James T. Martin, Gislason, Martin, Varpness & Janes, PA, Edina, MN, for respondent.

Considered and decided by HUDSON, Presiding Judge; HALBROOKS, Judge; and ROSS, Judge.

OPINION

ROSS, Judge.

This is a coverage dispute between two insurance companies. Luke Hylden was driving his father's pickup truck when he collided with another car and injured the driver. Hylden's father had lent him the truck because the car Hylden usually drove, owned by his mother, was broken down. Hylden was insured under the policies that each of his parents had taken out for his and her respective vehicle. Hylden's father's insurer, Economy Premier, paid damages to the victim and then sued Western National, the insurer for Hylden's mother, seeking a declaratory judgment for reimbursement stating that Western National, not Economy Premier, is responsible for the primary coverage. The district court interpreted the policy language and granted summary judgment to Western National. Because we read Western National's policy as providing only excess liability coverage and not primary coverage under the circumstances, we affirm.

FACTS

Luke Hylden collided with Sheila Smith while he was driving his father's pickup truck in 2009. Smith was injured. Luke's parents are divorced, and Luke, then 18 years old, was living with his mother. She owned two vehicles insured by Western National Mutual Insurance Company. Hylden was an insured driver under that policy, and he customarily drove his mother's Ford LTD. But the LTD was inoperable in March 2009, pending repair. So Hylden got permission from his father to drive his Ford F–150 pickup truck. Hylden's father insured the F–150 under a policy issued by Economy Premier Assurance Company. Hylden was also an insured under that policy. After the collision, Smith negotiated with Economy Premier and Western National, settling on a total payment of $212,000.

Economy Premier then brought this action. It claims that Western National has the primary coverage for Hylden's collision ***752** even though the pickup he was driving is expressly identified in Hylden's father's Economy Premier policy. It argued to the district court that the pickup constituted a “temporary loaned vehicle” as that term appears in Hylden's mother's Western National policy, and that Western National's policy assumes primary coverage for that category of vehicle. The district court construed both companies' policies, rejected Economy Premier's proposed interpretation, deemed Economy Premier responsible for primary coverage, and entered summary judgment in Western National's favor. Economy Premier appeals that decision.

ISSUE

Does the truck Luke Hylden was driving qualify as a “temporary substitute vehicle” under

the Western National insurance policy at issue?

ANALYSIS

Economy Premier contends that the district court improperly decided the parties' competing summary judgment motions. We review an appeal from a grant of summary judgment on undisputed material facts de novo, as a question of law. *Kelly v. State Farm Mut. Auto. Ins. Co.*, 666 N.W.2d 328, 330 (Minn.2003). The parties have stipulated to the relevant facts. Interpreting an insurance policy also poses a question of law that we review de novo. *Mitsch v. Am. Nat'l Prop. & Cas. Co.*, 736 N.W.2d 355, 358 (Minn.App.2007), *review denied* (Minn. Oct. 24, 2007).

[1] Economy Premier argues that Western National bears the primary liability coverage for the collision. The argument must overcome a general presumption against it. That is, automobile insurance typically follows the vehicle rather than the driver. *Hilden v. Iowa Nat'l Mut. Ins. Co.*, 365 N.W.2d 765, 769 (Minn.1985). And in this case, Economy Premier issued the policy that covers the specific vehicle involved in the collision. So Economy Premier must rebut the presumption to prevail.

[2] How we interpret the insurance contracts will determine how we answer the question of coverage. We interpret insurance contracts under the general rules of contract law, giving terms their plain and ordinary meaning to honor the intent of the parties. *Midwest Family Mut. Ins. Co. v. Wolters*, 831 N.W.2d 628, 636 (Minn.2013).

[3] Economy Premier begins with the broad argument that Western National agreed to provide primary coverage, even though it was not required to do so, by promising expansively to "pay damages for 'bodily injury' or 'property damage' for which any 'insured' becomes legally responsible because of an auto accident." This argument is unpersuasive. We construe contract terms in light of the whole and will not read the policy language to negate a term if a viable alternate reading is consistent with the parties' general intent and would give meaning to every term. *Eng'g & Const. Innovations, Inc. v. L.H. Bolduc Co.*, 825 N.W.2d 695, 705 (Minn.2013). Economy Premier reads narrowly language that is qualified by the "other insurance" provision in Western National's contract, which imposes limits on the coverage guaranteed elsewhere in the policy. Because we read the contract as a whole in light of all provisions, we believe that the broad statements of coverage on which Economy Premier relies do not end the analysis; they must instead be considered together with the limitations in Western National's contract.

Hylden's father's Economy Premier policy—the policy that names the pickup involved in the accident—contains an "other ***753** insurance" provision. The provision states that "[i]f you or anyone else insured by [this policy] for liability claims also have coverage under some other policy providing liability coverage, [this policy] will be excess over the other liability insurance." By contrast, Hylden's mother's policy commits Western National to "pay damages for 'bodily injury' or 'property damage' for which any 'insured' becomes legally responsible because of an auto accident." The policy also includes an "other insurance" provision, outlined in an endorsement that amends policies underwritten in Minnesota:

1. If there is other applicable insurance, we will pay only our share of the loss. Our share is the proportion that our limit of liability bears to the total of all applicable limits. Except as provided in 2. below, any insurance we provide for a vehicle you do not own, including any vehicle while used as a temporary substitute for "your covered auto," shall be excess over any other collectible insurance.

2. With respect to a vehicle you do not own which is a "rental vehicle" or "temporary loaned vehicle," we will provide coverage on a primary basis.

The first paragraph of the amended "other insurance" provision of Western National's policy is nearly identical to the provision found in Western National's standard policy, but the second paragraph, which includes the disputed term "temporary loaned vehicle," is only present in a Minnesota-specific amendment to the policy. The Minnesota-specific amendment also defines "rental vehicle" and "temporary loaned vehicle," terms included in the second paragraph of the amended "other insurance" provision. Western National's policy therefore effectively creates two categories of vehicles for purposes of its "other insurance" provision in Minnesota insurance policies like the one issued to Hylden's mother: those vehicles (such as "rental vehicles" or "temporary loaned vehicles") for which Western National assumes *primary* liability coverage, and those vehicles (such as "temporary substitute" vehicles) for which it will provide only *excess* insurance coverage over the coverage provided by some other insurer.

The epicenter of this lawsuit is the term "temporary loaned vehicle" in Western National's policy. Western National's policy defines the term, in pertinent part, as "a ... pickup ... if such a vehicle is loaned as a replacement for 'your covered auto' being serviced or repaired regardless of whether the customer, who is provided the replacement vehicle, is charged a fee for the use of such vehicle." The policy does not define the term "temporary substitute."

The parties hotly contest the meaning we should ascribe to these terms. Economy Premier contends that Hylden's father's pickup fits the definition of a "temporary loaned vehicle" and that Western National therefore must provide primary coverage for the damages caused by the accident and Economy Premier is only secondarily liable. It urges that because Western National drafted an ambiguous "other insurance" provision, Western National's coverage is primary. The allegedly ambiguous provision states that Western National will provide primary coverage for any accident that occurs while an insured is driving a "temporary loaned vehicle" but only excess coverage if the insured is driving a "temporary substitute" vehicle. Economy Premier contends that the truck fits the definition of a "temporary loaned vehicle" because it was "loaned [to Hylden] as a replacement for 'your covered auto' being serviced or repaired." Western National ***754** asserts that the truck was instead a "temporary substitute" for Hylden's "covered auto," insisting that the "temporary loaned vehicle" category applies only to vehicles provided temporarily by repair shops while a covered vehicle is being serviced. Because the policy does not *expressly* support either position, Economy Premier maintains that an ambiguity arises and that the ambiguity must be resolved by applying the doctrine of *contra proferentem.* Applying that doctrine, argues Economy Premier, we should construe the ambiguous terms against Western National providing only excess coverage and in favor of Western National providing primary coverage. We are not persuaded.

[4][5] *Contra proferentem* has a usual application. In the typical coverage contest between an insurer and its insured, ambiguous terms in the insurance policy are construed in favor of the insured. *Kastning v. State Farm Ins. Cos.*, 821 N.W.2d 621, 624 (Minn.App.2012). This rule of construction recognizes the disparity in bargaining power that typically exists between an insurer and an insured, particularly since insurance contracts are often contracts of adhesion. *Thommes v. Milwaukee Ins. Co.*, 641 N.W.2d 877, 880 (Minn.2002). Likewise, undefined terms subject to multiple interpretations are interpreted in favor of coverage. *Gen. Cas. Co. of Wis. v. Wozniak Travel, Inc.*, 762 N.W.2d 572, 575 (Minn.2009). We must decide whether Economy Premier is correct that the doctrine applies with the same force in this case, where the contest does not involve the two contracting parties but one contracting party and another entity.

Economy Premier does not explain why it is reasonable for us to apply the doctrine outside its typical context, but its assertion that we should do so raises a question of apparent first impression in Minnesota. Answering it requires a closer look at the doctrine. *Contra proferentem* is well established in contract and insurance law. The common law has recognized the doctrine since the days of Sir Francis Bacon ("[A] man's deeds and his words shall be taken strongliest against himself.") and Sir Edward Coke ("[I]t is a maxim in law, that every man's grant shall be taken by construction of law most forcible against himself."). Francis Bacon, *A Collection of Some Principal Rules and Maxims of the Common Laws of England, with Their Latitude and Extent*, Regula III (1636); 2 Edward Coke, *The First Part of the Institutes of the Laws of England; or, a Commentary upon Littleton* 183(a) (1853). William Blackstone also explained the rule as it applied to deeds:

> [T]he principle of self-preservation will make men sufficiently careful, not to prejudice their own interest by the too extensive meaning of their words: and hereby all manner of deceit ... is avoided; for men would always affect ambiguous and intricate expression, provided they were afterwards at liberty to put their own construction upon them.
>
> 2 William Blackstone, *Commentaries* *380.

The doctrine's basic rationale is that the proponent of a term is more likely aware of its possible ambiguities, especially when dealing with standard-form contracts. Restatement (Second) of Contracts § 206 cmt. a (1981). In the general context of contract law, *contra proferentem* has historically been regarded as a last resort, used only when other interpretive methods have failed to reveal the parties' intent. *Corbin on Contracts* § 24.27 (1998); *see, e.g., Yeaton v. Fry*, 9 U.S. 335, 341–42, 5 Cranch 335, 3 L.Ed. 117 (1809) (applying the doctrine when no other means of ascertaining intent were available); *Varnum v. Thruston*, 17 Md. 470, 496, 1861 WL ***755** 2156 (1861) (describing the doctrine as one "of strictness and rigor, and not to be resorted to but where other rules of exposition fail"). But the rule has assumed a more prominent role in American insurance law and is now the analytical starting point for courts interpreting ambiguous insurance language. *See, e.g., First Nat'l Bank v. Hartford Fire Ins. Co.*, 95 U.S. 673, 679, 5 Otto 673, 24 L.Ed. 563 (1877) (applying the rule without first assessing the parties' intent); *Mut. Life Ins. Co. of N.Y. v. Hurni Packing Co.*, 263 U.S. 167, 174, 44 S.Ct. 90, 91, 68 L.Ed. 235 (1923) ("The rule is settled that in case of ambiguity that construction of the policy will be adopted which is most favorable to the insured.").

[6] Minnesota law follows this approach and applies *contra proferentem* to interpret ambiguities in insurance contracts against the drafter and in favor of finding coverage. *Thommes,* 641 N.W.2d at 880. It does so because insurance policies are often contracts of adhesion, consisting largely of boilerplate terms that are proffered by sophisticated commercial entities and ordinarily accepted by professionally unsophisticated consumers. *Id.* The rule protects the insured, who is usually at a disadvantage in terms of knowledge, expertise, and bargaining power relative to her insurer, but the rule applies even to disputes involving a sophisticated insured with equal bargaining power. *Minn. Mining & Mfg. Co. v. Travelers Indem. Co.,* 457 N.W.2d 175, 180–81 (Minn.1990). *Contra proferentem* applied in these cases holds parties to the terms they offer in negotiation and provides an incentive, especially for insurance companies who are in a better position to prevent misunderstandings, to avoid including ambiguities. Restatement (Second) of Contracts § 206 cmt. a (1982); *cf. Rusthoven v. Commercial Standard Ins. Co.,* 387 N.W.2d 642, 645 (Minn.1986) (citing the Restatement and applying it in an insurance coverage dispute).

[7] This background leads us to decline Economy Premier's urging that we apply the doctrine to this dispute between two insurers, one of which was not a party to the disputed insurance contract. We have discussed why construing ambiguous terms against the drafter and in favor of the nondrafter is justified in a suit between the insurer and the insured. But Economy Premier gives us no reason to conclude that Minnesota law is committed to construing ambiguous contract terms against the insurer to favor a different insurer who is a stranger to the contract. And we have found no Minnesota case applying the doctrine in a suit between two insurers competing to avoid primary coverage. We are convinced that applying the doctrine here would remove it from its primary rationale.

Most jurisdictions agree. Although Minnesota courts have not addressed whether the doctrine of *contra proferentem* applies to nonparties to the contract, other courts have concluded that it does not apply to disputes between two insurance companies arguing over ambiguous language in one company's policy. *See, e.g., U.S. Fid. & Guar. Co. v. Heritage Mut. Ins. Co.,* 230 F.3d 331, 333 (7th Cir.2000) (quoting *Harden v. Monroe Guar. Ins. Co.,* 626 N.E.2d 814, 817 n. 2 (Ind.Ct.App.1993)) (applying Indiana law and assessing the policy's intent from a neutral perspective because plaintiff had not paid “a penny's premium” to defendant); *U.S. Fire Ins. Co. v. Gen. Reinsurance Corp.,* 949 F.2d 569, 573–74 (2d Cir.1991) (noting that New York law no longer applies the rule as between insurance companies); *U.S. Fid. & Guar. Co. v. W. Cas. & Sur. Co.,* 195 Kan. 603, 408 P.2d 596, 598 (1965) (finding “no need” to apply the rule in a ***756** dispute between insurers); *Travelers Ins. Co. v. Am. Cas. Co. of Reading, Pa.,* 151 Mont. 198, 441 P.2d 177, 180 (1968) (plaintiff insurer “should get no benefit from construing the policy against” defendant insurer); *Boston Ins. Co. v. Fawcett,* 357 Mass. 535, 258 N.E.2d 771, 776 (1970) (refusing to apply the doctrine in a dispute between insurer and reinsurer). *But see Farmers Auto. Ins. Ass'n v. St. Paul Mercury Ins. Co.,* 482 F.3d 976, 977–78 (7th Cir.2007) (noting that “argument for *contra proferentem* is pretty feeble” in dispute between insurers but applying it as required by Illinois law); *Commercial Standard Ins. Co. v. Gen. Trucking Co.,* 423 So.2d 168, 171 (Ala.1982) (disagreeing succinctly with argument that court should ignore *contra proferentem* in dispute between insurance carriers); *Empire Fire & Marine Ins. Co. v. Liberty Mut. Ins. Co.,* 117 Md.App. 72, 699 A.2d 482, 494

(Spec.App.1997) (interpreting ambiguous contract against drafter but noting that Maryland law does not recognize *contra proferentem*). We have no reason to conclude that Minnesota takes a different approach. We hold that *contra proferentem* does not apply in a coverage suit between insurers. We therefore analyze the ambiguous contract language here from a neutral perspective.

Economy Premier's reading of Western National's policy would have us classify Hylden's father's truck as both a "temporary loaned vehicle" and a "temporary substitute." It suggests that "temporary loaned vehicle" is merely a subcategory of "temporary substitute" vehicles, a class that could also be read to include "rental vehicles." Economy Premier's reading undermines the insurance policy as a whole. Classifying the truck as a "temporary loaned vehicle" would ignore the policy's distinction between the two categories ("loaned" and "substitute" vehicles) and violate the rule to interpret contract language to give effect to all terms. Western National provides primary coverage for one of these classes and only excess coverage for the other. If the truck fits both classifications, at least one contract provision is rendered superfluous, a rendering our interpretation should avoid if possible.

Our interpretation instead reconciles the two categories. The language of the second paragraph of the amended "other insurance" provision, which introduces the term "temporary loaned auto," appears to account for the requirement under Minnesota law that the drivers of vehicles on loan must maintain liability insurance for vehicles that they rent or vehicles they borrow from repair garages, specifically while their primary vehicle is being repaired. A survey of the language of Western National's policy and the evolution of relevant Minnesota law supports this reading.

[8] The caselaw interpreting Minnesota's No–Fault Act demonstrates that the act obligates the drivers of vehicles rented or on loan from a service center to maintain primary liability insurance to cover any collision they cause. Our appellate courts interpreted earlier incarnations of this statute to require the owners to carry primary insurance for cars driven by nonowners, including rental cars, *Hertz Corp. v. State Farm Mut. Ins. Co.,* 573 N.W.2d 686, 689 (Minn.1998), and cars lent to customers of repair garages, *Mut. Serv. Cas. Ins. Co. v. W. Bend Mut. Ins. Co.,* 599 N.W.2d 585, 588 (Minn.App.1999), *review denied* (Minn. Dec. 14, 1999). The legislature amended the law in 2000, effectively reversing this arrangement, specifying that coverage under the residual liability policy of the driver of a nonowned vehicle would be primary, and coverage under the policy of the vehicle owner excess, when

> ***757** [i]nsuring an operator of a rented motor vehicle if the vehicle is loaned as a replacement for a vehicle being serviced or repaired, regardless of whether a fee is charged for the use of the vehicle, provided that the vehicle so loaned is owned by the service or repair business.

Minn.Stat. § 65B.49, subd. 5a(j) (2000).

[9] A final change came in 2007, when the legislature amended the statute to read simply, "The plan of [liability coverage for] the owner of a rented motor vehicle is excess of any residual liability coverage insuring an operator of a rented motor vehicle." Minn.Stat. §

65B.49, subd. 5a(j) (2008). As part of this change, the legislature also amended the definition of a rented vehicle to include a vehicle that "is loaned as a replacement for a vehicle being serviced or repaired regardless of whether the customer is charged a fee for the use of the vehicle." Minn.Stat. § 65B.49, subd. 5a(b)(2) (2008). These changes were in place when Western National drafted and issued the Minnesota-specific policy at issue here. This history strongly indicates that Western National's policy tracks Minnesota law; that is, Western National intended to extend its primary liability coverage to collisions in which the insured was driving a vehicle obtained from a garage or repair facility during repair of the named, insured vehicle, not to cases involving just any vehicle borrowed from any source during repair.

Several characteristics of the policy support this conclusion as well. Western National policies do not always distinguish between a "temporary substitute" and a "temporary loaned vehicle," as its standard contract language indicates. The "other insurance" provision and definition of "temporary loaned vehicle" are both found only in the state-specific endorsements to the policy rather than in the body of the main contract. This distinction is specific to the Minnesota endorsement. Western National rightly highlights the context in which the term "temporary loaned vehicle" appears. The term is paired with and follows "rental vehicles" in the provision detailing vehicles for which Western National offers primary coverage. This placement juxtaposes "rental vehicles" and "temporary loaned vehicles" on the one hand, and "temporary substitutes" on the other. This bolsters Western National's assertion that "temporary loaned vehicles" are garage loaners rather than just any substitute vehicle an insured drives pending repair of her covered vehicle.

The use of the word "customer" in the definition of a "temporary loaned vehicle" also belies Economy Premier's reading of the contract. "Customer" in this context refers contextually to the individual "who is provided the replacement vehicle," and the policy defines a vehicle as temporarily loaned when it is "a replacement for 'your covered auto' being serviced or repaired regardless of whether the customer ... is charged a fee for the use of such vehicle." Economy Premier argues for a different meaning; it would have us hold that "customer" in this sentence means simply "insured," as in customer of the insurance company issuing the policy. That's quite a stretch.

Economy Premier attempts to support the argument grammatically. It maintains that the portion of the provision including the word "customer," beginning with the word "regardless," is nonrestrictive and therefore not essential to the meaning. The argument fails. Nonrestrictive clauses are generally distinguished from the indispensable portion of a sentence by a comma. *Chicago Manual of Style* § 6.31 (16th ed.2010). A clause that is not separated from the remainder of the sentence by a comma is essential. *Id.* During oral argument, Economy Premier acknowledged***758** through counsel that the usual rules of grammar undercut the argument but suggested that the court should treat the disputed phrase as nonrestrictive despite the absence of a comma, effectively inserting a comma. Nothing in the sentence's context would support the alteration, and we decline to change the contract. The clause beginning with "regardless" is restrictive.

The meaning suggested by the punctuation is consistent with the meaning suggested by the

syntax. The “customer” envisioned by the policy is either an “insured” under the policy, as Economy Premier contends, or someone having work done on his primary vehicle as the “customer” of a commercial facility, as Western National contends. The term “customer” does not appear anywhere else in the policy, while the term “insured” appears repeatedly. Automobile insurance contracts are technical instruments that lack creative flair; they refer to specific classes of people and things using exacting terms, often redundantly. So when a policy introduces a new term, the careful reader will presume that it carries a new idea. And when it repeats a common technical term (particularly here with “insured”—an exclusive term of art as fundamental to the industry as any other), the reader will not presume that the new word is simply the technical term's synonym. The Western National policy never refers to an “insured” by any other name than “insured.” The contract language generally and the context specifically give us no reason to think that the only time the word “customer” appears in the policy it means “insured.” For these reasons, we hold that the term “customer” in the Minnesota-specific provision is an insured who is an auto-repair customer.

Reading Western National's entire policy from a neutral perspective convinces us that Hylden was not driving a “temporary loaned vehicle” when he collided with Smith and that Economy Premier, not Western National, is obligated to provide primary coverage for Smith's damages. This conclusion eliminates any potential conflict between the “other insurance” provisions of each policy, and we therefore do not reach arguments arising from that issue.

DECISION

Because the doctrine of *contra proferentem* does not apply to require us to interpret Western National's insurance policy in favor of Economy Premier, we construe any ambiguities in the policy from a neutral perspective. Our neutral reading convinces us that Hylden's father's pickup truck was not a “temporary substitute vehicle” under that policy. Applying the remaining relevant language in the competing insurers' policies, we conclude that Economy Premier provides primarily liability coverage for Hylden's collision.

Affirmed.

Minn.App.,2013.
Economy Premier Assur. Co. v. Western Nat. Mut. Ins. Co.
839 N.W.2d 749

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15 S.W.2d 544
(Cite as: 15 S.W.2d 544)

Commission of Appeals of Texas, Section A.
G. A. STOWERS FURNITURE CO.
v.
AMERICAN INDEMNITY CO.

No. 1021-4915
March 27, 1929

Error to Court of Civil Appeals of First Supreme Judicial District.

Suit by the G. A. Stowers Furniture Company against the American Indemnity Company. Judgment for defendant was affirmed (295 S. W. 257), and plaintiff brings error. Reversed and remanded.

West Headnotes

[1] Insurance 217 3571

217 Insurance
217XXXI Civil Practice and Procedure
217k3571 k. Pleading. Most Cited Cases
(Formerly 217k629(1))

Insured's petition against automobile indemnity insurer, based on defendant's failure to settle action against insured for less than amount of policy, stated cause of action.

[2] Insurance 217 3347

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3346 Settlement by Liability Insurer
217k3347 k. In General. Most Cited Cases
(Formerly 217k514.2)

Automobile indemnity insurer defending suit against insured must exercise ordinary care in considering offer of settlement.

[3] Insurance 217 1810

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1810 k. Construction as a Whole. Most Cited Cases
(Formerly 217k146.2)

Court must give effect to all provisions of policy.

[4] Insurance 217 ⚿2412

217 Insurance
217XVIII Coverage--Fidelity and Guaranty Insurance
217k2412 k. Evidence. Most Cited Cases
(Formerly 217k514.21(2))

In action against indemnity insurer for failure to accept offer of settlement in action against plaintiff, circumstances and nature of injury to plaintiff in such action held admissible.

[5] Insurance 217 ⚿3381(4)

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3378 Actions
217k3381 Evidence
217k3381(4) k. Admissibility. Most Cited Cases
(Formerly 217k648)

In action against indemnity insurer for failure to settle action against plaintiff, testimony showing defendant's rule not to settle for more than one-half amount of policy held admissible.

***544** Atkinson & Atkinson and Fulbright, Crooker & Freeman, all of Houston, for plaintiff in error.

Fouts, Amerman, Patterson & Moore, of Houston, for defendant in error.

CRITZ, J.

This case involves issues that are questions of first impression in this court, and are so important to the jurisprudence of this state that we deem it advisable to make a very full and complete statement of the issues involved.

This suit was originally filed by the G. A. Stowers Furniture Company, plaintiff in error, hereinafter styled plaintiff, against American Indemnity Company, defendant in error, hereinafter styled defendant, for $14,103.15, together with interest, and for cause of action the petition states, in substance:

That defendant was a private corporation in the city of Galveston, and was engaged during the years 1919 and 1920 in the business of writing and issuing insurance policies and bonds to indemnify the assured against loss by reason of liability imposed by law upon the assured for injuries on account of bodily injuries, etc., and that the said indemnity company issued to said Stowers Furniture Company a policy of insurance for the sum of $5,000 which proposed to indemnify the said furniture company against loss by reason of injuries accidentally suffered

by any person or persons if such loss or damage so sustained was by reason of the said furniture company's ownership of the automobiles described in said policy.

It was further charged that defendant, indemnity company, agreed in said policy, and had reserved the right, to defend any suit in the name and behalf of said named assured for such damage or loss sustained if same was by reason of said plaintiff's ownership.

It was further provided that the furniture company should immediately, in the case of an accident, give notice to defendant, indemnity company, at Galveston and should forward to said indemnity company any summons or other process served upon them, and, when requested by said company, the assured should aid in effecting settlement, etc.

It was further stipulated in said policy that the assured, meaning said furniture company, should not voluntarily assume any liability, settle any claim or expense, except at its own cost, and should not engage in any negotiations of such settlement or legal proceedings without the consent of said insurance company, and the said insurance company reserved the right to settle any and all claims or suits brought against the plaintiff.

It was further alleged that the premiums were all paid on said policy, and the same was valid and subsisting and in full force and effect,***545** that said policy had been mislaid, and that proof would be offered of its contents.

It was further charged in said petition that on the 23d day of January, 1920, a truck belonging to said furniture company, and covered by said policy of insurance, which was hauling and delivering furniture and being operated by one of the said furniture company's servants, and was being driven on Austin street in the city of Houston, Tex., at about the hour of 7 p. m., came in contact with a wagon standing on the side of Austin street and was thereby disabled and so crippled that said servant could not longer operate it, and that it was left by the servant of said furniture company, without a light and without any one to watch it, and that shortly thereafter Miss Mamie Bichon, who was an employee in a drug store, left for her home at about 8:30 p. m. and was driven by Jamail in a Ford coupé very rapidly along said street, and came in collision with said truck; that the coupé was turned over, and that she was very seriously injured; and that about the 3d day of March, 1920, the said Miss Bichon brought suit for damages against said Stowers Furniture Company for $20,000.

It was further charged that defendant herein took charge of the defense of said suit for this plaintiff in accordance with the terms of said policy.

It was further charged that defendant herein employed counsel and proceeded to trial in said cause of Miss Bichon against the plaintiff, furniture company, and that, after hearing the evidence and the charge of the court, the jury returned a verdict for Miss Bichon for the sum of $12,207 besides cost; that there was an appeal by the defendant herein from said judgment; that the same was affirmed; and that this plaintiff paid to Miss Bichon the sum of $14,107.15, including interest and costs of court.

It was further charged that during the pendency of this suit, and before the trial, Miss Bichon offered to accept $4,000 in full settlement for the damages due her; that defendant

herein refused to pay more than $2,500, although its policy bound it to pay $5,000; that the defendant herein knew that the case which Miss Bichon had against this plaintiff was a very dangerous one, and that she was likely to get a judgment for far more than $5,000, and that a person of ordinary prudence would have settled said cause for said sum of $4,000; that defendant admitted that said offer of settlement was a good one and should be accepted; that it willfully and negligently refused to make such settlement, knowing at the time it did so that it was jeopardizing the interests of this plaintiff in a very large amount; that, in refusing to make such settlement, it did not act in good faith, and it did not act like a prudent person would have done under like circumstances; and that by reason of such conduct of said indemnity company the furniture company had been compelled to pay the said sum of more than $14,000.

The material portion of the defendant's answer as shown in the opinion of the Court of Civil Appeals, is as follows:

"That after the happening of the said accident made the basis of this suit the defendant investigated it, and after suit was filed and after citation was forwarded to it by plaintiff herein, it made defense of said suit and defended it through all the courts. That under the terms and provisions of said contract it was to have control of the defense of said suit and no settlement was to be made without its consent, it having the option of settling or defending the suit as it might deem best, and it was under no duty to settle said suit, and it elected to and did defend the said suit. That after making investigation in reference to said accident and the extent of the injuries suffered by Mamie Bichon, this defendant reached the conclusion that the facts of the accident were of such nature that it could and did reasonably suppose that judgment would ultimately result in a verdict for the defendant, and that the injuries suffered by Mamie Bichon as a result of the accident were not of a permanent nature or of such seriousness as to justify a settlement of this case for $4,000. * * *

"For further and special answer herein, defendant says that by the terms of said contract of indemnity its liability was limited, as hereinbefore alleged, to $5,000, with interest thereon at 6 per cent. from the date of the judgment to the affirmance thereof. This defendant says that it has already carried out the terms and provisions of said contract except the payment of $5,000 and interest thereon, which immediately upon the affirmance of this case by the Supreme Court was tendered to the plaintiff herein and plaintiff was notified that defendant was ready and willing to pay the same, but was notified by the plaintiff that plaintiff would not release this defendant from liability, which it was entitled to be released from if it complied with its contract, and stated it was useless to tender the actual money because plaintiff would not accept it; that this defendant has always been ready and willing to pay the limit of its liability, to wit, $5,000, with interest at 6 per cent. until plaintiff's notice it would not be accepted, and is now ready and willing to pay the same, which amount next above mentioned represents principal of $5,000 interest thereon to the date of the notification that tender would not be effective, together with court costs, which are also tendered, which notification to the plaintiff and the understanding that a complete release from liability would not be effected was within ten days of the affirmance of said case by the Supreme Court."

***546** The policy mentioned in the petition contains, among others, the following

provision:

"American Indemnity Company

"Home Office: Galveston, Texas.

"In consideration of the premium of this Policy, as expressed in Statement 5, and of the other statements which are set forth in the Schedule of Statements herein made, and which the Assured warrants to be true by the acceptance of this Policy, and also subject to the conditions of this Policy as hereinafter set forth:

"Does hereby agree

"To indemnify the Assured named and described in Statement 1 of the Schedule of Statements forming part hereof:

"Against loss by reason of the liability imposed by law upon the Assured for damages on account of bodily injuries, including death at any time resulting therefrom, accidentally suffered or alleged to have been suffered while this Policy is in force by any person or persons except employes of the Assured while engaged in operating, riding in or on, or caring for automobiles covered hereby.

"And in addition the company agrees:

"(A) To defend in the name and on behalf of the Assured any suits even if groundless, brought against the Assured to recover damages on account of such happenings as are provided for by the terms of the preceding paragraphs.

"(B) To pay irrespective of the limits of liability expressed in Condition 8 (Limits) hereof, all costs taxed against the Assured in any legal proceeding defended by the Company, all interest accruing after entry of judgment upon such part thereof as shall not be in excess of said liability and the expense incurred by the Assured for such immediate medical or surgical relief as is imperative at the time of the accident, together with all the expense incurred by the Company growing out of the investigation of such an accident, the adjustment of any claim or the defense of any suit resulting therefrom."

The policy further provides:

"This policy does not cover Injuries and/or Death, or Loss, Damage and/or Expense:

"Assumed by the Assured under any Contract or Agreement, oral or written."

The policy further provides:

"The Company's Liability is Limited:

"Under Clause One (Liability) regardless of the number of Assured involved, the Company's liability for the loss from an accident resulting in bodily injuries to or in/death of one person is limited to five thousand dollars ($5,000.00), and, subject to the same limit for

each person, the Company's total liability for loss from any one accident resulting in bodily injuries to or in the death of more than one person is limited to ten thousand dollars ($10,000.00).”

The policy further provides:

“No action shall lie against the Company to recover for any loss, Damage and/or Expense, under this Policy, unless it shall be brought by the Assured for Loss, Damage and/or Expense actually sustained and paid by him in money in satisfaction of a judgment after trial of the issue, and no such action shall lie to recover under any other agreement of the Company herein contained unless brought by the Assured himself to recover money actually expended by him. In no event shall any such action lie unless brought within ninety days after the right of action accrues, as herein provided.

“The Assured shall upon the occurrence of an accident give immediate written notice thereof to the Company's Home Office, at Galveston, Texas, or its Agent duly authorized by law to receive the same, with the fullest information obtainable. He shall give like notice with full particulars of any claim made on account of such accident. If, thereafter, any suit is brought against the Assured he shall immediately forward to the Company, every summons or other process served upon him. The Assured, when requested by the Company, shall aid in effecting settlements, securing evidence, the attendance of witnesses and in prosecuting appeals. The Assured shall not voluntarily assume any liability, settle any claim or incur any expense, except at his own cost, or interfere in any negotiation for settlement or legal proceeding without the consent of the Company previously given in writing. The Company reserves the right to settle any such claim or suit brought against the Assured.”

At the close of the testimony in the district court, the trial court withdrew the case from the jury, and entered judgment for the defendant. This judgment was, on appeal, affirmed by the Court of Civil Appeals. 295 S. W. 257.

The case is now before this court on writ of error granted on application of the plaintiff.

[1] We are of the opinion that the plaintiff's petition states a cause of action against the defendant for the amount sued for, and that the evidence in the case raised an issue of fact to be submitted to the jury by the trial court under proper instructions.

[2] The Court of Civil Appeals, in passing on the issues of this case holds: “We do not think the indemnity company was, by the terms of the policy, under any obligation to do more than faithfully defend the suit. As before stated, it had not agreed to settle the suit, but had reserved the right to do so. It had the unquestioned right to defend the suit to-the end that it might not be called upon to pay a judgment which might be rendered in favor of Miss Bichon.”

***547** As stated in the beginning, the matters involved in this litigation are of first impression in this state, and the holding of the Court of Civil Appeals is in the main supported by the authorities cited by that court.

We, however, are of the opinion that the Court of Civil Appeals was in error in the above holding, and that the better and sounder authorities, and those more in harmony with the spirit of our laws, support a contrary rule. Douglas v. United States Fidelity & Guaranty Co., 81 N. H. 371, 127 A. 708, 37 A. L. R. 1477; Mendota Electric Co. v. New York Indemnity Co., 169 Minn. 377, 211 N. W. 317; Cavanaugh Bros. v. General Accident, Fire & Life Assur. Corporation, 79 N. H. 186, 106 A. 604; Attleboro Mfg. Co. v. Frankford, Marine Accident & Plate Glass Ins. Co. (C. C. A.) 240 F. 573; Brown & McCabe, Stevedores, Inc., v. London Guarantee & Accident Co. (D. C.) 232 F. 298.

As shown by the above-quoted provisions of the policy, the indemnity company had the right to take complete and exclusive control of the suit against the assured, and the assured was absolutely prohibited from making any settlement, except at his own expense, or to interfere in any negotiations for settlement or legal proceeding without the consent of the company; the company reserved the right to settle any such claim or suit brought against the assured. Certainly, where an insurance company makes such a contract; it, by the very terms of the contract, assumed the responsibility to act as the exclusive and absolute agent of the assured in all matters pertaining to the questions in litigation, and, as such agent, it ought to be held to that degree of care and diligence which an ordinarily prudent person would exercise in the management of his own business; and if an ordinarily prudent person, in the exercise of ordinary care, as viewed from the standpoint of the assured, would have settled the case, and failed or refused to do so, then the agent, which in this case is the indemnity company, should respond in damages.

It is true that the policy is for $5,000, so far as this accident is concerned, but when the liability arose against plaintiff the indemnity company was in duty bound to exercise ordinary care to protect the interest of the assured up to the amount of the policy, for the reason that it had contracted to act as his agent, and assumed full and absolute control over the litigation arising out of the accident covered by the policy. The provisions of the policy giving the indemnity company absolute and complete control of the litigation, as a matter of law, carried with it a corresponding duty and obligation, on the part of the indemnity company, to exercise that degree of care that a person of ordinary care and prudence would exercise under the same or similar circumstances, and a failure to exercise such care and prudence would be negligence on the part of the indemnity company.

[3] It is the duty of the court to give effect to all the provisions of the policy, and it would certainly be a very harsh rule to say that the indemnity company, in a case such as this, owed no duty whatever to the insured further than the face of the policy, regardless of whether it was negligent in discharging its duties as the sole and exclusive agent of the assured, in full and complete control. Such exclusive authority to act in a case of this kind does not necessarily carry with it the right to act arbitrarily. Douglas v. United States, etc., Guaranty Co., supra.

In the Douglas Case, supra, the Supreme Court of New Hampshire lays down the law, which we think applies to the issues of the case at bar, as follows:

“The fundamental question is, Does or does not the insurer owe to the insured a duty in the

matter of a settlement? If it does not owe such a duty, it is not liable either for a failure to act or for the manner of action. It may refrain from completing a settlement for any reason, however essentially dishonest, and still there would be no liability. If, as the cases roundly state, it has an exclusive and absolute option, no one can question its motives for the exercise or nonexercise of the privilege. No case has gone that far. All acknowledge a liability for fraudulent conduct, or lack of good faith, in refusing to settle. But they are silent as to any reasoning which would sustain such liability and at the same time deny responsibility for negligent conduct.

"The whole question of insurance against loss may be laid out of the case, and still the defendant would be accountable for negligence. It has contracted to take charge of the defense of this claim. That contract created a relation out of which grew the duty to use care when action was taken. The insurer entered upon the conduct of the affair in question. It had and exercised authority over the matter in every respect, even to negotiating for a settlement. It is difficult to see upon what ground it could escape responsibility when its negligence resulted in damage to the party it had contracted to serve. Attleboro Manufacturing Co. v. Company, 240 F. 573, 153 C. C. A. 377.

"Denial of agency upon the part of the insurer is put upon the ground that, if there were such a relation the insurer would be bound to consider the interests of the insured, when in conflict with its own. It is then said that, when there is such conflict, the insurer may consult its own interests solely. Therefore, it is concluded, there can be no agency.

"This reasoning seems to imply that one party cannot be the agent of the other party. But the law is plainly otherwise. The parties may make that sort of an agreement if they see fit. The result of such a compact is not ***548** to leave the promissor free to act as though he had made no promise. On the contrary, his conduct will be subject to closer scrutiny than that of the ordinary agent, because of his adverse interest. The fact that here the insurer stood to lose but a part of the claim, and that as to the balance of the chances of loss growing out of mismanagement of the defense were upon the insured, is an added reason for holding the defendant to the use of reasonable care in the exercise of its exclusive control over the negotiations. Where one acts as agent under such circumstances, he is bound to give the rights of his principal at least as great consideration as he does his own. Colby v. Copp, 35 N. H. 434, and cases cited; Richards v. Insurance Co., 43 N. H. 263. The insurer cannot betray the trust it has undertaken nor be relieved from the usual rule that in such a case an agent must serve as he has promised to serve."

In the Cavanaugh Case, supra, the same court announces the same rule as is announced in the Douglas Case.

In our opinion the other authorities above cited sustain the rule announced by us, and, while there are authorities holding the contrary rule, we are constrained to believe that the correct rule under the provisions of this policy is that the indemnity company is held to that degree of care and diligence which a man of ordinary care and prudence would exercise in the management of his own business.

[4] The Court of Civil Appeals holds that the trial court did not err in refusing to permit Miss Bichon and others, all witnesses for plaintiff, to testify as to the serious nature of her injuries. We think this holding is error. Further, we are of the opinion that the serious nature of Miss Bichon's injuries and all the facts and circumstances surrounding her injury, are material as bearing on the question of negligence on the part of the indemnity company in failing and refusing to make the settlement.

Of course knowledge on the part of the indemnity company is also an issue. The facts and circumstances surrounding the original injury, and the extent of same, would not raise the issue of negligence on the part of the indemnity company unless it had knowledge thereof, or by the exercise of ordinary care could have had such knowledge.

[5] We think, further, that the testimony offered by plaintiff, to the effect that it was a rule of the indemnity company never to make a settlement for more than one-half the amount of the policy, should have been admitted as bearing on the issue of negligence on the part of the indemnity company.

What we have said disposes of all the assignments.

We recommend that the judgments of the Court of Civil Appeals and of the district court be both reversed and the cause remanded to the district court for a new trial.

CURETON, C. J.

Judgments of the district court and Court of Civil Appeals reversed, and cause remanded to the district court.

We approve the holdings of the Commission of Appeals on the questions discussed in its opinion.

Tex.Com.App. 1929
G.A. Stowers Furniture Co. v. American Indem. Co.
15 S.W.2d 544

END OF DOCUMENT

327 S.W.3d 118, 54 Tex. Sup. Ct. J. 367
(Cite as: 327 S.W.3d 118)

Supreme Court of Texas.
GILBERT TEXAS CONSTRUCTION, L.P., Petitioner,
v.
UNDERWRITERS AT LLOYD'S LONDON, Respondent.

No. 08–0246.
Argued Oct. 6, 2009.
Decided Dec. 17, 2010.

Background: Insured general contractor brought breach of contract action against excess liability insurer, arising from insurer's refusal to provide coverage for insured's settlement of breach of contract claim brought by owner of building that sustained water damage as an alleged result of insured's construction activities. The 160th Judicial District Court, Dallas County, Joseph M. Cox, J., granted insured's summary judgment motion as to coverage and granted insurer's summary judgment motion as to insured's claim for damages under an estoppel theory. Insurer and insured appealed. The Dallas Court of Appeals, 245 S.W.3d 29, affirmed in part and reversed and rendered in part. Insured petitioned for review.

Holdings: On rehearing, the Supreme Court, Johnson, J., held that:
(1) contractual liability exclusion in the excess policy was not limited to liability assumed for conduct of a third party, abrogating *Lennar Corp. v. Great Am. Ins. Co.*, 200 S.W.3d 651;
(2) exception to the contractual liability exclusion, providing that the exclusion did not apply if the insured would have been liable for the damages in the absence of the contract, did not apply to insured's settlement payment; and
(3) insured was not entitled to recover its settlement payment under an estoppel theory.

Affirmed.

West Headnotes

[1] Insurance 217 ⚿2117

217 Insurance
217XV Coverage—in General
217k2114 Evidence
217k2117 k. Burden of proof. Most Cited Cases

The insured has the burden of establishing coverage under the terms of the policy.

[2] Insurance 217 ⚿2117

217 Insurance
217XV Coverage—in General
217k2114 Evidence
217k2117 k. Burden of proof. Most Cited Cases

If the insured proves coverage under the policy, then to avoid liability the insurer must prove the loss is within an exclusion.

[3] Insurance 217 ⚿2117

217 Insurance
217XV Coverage—in General
217k2114 Evidence
217k2117 k. Burden of proof. Most Cited Cases

If the insurer proves that an exclusion applies to prevent the liability of the insurer under the policy, the burden shifts to the insured to show that an exception to the exclusion brings the claim within coverage of the policy.

[4] Appeal and Error 30 ⚿1175(1)

30 Appeal and Error
30XVII Determination and Disposition of Cause
30XVII(D) Reversal
30k1175 Rendering Final Judgment
30k1175(1) k. In general. Most Cited Cases

When both sides move for summary judgment, and the trial court grants one motion and denies the other, reviewing courts consider both sides' summary-judgment evidence, determine all questions presented, and render the judgment the trial court should have rendered.

[5] Courts 106 ⚿247(7)

106 Courts
106VI Courts of Appellate Jurisdiction
106VI(B) Courts of Particular States
106k247 Texas
106k247(7) k. Review by or certificate to Supreme Court by Court of Civil Appeals of questions where its decision conflicts with or overrules that of another Court of Civil Appeals or that of the Supreme Court. Most Cited Cases

Supreme Court had jurisdiction over insured's appeal of opinion of Court of Appeals holding that contractual liability exclusion contained in excess liability policy applied to preclude coverage of insured's liability for third-party claim, as opinion of Court of Appeals conflicted with decision of court of appeals in another judicial district. V.T.C.A., Government Code § 22.001(a)(2).

[6] Insurance 217 ⚿2278(8)

217 Insurance
217XVII Coverage—Liability Insurance
217XVII(A) In General

217k2273 Risks and Losses
217k2278 Common Exclusions
217k2278(8) k. Contractual liabilities. Most Cited Cases

Contractual liability exclusion contained in general contractor's excess liability policy, excluding coverage for bodily injury or property damage for which insured was required to pay damages by reason of the "assumption of liability in a contract or agreement," barred coverage when contractor assumed liability for damages in a contract, not just when contractor assumed the liability of a third party through a contract, and thus the exclusion applied to breach of contract claim brought by owner of damaged building adjacent to the construction site, which claim was based on provision of construction contract in which contractor agreed to protect from damage all improvements and utilities on adjacent property; abrogating *Lennar Corp. v. Great Am. Ins. Co.*, 200 S.W.3d 651.

[7] Appeal and Error 30 ⚿173(14)

30 Appeal and Error
30V Presentation and Reservation in Lower Court of Grounds of Review
30V(A) Issues and Questions in Lower Court
30k173 Grounds of Defense or Opposition
30k173(14) k. Actions on insurance policies. Most Cited Cases

Appeal and Error 30 ⚿766

30 Appeal and Error
30XII Briefs
30k766 k. Defects, objections, and amendments. Most Cited Cases

Insured preserved for appeal its argument that Court of Appeals erred by determining that exclusion in excess liability policy precluded coverage of insured's liability for third-party claim, notwithstanding that insured did not brief issue in Court of Appeals, where insured prevailed on issue at trial court and challenged Court of Appeals' reversal in motion for rehearing and in its petition for review to Supreme Court. Rules App.Proc., Rule 53.2(f).

[8] Insurance 217 ⚿1806

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1806 k. Application of rules of contract construction. Most Cited Cases

Insurance 217 ⚿1813

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1811 Intention

217k1813 k. Language of policies. Most Cited Cases

An insurance policy is construed according to general rules of contract construction to ascertain the parties' intent, and court first looks at the language of the policy because the court presumes parties intend what the words of their contract say.

[9] Insurance 217 ⚿1810

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1810 k. Construction as a whole. Most Cited Cases

When court construes an insurance contract, the court examines the entire agreement and seeks to harmonize and give effect to all provisions so that none will be meaningless.

[10] Insurance 217 ⚿1822

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1822 k. Plain, ordinary or popular sense of language. Most Cited Cases

Insurance policy's terms are given their ordinary and generally accepted meaning unless the policy shows the words were meant in a technical or different sense.

[11] Contracts 95 ⚿143(3)

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k143 Application to Contracts in General
95k143(3) k. Rewriting, remaking, or revising contract. Most Cited Cases

Courts strive to honor the parties' agreement and not remake their contract by reading additional provisions into it.

[12] Insurance 217 ⚿1813

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1811 Intention
217k1813 k. Language of policies. Most Cited Cases

The parties' intent in an insurance contract is governed by what they said in the contract, not by what one side or the other alleges they intended to say but did not.

[13] Insurance 217 ⚿2268

217 Insurance
217XVII Coverage—Liability Insurance
217XVII(A) In General
217k2267 Insurer's Duty to Indemnify in General
217k2268 k. In general. Most Cited Cases

Insurance 217 ⚿2914

217 Insurance
217XXIII Duty to Defend
217k2912 Determination of Duty
217k2914 k. Pleadings. Most Cited Cases

An insurer's duty to defend is determined under the eight-corners doctrine, while the duty to indemnify is determined by the facts as they are established in the underlying suit.

[14] Insurance 217 ⚿2278(8)

217 Insurance
217XVII Coverage—Liability Insurance
217XVII(A) In General
217k2273 Risks and Losses
217k2278 Common Exclusions
217k2278(8) k. Contractual liabilities. Most Cited Cases

Exclusion of coverage in excess liability insurance policy for contractually assumed liability was unambiguous, and thus Supreme Court was not required to interpret exclusion in favor of coverage.

[15] Insurance 217 ⚿1836

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1836 k. Favoring coverage or indemnity; disfavoring forfeiture. Most Cited Cases

Terms in insurance policies that are subject to more than one reasonable construction are interpreted in favor of coverage.

[16] Insurance 217 ⚿1835(2)

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers

217k1835 Particular Portions or Provisions of Policies
217k1835(2) k. Exclusions, exceptions or limitations. Most Cited Cases

Where an ambiguity involves an exclusionary provision of an insurance policy, the court must adopt the construction urged by the insured as long as that construction is not unreasonable, even if the construction urged by the insurer appears to be more reasonable or a more accurate reflection of the parties' intent.

[17] Insurance 217 ⚿1808

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1808 k. Ambiguity in general. Most Cited Cases

An ambiguity does not exist in an insurance policy simply because the parties interpret the policy differently.

[18] Contracts 95 ⚿143(2)

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k143 Application to Contracts in General
95k143(2) k. Existence of ambiguity. Most Cited Cases

If a contract as written can be given a clear and definite legal meaning, then it is not ambiguous as a matter of law.

[19] Insurance 217 ⚿2278(8)

217 Insurance
217XVII Coverage—Liability Insurance
217XVII(A) In General
217k2273 Risks and Losses
217k2278 Common Exclusions
217k2278(8) k. Contractual liabilities. Most Cited Cases

Exception to contractual liability exclusion in general contractor's excess liability insurance policy, providing that the exclusion did not apply if the insured would have been liable for the damages in the absence of the contract in which insured assumed liability for damages, did not apply to breach of contract claim brought by owner of damaged building adjacent to the construction site, which claim was based on provision of construction contract in which contractor agreed to protect from damage all improvements and utilities on adjacent property; building owner's tort claims against contractor had been dismissed due to governmental immunity, such that the only viable claim underlying contractor's settlement with building owner was breach of contract.

[20] Indemnity 208 ⚿42

208 Indemnity
208II Contractual Indemnity
208k42 k. Accrual of liability. Most Cited Cases

A claim based on a contract that provides indemnification from liability does not accrue until the indemnitee's liability becomes fixed and certain.

[21] Appeal and Error 30 ⚿1178(1)

30 Appeal and Error
30XVII Determination and Disposition of Cause
30XVII(D) Reversal
30k1178 Ordering New Trial, and Directing Further Proceedings in Lower Court
30k1178(1) k. In general. Most Cited Cases

Case would not be remanded for further proceedings before Court of Appeals to permit appellant to pursue alternative legal theory, as alternative theory was already effectively considered by Court on appeal.

[22] Insurance 217 ⚿3106

217 Insurance
217XXVI Estoppel and Waiver of Insurer's Defenses
217k3105 Claims Process and Settlement
217k3106 k. In general. Most Cited Cases

Even if general contractor that worked on light-rail project was deprived of the opportunity to make an informed decision when its excess liability insurer directed contractor to seek summary judgment on building owner's tort claims based on governmental immunity, but did not inform contractor of the insurer's position that the excess policy did not cover building owner's remaining breach of contract claim, contractor was not prejudiced by such deprivation, and thus contractor could not recover from insurer under an estoppel theory the settlement payment it made to building owner on the breach of contract claim; contractor did not have coverage for the contract claim regardless of whether it asserted the immunity defense as directed.

***121** Linda Jene Burgess, Craig T. Enoch, Winstead PC, Lee H. Shidlofsky, Douglas Paul Skelley, Visser Shidlofsky LLP, Austin, Andrew T. McKinney, McKinney & Cooper, L.L.P., Houston, for Petitioner.

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Claude Stuart III, Phelps Dunbar, Houston, for Amicus Curiae.

Patrick J. Wielinski, for Associated General Contractors of America, American Contractors

Ins. Group, Ltd.

Micah Ethan Skidmore, for United Policyholders.

Timothy Poteet, for Texas Association of Defense Counsel.

Justice JOHNSON delivered the opinion of the Court.

We deny Gilbert Texas Construction's motion for rehearing. We withdraw our opinion of June 4, 2010 and substitute the following in its place.

During a Dallas Area Rapid Transit Authority (DART) construction project, unusually heavy rains resulted in water damage to a building adjacent to the construction site. The owner of the building sued DART and its contractors, alleging that construction activities caused the water damage. The building owner sued the general contractor in tort and for breach of contract. In the breach of contract claim, the building owner alleged that the general contractor assumed liability for the damage under its contract with DART. Except for the breach of contract claim, the trial court granted summary judgment for the general contractor on the basis of governmental immunity. The general contractor later settled the breach of contract claim and sought indemnity from its insurers. The excess insurer denied coverage.

We address two issues. The first is whether the contractual liability exclusion in a Commercial General Liability (CGL) policy excludes coverage for property damage when the only basis for liability is that the insured contractually agreed to be responsible for the damage, and if so, whether an exception to the exclusion operates to restore coverage. We hold that the exclusion applies, the exception does not, and there is no coverage. The second issue is whether Gilbert is entitled to recover its settlement payment under an estoppel theory. We hold it is not.

I. BACKGROUND

A. The Underlying Suit

In 1993, DART contracted with Gilbert Texas Construction, L.P., as general contractor, ***122** to construct a light rail system. One part of the contract required Gilbert to protect the work site and surrounding property:

> 10. *Protection of Existing Site Conditions*
>
> a. The Contractor shall preserve and protect all structures ... on or adjacent to the work site....
>
> b. The Contractor shall protect from damage all existing improvements and utilities (1) at or near the work site and (2) on adjacent property of a third party ... [and] repair any damage to those facilities, including those that are the property of a third party, resulting from failure to comply with the requirements of this contract or failure to exercise reasonable care in performing the work. If the Contractor fails or refuses to repair the damage promptly, [DART] may have the necessary work performed and charge the cost to the Contractor.

During construction, Dallas suffered an unusually heavy rain, and a building adjacent to

the construction area was flooded. RT Realty (RTR), the building's owner,[FN1] sued DART, Gilbert, and other persons and entities involved in the construction. RTR alleged various theories of liability, including violations of the Texas Transportation Code and the Texas Water Code, nuisance, and trespass. RTR also claimed it was a third-party beneficiary of the contract between Gilbert and DART and that Gilbert was liable to RTR for breach of that contract.

FN1. Various interveners eventually joined the suit, including RTR's property insurers and persons who had offices in the flooded building.

DART provided insurance for the project through an Owner Controlled Insurance Program. Gilbert's primary coverage was by a CGL policy with Argonaut Insurance Company. Gilbert also had several layered excess coverage policies [FN2] through Underwriters at Lloyd's London [FN3] (Underwriters). Argonaut assumed Gilbert's defense and provided a list of approved defense counsel to Gilbert, who selected attorney James Grau to defend it. The original answer Grau filed for Gilbert contained a pleading asserting that Gilbert had sovereign immunity.[FN4]

FN2. Underwriters' policies generally followed form, meaning the policies tracked the essential terms of the primary policy. Underwriters' policies also had separate provisions and exclusions applicable to the excess policies. We will generally refer to Underwriters' policies collectively as “the policy” for ease of reference. Because our analysis focuses on provisions found in the primary policy, the policy language we reference, unless specifically noted otherwise, will be that of Argonaut's primary policy, which is incorporated by Underwriters' policy.

FN3. The policies were underwritten and risks participated in by various Members of the Lloyd's market and individual insurance companies. The underwriters and participating insurers will be referred to collectively as “Underwriters.”

FN4. The State has sovereign immunity and subdivisions have what is called governmental immunity. The parties refer to DART's immunity and that of Gilbert, as DART's contractor, as sovereign immunity. However, we will use the term “governmental immunity” throughout this opinion as that is the proper terminology.

Through its coverage counsel, Underwriters sent a series of reservation of rights letters to Gilbert. The letters generally (1) reviewed the claims made by RTR in each successive petition, (2) noted that under its policy, Underwriters did not have a duty to defend Gilbert and its obligation to indemnify Gilbert did not depend on allegations made in RTR's pleadings but would be determined by the judgment ***123** rendered and facts found in the suit, (3) stated that a coverage determination was not possible because no judgment had yet been entered and no fact finding accomplished, and (4) referenced various policy provisions that might preclude coverage for the damages being sought from Gilbert. In addition, the letters reserved Underwriters' rights to deny coverage under the policies and noted the potential conflict of interest between Gilbert and Underwriters because of Underwriters' position that damages claimed by RTR might not be covered. Underwriters' policy included a provision allowing

Underwriters to associate with Gilbert in defense of claims.

Other defendants also responded to RTR's suit, in part, by claiming they had governmental immunity. The defendants moved for summary judgment on the basis of immunity. The trial court granted the motions for summary judgment except for RTR's claims against Gilbert for breach of contract.

A few weeks after the trial court granted partial summary judgment to Gilbert, Underwriters sent another reservation of rights letter. In that letter, Underwriters, for the first time, took the specific position that RTR's breach of contract claim was not covered because Underwriters' policy excluded coverage for contractual liability. Gilbert settled RTR's breach of contract claim for $6.175 million. Underwriters denied coverage.

B. The Coverage Suit

Gilbert sued Underwriters for breach of contract and Insurance Code violations, also urging that Underwriters waived its right to deny coverage and was estopped to deny coverage. Both parties moved for summary judgment on all issues. The trial court granted Gilbert's motion as to coverage and granted Underwriters' motion as to Gilbert's statutory, waiver, and estoppel claims.

Underwriters and Gilbert both appealed. The court of appeals reversed and rendered judgment for Underwriters, holding that the breach of contract claim (1) fell within the policy's contractual liability exclusion and (2) was not excepted from the exclusion. 245 S.W.3d 29, 34–35 (Tex.App.-Dallas 2007, pet. granted). It additionally held that Underwriters had not waived its policy defenses and was not estopped from raising the defense of non-coverage because Underwriters had not assumed Gilbert's defense. *Id.* at 37.

In this Court, Gilbert asserts that (1) the contractual liability exclusion does not apply because Gilbert's liability arises from its own breach of contract and not from another's liability that Gilbert assumed; (2) even if the exclusion applies, an exception to the exclusion brings the breach of contract claim back into coverage because Gilbert would have been liable to RTR in the absence of its contract with DART; and (3) in the alternative, Underwriters asserted control over Gilbert's defense and prejudiced Gilbert, so under an estoppel theory Gilbert should be awarded damages for the amount it paid to settle RTR's lawsuit.

We agree with the court of appeals: the contractual exclusion applies to the breach of contract claim and the exception for liability the insured would have absent its contract is inapplicable. Further, we determine that Gilbert was not prejudiced by Underwriters' actions and Underwriters is not required to pay damages to Gilbert under an estoppel theory.[FN5]

FN5. Underwriters also asserted issues the court of appeals did not reach: (1) an exclusion in the excess policy bars coverage for breach of contract; (2) RTR's claim did not involve a covered occurrence resulting in liability for which Gilbert was obligated to pay damages; and (3) Gilbert lacked a reasonable basis for settling RTR's claim when there was no potential liability or basis for a judgment against Gilbert. In this Court, Underwriters argues those issues warrant remand to the court of appeals in the event we reverse. Because we affirm the court of appeals' judgment, we do not

reach the remand issues.

*124 II. DISCUSSION

A. Standard of Review

[1][2][3] The parties do not dispute the applicable burdens of proof. Initially, the insured has the burden of establishing coverage under the terms of the policy. *Ulico Cas. Co. v. Allied Pilots Ass'n*, 262 S.W.3d 773, 782 (Tex.2008). If the insured proves coverage, then to avoid liability the insurer must prove the loss is within an exclusion. *Id.* If the insurer proves that an exclusion applies, the burden shifts back to the insured to show that an exception to the exclusion brings the claim back within coverage. *Comsys Info. Tech. Servs., Inc. v. Twin City Fire Ins. Co.*, 130 S.W.3d 181, 193 (Tex.App.-Houston [14th Dist.] 2003, pet. denied); *see also Century Sur. Co. v. Hardscape Constr. Specialties, Inc.*, 578 F.3d 262, 265 (5th Cir.2009).

[4] When both sides move for summary judgment, as they did here, and the trial court grants one motion and denies the other, reviewing courts consider both sides' summary-judgment evidence, determine all questions presented, and render the judgment the trial court should have rendered. *Embrey v. Royal Ins. Co. of Am.*, 22 S.W.3d 414, 415–16 (Tex.2000).

B. Jurisdiction

[5] As a preliminary matter, Underwriters argues that we lack jurisdiction. Gilbert contends, in part, that we have jurisdiction because the court of appeals' opinion conflicts with opinions of other courts of appeals on a question of law material to the decision of the case. *See* TEX. GOV'T CODE § 22.001(a)(2). We agree with Gilbert. The court of appeals' decision is contrary to a decision of the Fourteenth Court of Appeals that held the contractual liability exclusion is limited to liability assumed for conduct of a third party, such as in an indemnity or hold-harmless agreement. *See Lennar Corp. v. Great Am. Ins. Co.*, 200 S.W.3d 651, 693 (Tex.App.-Houston [14th Dist.] 2006, pet. denied). Here, the court of appeals held that the exclusion applies because Gilbert assumed liability in its contract with DART. 245 S.W.3d at 34. We have jurisdiction pursuant to section 22.001(a)(2) of the Government Code.

C. Contractual Liability Exclusion

[6] Coverage A of the policy, which is entitled “Bodily Injury and Property Damage Liability,” provides that the insurer “will pay those sums that the insured becomes legally obligated to pay as damages because of ‘bodily injury’ or ‘property damage’ to which this insurance applies.... The ‘bodily injury’ or ‘property damage’ must be caused by an occurrence.” Exclusion 2(b) provides that the 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) Assumed in a contract or agreement that is an “insured contract;” or
>
> (2) That the insured would have in the absence of the contract or agreement.

The policy's definitions section provides a definition of “insured contract.” The term is

defined as seven types of agreements, the last of which is an agreement to assume another's tort liability:

***125** "Insured contract" means:

a. A lease of premises;

b. A sidetrack agreement;

...

g. That part of any other contract or agreement pertaining to your business under which you assume the tort liability of another to pay damages because of "bodily injury" or "property damage" to a third person or organization, if the contract or agreement is made prior to the "bodily injury" or "property damage." Tort liability means a liability that would be imposed by law in the absence of any contract or agreement.

Underwriters does not argue that RTR's claim is not within the general terms of the policy; rather, it asserts that exclusion 2(b)—the contractual liability exclusion—precludes coverage because at the time Gilbert settled, the trial court had already granted summary judgment on all RTR's statutory and tort claims, and the only basis for liability remaining was for breach of contractual obligations Gilbert assumed in its contract with DART. Gilbert contends the contractual liability exclusion applies more narrowly. It contends the exclusion applies only in the limited situation in which the insured has assumed the liability *of another* such as in hold-harmless or indemnity agreements. Gilbert argues that to hold otherwise runs afoul of our decision in *Lamar Homes, Inc. v. Mid–Continent Cas. Co.,* 242 S.W.3d 1 (Tex.2007), in which we stated that a breach of contract claim can involve an occurrence and coverage does not turn on the label of the cause of action. Finally, Gilbert contends that, at the very least, the exclusion is ambiguous and must be interpreted in favor of coverage.

1. Preservation on Appeal

[7] Underwriters argues at the outset that Gilbert waived its argument regarding the inapplicability of the exclusion because Gilbert did not timely assert and brief the issue in the court of appeals. *See* TEX.R.APP. P. 53.2(f). As Underwriters observes, the court of appeals did not consider, in depth, the applicability of the exclusion because Gilbert did not dispute its applicability in its initial appeal. 245 S.W.3d at 34. Gilbert argues that it prevailed on the exclusion issue in the trial court and did not need to initially raise the issue in the court of appeals. We agree with Gilbert.

After the court of appeals reversed the trial court's judgment on this issue, Gilbert challenged the court of appeals' judgment both in a motion for rehearing in the court of appeals and in its petition for review. While ordinarily a party waives a complaint not raised in the court of appeals, a complaint arising from the court of appeals' judgment may be raised either in a motion for rehearing in that court or in a petition for review in this Court. *See* TEX.R.APP. P. 53.2(f); *Bunton v. Bentley,* 153 S.W.3d 50, 53 (Tex.2004). Gilbert did not waive the issue.

2. Scope of the Exclusion

The policy at issue is a standard CGL policy developed by the Insurance Services Office, Inc. (ISO).[FN6] *See Lamar Homes,* 242 S.W.3d at 5; 2 JEFFREY W. STEMPEL, STEMPEL ON INSURANCE CONTRACTS § 14.01 (3d ed.2007). The meaning of the terms and exclusions within a standard policy should theoretically be the same in Texas as in other states. *See Lamar Homes,* 242 S.W.3d at 5. However, a lack of consensus on the meaning of terms in a CGL policy is ***126** not unusual. As noted above, Texas courts of appeals have reached different conclusions about the exclusion's effect, as have other state and federal courts.

FN6. The ISO is an insurance industry organization which drafts standard forms used by insurers. *See Lamar Homes,* 242 S.W.3d at 5 n. 1.

[8][9][10][11] The principles courts use when interpreting an insurance policy are well established. Those principles include construing the policy according to general rules of contract construction to ascertain the parties' intent. *Don's Bldg. Supply, Inc. v. OneBeacon Ins. Co.,* 267 S.W.3d 20, 23 (Tex.2008); *Kelley–Coppedge, Inc. v. Highlands Ins. Co.,* 980 S.W.2d 462, 464 (Tex.1998). First, we look at the language of the policy because we presume parties intend what the words of their contract say. *See Don's Bldg. Supply,* 267 S.W.3d at 23. We examine the entire agreement and seek to harmonize and give effect to all provisions so that none will be meaningless. *See MCI Telecomms. Corp. v. Tex. Utils. Elec. Co.,* 995 S.W.2d 647, 652 (Tex.1999). The policy's terms are given their ordinary and generally-accepted meaning unless the policy shows the words were meant in a technical or different sense. *Don's Bldg. Supply,* 267 S.W.3d at 23; *see also Sec. Mut. Cas. Co. v. Johnson,* 584 S.W.2d 703, 704 (Tex.1979). Courts strive to honor the parties' agreement and not remake their contract by reading additional provisions into it. *See Nat'l Union Fire Ins. Co. of Pittsburgh, PA v. Crocker,* 246 S.W.3d 603, 606 (Tex.2008). With these principles in mind, we turn to the language of the exclusion.

Considered as a whole, the contractual liability exclusion and its two exceptions provide that the policy 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, except for enumerated, specific types of contracts called "insured contracts" and except for instances in which the insured would have liability apart from the contract. In this case, Gilbert agreed under its contract with DART to "repair any damage to ... facilities, including those that are the property of a third party, resulting from failure to comply with the requirements of this contract or failure to exercise reasonable care in performing the work." RTR originally sued on tort and statutory theories of liability, then added a breach of contract claim. But Gilbert prevailed on its summary-judgment motion, leaving only RTR's breach of contract claim. Thus, the only liability theory remaining at the time Gilbert settled arose from Gilbert's contract with DART and Gilbert does not claim there are facts that could result in its being liable under some theory besides breach of contract. Underwriters argues that the exclusion unambiguously applies to the breach of contract claim.

Gilbert, however, argues that the policy's plain language is not as plain as it might seem. Citing several authorities, Gilbert contends that in order to give meaning to the word "assumption" in the exclusion, the liability assumed must be that of another. *E.g., Am. Family*

Mut. Ins. Co. v. Am. Girl, Inc., 268 Wis.2d 16, 673 N.W.2d 65, 80–81 (2004) ("The term 'assumption' must be interpreted to add something to the phrase 'assumption of liability in a contract or agreement.' Reading the phrase to apply to all liabilities sounding in contract renders the term 'assumption' superfluous."). In other words, Gilbert would have us read the exclusion to say " 'property damage' for which the insured is obligated to pay damages by reason of the assumption of *another's* liability in a contract or agreement." Underwriters counters that we should not judicially rewrite the exclusion by inserting the word "another's" into it. We agree with Underwriters.

***127** [12] The exclusion bars coverage for liability of a third party that is assumed, such as that assumed by an indemnity agreement. But had it been intended to be so narrow as to apply *only* to an agreement in which the insured assumes liability of another party by an indemnity or hold-harmless agreement, it would have been simple to have said so. The parties' intent is governed by what they said in the insurance contract, not by what one side or the other alleges they intended to say but did not. *See Fortis Benefits v. Cantu*, 234 S.W.3d 642, 647, 649 (Tex.2007) (noting that contract rights arise from the parties' agreement and declining to "judicially rewrite the parties' contract by engrafting extra-contractual standards"); *Fiess v. State Farm Lloyds*, 202 S.W.3d 744, 753 (Tex.2006) ("[W]here the language is plain and unambiguous, courts must enforce the contract as made by the parties, and cannot make a new contract for them, nor change that which they have made under the guise of construction.").

The exclusion applies when the insured is obligated to pay damages "by reason of the assumption of liability in a contract or agreement." Those terms are not defined, so we give them their "generally accepted or commonly understood meaning." *Lamar Homes*, 242 S.W.3d at 8 (citing *W. Reserve Life Ins. Co. v. Meadows*, 152 Tex. 559, 261 S.W.2d 554, 557 (1953)). To "assume" means to "undertake." WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 133 (2002). "Liability" is "[t]he quality or state of being legally obligated or accountable." BLACK'S LAW DICTIONARY 997 (9th ed.2009). Independent of its contractual obligations, Gilbert owed RTR the duty to comply with law and to conduct its operations with ordinary care so as not to damage RTR's property, and absent its immunity it could be liable for damages it caused by breaching its duty. In its contract with DART, however, Gilbert undertook a legal obligation to protect improvements and utilities on property adjacent to the construction site, and to repair or pay for damage to any such property "resulting from a failure to comply with the requirements of this contract *or* failure to exercise reasonable care in performing the work." (emphasis added). The latter obligation—to exercise reasonable care in performing its work—mirrors Gilbert's duty to RTR under general law principles. The obligation to repair or pay for damage to RTR's property "resulting from a failure to comply with the requirements of this contract" extends beyond Gilbert's obligations under general law and incorporates contractual standards to which Gilbert obligated itself. The trial court granted summary judgment on all RTR's theories of liability other than breach of contract, so Gilbert's only potential liability remaining in the lawsuit was liability in excess of what it had under general law principles. Thus, RTR's breach of contract claim was founded on an obligation or liability contractually assumed by Gilbert within the meaning of the policy exclusion.

Further, considering the exclusion and its exceptions as a whole reinforces our conclusion.

See MCI Telecomms., 995 S.W.2d at 652 ("When interpreting a contract, we examine the entire agreement in an effort to harmonize and give effect to all provisions of the contract so that none will be meaningless."); *Kelley–Coppedge, Inc.,* 980 S.W.2d at 464 (observing that we must "attempt to give effect to all contract provisions so that none will be rendered meaningless"). The first exception—the insured-contract exception—lists six specific types of contracts to which the exclusion does not apply. The seventh and final item in the list addresses assumption of another's tort liability: "That part of any other contract or agreement pertaining to your business under which you assume the ***128** tort liability *of another* to pay damages because of 'bodily injury' or 'property damage' to a third person or organization...." (emphasis added). The fact that the definition explicitly references assumption of the tort liability *of another* demonstrates that the parties are capable of using such narrow, specific language when that is their intent.

Gilbert argues that the exclusion should be read as applying to all situations in which the insured assumes another's liability while the insured-contract exception to the exclusion should be read as applying only to agreements in which the insured assumes another's tort liability. We agree that the insured-contract exception brings back into coverage contracts in which the insured assumes the tort liability of another—it says it does. But the exclusion does not say it is limited to the narrow set of contracts by which the insured assumes the liability of another person; the exclusion's language applies without qualification to liability assumed by contract except for two situations: (1) specified types of contracts referred to as "insured contracts," including indemnity agreements by which the insured assumes another's tort liability, and (2) situations in which the insured's liability for damages would exist absent the contract—in other words, situations in which the insured's liability for damages does not depend solely on obligations assumed in the contract.

Gilbert further argues that if the exclusion were meant to apply to a breach of contract claim like the one at issue in this case, it could easily have said just that. To illustrate its argument, Gilbert points to language in another section of the policy—"Coverage B. Personal and Advertising Injury Liability." As we understand it, Gilbert's argument is that Coverage B has an exclusion for both personal injury and advertising injury that is substantively the same as Coverage A's contractual liability exclusion, except Coverage B's exclusion does not provide coverage for "insured contracts" as does the Coverage A exclusion:

> This insurance does not apply to:
>
> a. "Personal injury" or "advertising injury:"
>
> ...
>
> (4) For which the insured has assumed liability in a contract or agreement. This exclusion does not apply to liability for damages that the insured would have in the absence of the contract or agreement.

Gilbert argues that if the foregoing exclusion applied to all contractual obligations, then a separate exclusion in Coverage B specific to advertising injury would be unnecessary. That particular exclusion provides as follows:

b. “Advertising injury” arising out of:

(1) Breach of contract, other than misappropriation of advertising ideas under an implied contract.

According to Gilbert, if Coverage B's contractual liability exclusion excluded all breach of contract claims, then the express breach of contract claim exclusion for advertising injury would be unnecessary. We are not persuaded. We do not hold that the exclusion in Coverage A precludes liability for all breach of contract claims. We hold that it means what it says: it excludes claims when the insured assumes liability for damages in a contract or agreement, except when the contract is an insured contract or when the insured would be liable absent the contract or agreement. The express breach of contract exclusion in Coverage B, on the other hand, excludes all claims “arising out of” a breach of contract—a potentially larger ***129** category of claims than is excluded under the contractual liability exclusion.[FN7]

FN7. In its post-submission brief, Gilbert notes that some insurance policies include an express breach of contract exclusion in Coverage A of the policy. This, according to Gilbert, is further evidence that the contractual liability exclusion is not intended to exclude general breach of contract claims. We are not persuaded by the argument because the policy we are interpreting does not include such language in Coverage A, and each policy must be interpreted according to its own specific provisions and coverages.

3. Holdings from Other Jurisdictions

Other jurisdictions have interpreted the exclusion differently than the way we do today. Gilbert points out that some jurisdictions, including the federal Fifth Circuit, have suggested, and held, that the exclusion applies to a limited category of cases in which the insured assumes the liability of another, such as in an indemnity or hold-harmless agreement.[FN8] Underwriters,***130** on the other hand, cites cases interpreting the exclusion as we do—not limiting the exclusion's scope to only those situations in which the insured has assumed the liability of another.[FN9] While we believe our interpretation of the policy accords with longstanding principles of insurance contract interpretation, we consider it worthwhile to examine the rationale of courts reaching contrary conclusions.

FN8. *See, e.g., Ferrell v. W. Bend Mut. Ins. Co.,* 393 F.3d 786, 795 (8th Cir.2005) (suggesting exclusion applies only where insured assumes liability of a third party); *Federated Mut. Ins. Co. v. Grapevine Excavation Inc.,* 197 F.3d 720, 726 (5th Cir.2000) (the insured was not sued as the contractual indemnitor of a third party's conduct but rather for its own conduct, so the contractual liability exclusion was inapplicable); *Olympic, Inc. v. Providence Wash. Ins. Co.,* 648 P.2d 1008, 1011 (Alaska 1982) (“ ‘Liability assumed by the insured under any contract’ refers to liability incurred when one promises to indemnify or hold harmless another, and does not refer to the liability that results from breach of contract.”); *ACUITY v. Burd & Smith Constr., Inc.,* 721 N.W.2d 33, 40 (N.D.2006) (liability assumed by the insured in a CGL policy is “generally understood and interpreted by the courts to mean the liability *of another* which one ‘assumes' in the sense that one agrees to indemnify or

hold the other person harmless"); *Gibbs M. Smith, Inc. v. U.S. Fid. & Guar. Co.*, 949 P.2d 337, 341 (Utah 1997) ("Courts have over and over again interpreted the phrase 'liability assumed by the insured under any contract' to apply only to indemnification and hold-harmless agreements, whereby the insured agrees to 'assume' the tort liability of another."); *Am. Family Mut. Ins. Co.*, 673 N.W.2d at 70 (Wis.2004) (contractually-assumed liability clause excludes coverage for liability "where the insured has contractually assumed the liability of another, as in an indemnification or hold-harmless agreement"); 4 PHILLIP L. BRUNER & PATRICK J. O'CONNOR, BRUNER AND O'CONNOR ON CONSTRUCTION LAW § 11:109 (2010) (criticizing the court of appeals' judgment in this case and observing that the exclusion addresses "situations where the insured assumes the liability of another and, as a consequence, the insurer is placed in the position of extending coverage to a third party's liabilities for which the insurer performed no underwriting. In other words, the exclusion applies to the 'assumed' liability of another, not one's own liability due to a contractual undertaking."); C.T. Drechsler, Annotation, *Scope and Effect of Clause in Liability Policy Excluding from Coverage Liability Assumed by Insured Under Contract Not Defined In Policy, Such as One of Indemnity*, 63 A.L.R.2d 1122 (2009) ("[T]he contractual liability exclusion clause is not effective primarily in the two following situations: (1) where the insured is the one who is solely responsible for the injury, and (2) where the insured is the actively negligent wrongdoer."); 21 ERIC MILLS HOLMES, HOLMES' APPLEMAN ON INSURANCE § 132.3, 36–40 (2d ed.1996) (noting that the contractual liability exclusion clause refers to the assumption of another's liability as in an indemnity agreement); 2 ROWLAND H. LONG, THE LAW OF LIABILITY INSURANCE § 10.05[2], 10–61 (1st ed. 2006) ("Although it could be argued that one assumes liability (*i.e.*, a duty of performance, the breach of which will give rise to liability) whenever one enters into a binding contract, in the CGL policy and other liability policies an 'assumed' liability is generally understood and interpreted by the courts to mean the liability *of another* which one 'assumes' in the sense that one agrees to indemnify or hold the other person harmless therefor."); 1 BARRY R. OSTRAGER & THOMAS R. NEWMAN, HANDBOOK ON INSURANCE COVERAGE DISPUTES § 7.05, 546 (14th ed. 2008) ("[C]ourts have consistently interpreted the phrase 'liability assumed by the insured under any contract' to apply only to indemnification and hold-harmless agreements, whereby the insured agrees to 'assume' the tort liability of another. This phrase does not refer to the insured's breaches of its own contracts."); 2 JEFFREY W. STEMPEL, STEMPEL ON INSURANCE CONTRACTS § 14.14 (3d ed. 2006 & Supp.2009) ("The CGL coverage for a policyholder's liability assumed by contract 'refers to liability incurred when one promises to indemnify or hold harmless another, and does not refer to liability that results from breach of contract.' ") (quoting *Olympic*, 648 P.2d at 1011).

FN9. *See, e.g., Nationwide Mut. Ins. Co. v. CPB Int'l Inc.*, No. 3:06–CV–0363, 2007 WL 4198173, at *8 (M.D.Pa. Nov.26, 2007) ("Exclusion (b) is simply further clarification in the policy that contract-based claims are not covered."); *CIM Ins. Corp. v. Midpac Auto Ctr., Inc.*, 108 F.Supp.2d 1092, 1099–1100 (D.Haw.2000) (clause in policy stating that policy does not apply to liability assumed under any contract or

> agreement means that any claim that is dependent on the existence of an underlying contract is not covered); *Monticello Ins. Co. v. Dismas Charities, Inc.,* No. 3:96CV–550–S, 1998 WL 1969611, at *2 (W.D.Ky. Apr.3, 1998) (exclusion for liability assumed by the insured under any contract or agreement does not arise only when a party assumes the liability for another party; rather, the plain meaning of the policy excludes a breach of contract claim from coverage); *Silk v. Flat Top Constr., Inc.,* 192 W.Va. 522, 453 S.E.2d 356, 359 (1994) (exclusion removed coverage for breach of contract); *See also TGA Dev., Inc. v. N. Ins. Co. of N.Y.,* 62 F.3d 1089, 1091–92 (8th Cir.1995) (exclusion for which the insured has assumed liability in a contract or agreement plainly excluded coverage for contractual claims and not just hold-harmless or indemnity agreements); *but see Ferrell,* 393 F.3d at 795 (without overruling or mentioning *TGA Development,* holding that the contractual liability exclusion applies only to situations where the insured has contractually assumed a third party's liability, such as in an indemnification or hold-harmless agreement).

Most courts that have held the exclusion to be limited in nature and to apply only when indemnity or hold-harmless agreements are involved have relied on a case from the Alaska Supreme Court, *Olympic, Inc. v. Providence Washington Insurance Co. of Alaska,* 648 P.2d 1008 (Alaska 1982), which interpreted an earlier version of the standard CGL form.[FN10] When *Olympic* was decided in 1982, the CGL policy contained an exclusion for contractual liability that was similar to the exclusion in the CGL policy before us, but which included an exception for "incidental contracts" rather than "insured contracts." *See id.,* at 1010; 21 ERIC MILLS HOLMES, HOLMES' APPLEMAN ON INSURANCE § 132.3[B][1] (2d ed.1996) (explaining the 1973 CGL contractual liability exclusion). The definition of "incidental contract" was narrower than the definition of "insured contract"; it did not include an explicit exception for certain indemnity or hold-harmless agreements as does the current CGL policy. *See* 21 ERIC MILLS HOLMES, HOLMES' APPLEMAN ON INSURANCE § 132.3 [B] [1]. Instead, coverage for specific indemnity or hold-harmless agreements was generally provided through a broad-form endorsement to the CGL policy. *See* 2 ROWLAND H. LONG, THE LAW OF LIABILITY INSURANCE § 10.05[2] (2006).

> FN10. Prior to 1986, the CGL policy was called the Comprehensive General Liability Insurance Policy.

In 1986, the ISO revised the CGL form to generally provide coverage for indemnity and hold-harmless agreements through the insured-contract exception within the general CGL policy, as opposed to through a broad-form endorsement. *See* 21 ERIC MILLS HOLMES, HOLMES' APPLEMAN ON INSURANCE § 132.3[B] (explaining that the purpose of the 1986 revision was to "combine ***131** the essence of the former 1973 [contractual liability exclusion] with the expanded liability coverage formerly provided under the broad-form endorsement"); *see Am. Family Mut. Ins. Co.,* 673 N.W.2d at 81.

With this history in mind, we examine *Olympic.* In that case, a lessee agreed to obtain insurance indemnifying its lessor, but obtained insurance indemnifying only itself in case of breach of the lease between the parties. *Olympic,* 648 P.2d at 1009–10. When a firefighter was killed in a fire on the leased premises, the firefighter's estate sued both lessee and lessor. *Id.* at

1010. The lessor's insurer settled with the firefighter's estate, then sued the lessee's liability insurer to recover part of the settlement. *Id.* The lessor's insurer claimed the lessee's insurer was liable because the lessee breached the lease agreement. *Id.* The lessor's insurer asserted that the lessee's insurer's incidental contract exception to the contractual liability exclusion for "any written ... lease of premises" implied that the policy insured against liability pursuant to any contract that was an incidental contract, i.e. the lease agreement. *Id.* The Alaska Supreme Court disagreed, holding that " '[l]iability assumed by the insured under any contract' refers to liability incurred when one promises to indemnify or hold harmless another, and does not refer to the liability that results from breach of contract." *Id.* at 1011. According to the court, because the exclusion was limited to indemnity and hold-harmless agreements and did not apply, the exception to the exclusion for leases could not bring the claim into coverage because the contract was not an indemnity or hold-harmless agreement. *Id.* Accordingly, the court held that the lessee's policy did not cover its failure to procure proper insurance coverage. *Id.* at 1013–14.

The *Olympic* court was interpreting the pre–1986 contractual liability exclusion, thus the court did not have a specific exception for indemnity or hold-harmless agreements before it as part of the contract. The court was not faced with a circular reading of the exclusion and insured-contract exception as we are in the instant dispute. However, the rationale behind the *Olympic* decision lends support to our interpretation of the exclusion. In reaching its holding, the *Olympic* court relied, at least in part, on its perception that breach of contract claims generally are not covered absent tort liability. The court noted in its opinion that the general terms of the policy applied only to liability imposed by law for torts, and not to damages for breach of contract. *Id.* at 1012. Thus, "[t]he contractual liability exclusion functions to relieve the insurer of responsibility for any 'extra' liability that the insured undertakes by contract beyond the liability imposed by law for negligence." *Id.* at 1011 n. 6. Moreover, the lessee in *Olympic* had a separate contractual liability policy listing specific contracts that were included in coverage, but the separate policy did not apply to the lease covenant because it did not list the covenant. A similar situation exists here: the policy did not have an endorsement adding Gilbert's contract with DART as an insured contract.

We disagree, by and large, with courts' and treatises' conclusions that the language of the contractual liability exclusion before us applies only to indemnity or hold-harmless agreements for the reasons mentioned above. Insurance policy interpretation principles emphasize a policy's plain language in determining its intended coverage. *See, e.g., Lamar Homes,* 242 S.W.3d at 14 (stating in regard to a CGL policy that coverage for a particular risk "depends, as it always has, on the policy's language, and thus is subject to change ***132** when the terms of the policy change"); *Fortis Benefits,* 234 S.W.3d at 647 (noting that insurance contract rights arise from the insurance contract language); *Fiess,* 202 S.W.3d at 753 ("For more than a century this Court has held that in construing insurance policies 'where the language is plain and unambiguous, courts must enforce the contract as made by the parties, and cannot make a new contract for them, nor change that which they have made under the guise of construction.' ") (quoting *E. Tex. Fire Ins. Co. v. Kempner,* 87 Tex. 229, 27 S.W. 122, 122 (1894)); *but see Puckett v. U.S. Fire Ins. Co.,* 678 S.W.2d 936, 938–39 (Tex.1984) (holding that an aviation insurance policy's failure to include a causal connection requirement

between the breach of the policy and the accident violated Texas public policy). We hold that the exclusion means what it says. It applies when the insured assumes liability for bodily injury or property damages by means of contract, unless an exception to the exclusion brings a claim back into coverage or unless the insured would have liability in the absence of the contract or agreement.

4. *Lamar Homes*

Gilbert argues that to adopt Underwriters' interpretation of the exclusion "effectively eviscerates" our decision in *Lamar Homes.* In *Lamar Homes,* we said a breach of contract can constitute an occurrence that causes property damage, thus bringing some breach of contract claims within the general grant of coverage for purposes of determining a duty to defend. *Lamar Homes,* 242 S.W.3d at 13. We explained that "the label attached to the cause of action—whether it be tort, contract, or warranty—does not determine the duty to defend" and that "any preconceived notion that a CGL policy is only for tort liability must yield to the policy's actual language." *Id.* Gilbert contends that if the exclusion in Underwriters' policy can operate to exclude general breach of contract claims, then our opinion in *Lamar Homes* would not have been necessary. Underwriters counters that our *Lamar Homes* decision did not interpret the exclusion but instead dealt with whether unintended construction defects could constitute an accident that would fall within the definition of an occurrence in the CGL policy's general grant of coverage.

[13] We disagree that our interpretation of the exclusion in the policy runs afoul of our decision in *Lamar Homes.* The contractual liability exclusion was not at issue in *Lamar Homes.* There we considered whether property damage to a house that resulted from construction defects could nevertheless come within the general terms of liability coverage because the damage resulted from an occurrence as defined by the CGL policy. *See id.* at 10 ("The CGL's insuring agreement grants the insured broad coverage for property damage and bodily injury liability, which is then narrowed by exclusions that 'restrict and shape the coverage otherwise afforded.' ") (quoting *Weedo v. Stone–EBrick, Inc.,* 81 N.J. 233, 405 A.2d 788, 790 (1979)). Whether a claim triggers an insurer's duty to defend and whether a claim eventually is covered or excluded for purposes of indemnity are different questions. *See D.R. Horton–Tex., Ltd. v. Markel Int'l Ins. Co.,* 300 S.W.3d 740, 743 (Tex.2009) (observing that "the duty to defend and the duty to indemnify 'are distinct and separate duties' ") (quoting *Utica Nat'l Ins. Co. of Tex. v. Am. Indem. Co.,* 141 S.W.3d 198, 203 (Tex.2004)). In *Lamar Homes,* we did not address the duty to indemnify, but rather the separate duty to defend. An insurer's duty to defend is determined under the eight-corners doctrine, while the duty to indemnify is determined by the facts as they are established ***133** in the underlying suit. *Id.* at 744 (quoting *Pine Oak Builders, Inc. v. Great Am. Lloyds Ins. Co.,* 279 S.W.3d 650, 656 (Tex.2009)). Here, the facts demonstrate that Gilbert settled RTR's breach of contract claim after the trial court granted judgment in Gilbert's favor on all theories of liability besides the contractual one. And Gilbert does not contend the trial court erred in granting summary judgment on these other theories or that any liability it might have had to RTR arose from some source other than the breach of contract claim. Thus, RTR's only claim that remained pending against Gilbert fell within the policy's contractual exclusion for purposes of determining Underwriters' duty to indemnify.

5. Ambiguity

[14] Gilbert argues that even if we hold the exclusion applies to the facts of this case, the exclusion is ambiguous and we must interpret it in favor of coverage. According to Gilbert, the exclusion could apply to general breach of contract claims *or* it could only apply to contracts for indemnity, depending on one's interpretation. Underwriters counters that the exclusion is unambiguous.

[15][16][17][18] Terms in insurance policies that are subject to more than one reasonable construction are interpreted in favor of coverage. *Comsys*, 130 S.W.3d at 194; *Evergreen Nat'l Indem. Co. v. Tan It All, Inc.*, 111 S.W.3d 669, 676 (Tex.App.-Austin 2003, no pet.). "Where an ambiguity involves an exclusionary provision of an insurance policy, we 'must adopt the construction ... urged by the insured as long as that construction is not unreasonable, even if the construction urged by the insurer appears to be more reasonable or a more accurate reflection of the parties' intent.' " *Balandran v. Safeco Ins. Co. of Am.*, 972 S.W.2d 738, 741 (Tex.1998) (quoting *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Hudson Energy Co.*, 811 S.W.2d 552, 555 (Tex.1991)). But an ambiguity does not exist simply because the parties interpret a policy differently. *See Am. Mfrs. Mut. Ins. Co. v. Schaefer*, 124 S.W.3d 154, 157 (Tex.2003). If a contract as written can be given a clear and definite legal meaning, then it is not ambiguous as a matter of law. *Progressive County Mut. Ins. Co. v. Sink*, 107 S.W.3d 547, 551 (Tex.2003); *Grain Dealers Mut. Ins. Co. v. McKee*, 943 S.W.2d 455, 458 (Tex.1997).

We agree with Underwriters that the exclusion is not ambiguous. The exclusion is straightforward and not reasonably subject to two interpretations. It applies to liabilities the insured assumes by contract or agreement and not just to a particular subset of liabilities such as indemnity contracts. As discussed above, interpreting the exclusion as narrowly as Gilbert urges would yield a circular reading when the exclusion is considered in context with the insured-contract exception to the exclusion. In order to interpret the policy in a manner that harmonizes and gives effect to all provisions so that none are meaningless, Underwriters' interpretation is the only reasonable interpretation. *See MCI Telecomms. Corp.*, 995 S.W.2d at 652.

D. Second Exception to the Exclusion

[19] Gilbert next argues that the second exception to the exclusion brings RTR's claim back into coverage. The second exception provides that the exclusion "does not apply to liability for damages ... [t]hat the insured would have in the absence of the contract or agreement." Gilbert urges that (1) in the absence of its contract with DART, Gilbert would have been liable to RTR in tort because without the contract Gilbert would not have enjoyed governmental immunity status; (2) to hold otherwise would defeat the purpose ***134** of CGL coverage because there would not be coverage when there are multiple causes of action and the tort claim is dismissed for some reason; and (3) the exception must be construed broadly in favor of coverage. Underwriters counters that the duty to indemnify is based on the actual facts proven and adjudicated liability, and the only liability theory remaining when Gilbert settled with RTR was the breach of contract claim. We agree with Underwriters.

[20] As the court of appeals observed, it is well settled that "a claim based on a contract that provides indemnification from liability does not accrue until the indemnitee's liability

becomes fixed and certain." 245 S.W.3d at 35 (quoting *Ingersoll–Rand Co. v. Valero Energy Corp.,* 997 S.W.2d 203, 205 (Tex.1999)); *see Hartrick v. Great Am. Lloyds Ins. Co.,* 62 S.W.3d 270, 275 (Tex.App.-Houston [1st Dist.] 2001, no pet.) ("[T]he duty to indemnify arises from proven, adjudicated facts.").

While this case involves a policy exception, not an indemnity provision as in the cases referenced above, the contract language similarly guides our analysis. *See Ingersoll–Rand,* 997 S.W.2d at 207. As modified by the second exception, the exclusion precludes the insurer's liability for indemnity if the insured is obligated to pay only because of its contractually assumed liability. If the insured's liability is because of an otherwise covered basis in addition to its contractually-assumed liability, the second exception brings the claim back into coverage. *See Sw. Bell Tel. Co. v. DeLanney,* 809 S.W.2d 493, 494–95 (Tex.1991) (recognizing that tort obligations are imposed by law independent of contractual obligations, but the acts of a party may simultaneously breach duties in tort and contract); *Cagle v. Commercial Standard Ins. Co.,* 427 S.W.2d 939, 943–44 (Tex.Civ.App.-Austin 1968, no writ) ("[W]here the express contract actually adds nothing to the insured's liability, the contractual liability exclusion clause is not applicable, but where insured's liability would not exist except for the express contract, the contractual liability clause relieves the insurer of liability."). Therefore, to determine whether the exception applies, we must decide whether Gilbert proved it would have had liability for RTR's damages absent its contractual undertaking. *See Comsys,* 130 S.W.3d at 193.

Gilbert asserts that if no contract existed in the first place, it would not have had immunity and RTR's negligence claim against Gilbert would not have been subject to an immunity defense. Assuming, without deciding, that Gilbert is correct, the argument misses the mark. The determination of an indemnity obligation is based on the actual facts of the case as proven and the language of the indemnity agreement. Here, the existence of the contract between Gilbert and DART was merely an underlying fact that was to be considered in determining Underwriters' indemnity obligation. *See Ingersoll–Rand,* 997 S.W.2d at 208 (noting that an indemnification cause of action accrues when the indemnitee's liability becomes fixed and certain). Because RTR's tort claims were properly dismissed, the only viable claim underlying Gilbert's settlement was for breach of contract. Gilbert asserts no other basis for its settlement than the breach of contract claim; thus, Gilbert's settlement payment for which it seeks indemnity simply was not a liability for damages it had apart from its contract with DART, as it must have been in order for the second exception to apply.

Gilbert correctly argues that our decisions require us to interpret an exception to an exclusion broadly in favor of coverage. *See Evanston Ins. Co. v. ATOFINA Petrochems., Inc.,* 256 S.W.3d 660, 668 ***135** (Tex.2008). But that principle does not mean we should distort the exception in order to find coverage where none exists. Gilbert would have us disregard the actual facts underlying its settlement and hold that the exception applies even to potential liability that Gilbert *might* have had if it had not entered into a contract with DART. We decline to do so. Indemnity under a liability policy depends on the actual facts and adjudicated liability, not possible scenarios that did not occur.

Gilbert also argues that interpreting the exception to apply only to actual proven facts and

adjudicated liability will bar coverage anytime a tort claim is dismissed during litigation and a contractual claim remains—for example, where a tort claim is dismissed based on a statute of limitations defense but a breach of contract claim remains. We understand Gilbert's concerns, but speculation about coverage of insurance policies based on surmised factual scenarios is a risky business because small alterations in the facts can warrant completely different conclusions as to coverage. It is proper that we await a fully developed, actual case to decide an issue not presented here. We note, however, as did the court of appeals, that it is common for insurance coverage determinations to depend on the final basis for the insured's liability. 245 S.W.3d at 35. For example, when a claim alleges that an insured caused damages by both negligent and intentional conduct, "a judgment based upon [negligent] conduct often triggers the duty to indemnify, while a judgment based on [intentional conduct] usually establishes the lack of a duty." *Farmers Tex. County Mut. Ins. Co. v. Griffin*, 955 S.W.2d 81, 84 (Tex.1997).

Finally, contrary to Gilbert's assertions, to hold that the second exception does not apply here does not run afoul of our decision in *Lamar Homes*, in which we said that a cause of action's label does not determine whether an insurer has a duty to defend. *See Lamar Homes,* 242 S.W.3d at 13. The second exception contemplates a situation in which an insured's liability for damages results from matters that are within the policy's coverage in addition to or in lieu of the insured's contractually-assumed liability, but it does not prescribe whether the covered liability must be based in contract or tort. Moreover, *Lamar Homes* concerned a duty to defend rather than a duty to indemnify. *Id.* at 4–5. These are separate duties and are determined differently. *D.R. Horton–Tex., Ltd.*, 300 S.W.3d at 744 n. 2 ("In contrast [to the duty to defend], the duty to indemnify arises only once liability has been conclusively determined.") (quoting 14 LEE R. RUSS & THOMAS F. SEGALLA, COUCH ON INSURANCE § 200:3 (3d ed.2009)).

The exception for liability for damages Gilbert would have in the absence of the DART contract is inapplicable where, as here, the insured has governmental immunity and liability is based on its contract. If particular relationships of the parties, their contracts, and applicable legal principles create unusual circumstances, as they do here, it is incumbent on the parties to take those relationships, circumstances, and applicable legal principles into account when entering into contracts and insurance agreements. If we held as Gilbert proposes, we would be remaking the parties' insurance agreement. We decline to do so.[FN11]

FN11. Underwriters raises additional arguments which we need not address. First, Underwriters asserts that Gilbert was not cloaked with governmental immunity based on the DART contract per se, but based on Gilbert's status as a governmental contractor and its performance of specific governmental functions. *See* TEX. TRANSP. CODE § 452.056(d) ("A private operator who contracts with an authority under this chapter is not a public entity for purposes of any law of this state except that an independent contractor of the authority that ... performs a function of the authority or an entity ... that is created to provide transportation services is liable for damages only to the extent that the authority or entity would be liable if the authority or entity were performing the function...."). Our holding precludes the need to determine whether Gilbert would have had immunity under the statute even in the absence of its particular contract, and we express no opinion on the question. Second, Underwriters

> argues that although its policy is a following-form policy generally, a separate exclusion in the excess policy bars coverage for "the failure of the Insured to complete a contract on time or to comply with any contractual obligations." Because we hold that the contractual liability exclusion in the underlying primary policy bars coverage for RTR's claim and exceptions to the exclusion do not bring the claim back into coverage, we do not reach the issue of the separate contractual exclusion in the excess policy.

***136 E. Estoppel**

Finally, Gilbert argues that if we determine no coverage exists under the policy, Gilbert is entitled to recover under an estoppel theory because Underwriters assumed control of Gilbert's defense and prejudiced Gilbert as a result. Underwriters responds that (1) Gilbert waived the issue because it did not raise it in the court of appeals, (2) Underwriters did not assume Gilbert's defense, and (3) Gilbert was not prejudiced by Underwriters' actions. We first address the procedural question.

[21] In the court of appeals, Gilbert argued that coverage existed by virtue of waiver and estoppel. After the court of appeals released its decision, we overruled cases on which Gilbert relied and held that the doctrine of estoppel may not be used to create insurance coverage where none exists under the policy. *Ulico,* 262 S.W.3d at 780. Following our decision in *Ulico,* Gilbert reframed its argument to argue that it is entitled to damages by virtue of estoppel. Our rules provide that a case may be remanded for further proceedings in light of changes in the law. TEX.R.APP. P. 60.2(f). However, an analysis pursuant to our *Ulico* opinion is substantively the same as that undertaken by the court of appeals in addressing Gilbert's estoppel issue: a determination must be made as to whether Underwriters assumed control of Gilbert's defense and is estopped to refuse to pay damages Gilbert suffered because of Underwriters' actions. We see no need to remand the case to allow the court of appeals to consider an argument it has effectively already considered. In light of the unusual circumstances, we conclude that Gilbert is entitled to make its estoppel argument, so we will consider its merits. *See Westgate, Ltd. v. State,* 843 S.W.2d 448, 455 (Tex.1992).

In *Ulico,* we explained the estoppel doctrine as it relates to coverage when an insurer assumes an insured's defense:

> [I]f an insurer defends its insured when no coverage for the risk exists, the insurer's policy is not expanded to cover the risk simply because the insurer assumes control of the lawsuit defense. But, 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.

Ulico, 262 S.W.3d at 787.

[22] Gilbert asserts that Underwriters directed Gilbert to seek summary judgment on RTR's tort claims based on governmental immunity, but did not inform Gilbert of Underwriters' position that the insurance policy did not cover breach of contract claims. Gilbert contends it was prejudiced because Underwriters' actions deprived it of the

opportunity to make an informed decision about which risk to take: ***137** (1) assert the immunity defense and risk Underwriters' denying coverage for the breach of contract claim, or (2) refuse to assert the immunity defense and risk Underwriters' denying coverage because Gilbert breached the cooperation clause.[FN12]

> FN12. We assume the validity of Gilbert's argument. However, both Grau and Gilbert's claims manager testified that at a mediation before the hearing on Gilbert's summary judgment motion one of Underwriters' attorneys told Grau the breach of contract claim might not be covered if summary judgment were granted on the basis of immunity.

The court of appeals concluded that Underwriters did not assume control of Gilbert's defense. 245 S.W.3d at 37. We 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 regardless of whether it asserted the immunity defense as Underwriters directed it to do.

Gilbert primarily relies on our decision in *Employers Casualty Co. v. Tilley,* 496 S.W.2d 552 (Tex.1973), to support its claim of prejudice. *Tilley* involved a suit in which Employers sought a declaratory judgment that it did not have coverage for a personal injury suit in which Joe Tilley was a defendant. When Tilley reported that he had been sued, Employers and Tilley entered into a standard non-waiver agreement and Employers retained an attorney to defend him. *Id.* at 554. Employers questioned whether Tilley had timely reported the accident on which the suit was based, but it did not specifically advise Tilley that a conflict of interest existed because of the late notice issue. Nor did the defense attorney advise Tilley that the attorney had a conflict of interest in that he was simultaneously defending Tilley and gathering coverage information favorable to Employers. *Id.* Employers later denied coverage, in part, on the basis of evidence developed by the defense attorney. *Id.* We held, largely on public policy grounds, that Tilley was prejudiced by Employers' actions and Employers was estopped to deny coverage. *Id.* at 561.

The facts of this case are not similar to those present in *Tilley,* and the prejudice Tilley suffered is different from the type of prejudice Gilbert claims. First, unlike the insurer in *Tilley,* Underwriters did not have a duty to defend Gilbert, nor did it retain Gilbert's defense attorney, Grau. There is no claim by Gilbert that Grau simultaneously defended Gilbert and represented Underwriters in regard to coverage, had a conflict of interest with Gilbert, developed and provided evidence to Underwriters that harmed Gilbert's coverage position without advising Gilbert, or in any other way breached his duty to Gilbert. To the contrary, Grau advised Gilbert to obtain coverage counsel and Gilbert knew Grau was not involved in coverage issues. Further, the suit with RTR was supervised by Gilbert's in-house claims manager who had over twenty-six years of experience in insurance claims and was monitored by in-house attorneys of Gilbert's parent corporation. Second, Underwriters consistently advised Gilbert during the pendency of RTR's case that coverage would be based on the actual facts underlying RTR's claims as they were determined to exist.

Gilbert does not explain how it was prejudiced by being unable to make an informed

decision about whether to assert immunity when the ultimate risk to Gilbert under either choice—whether asserting immunity or refusing to assert immunity—was the same. While Gilbert claims that if it did not assert immunity Underwriters would have denied coverage for lack of ***138** cooperation, there is no evidence that Gilbert would have had coverage for the claims even if it had refused to assert the immunity defense. Gilbert does not contest that the facts established in RTR's suit showed that all the contractors were immune. Further, there is no evidence that, regardless of whether Gilbert asserted immunity, Underwriters would have changed its position that coverage would be determined based on the facts of RTR's claim. Gilbert's lack of prejudice is reflected in a statement made by an attorney for its parent company. The attorney acknowledged that it likely would not have mattered whether Gilbert raised and pursued the issue of governmental immunity because the trial court ruled that governmental immunity extended to all the contractors. *See D.R. Horton–Tex., Ltd.*, 300 S.W.3d at 744 (noting that the duty to indemnify is determined by the facts as they are established in the underlying suit); *Pine Oak Builders, Inc.*, 279 S.W.3d at 656. Thus, Underwriters did not have coverage for RTR's claims regardless of whether Gilbert would have breached the policy's cooperation clause if it had refused to assert immunity, a question on which we express no opinion.

In sum, there is no evidence that if (1) Underwriters had advised Gilbert of Underwriters' belief that the breach of contract claim would not be covered if Gilbert succeeded in obtaining summary judgment on RTR's tort claims and (2) Gilbert had chosen not to pursue the summary judgment, then Underwriters would have settled the claim on behalf of Gilbert or been liable to indemnify Gilbert for the settlement. Thus, there is no evidence that Gilbert was prejudiced by not being able to make an informed decision as it claims.

III. CONCLUSION

We agree with the court of appeals that the trial court (1) erred in granting Gilbert's motion for summary judgment on the issue of coverage and (2) correctly granted Underwriters' motion for summary judgment on the issue of estoppel. We affirm the court of appeals' judgment.

Justice LEHRMANN did not participate in the decision.

Tex.,2010.
Gilbert Texas Const., L.P. v. Underwriters at Lloyd's London
327 S.W.3d 118, 54 Tex. Sup. Ct. J. 367

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Supreme Court of Texas.
GODDARD
v.
EAST TEXAS FIRE INS. CO.

November 30, 1886.

Appeal from Kaufman county.

Action on a policy of insurance. Judgment for defendant. Plaintiff appealed. The facts are stated in the opinion.

West Headnotes

Insurance 217 ⚿1846

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1838 Materials Related or Attached to Policies
217k1846 k. Attachments in general. Most Cited Cases
(Formerly 217k150)

Words in a slip attached by mucilage to an insurance policy in such a place and in such a manner as to have no connection with the other conditions of the policy, though the word "condition" is used therein, will not be treated as a condition of the policy.

Insurance 217 ⚿1839

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1838 Materials Related or Attached to Policies
217k1839 k. In general. Most Cited Cases
(Formerly 217k151(1))

Where a doubt as to whether a paper other than the policy was regarded by the insurer and the insured as a part of the policy, the doubt will be resolved in favor of the insured.

Insurance 217 ⚿2969

217 Insurance
217XXIV Avoidance
217XXIV(A) In General
217k2967 Warranties

217k2969 k. Distinguished from representations. Most Cited Cases
(Formerly 217k266)

It is a cardinal principle of insurance law that, in order to constitute any statement or promise of the insured a warranty, it must be made part of the policy, either by appearing in the body of the instrument, or by a proper reference in the policy to some other paper in which it is to be found. If contained in a paper annexed to the policy, but to which no reference is made therein, it is not sufficient.

Insurance 217 ⚿3054(1)

217 Insurance
217XXV Forfeiture
217XXV(B) Particular Kinds of Insurance
217k3047 Property and Title Insurance
217k3054 Keeping Books, Papers, and Safe
217k3054(1) k. In general. Most Cited Cases
(Formerly 217k335(1))

On a piece of paper attached by mucilage to a blank space on the face of the policy, it was stated that the insured agreed to keep a set of books and a copy of an inventory in an iron safe. The place on the policy where the clause was thus posted was in the middle of a sentence with which it had no proper connection and which purported to contain the promises entered into by the insurance company. The existence of the clause was not known to the insured. In an action on the policy the evidence showed that no iron safe was kept, but there was no evidence of fraud or resulting injury to the insurer. Held, that the clause was at most a representation and not a warranty, the method of attaching it precluding it from being invested with any higher dignity than a mere representation.

***70 **907** *Wood & Charlton*, for appellant.

Whitaker & Bonner, for appellee.

WILLIE, C. J.

It is apparent from the case made by the evidence that the failure of Goddard to keep his books and inventory in an iron safe at night did not arise from any intention on his part to deprive the insurance company of evidence as to the amount of stock, tools, and machinery he had on hand at the time of the fire. He was wholly ignorant of the existence of any clause in the policy imposing this duty upon him. It is not made to appear that the company has been damaged in the least by reason of Goddard's default in this respect; for the value of the stock at the time the inventory was made was fully proved, and the amount of subsequent sales, which were all for cash, could be easily ascertained from the accounts kept in the books which were preserved and open to the inspection of the company and the court. If there has been neither fraud on the part of Goddard, nor loss to the company by reason ***71** of his non-compliance with said clause, it cannot be said that it was material to the risk, and the policy is not avoided unless the provisions of the clause constitute a warranty. If they did, the law

exacts a compliance with their terms, according to their true intent and meaning, whether material or not, or whether known to the assured or not, if he had the opportunity; and it was his duty, under the circumstances, to acquaint himself with them. *Ripley* v. *AEtna Ins. Co.*, 30 N. Y. 136; *Witherell* v. *Insurance, Co.*, 49 Me. 200; May, Ins. 161; Wood, Ins. §§ 58, 176.

Treating this as a case where the assured was charged with knowledge that the clause in question was attached to the policy, as it appears in the original sent up for our inspection, the question is, did this constitute it a warranty that the assured would perform the promises contained in the clause, or the policy should be void? It is a cardinal principle of the insurance law that, in order to constitute any statement or promise of the insured a warranty, it must be made part of the policy, either by appearing in the body of the instrument, or by a proper reference in the policy to some other paper in which it is to be found. Wood, Ins. § 176, p. 340. It is in the nature of a condition precedent, and, as such, must form a part of the contract between the parties. Id. § 58; *Farmers' Loan, etc., Co.* v. *Snyder*, 16 Wend. 481. The policy is the contract; and if outside papers are to be imported into it, this must be done in so clear a manner as to leave no doubt of the intention of the parties. *Farmers' Loan, etc., Co.* v. *Snyder, supra; Insurance Co.* v. *Southard*, 8 B. Mon. 634. When there is doubt as to the intention of the parties to treat the paper as part of the policy, the courts give the benefit of the doubt to the assured, and construe the policy liberally in his favor. *Stone* v. *United States Casualty Co.*, 34 N. J. Law, 376. This is in accord with the general rule that the language of the policy, being in the language of the underwriters, if susceptible of two interpretations, that must be adopted which will sustain the claim of the assured, and give him the indemnity it was his object to secure. *Western Ins. Co.* v. *Cropper*, 32 Pa. St. 351.

The clause which the appellee seeks in this case to have construed as part of the policy is not written or printed upon the same paper***72** with the rest of that instrument, nor was it referred to in the policy as forming a part of the contract between the appellant and the insurance company. It is clear, therefore, that its conditions cannot be treated as entering into that contract, if it is to be considered as a separate and detached paper. But the edge of the paper upon which the clause is printed is made, by means of mucilage, to adhere to a blank space on the face of the policy, and upon this single fact rests the whole claim of the appellee to have the clause considered as one of the warranties and conditions of that instrument. In the case of *Bean* v. *Stupart*, 1 Doug. 11, these words were written on the margin of a marine policy ****908** of insurance: 'Thirty seamen, besides passengers.' Those words were held by Lord MANSFIELD to constitute a warranty that the insured ship sailed with that number of seamen, so that the policy would be avoided if a less number of seamen manned the vessel. He gave to the words the same effect as if they had been written in the policy itself. In the subsequent case of *Kenyon* v. *Berthon*, reported in a note to *Bean* v. *Stupart*, the same principle was announced by the same judge, and the words, 'In port twenty-ninth of July, 1776,' written transversely on the margin of the policy, were held to constitute a warranty, which, if not strictly complied with to a day, would avoid the policy. In the subsequent case of *Pawson* v. *Barneve*, 1 Doug. 12, note, Lord MANSFIELD held that though a written paper be wrapt up in the policy when it is brought to the underwriters to subscribe, and shown to them at the time, it is not a warranty, or to be considered as a part of the policy itself, but only as a representation. He held the same thing in *Bize* v. *Fletcher*, 1 Doug. 284, in reference to the

statements in a piece of paper wafered to the policy at the time the underwriters subscribed it. The statements on the papers in question in these two last cases were similar to those passed upon in *Bean* v. *Stupart* and *Kenyon* v. *Berthon*. In one case they related to the equipment of the ship in men and guns; and in the other to her condition as to repairs and strength, several particulars of the intended voyage being also mentioned.

Thus, a clear distinction is drawn by that eminent judge between statements and promises written in the policy itself, though upon the margin, and those detached from it, or contained in a separate piece of paper, and made to adhere to the policy. In the former case they are warranties; in the latter, they are, at best, no more than representations. ***73** These cases are old, but we are not informed that they have ever been overruled. On the contrary, they are cited with special approbation by some of the most respectable courts of the United States, and quoted by text writers as expressing the law, of the present time. *Insurance Co.* v. *Southard*, 8 B. Mon. 637; *Farmers' Loan, etc., Co.* v. *Snyder*, 16 Wend. 492; May, Ins. 162, 163; Wood, Ins. 416, 419.

These decisions may well be supported by the principles we have already announced. The underwriters prepare the contract to suit themselves. They can exact any lawful conditions they choose to guard against fraud, negligence, want of interest, etc., but they must do so in a manner not calculated to mislead the parties with whom they deal. They have it in their power to express their meaning in a way not to be misunderstood, or to be capable of any other construction except that which they must know the assured will give to the language. If they do not embody their warranties in the policy itself, or import them into that instrument by a proper reference to other papers in which they are contained, and the contract is capable of an interpretation which will make them mere representations, they must expect that it will be so construed. But without attempting to decide that there are no circumstances under which a foreign paper attached to a policy, without any reference to it made in that instrument, may form acondition of the contract, and be construed as a warranty, or that this clause might not have been attached to the present policy at such a place and in such a manner as to give it that effect, we are clear that the clause under consideration is not so attached to the policy as to give it any higher dignity than that of a mere representation. It is placed after a description of the property insured, and in the midst of the covenants assumed by the underwriters, and makes the policy read thus: 'The East Texas Fire Insurance Company of Tyler, Texas, organized January, 1875, in consideration of eighty-four dollars, and of the agreements herein contained, does insure Goddard & Corley to the amount of twelve hundred dollars,—$1,000 on their stock of stoves and hollowware, tin, tinware, and tinners' material; and $200 on their tools and machinery,—all while contained in the one-story, frame, shingle-roof building, and shed adjoining ****909** on the east, occupied by assured, and situated at No. 200, on Moore avenue, corner of Adelaide street, block No. 77, Terrel, Texas. *Three-fourths Loss and Iron-safe Clause*. It is agreed and understood to ***74** be a condition of this insurance that in case of any loss or damage under this policy, this company shall be liable only for three-fourths of said loss, not exceeding the sum herein insured, the other one-fourth to be borne by the assured; and, in event of other insurance hereon, this company to be liable only for its proportion of three-fourths of such loss or damage. It is understood and agreed that the assured shall keep a set of books, showing a record of this or their business including all

purchases and sales, both for cash and on credit, as well as a copy of his or their last inventory, warranted to be kept in an iron safe at night. Against all such immediate or proximate loss or damage by the assured as may occur by fire to the property above specified, but not exceeding the interest of the assured in the property, and except as hereinafter provided,' etc.; setting forth the time the policy is to last, how the damage is to be estimated, the date at which the loss is to be paid, etc. The policy then concludes by reciting the terms, conditions, and warranties upon which it is given.

It will be seen that the clause in question is inserted in the midst of a sentence with which it has no proper connection,—a sentence which purports to contain the promises made on the part of the insurance company, and not those entered into by Goddard & Cooley. It is, therefore, not only out of place, but, taken in connection with its context, is devoid of meaning. Not only so, but the policy expressly names the conditions and terms upon which it is executed, and the warranties which the assured is obligated to make good and perform; yet no warranty or condition of the kind stated in the clause in question is found among them.

Now, there are some other principles of insurance law applicable to the state of case made by the policy, as we have recited it. The first of these is: 'Words purporting to be a condition upon which the policy was issued must be set forth in such a place, and in such manner, in the policy, as leaves no doubt they were so intended; and words inserted promiscuously therein, having no connection with other conditions of the policy, although the word 'condition' is used, will not be treated as a condition of the policy.' Wood, Ins. §§ 59, 60. See, also, May, Ins. 170. This principle is well illustrated by the case of *Kingsley* v. *New England Mut. Fire Ins. Co.*, 8 Cush. 393. There the words, 'on condition that the applicants take all risk from cotton waste,' inserted between the statement of the sum insured ***75** on the property and the description of its location, were held not to constitute a condition or warranty. The present case is much stronger than the one cited. There the words were written on the face of the policy; here they are printed on a slip, and attached to it. There, though wrongly located, they do not interfere materially with the sense of the sentence in which they are embodied; here they do. There the word 'condition' is expressly used in connection with the clause; here it is not. Moreover, while it is used in the preceding sentence fixing the liability of the company at three-fourths the value of the property destroyed, it is omitted in the iron-safe clause altogether. This must have been done through design, and the design must have been to prevent the latter clause from being construed as a condition. However this may be, the policy is brought fully within the principle of law just announced, and the clause under discussion must be held not to be a warranty.

There is still another rule of law applicable to this policy, which is that, when an instrument of this character is inconsistent or ambiguous in its provisions, it must be construed most favorably for the assured. Wood, Ins. § 59, and notes; *Hoffman* v. *AEtna Ins. Co.*, 32 N. Y. 405; *AEtna Ins. Co.* v. *Jackson*, 16 B. Mon. 242; May, Ins. 183, 184. The inconsistencies and ambiguities of this policy have already been made apparent. In the first part it ****910** recites certain undertakings assumed by the assured; and then in the latter part, which is held to be the most binding portion of such a contract, it sets forth specifically what are the terms of the policy which are to be considered conditions and warranties. To take the most favorable view for the appellee, the policy leaves it doubtful whether the promises exacted of the

assured in the first part of the instrument are to be superadded as warranties to those enumerated in the last part, or whether the latter are to be considered the only warranties, leaving the former to be superadded as warranties to those case, as we have seen, the doubt must be resolved in favor of the assured. The makers of the policy could have made this meaning clear by including the iron-safe clause in the body of the policy at its proper place, but they have chosen to place it where its meaning and construction is obscured, and they must abide the consequences.

We are of opinion that the court below should have held the clause in question to have been no more than a representation; and as it was not pleaded as such by the appellee, and the proof did not show any fraud committed by ***76** the appellant, or injury suffered by the company, by reason of its not having been literally fulfilled, judgment should have been rendered for the appellant for the full amount claimed by him,—the court having found that three-fourths of the value of the property lost was at least equal to the amount for which it was insured. For the error of the court below in the matter stated its judgment will be reversed, and this court, proceeding to render such judgment as should have been rendered below, orders and adjudges that the appellant recover of the appellee the sum of $1,200, with interest thereon from November 30, 1885, and all costs of this and of the lower court.

Tex. 1886
Goddard v. East Texas Fire Ins. Co.
67 Tex. 69, 1 S.W. 906, 60 Am.Rep. 1

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Supreme Court of Texas.
HIBERNIA INS. CO.
v.
BILLS.[FN1]

FN1 Rehearing denied.

Feb. 25, 1895.

Error to court of civil appeals of Fifth supreme judicial district.

Action by R. D. Bills against the Hibernia Insurance Company on a policy of fire insurance. From the reversal by the court of civil appeals of a judgment in his favor for part of the insured property, plaintiff brings error. Reversed.

West Headnotes

Insurance 217 ⚿1856

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1856 k. Entire or severable nature of policies or contracts. Most Cited Cases
(Formerly 217k179)

A fire policy covering a building and separately valued articles of machinery and personal property in and about it is severable.

Insurance 217 ⚿2988

217 Insurance
217XXIV Avoidance
217XXIV(B) Particular Kinds of Insurance
217k2987 Property or Title Insurance
217k2988 k. In general. Most Cited Cases
(Formerly 217k253)

Where a policy covers both real and personal property, a misrepresentation which will avoid the policy as to the realty will not necessarily render it void as to the personalty.

Insurance 217 ⚿2992(1)

217 Insurance
217XXIV Avoidance
217XXIV(B) Particular Kinds of Insurance

217k2987 Property or Title Insurance
217k2992 Title or Interest of Insured
217k2992(1) k. In general. Most Cited Cases
(Formerly 217k282(1), 217k282)

A fire insurance policy covering a building, and also separately valued articles of machinery and personal property in and about it, is avoided only as to the building, which was situated on leased ground, and not as to the other property, by a clause that the "entire policy shall be void if the subject of insurance be a building on ground not owned by the insured in fee simple."

****1064 *548** McKie & Autry, for plaintiff in error.

***549** Leake, Shepard & Miller and Barry & Etheridge, for defendant in error.

***550** BROWN, J.

The Hibernia Insurance Company issued to R. D. Bills, upon his gin house and machinery, a policy of fire insurance in the sum of $1,430, the gin house being specified in the face of the policy as insured in the sum of $370, and the other items of property, separately valued at different amounts, making the total amount of insurance. The premium for the whole was the sum of $114.40. All the property was situated in and connected with the gin house, so as to be subject to destruction by the same fire. The gin house was situated upon a tract of land leased by Bills. The policy contained the following clause: 'This entire policy * * * shall be void * * * if the subject of insurance be a building on ground not owned by the insured in fee simple.' The building and all the personal property were destroyed by fire, and suit was instituted upon the policy. Defendant pleaded the above condition of the policy, and alleged that the building was upon ground not owned by Bills in fee simple, and therefore the policy was void as to the whole. It was admitted that the gin house was on leased ground, and plaintiff's counsel conceded that he could not recover for the gin house, but claimed that the policy was valid as to the other property. Upon trial the plaintiff recovered for all except the gin house, from which judgment the defendant appealed, and the court of civil appeals reversed the judgment of the district court, and remanded the case to the district court, with instructions to enter judgment for the plaintiff, Bills, for $114.40, the amount of premium paid.

The policy of insurance upon which this suit was instituted was evidently prepared by filling in the blanks in a form intended to embrace a house or personal property or both, and contains clauses applicable to the two, also such as are applicable to each class of property separately. The property insured consisted of a gin house, valued at $370, and machinery and other things situated in the house, each item valued separately, aggregating the sum of $1,430; the premium being a gross sum of $114.40.

Three assignments of error were presented to the court of civil appeals, all, however, stating in different forms the proposition that the policy sued upon was rendered entirely void by the fact that the gin house was upon land not owned by the assured in fee simple. Fraud in the application for insurance is not presented in these assignments, and therefore will not be considered by this court. The question to be decided arises upon the following language used

in the policy: 'This entire policy shall be void if the subject of insurance***551** be a building on ground not owned by the insured in fee simple.' We have inserted the language as it would read in its application to this question, omitting intervening words not applicable. It is claimed on the part of the plaintiff that this policy is a divisible contract, and that it may be void as to the building and valid as to the other property insured. On the other hand, the defendant claims that it is an entire contract, and is void in all its parts, if void at all. It is unnecessary to enter into a discussion of the rules which govern in determining whether a policy of insurance, upon different articles, separately valued, is to be held entire or not. There is much division among the courts upon the question. It would, indeed, be difficult to decide as to which has the greater number of cases in its support, and sound reasons can be given in support of each side of the controversy. The language in this policy, however, is so definite upon the subject that there is no room for construction. The insurance company selected the words in which to express the terms and conditions upon which the forfeiture could be enforced, and must abide by the effect to which they are entitled under the established rules of construction. The plaintiff accepted the policy, and is equally bound by them under the law applicable to his rights. The terms being that the policy shall be entirely void upon a certain state of case, it cannot become void in part in that event. A contract cannot be entirely void, and at the same time partially valid. Entirely void means in toto, in all its parts, and as to all rights claimed under it. We agree with counsel for defendant that the contract is entire, and that, if the facts bring the case within the language of the clause expressing the conditions of forfeiture, it is void as to all the property embraced. Plaintiff has yielded his claim as to the gin house, and we shall not discuss the effect upon that, except in so far as it is involved in the construction of the words used. The language was selected by the defendant to express the terms of forfeiture imposed by it, and the language will be strictly construed against it for that and for the additional reason that forfeitures are not favored, and will not be declared, unless the case comes within the terms prescribed. Goddard v. Insurance Co., 67 Tex. 71, 1 S. W. 906; Wood, Ins. p. 161, § 60; Insurance Co. v. Hazlewood, 75 Tex. 347, 12 S. W. 621. In order for the clause of forfeiture to be given effect, it must clearly embrace the case made by the facts. Boon v. Insurance Co., 40 Conn. 575; Insurance Co. v. Robinson, 64 Ill. 265. In the case last cited the policy provided that the company should not be liable if the loss was occasioned by explosion of certain things mentioned therein. There was an explosion of one of the kinds of explosives mentioned, in a different building, that set the fire, which fire was communicated to the property covered by the policy, and the loss occurred by fire thus caused by an explosion. ****1065** The court held that this was not within the language of the ***552** contract, and the exemption from liability did not exist. In the other case (Boon v. Insurance Co.) the policy provided that the company should not be liable for any loss or damage 'by fire which may happen or take place by means of any invasion, insurrection, riot, or civil commotion, or of any millitary or usurped power.' The property was situated in a town in Missouri, which was occupied by the Federal troops during the late war, and a superior force of Confederate troops attacked the town, when the commander of the United States troops, in order to prevent the stores falling into the hands of the Confederates, set fire to the building in which such stores were, from which the fire spread, and consumed the property insured. The court held that this did not exempt the company, because it did not fall within the terms of the policy. If the conditions or warranties be repugnant to the portions of the policy describing the subject of insurance, the condition must yield to that portion which expresses the terms of liability; as

if, for instance, the body of the policy grants insurance upon a stock such as is usually carried in a 'country store,' or such as is usually carried in a 'retail store,' and in the conditions prescribing that the carrying in the stock certain articles named as extra hazardous will cause a forfeiture of the policy, and it appear from the evidence that the articles expressly named are usually carried in such stocks and embraced in the terms of the policy, describing the subject, the clause of forfeiture must yield to the language of the body of the policy, and the forfeiture will not be enforced. Wood, Ins. p. 169, § 64; Pindar v. Insurance Co., 36 N. Y. 648; Whitmarsh v. Insurance Co., 16 Gray, 359. These authorities suffice to illustrate the rule that the terms of the policy must be broad enough to cover, under a strict construction, the facts of the case under consideration, and that every doubt arising upon the terms of the instrument must be resolved against the insurer. With this rule in view, we will examine the case now before the court, upon this point. 'The subject of the insurance' in this policy was the property insured. This consisted of a building, and various other articles of personal property, separately valued. In order to sustain the contention of the defendant, we must import into the clause of forfeiture words to give to it the effect as if it read thus: 'If the subject of insurance or any part of it be a building,' etc., as in the case of Smith v. Insurance Co., 118 N. Y. 526, 23 N. E. 883. The court, however, will not imply anything in favor of a forfeiture, but must try the matter by the language used by the parties. 'The subject of insurance,' as used in the condition of forfeiture, means a definite single subject; that is, a house, one house, and not a house and other property. If we consider all of the insured property (consisting of a house and many pieces of machinery) as constituting ***553** the subject, then the subject was not a house, and the facts do not fall within the terms of the contract. If we consider each piece of property as a separate subject of insurance, the house was not the subject, but one of the subject; and, in either case, the facts proved do not establish the contingency upon the happening of which the policy is to be entirely void. The court of civil appeals erred in reversing the judgment of the district court and rendering judgment for the defendant, for which error the judgment of the court of civil appeals is reversed, and the judgment of the district court is affirmed.

Tex. 1895
Hibernia Ins. Co. v. Bills
29 L.R.A. 706, 87 Tex. 547, 29 S.W. 1063, 47 Am.St.Rep. 121

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5 Tiffany 405, 32 N.Y. 405, 1865 WL 3325 (N.Y.), 88 Am.Dec. 337
(Cite as: 5 Tiffany 405, 32 N.Y. 405 (N.Y.), 1865 WL 3325 (N.Y.))

Court of Appeals of New York.
HOFFMAN & PLACE
v.
ÆTNA FIRE INSURANCE CO.

June Term, 1865.

***1** The effect of the usual proviso against sales, in policies of insurance, is not to interdict sales of the owners as between themselves, but only sales of proprietary interests by the parties insured to third persons.

The *dicta* to the contrary, in the case of *Murdock v. Chenango Insurance Co.* (2 Comst., 210), disapproved.

In the construction of contracts, words are not to be taken in their broadest import, when they are equally appropriate in a sense limited to the object the parties had in view, and their apparent intent as deduced from the whole instrument.

Where the language of a promisor may be understood in more senses than one it is to be interpreted in the sense in which he had reason to suppose it was *understood* by the promisee.

If it be uncertain, in view of the general tenor of an instrument and the apparent object of the parties, whether given words were used in an enlarged or a restricted sense, other things being equal, that construction should be adopted which is most *beneficial* to the promisee.

Conditions and provisos in policies of insurance are to be construed strictly against the underwriters, as they tend to narrow the range and limit the force of the principal obligation.

Every intendment is to be made against a construction of a contract under which it would operate as a snare.

Where a fluctuating stock of goods was insured by a mercantile firm, and one of its members retired, it was held that goods subsequently purchased by the continuing members of the firm, who acquired the interest of the retiring partner, were within the protection of the policy.

THE action was on a policy of insurance for $6,000, issued in February, 1861, to Hoffman, Place & Co., of New York, covering their stock of merchandise, including not only their own goods, but those held by them in trust or on commission, or sold but not delivered, in their brick and marble store in Broadway. The policy contained, among other things, a printed proviso that it should be null and void, “if the said property shall be sold or conveyed.” The insurance was renewed in February, 1862. On the 7th of March following, Silvernail, one of the partners, retired from the business, selling out his interest to Hoffman & Place, by whom the business was continued. They subsequently, with the written consent of

the company, removed the business and stock to their new brick and marble store in Duane street. The loss occurred on the 9th of April; and the company declining to pay, the present action was brought.

It was tried in the Superior Court before Judge MONELL, and the jury found a verdict for the plaintiffs. The judgment was affirmed on appeal, and the present appeal is from that decision.

The principal questions of law raised on the trial were, whether the transfer avoided the sale, and if not, whether goods afterwards added to the stock were within the protection of the policy.

West Headnotes

Insurance 217 ⚿1832(1)

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1832 Ambiguity, Uncertainty or Conflict
217k1832(1) k. In general. Most Cited Cases
(Formerly 217k146(3))

If it is uncertain, in view of the general tenor of a policy of insurance and the apparent object of the parties, whether given words are used in a restricted or enlarged sense, other things being equal, that construction should be adopted which is most beneficial to the insured.

Insurance 217 ⚿1831

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1831 k. In general. Most Cited Cases
(Formerly 217k146(3))

Conditions and stipulations in a policy of insurance are to be construed most strongly against the insurance company.

Insurance 217 ⚿2138(1)

217 Insurance
217XVI Coverage—Property Insurance
217XVI(A) In General
217k2130 Property Covered or Excluded
217k2138 Newly Acquired Property

217k2138(1) k. In general. Most Cited Cases
(Formerly 217k166)

Where a fluctuating stock of goods was insured by a mercantile firm, and one of its members retired, it was *held* that goods subsequently purchased by the continuing members of the firm, who acquired the interest of the retiring partner, were within the protection of the policy.

Insurance 217 ⚿3051

217 Insurance
217XXV Forfeiture
217XXV(B) Particular Kinds of Insurance
217k3047 Property and Title Insurance
217k3051 k. Change of title or interest. Most Cited Cases
(Formerly 217k328(3))

The effect of the usual proviso against sales in policies of insurance is not to interdict sales of the owners as between themselves, but only sales of proprietary interests by the parties insured to third persons.

John H. Reynolds, for the appellants.

Grosvenor P. Lowrey, for the respondents.

PORTER, J.

***2** The weight of judicial authority in this State is against the doctrine that a policy issued to a firm is forfeited by a transfer of interest as between the parties assured. As a contrary opinion has prevailed to some extent, it may be well briefly to retrace the history of this question in our courts.

It first arose in 1840, on the trial of the case of *McMasters v. The Westchester Mutual Insurance Co.* (25 Wend., 379). The policy was issued to McMasters & Bruce. Evidence was given tending to show that the interest of Bruce in the partnership property was assigned before the loss to McMasters. At the circuit, it was held by Judge RUGGLES, as matter of law, that such a sale by one partner to another would not relieve the insurers. The plaintiffs recovered, and a new trial was denied; but it did not become necessary to consider this question on review, the jury having found specially that the interest was not in fact transferred.

The case of *Howard & Ryckman v. The Albany Ins. Co.* was decided in 1846, and turned on a mere question of misjoinder, arising on a demurrer to the defendants' plea that before the loss one of the plaintiffs transferred to the other his interest in the property insured. It was held that under these circumstances, a *joint* action could not be maintained by the original parties; and from this decision Chief Justice BRONSON dissented. (3 Denio, 301.)

The case mainly relied on by the appellants, is that of *Murdock & Garrett v. The*

Chenango Mutual Insurance Company, decided in this court in 1849. (2 Comst., 210.) It did not involve the question now under discussion. The property insured was a building, owned at the date of the policy by the plaintiffs as tenants in common. Garrett afterwards conveyed to Murdock, the other plaintiff, his undivided half of the property. The company indorsed a consent in writing to the conveyance, with a stipulation that the policy should remain good to Murdock as sole owner of the property. Under a special provision in the charter of the company, this gave the grantee, as the sole party in interest, a right to maintain the action in his own name--equivalent to that now given by the general law to the real party in interest. (Laws of 1836, 314; 42, sec. 7.) The building was afterwards destroyed by fire, and an action was brought in the joint names of Murdock and Garrett. It was claimed by the defendants and adjudged by the court that the misjoinder of Garrett was fatal, as he had no interest in the action. Mr. Hill, who argued the cause for the defendants, insisted that, as Murdock was the sole owner at the time of the loss, the action might and should have been brought by him alone. No question was made, and under the stipulation indorsed on the policy none could be made, as to the liability of the company to Murdock for the entire loss, unless absolved from it on other grounds. Opinions were delivered by Judges CADY, STRONG and JEWETT, all holding the *misjoinder* to be fatal. The opinion of Judge STRONG was put on the specific ground that Murdock succeeded to all the rights of Garrett, and the action should, therefore, have been brought in his own name. Judge CADY conceded that it was not material to inquire whether Murdock might not have maintained an action in his own name. The observations on this question in the course of his opinion are, therefore, not to be regarded as views expressed by the court, but as the *obiter dicta* of the learned judge. They are entitled to high consideration as the views of an able and eminent jurist, but they have not the controlling force of authority.

***3** In 1850, the direct question now involved was first discussed and decided in the Supreme Court. (*Tillou v. Kingston Mut. Ins. Co.*, 7 Barb., 570.) The policy in that case had been issued in 1842, to the firm of Tillou, Doty & Crouse. In 1844, it was assigned by them to one Ketchum, with the written consent of the company, as security for the payment of a mortgage on the premises. Subsequently, and before the loss, Crouse, without the consent of the company, sold his interest in the property to the other two partners. It was provided by law, in the act of incorporation, that any policy issued by the company should become void, *upon the alienation, by sale or otherwise*, of the property insured. (Laws of 1836, 44; 466.) The action was brought in the names of the original parties, for the benefit not only of the assignee of the policy, but also of the then owners of the property. The court adjudged that a sale by one joint owner to another, of his interest in the property insured, was not a cause of forfeiture within the intent and import of this provision. They also held--the decision in 2 Comstock not having then been reported--that the recovery could be sustained, not only for the amount due to the assignee of the policy, but also for the surplus due to the owners.

When the case came before this court on appeal, the judgment was sustained to the extent of the interest of the assignee, who, in virtue of the consent of the company, was entitled to sue in the names of the original parties, as the action was commenced before the adoption of the Code. The judgment was, of course, modified by striking out the excess recovered by the owners; as it had been settled in the case of *Murdock v. The Chenango Insurance Co.* that, to

the extent of their claim, the misjoinder of Crouse as a plaintiff was a fatal ground of objection. The opinion of the court, delivered by Judge FOOT, shows the modification to have been made on the authority of that decision. Through an oversight, such as occasionally happens in all reports, the point of the decision was misapprehended in the note of the case on which the appellants rely. (5 N. Y., 405; 17 Id., 399.)

The precise question was again presented for judgment in 1853, in the case of *Wilson v. The Genesee Mut. Ins. Co.* (16 Barb., 511). The insurance was on the mercantile stock of Dixon & Co., a firm in Michigan, consisting of A. H. Dixon and Samuel G. Goss. Shortly afterward the firm was dissolved. Dixon succeeded, by purchase, to the interest of Goss, and continued the business on his own account down to the time of the fire. The action was brought by Wilson, to whom Dixon subsequently assigned the claim. Two defenses were interposed. The first was, that the policy was forfeited by the transfer from one partner to the other, of his interest in the property insured; the other was, that it was forfeited by Dixon's afterwards obtaining a further insurance on the goods, without the written consent of the company; though such a consent was obtained from their local agent in Michigan. The court overruled both defenses, and held that the policy was not forfeited, either by the sale made by the retiring partner, or by the subsequent insurance effected by his successor in interest, with the consent of the Michigan agent.

***4** The case was heard in this court, on appeal, in 1856. (4 Kern., 418.) The counsel for the defendant insisted, as a principal point, that the sale by one partner to the other avoided the policy, and cited the cases of *Howard v. The Albany Ins. Co., Murdock v. The Chenango Ins. Co.,* and *Tillou v. The Kingston Ins. Co.,* as authorities supporting the proposition. Judge COMSTOCK, who delivered the opinion of the court, did not deem it worthy even of a passing notice, but disposed of the case on a subsequent and subordinate point. He was of opinion, and the court so held, that the consent of the Michigan agent to the further insurance by Dixon, was not binding upon the company, as it appeared, by his power of attorney, that his authority was limited to receiving applications for insurance. No member of the court intimated a doubt of the correctness of the adjudication, that the sale by one partner to the other did not invalidate the policy; and of the seven judges who took part in the decision, two were in favor of a general affirmance.

In 1857, the Supreme Court had occasion incidentally to reaffirm the proposition, that the validity of a policy is not affected by transfers of interest as between the parties assured, in the case of *Dey v. The Poughkeepsie Mut. Ins. Co.* (23 Barb., 627).

The attention of this court was drawn the following year to the decision of the Supreme Court, in the case of *Tillou v. The Kingston Ins. Co.,* that transfers as between the assured are not within the prohibition against alienation; and that decision was approved by Judge PRATT, who delivered the prevailing opinion. (*Buffalo Steam Engine Works v. The Sun Mut. Ins. Co.,* 17 N. Y., 412.)

It is quite apparent, therefore, that, in this State, there is a decisive preponderance of judicial authority against the recognition of a sale by one to another of the assured, as cause of forfeiture within the meaning of the proviso. But if the authorities were in equipoise, and the

solution of the question depended on general reasoning and the application of settled and familiar principles of law, our conclusion would be in accordance with that of the court below.

The terms of the proviso are, that the policy shall be null and void, "if the said property shall be sold and conveyed." But these words are, themselves, vague and indeterminate. Are they to be understood in their largest sense, without restriction or limitation? Clearly not; for we find, on referring to other portions of the policy, that it was issued to the assured as merchants, and that it covered a stock of goods which it was their business to sell from day to day. Is the proviso applicable to the particular goods in the store at the date of the insurance? Such a construction would not only defeat the purpose of protecting a fluctuating stock, but it would annul the policy at once, for it would bring the first mercantile sale at the counter within the terms of the condition. What description of sales and conveyances, then, did the parties contemplate when this provision was framed? Evidently such, and such only, as would transfer the proprietary interest of those with whom the insurers contracted, to others with whom they had not consented to contract. They testified their confidence in each of the assured, by issuing to them the policy; but they did not choose to repose blind confidence in others who might succeed to the ownership. If the assured parted with the possession, as well as the title to the goods, the insurers knew, of course, that their liability would cease; but they were aware that, in the exigencies incident to business, parties often retain the control, posssession and apparent ownership of goods, after parting with all their title. To guard against such contingencies, they chose to provide for the forfeiture of the policy on the transfer of the title to others, even though the business should continue to be conducted by the assured.

***5** It is suggested that the proviso may have been designed to secure the continuance in the firm, of the only member in whom the insurers reposed confidence. The only evidence of their confidence in either, is the fact that they contracted with all; and the theory is rather fanciful than sound, that they may have intended to conclude a bargain with rogues, on the faith of a proviso that an honest man should be kept in the firm to watch them. Certainly, nothing appears in the present case to indicate that all the assured were not equally worthy of confidence; and it is not to be presumed that, in any case, underwriters would deliberately insure those whose integrity they had reason to distrust.

The policy in question having been issued to a mercantile firm, the company must be deemed to have had in view the fluctuating nature of a partnership business, and the changes of relative interest incident to that relation. These might be very important to the assured, though wholly immaterial to the risk. It is manifest that mere variations in the character and amounts of the interests of the assured as between themselves, did not constitute the mischief at which the proviso was aimed. If the applicants had originally objected to the form of the policy, on the ground that the effect of the clause might be to prevent the increase by a partner of his interest from one-fourth to one-third of the business, by purchase from the other members of the firm, the answer would undoubtedly have been that such a change was not within the operation or intent of the proviso. There is probably not a business firm in the State, which would accept at the usual rates, a policy declaring *in terms* that the premium should be forfeited and the insurance annulled, by a mere change of interest as between the partners. In this instance there is no such declaration; and an *implication* so repugnant to the

evident design of the contract, is not to be deduced from the unguarded use of general words, if they can be fairly limited to the appropriate and obvious sense in which they were employed by the parties.

The design of the provision was, not to interdict all sales, but only sales of proprietary interests by parties insured to parties not insured. If the words were taken literally, a renewal of the policy would be required at the close of each day's sales. Indeterminate forms of expression, in such a case, are to be understood in a sense subservient to the general purposes of the contract. It is true that the language of the proviso against sales, was not guarded by a special *exclusion* of changes of interest as between the assured, or of the sales of merchandise in the usual course of their business; but this was for the obvious reason that there was nothing in the tenor of the instrument to denote, that the *application* of the clause to such a case was within the contemplation of the underwriters. “The matter in hand is always presumed to be in the mind and thoughts of the speaker, though his words seem to admit a larger sense; and therefore the generality of the words used, shall be restrained by the particular occasion.” (Powell on Contracts, 389; *Van Hagen v. Van Rensselaer,* 18 Johns., 423.) Thus, in an action on a life policy, containing a proviso that it should be void “in case the assured should die by his own hands,” it was held by this court, that though in terms it embraced all cases of suicide, it could not properly be applied to self-destruction by a lunatic, as there was no reason to suppose that such a case was within the purpose of the clause or the contemplation of the parties. (*Breasted v. Farmers' Loan and Trust Co.,* 4 Seld., 299.) “All words,” says Lord BACON, “whether they be in deeds, or statutes, or otherwise, if they be general, and not express and precise, shall be restrained unto the fitness of the matter and the person. (Bacon's Law Maxims, Reg., 10.)

***6** Reading the proviso as it was read by the parties, it is easy to discern the purpose of its insertion. It was to protect the company from a continuing obligation to the assured, it the title and beneficial interest should pass to others, whom they might not be equally willing to trust. Words should not be taken in their broadest import, when they are equally appropriate in a sense limited to the object the parties had in view. (22 N. Y., 443; 4 Kernan, 615, 622; 5 Duer, 340; 7 Hill, 255; 1 Duer on Ins., 163, § 8.)

The terms of the policy were not such as would naturally suggest even a query in the minds of the assured, whether a transfer of interest as between themselves would work a forfeiture of the insurance, and relieve the company from its promise to indemnify both--the buyer as well as the seller--the premium being paid in advance, and the risk remaining unchanged. One of two joint payees of a non-negotiable note would hardly be more surprised to be met with a claim, that by buying the interest of his associate he had extinguished the obligation of the maker to both.

It is a rule of law, as well as of ethics, that where the language of a promisor may be understood in more senses than one, it is to be interpreted in the sense in which he had reason to suppose it was *understood* by the promisee. (*Potter v. Ontario Ins. Co.,* 5 Hill, 149; *Barlow v. Scott,* 24 N. Y., 40.)

It is also a familiar rule of law, that if it be left in doubt, in view of the general tenor of the

instrument and the relations of the contracting parties, whether given words were used in an enlarged or a restricted sense, other things being equal, that construction should be adopted which is most *beneficial* to the promisee. (Coke's Litt., 183; Bacon's Law Maxims, Reg., 3; *Doe v. Dixon,* 9 East, 16; *Marvin v. Stone,* 2 Cowen, 806.) This rule has been very uniformly applied to conditions and provisos in policies of insurance, on the ground that though they are inserted for the benefit of the underwriters, their office is to limit the force of the principal obligation. (*Yeaton v. Fry,* 5 Cranch, 341; *Palmer v. Western Ins. Co.,* 1 Story's R., 364, 365; *Petty v. Royal Exchange Ins. Co.,* 1 Burrows, 349.) In the case first cited, the action was for a marine loss, and one of the issues was, whether a recovery was barred by the entry of a ship into a blockaded port, such ports being excepted by the policy. The court held, that though the case was within the terms, it was not within the intent of the exception; and that as the risk contemplated in the clause was merely that of capture, the rule of liberal construction must be applied in favor of the promisee. The reason assigned by Chief Justice MARSHALL was, that "the words are the words of the insurer, not of the insured; and they take a particular risk out of the policy, which but for the exception would be comprehended in the contract."

***7** The appellants also encounter another rule equally at variance with the proposition they seek to maintain: "Conditions providing for disabilities and forfeitures are to receive, when the intent is doubtful, a strict construction against those for whose benefit they are introduced." (*Livingston v. Sickles,* 7 Hill, 255; *Catlin v. Springfield Ins. Co.,* 1 Sumn., 434; *Breasted v. Farmers' Loan and Trust Co.,* 4 Seld., 305.) This rule, applicable to all contracts, has peculiar force in cases like the present, where the attempt is to seize upon words introduced as a safeguard against fraud, and make them available to defeat the claim of the assured on the theory of a technical forfeiture without fault. If the policy admits of such a construction, it is due to the dexterity of the draftsman, and not to a meeting of the minds of the parties. There was nothing in the tenor of the contract to indicate to the owners that under this proviso the promise of indemnity might fail, though they did not part with the property; nor to warn them that the insurance did not protect the entire stock of goods in their store, whether they bought it from each other or from third parties. Even after the transfer of interest as between themselves, there was nothing in the policy to apprise them that their rights under it were forfeited, and that without a new insurance their property was unprotected. The general words employed are too indeterminate in their import, to create a disability so profitless to the company and so injurious to the assured.

It was suggested, rather than insisted, on the argument, that the company may have intended to make the proviso more stringent and comprehensive than it was assumed to be by the plaintiffs; and that they are bound by the words to which they assented, even if they did not fully apprehend their effect. The obvious answer is, that it would be just to neither party to assume that the insurers aimed at drawing customers into the payment of premiums, by holding out illusory promises, couched in vague and deceptive terms, for the very purpose of enabling them to elude liability. Nothing but the clearest expression of such a design would justify the assumption, that an executed contract was intended by either party as a snare. If technical forfeitures could be sustained by such intendments, the effect would be to weaken private confidence in commercial faith, and occasion just solicitude as to the security of important rights.

The other exceptions presented in the case were argued with great ability by the respective counsel, but the disposition to be made of the more important of these is mainly dependent on our views of the principal question. They are fully considered in the opinion delivered by Judge ROBERTSON in the court below, and it is sufficient for us to express our concurrence in his conclusions.

***8** The appellants seem to suppose that there is a technical embarrassment on the question of damages, growing out of the fluctuating character of the stock, and the continuance of the business by the remaining members of the firm, who succeeded, under the transfer, to the interest of the retiring partner. Looking to the nature and design of the contract of insurance, we find no such embarrassment. The language of this court, on a former occasion, is equally appropriate in the case at bar: "It was manifestly the intention of the parties to the policy, that it should cover, to the amount of the insurance, any goods of the character and description specified in the policy, which, from time to time during its continuation, might be in the store. A policy for a long period upon goods in a retail shop, applies to the goods successively in the shop from time to time. Any other construction of a policy of insurance, upon a stock in trade continually changing, would render it worthless as an indemnity." (*Hooper v. Hudson Fire Ins. Co.,* 17 N. Y., 425.)

The plaintiffs were parties to the contract made with the defendant. They were conducting the business contemplated by the terms of the policy. The insurance was intended to cover the mercantile stock of which the assured were proprietors, stored, from time to time, in the building in which that business was conducted. There was no substantial change material to the risk, and clearly none within the intent of the proviso. Each member of a partnership firm, as Lord HARDWICKE said, is "seized *per my et per tout*" of the common stock and effects. (*West v. Skip,* 1 Vesey Sen., 242.) This interest of each and all, the policy in question was designed to protect; and its language, fairly construed, is in harmony with this intent. There is no reason why the full measure of agreed indemnity should be withheld from the plaintiffs, who were owners at the date of the insurance, and sole owners at the time of the loss. (*Hooper v. Hudson River Ins. Co.,* 17 N. Y., 425, 426; *Wilson v. Genesee Mut. Ins. Co.,* 16 Barb., 511; *Jefferson Ins. Co. v. Cotheal,* 7 Wend., 73; Code, § 111.)

The judgment should be affirmed, with costs.

Judgment affirmed.

N.Y. 1865.
Hoffman & Place v. Aetna Fire Ins. Co.
5 Tiffany 405, 32 N.Y. 405, 1865 WL 3325 (N.Y.), 88 Am.Dec. 337

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658 N.W.2d 522
(Cite as: 658 N.W.2d 522)

Supreme Court of Minnesota.
The HOME INSURANCE COMPANY, et al., Respondents,
v.
NATIONAL UNION FIRE INSURANCE OF PITTSBURGH, Pennsylvania, Petitioner, Appellant,
Travelers Insurance Company, Petitioner, Appellant.

No. C1-01-1429.
Feb. 20, 2003.
As Modified on Denial of Rehearing April 3, 2003.

General liability insurer for some of corporation's subsidiaries brought action seeking reimbursement of defense costs, incurred in action against corporate parent and subsidiaries, from general liability insurer of Delaware subsidiary and from excess/umbrella insurer. Insureds intervened. The Hennepin County District Court, Catherine L. Anderson, J., granted summary judgment for defendant-insurers, and plaintiff-insurer and insureds appealed. The Court of Appeals, Robert H. Schumacher, J., 643 N.W.2d 307, affirmed in part, reversed in part, and remanded. Review was granted. The Supreme Court, Meyer, J., held that: (1) as a matter of first impression, insured gives formal "tender of defense" request to a primary or umbrella insurer by providing notice of the claim or suit and an opportunity for the insurer to defend; (2) primary insurer had standing to seek reimbursement or contribution due to its loan receipt agreement with insured; (3) coverage of excess liability policy for insured's defense costs was not triggered; (4) advertising injury coverage of umbrella policy dropped down to primary coverage; (5) insured discharged duty to maintain the requisite primary coverage; (6) umbrella insurer's breach of duty to defend excused insured's failure to provide notice that defense costs were reaching $750,000; and (7) primary insurer was required to defend subsidiary created by change in state of incorporation.

Affirmed in part, reversed in part, and remanded.

West Headnotes

[1] Appeal and Error 30 ⚿893(1)

30 Appeal and Error
30XVI Review
30XVI(F) Trial De Novo
30k892 Trial De Novo
30k893 Cases Triable in Appellate Court
30k893(1) k. In General. Most Cited Cases

Supreme Court had de novo review of all issues, because the appeal was from a summary judgment and the interpretation of insurance policies is a question of law.

[2] Insurance 217 ⚿3524

217 Insurance
217XXX Recovery of Payments by Insurer
217k3511 Subrogation Against Third Parties; Right to Proceeds of Action or Settlement
217k3524 k. Loan Receipts and Similar Transactions. Most Cited Cases

Insurance 217 ⚿3531

217 Insurance
217XXX Recovery of Payments by Insurer
217k3529 Contribution Among Insurers
217k3531 k. Primary and Excess Insurers. Most Cited Cases

Loan receipt agreement in which primary liability insurer loaned money to insured for defense costs while reserving right to seek reimbursement from other insurers gave standing to the primary insurer to pursue reimbursement or contribution from other insurers for costs to defend mutual insured.

[3] Insurance 217 ⚿3506(2)

217 Insurance
217XXX Recovery of Payments by Insurer
217k3501 Reimbursement of Payments
217k3506 Liability Insurance
217k3506(2) k. Defense Costs. Most Cited Cases

Insurance 217 ⚿3524

217 Insurance
217XXX Recovery of Payments by Insurer
217k3511 Subrogation Against Third Parties; Right to Proceeds of Action or Settlement
217k3524 k. Loan Receipts and Similar Transactions. Most Cited Cases

The general rule is that one liability insurer cannot pursue reimbursement from another insurer for defense costs incurred in defending a mutual insured; however, an exception to the general rule exists when a loan receipt agreement is in place.

[4] Insurance 217 ⚿2270(1)

217 Insurance
217XVII Coverage--Liability Insurance
217XVII(A) In General
217k2267 Insurer's Duty to Indemnify in General
217k2270 Defense Costs, Supplementary Payments and Related Expenses
217k2270(1) k. In General. Most Cited Cases

Insurance 217 ⚿2397

217 Insurance
217XVII Coverage--Liability Insurance
217XVII(B) Coverage for Particular Liabilities
217k2394 Excess and Umbrella Liability Coverage
217k2397 k. Particular Exclusions. Most Cited Cases

Coverage of excess liability policy for insured's defense costs was not triggered, and, thus, primary liability insurer was not entitled to collect them from excess insurer; the excess policy included defense costs in the definition of ultimate net loss and excluded coverage for defense expenses if covered by underlying policies, and the limits of the primary insurer's duty to defend were not surpassed.

[5] Insurance 217 ⚿2270(1)

217 Insurance
217XVII Coverage--Liability Insurance
217XVII(A) In General
217k2267 Insurer's Duty to Indemnify in General
217k2270 Defense Costs, Supplementary Payments and Related Expenses
217k2270(1) k. In General. Most Cited Cases

Insurance 217 ⚿2396

217 Insurance
217XVII Coverage--Liability Insurance
217XVII(B) Coverage for Particular Liabilities
217k2394 Excess and Umbrella Liability Coverage
217k2396 k. Scope of Coverage. Most Cited Cases

Advertising injury coverage of umbrella liability policy for idea misappropriation under an implied contract, defamation, piracy, and unfair competition was broader than primary liability coverage in suit and dropped down to primary coverage in suit alleging that insured divulged trade secrets, competed unfairly, and infringed patents; thus, insurer was liable for defense costs associated with those claims on which its coverage was primary.

[6] Insurance 217 ⚿2913

217 Insurance
217XXIII Duty to Defend
217k2912 Determination of Duty
217k2913 k. In General; Standard. Most Cited Cases

A duty to defend an insured arises if any part of the claim is arguably within the scope of the liability policy's coverage.

[7] Insurance 217 ⚿2939

217 Insurance

217XXIII Duty to Defend
217k2936 Evidence
217k2939 k. Burden of Proof. Most Cited Cases

The burden is on the liability insurer to prove that a claim clearly falls outside the coverage and that the insurer owes no duty to defend.

[8] Insurance 217 ⚿2395

217 Insurance
217XVII Coverage--Liability Insurance
217XVII(B) Coverage for Particular Liabilities
217k2394 Excess and Umbrella Liability Coverage
217k2395 k. In General. Most Cited Cases

Insurance 217 ⚿2923

217 Insurance
217XXIII Duty to Defend
217k2920 Scope of Duty
217k2923 k. Effect of Other Insurance. Most Cited Cases

Narrowing of the primary liability coverage for advertising injury during policy period was not a failure of the insured to maintain the requisite primary coverage and did not make the umbrella coverage excess; the umbrella coverage was broader than the primary coverage at the inception of the policy, and, thus, the narrowing of the primary coverage did not totally relieve the umbrella insurer of its duty to defend.

[9] Insurance 217 ⚿2395

217 Insurance
217XVII Coverage--Liability Insurance
217XVII(B) Coverage for Particular Liabilities
217k2394 Excess and Umbrella Liability Coverage
217k2395 k. In General. Most Cited Cases

Insurance 217 ⚿2923

217 Insurance
217XXIII Duty to Defend
217k2920 Scope of Duty
217k2923 k. Effect of Other Insurance. Most Cited Cases

Insured properly maintained its primary liability coverage during period of umbrella policy, even though the primary policy no longer included advertising injury coverage for defamation, piracy, and unfair competition, and, thus, umbrella insurer provided primary coverage and owed a duty to defend claims under its broader coverage for defamation, piracy, and unfair competition; the underlying coverage was consistent during the period of the

umbrella policy.

[10] Insurance 217 ⚿2919

217 Insurance
217XXIII Duty to Defend
217k2916 Commencement of Duty; Conditions Precedent
217k2919 k. Tender or Other Notice. Most Cited Cases

Before a liability insurer's duty to defend is triggered, the formal tender of a defense request is a condition precedent to the recovery of attorney fees that a party incurs defending claims that a third party is contractually obligated to pay.

[11] Insurance 217 ⚿2919

217 Insurance
217XXIII Duty to Defend
217k2916 Commencement of Duty; Conditions Precedent
217k2919 k. Tender or Other Notice. Most Cited Cases

An insured gives formal “tender of defense” request to a primary or umbrella insurer by providing notice of the claim or suit and an opportunity for the insurer to defend; an insured is not required to expressly request a defense in order to trigger the duty to defend.

[12] Insurance 217 ⚿2919

217 Insurance
217XXIII Duty to Defend
217k2916 Commencement of Duty; Conditions Precedent
217k2919 k. Tender or Other Notice. Most Cited Cases

Once an insured gives notice to a liability insurer, even without an express request for a defense, it should be the responsibility of the insurer to contact the insured to determine whether the insurer's assistance in the suit is required.

[13] Insurance 217 ⚿3111(3)

217 Insurance
217XXVI Estoppel and Waiver of Insurer's Defenses
217k3105 Claims Process and Settlement
217k3111 Defense of Action Against Insured
217k3111(3) k. Refusal, or Breach of Duty, to Defend. Most Cited Cases

Umbrella liability insurer's breach of duty to defend insured suspended insured's performance and excused its failure to provide notice that defense costs were reaching $750,000 and that umbrella insurer would soon become liable under defense costs endorsement.

[14] Indemnity 208 ⚿31(3)

208 Indemnity
208II Contractual Indemnity
208k31 Construction and Operation of Contracts
208k31(3) k. Parties in General. Most Cited Cases

When a third party to the contract seeks to enforce an indemnification right that runs to the benefit of that third party, equitable principles must be applied.

[15] Equity 150 ⚿65(1)

150 Equity
150I Jurisdiction, Principles, and Maxims
150I(C) Principles and Maxims of Equity
150k65 He Who Comes Into Equity Must Come with Clean Hands
150k65(1) k. In General. Most Cited Cases

One who comes into equity must come with clean hands.

[16] Insurance 217 ⚿2921

217 Insurance
217XXIII Duty to Defend
217k2920 Scope of Duty
217k2921 k. In General. Most Cited Cases

Insured which was created when its parent corporation incorporated it in Delaware and merged Minnesota subsidiary with the same name into the parent was implicated in lawsuit against the subsidiary corporation, and, thus, liability insurer owed duty to defend; the caption of the complaint named the subsidiary corporation and referred to merger with parent and status as Delaware corporation, this description implicated both entities, and the complaint described activities after the Minnesota corporation ceased to exist and sought injunction.

[17] Pleading 302 ⚿34(1)

302 Pleading
302I Form and Allegations in General
302k34 Construction in General
302k34(1) k. In General. Most Cited Cases

Courts are to construe pleadings liberally.

[18] Insurance 217 ⚿2913

217 Insurance
217XXIII Duty to Defend
217k2912 Determination of Duty

217k2913 k. In General; Standard. Most Cited Cases

Insurance 217 ⚿2939

217 Insurance
217XXIII Duty to Defend
217k2936 Evidence
217k2939 k. Burden of Proof. Most Cited Cases

A liability insurer's duty to defend an insured on a claim arises when any part of the claim is arguably within the scope of the policy's coverage, and an insurer that wishes to escape that duty has the burden of showing that all parts of the cause of action fall clearly outside the scope of coverage.

***524** *Syllabus by the Court*

1. A loan receipt agreement entered into between an insurer and an insured gives standing to that insurer to pursue reimbursement from another insurer for defense costs incurred in defending their mutual insured.

2. An insured gives formal tender of a defense request to a primary or umbrella insurer upon providing notice of the claim or suit and an opportunity for the insurer to defend.

3. An umbrella insurer breaches the insurance contract by failing to defend its insured's lawsuit, suspending the insured's duty to give notice of defense costs arising out of the lawsuit. Whether the suspension may benefit a third party to the contract depends on the application of equitable principles.

4. Travelers had a duty to defend its insured because the pleadings are construed broadly and a claim against its insured was arguably made in the underlying complaint.

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Mathew M. Meyer, Thomas Shroyer, Moss & Barnett, P.A., Minneapolis, Thomas Holden, Jon K. Adams, Walnut Creek, CA, for appellant, Travelers.

James T. Martin, Gislason, Martin & Varpness, P.A., Edina, for respondents.

Heard, considered, and decided by the court en banc.

O P I N I O N

MEYER, Justice.

This case is part of Cargill, Inc.'s ongoing efforts to recover its expenses in defending itself and three of its subsidiaries in a patent infringement suit. We are asked to determine the nature and extent of three insurers' duties to reimburse Cargill for its defense costs. The patent infringement suit will be reviewed briefly, followed by Cargill's insurance coverage at the time of the suit, and then the legal issues in the instant case will be presented.

Life Point Systems, Inc. (Life Point) owned proprietary rights to three patents in a spread spectrum radio frequency device. Beginning in late 1988, Life Point attempted to negotiate licensing agreements with Cargill and several of its subsidiary companies: Waycrosse, Inc.; Willknight, Inc.; and Silent Knight Security***525** Systems, Inc. (we will refer to the four collectively as Cargill). In the course of negotiations, Cargill received various documents and information regarding the device after executing a confidentiality agreement. However, the negotiations ended without an agreement.

In May of 1993, Life Point sued Cargill (the Life Point action) alleging that the Cargill subsidiaries improperly used the Life Point Device in brochures and advertising, in soliciting business, and took advantage of confidential information disclosed during negotiations. The Life Point complaint alleged patent infringement, tortious interference of contract, divulgence of trade secrets, unfair competition, and false advertising. All counts included an allegation that the conduct complained of was ongoing and would continue unless enjoined by the court. In addition to injunctive relief, the Life Point complaint sought compensatory and treble damages totaling $460 million.

Cargill retained attorneys to defend the various Cargill entities under a joint defense arrangement. The joint defense was successful; the claims against Cargill in the Life Point action were dismissed. The defense costs totaled approximately $3 million.

During the period in question, Cargill or its subsidiaries were insured under general liability policies and umbrella policies from three different insurers: the Home Insurance Company (Home), Travelers Indemnity Company of Connecticut (Travelers), and National Union Fire Insurance Company of Pittsburgh, Pennsylvania (National Union).

A. Home Insurance Company

Upon being served with the complaint in the Life Point action, Cargill immediately notified its primary insurer, Home, by sending it copies of the Life Point complaint. Home accepted this tender of defense subject to a reservation of rights. Pursuant to that reservation of rights, Home commenced a declaratory action against Cargill seeking a declaration that it had no duty to defend or indemnify Cargill for the claims asserted in the Life Point action. That declaratory judgment action eventually was moved to federal court in Minnesota where a federal judge decided that Home indeed had to defend the suit. *Home Ins. Co. v. Waycrosse, Inc.*, 990 F.Supp. 720, 730-31 (D.Minn.1996), *aff'd*, 131 F.3d 143 (8th Cir.1997). Neither Travelers nor National Union was involved in the suit and the federal court did not determine whether they shared any responsibility for the defense of the Life Point action.

Home continued to dispute its responsibility, and eventually Cargill and its subsidiaries brought suit to enforce the declaratory judgment in U.S. District Court in 1999. Four years after Home was first adjudged responsible, it entered into a loan receipt agreement with Cargill in May of 2000. In the loan receipt agreement, Home pledged to “loan” $2,450,000 to Cargill, as reimbursement for defense costs, while reserving its right to seek reimbursement from other insurers; Cargill released any claims against Home, and Cargill agreed to repay Home's “loan” with any settlement or judgment from National Union or Travelers.

B. National Union Fire Insurance of Pittsburgh, Pennsylvania

Cargill had an umbrella policy from 1989 to 1994 through National Union with a limit of $25 million, and that policy listed as insureds: Waycrosse; Cargill; and any subsidiary in which Cargill had greater than 50% ownership. Thomas Peiffer, of Cargill's insurance department, sent a copy of the Life Point complaint to National***526** Union with a letter in July of 1993 (the complaint was initially served in May of 1993). His correspondence in July and August of 1993 pointed out that the defendants were Cargill subsidiaries and placed National Union "on notice of potential excess exposure." National Union responded to the notice from Cargill with a series of correspondence from its attorney, first asserting that the Life Point claims were not covered by the National Union policy and then simply closing the file.

Three provisions of the National Union policy are pertinent to this case: Insuring Agreement I, Insuring Agreement II, and the defense costs endorsement. Insuring Agreement I is an excess insurance provision, promising to pay Cargill for "net losses" it incurs that exceed the limit of its primary coverage. Insuring Agreement II is a gap-filling provision, promising to defend Cargill as a primary insurer for losses covered by National Union but not covered by the primary insurer. The defense costs endorsement is an indemnification provision, pledging to indemnify the underlying insurer for defense costs that exceed $750,000 if particular conditions are met.

C. Travelers Insurance Company

Waycrosse, one of the Cargill subsidiaries and a defendant in the Life Point suit, was initially incorporated in Minnesota and insured under Cargill's primary policy with Home. After Waycrosse incorporated in Delaware,[FN1] it took out a general liability policy with Travelers from June of 1991 through at least 1995. Waycrosse II sent notice to Travelers of the Life Point action. Travelers responded in July of 1994 by denying coverage, based on an assertion that Waycrosse was acting through a joint venture, but reserving its right to assert additional defenses later.

> FN1. In 1991 Waycrosse, Inc. incorporated in Delaware (Waycrosse II), and the Minnesota entity (Waycrosse I) merged into Cargill.

D. The present action

Prior to the loan receipt agreement, Home instituted this suit against National Union and Travelers, seeking reimbursement of defense costs incurred in the Life Point action. Cargill and the subsidiaries entered the suit as intervenors after the loan receipt agreement was finalized. Both National Union and Travelers moved for summary judgment.

The district court granted summary judgment to National Union and Travelers. The district court ruled that National Union did not have to reimburse Cargill for three reasons: (1) Cargill did not experience a "net loss" needed to invoke the excess coverage in Insuring Agreement I; (2) Cargill failed to specifically request that National Union defend it in the Life Point action, which was necessary to trigger National Union's duty to defend; and (3) Cargill did not comply with the conditions of the defense costs endorsement, rendering it inoperative. The district court also held that Travelers did not owe any reimbursement, because Travelers had

no duty to defend Waycrosse since the Life Point complaint referred to the Minnesota version of Waycrosse (Waycrosse I), not the Delaware incarnation (Waycrosse II), and Travelers did not insure Waycrosse I.

The court of appeals reversed on four key issues. *Home Ins. Co. v. National Union Fire Ins.*, 643 N.W.2d 307 (Minn.App.2002). Although the court of appeals agreed that there had been no "net loss" as described in Insuring Agreement I, it found National Union was Cargill's primary insurer under the gap-filling provisions***527** of Insuring Agreement II for the portion of Cargill's defense costs attributable to claims covered only by National Union. The court of appeals held that a specific request was not needed to invoke National Union's duty to defend as long as the insurer had notice of the suit and an opportunity to defend. It then ruled that since National Union had first breached its duty to defend under Insuring Agreement II, Cargill was excused from its failure to comply with the defense costs endorsement and National Union must indemnify Home. The court of appeals also held that Travelers owed reimbursement to Cargill because its insured was arguably named in the complaint.

This case presents six issues with respect to the obligations of Home, National Union, and Travelers to defend Cargill:

1. Whether Home has standing to seek reimbursement from National Union and Travelers for the defense costs incurred in the Life Point action.

2. Whether National Union owes reimbursement under Insuring Agreement I for defense costs incurred in the Life Point action.

3. Whether National Union's umbrella policy afforded broader coverage for advertising injury than Home's policy such that National Union's duty to defend was triggered under Insuring Agreement II.

4. Whether Cargill's "tender of defense" was sufficient to trigger National Union's duty to defend.

5. Whether Cargill's failure to give notice under the defense costs endorsement is excused by National Union's prior breach of its duty to defend.

6. Whether Travelers owes reimbursement for defense costs incurred.

I.

[1] This court has de novo review of all issues, both because this is an appeal from summary judgment and because the interpretation of insurance policies is a question of law. *Sentinel Mgmt. Co. v. Aetna Cas. & Sur. Co.*, 615 N.W.2d 819, 827 (Minn.2000); *Haarstad v. Graff*, 517 N.W.2d 582, 584 (Minn.1994).

[2] The first issue is whether Home has standing to sue National Union and Travelers for reimbursement of defense costs. National Union moved for summary judgment arguing that Home lacked standing to maintain an action against another insurer since there was no contractual relationship between the two insurers. The district court found that Home had

standing to pursue reimbursement from National Union and Travelers for defense costs incurred in defending the Life Point action pursuant to the loan receipt agreement. The court of appeals affirmed. We agree and affirm the district court's determination.

[3] The general rule is that one insurer cannot pursue reimbursement from another insurer for defense costs incurred in defending a mutual insured. *Iowa Nat'l Mut. Ins. Co. v. Universal Underwriters Ins. Co.*, 276 Minn. 362, 368-69, 150 N.W.2d 233, 237 (1967). However, we recognize an exception to this general rule when a loan receipt agreement is in place. *Jostens, Inc. v. Mission Ins. Co.*, 387 N.W.2d 161, 167 (Minn.1986). The loan receipt agreement in the instant case is substantively identical to the agreement entered into in *Jostens*, and gives Home standing to seek contribution. *See id.* at 163. Therefore, we hold that Home has standing to sue National Union and Travelers for reimbursement of defense costs.

***528** II.

[4] The first substantive issue with respect to National Union's obligations is whether it owes any reimbursement under the excess coverage provided in Insuring Agreement I, which offers indemnification for any loss above the retained limit of the primary insurance. Cargill and Home, the primary insurer, seek to collect defense costs from National Union, the umbrella insurer, under Insuring Agreement I, in which National Union agreed:

> To pay on behalf of the Insured that portion of the ultimate net loss in excess of the retained limit as hereinafter defined, which the Insured shall become legally obligated to pay as damages for liability imposed upon the Insured by law, or liability assumed by the Insured under contract because of (i) personal injury, (ii) property damage, or (iii) advertising liability, as defined herein caused by an occurrence.
>
> * * * *
>
> [Where "Ultimate Net Loss" is defined as:]
>
> * * * Except as provided in Insuring Agreement II, "Defense", the term "Ultimate Net Loss" shall mean the total sum which the insured, or any company as its insurer, or both become obligated to pay by reason of personal injury, property damage, or advertising liability claims, either through adjudication or compromise, and shall also include hospital, medical, and funeral charges and all sums paid or payable as salaries, wages, compensation, fees, charges, interest, expenses for doctors, nurses, and investigators and other persons, and for settlement, adjustment, investigation and *defense of claims* and excluding only the salaries of the Insured or any of the underlying Insurer's permanent employees.
>
> *The Company shall not be liable for expenses as aforesaid when such are covered by underlying policies of insurance whether collectible or not.*

(Emphasis added.) Relevant to our analysis is the language in the insurance policy providing that net loss includes defense costs and that losses are not collectible under Insuring Agreement I if covered by the primary policy. The district court reasoned that since Home had been adjudged to have a duty to defend, the excess coverage in Insuring Agreement I was not triggered. The court of appeals agreed, dismissing Home's contention that such a construction

rendered the agreement illusory, or frustrated the insured's reasonable expectations.

Home's attempts to argue that Insuring Agreement I was either breached or was illusory are unpersuasive. Once the definitions of the policy terms are included, Insuring Agreement I is a promise by National Union to pay Cargill's legal liabilities that exceed either one million dollars (the retained limit) if the claim is uninsured, or the underlying insurance limits if any apply. Neither Home nor Cargill has alleged that the limits of Home's duty to defend Cargill were surpassed.[FN2] No breach can occur if the agreement was never triggered. Similarly, Home's argument that Insuring Agreement I is ambiguous and illusory is not persuasive. The agreement describes excess, not illusory, coverage. National Union's coverage under Insuring Agreement I, therefore, has not been triggered. We affirm the court of appeals and hold that Cargill and Home ***529** may not collect defense costs from National Union under Insuring Agreement I.

> FN2. Home's brief to this court mentioned that "[t]he Home policy certainly does not include costs of defense as part of the dollar limit of coverage," implying that there is no limit to its obligation for defense costs.

III.

[5] We next analyze whether Insuring Agreement II, the gap-filling provision of Cargill's policy with National Union, afforded broader coverage for advertising injury than Home's primary policy. Under Insuring Agreement II, National Union contracted to provide Cargill's defense in instances where National Union covered an injury that the underlying insurer (in this case Home) did not. Therefore, if some of the claims in the Life Point action were covered solely by National Union, National Union had a duty to defend Cargill. The relevant part of the policy reads:

> (The provisions of this Insuring Agreement apply solely to occurrences covered under this policy but not covered by any underlying policies listed in the Schedule of Underlying Insurance or any other underlying insurance providing coverage to the Insured, whether collectible or not. This Insuring Agreement shall also apply to occurrences not covered by any underlying insurance due to exhaustion of any aggregate limits by reason of any losses paid thereunder.)
>
> The Company shall:
>
> (a) defend any suit against the Insured alleging liability insured under the provisions of this policy and seeking recovery for damages on account thereof even if such suit is groundless, false or fraudulent, but the Company shall have the right to make such investigation and negotiation and settlement of any claim or suit as may be deemed expedient by the Company.

This policy term is essentially identical to the umbrella insurer's policy language in *Jostens,* 387 N.W.2d at 165 n. 3. We held in *Jostens* that this policy term obligated the umbrella insurer to pay for defense costs for defending claims arising solely under the umbrella insurer's broader (thus primary) coverage.

National Union contends that its coverage was not broader than Home's coverage because it did not cover any types of loss that Home did not also cover. If National Union is right, that its coverage was merely excess, then it had no duty to defend under Insuring Agreement II. The district court found National Union's coverage was broader because the National Union policy included the term “unfair competition” in its definition of advertising injury, while the Home policy did not. The court of appeals agreed that National Union's advertising injury coverage was broader, noting that it also included defamation and piracy, while Home's did not.

[6][7] A duty to defend an insured arises if any part of the claim is *arguably* within the scope of the policy's coverage, and the burden is on the insurer to prove that a claim clearly falls outside the coverage. *Prahm v. Rupp Constr. Co.*, 277 N.W.2d 389, 390 (Minn.1979). We are persuaded, as were the lower courts, that some of the claims in the Life Point action were *arguably* covered under Insuring Agreement II, and not covered by underlying policies, triggering National Union's duty to defend. In the first policy period, National Union's coverage was broader in that it covered “idea misappropriation under an implied contract,” while Home had no such provision. In the second policy period, National Union's coverage was broader by covering defamation, piracy, and unfair competition, while Home's coverage had no such provisions. These additional terms are important in a lawsuit that alleges Cargill divulged trade secrets, competed unfairly, and infringed patents among other claims. Thus, National Union is liable for defense costs associated ***530** with those claims on which its coverage is primary.

[8] National Union further argues that Cargill failed to maintain the requisite primary coverage during the period of National Union's umbrella coverage, which increased National Union's exposure on the policy and, in effect, converted its excess coverage to umbrella coverage. In other words, had Cargill properly maintained the requisite underlying coverage, National Union's coverage would not be implicated because all claims would be covered on the primary policies. National Union urges us to hold that its coverage is not primary on *any* of the Life Point claims because Cargill did not adequately maintain its primary coverage. Under Insuring Agreement II, Cargill was required to *maintain* consistent primary insurance coverage during the period of the umbrella policy. The relevant part of the National Union policy reads:

> **Maintenance of Underlying Insurance.** The policy or policies referred to in the attached “Schedule of Underlying Insurances,” and any renewal or replacement thereof, not more restrictive, shall be *maintained* by the Insured in full effect during the currency of this policy *without alteration of terms or conditions* except for any reduction of the aggregate limit or limits contained therein solely by payment of claims. Failure of the Insured to comply with the foregoing shall not invalidate this policy but in the event of such failure, the Company shall only be liable to the same extent as it would have been had the Insured so maintained such policy or policies.

(Emphasis added.) During the first umbrella policy period, June 1989 to June 1990, National Union's policy language required Cargill to maintain its primary insurance without change of terms or conditions. The primary insurer, Home, did change its definition of

advertising injury in the middle of that policy period. Even at the beginning of that period, however, National Union's umbrella policy was broader than Home's primary policy because it covered claims for "idea misappropriation under an implied contract," leaving open a possibility that such claims would be covered only by National Union. We conclude that because National Union's umbrella coverage at the beginning of the first policy period was broader than the primary coverage *then in force*, a subsequent narrowing of the primary coverage during the first policy period does not totally relieve National Union of its duty to defend.

[9] When National Union agreed to a second umbrella policy with Cargill in 1990, Home's definition of advertising injury had *already* changed. Home's policy with Cargill in effect starting in January 1990 no longer included defamation, piracy, and unfair competition, as had the Home policy in effect from 1988, but had a new provision covering "misappropriation of advertising ideas or styles of doing business." Cargill's underlying coverage was consistent during the period of the new policy as required. During the second umbrella policy period, National Union's coverage was broader than Home's coverage and indemnified against defamation, piracy, and unfair competition. We conclude that Cargill properly maintained its primary policies during the second policy period and National Union's coverage became primary for claims under its broader coverage, triggering its duty to defend. We hold that Insuring Agreement II is triggered and National Union is liable for defense costs associated with those claims on which coverage is primary.

IV.

Having determined that National Union's policy was at least arguably primary ***531** with respect to one or more of the Life Point claims, we turn now to the question of what constitutes a legal "tender of defense" sufficient to trigger an insurer's duty to defend. The district court opined that an insured must make an express request for defense, while the court of appeals determined that an insured's notice to the insurer with an opportunity to defend is sufficient. At issue is whether Cargill's tender to National Union triggered a duty to defend. National Union's umbrella policy provides that with respect to occurrences not covered by underlying insurance, National Union shall defend any suit "alleging liability insured under the provisions of this policy and seeking recovery for damages on account thereof." The policy further required Cargill to give "immediate notice" to National Union "[w]henever the insured has information from which the insured may reasonably conclude that an Occurrence covered hereunder * * * is likely to involve this policy."

The Life Point complaint was sent to Cargill's insurance department. Thomas Peiffer, an attorney in the insurance department with the title of "Casualty Insurance Specialist," provided a copy of the Life Point complaint to National Union in July of 1993. After requesting more information, Jonathan Sher, an attorney for National Union, responded by letter in December of 1993 and suggested that none of the claims in the Life Point action were covered under the National Union policy. Sher also questioned whether Cargill had maintained the appropriate underlying insurance. Cargill responded immediately by confirming its underlying policies. National Union closed its file, after twice referring to the defense of the Life Point suit having been "tendered." In 1995, National Union revisited the issue and wrote letters to Cargill opining that the underlying claim did not implicate its

policies.

When Home sued National Union for a portion of Cargill's defense costs, National Union refused, claiming it did not owe any of Cargill's defense costs because Cargill never gave a "formal tender of defense" to National Union. The district court agreed and determined that Cargill had not "tendered the defense" to National Union insofar as Cargill had failed to make "a specific request for a defense." The court of appeals reversed and held that once an insured gives the insurer both notice of a claim and the opportunity to defend, the tender is complete. We affirm the court of appeals.

[10] Before an insurer's duty to defend is triggered, "the formal tender of a defense request is a condition precedent to the recovery of attorney fees that a party incurs defending claims that a third party is contractually obligated to pay." *SCSC Corp. v. Allied Mutual Ins. Co.*, 536 N.W.2d 305, 316 (Minn.1995). In *SCSC Corporation*, an insured had to pay out-of-pocket its cleanup, investigation, and defense costs stemming from a groundwater contamination claim, and sued its primary insurer and umbrella insurer to recover the defense costs. *Id.* at 309-10. SCSC, the insured, did not inform the primary insurer of the occurrence until almost one year after the regulatory agency contacted SCSC. *Id.* at 317. At that time, SCSC specifically requested the insurer indemnify its losses. *Id.* This court held that SCSC did not invoke the insurer's duty to defend until it tendered its defense request, so only the costs incurred after the tender of defense had to be reimbursed. *Id.* Because SCSC had specifically requested indemnification, we did not determine whether its tender of defense was legally sufficient in that case, and we have not since enunciated the content of a tender of ***532** defense.[FN3]

> FN3. In 1996, the Eighth Circuit attempted to give content to "formal tender" under Minnesota law by looking at the facts of *SCSC Corporation* to determine what we meant by formal tender. *See C.J. Duffey Paper Co. v. Liberty Mut. Ins. Co.*, 76 F.3d 177, 178 (8th Cir.1996). Because the Eighth Circuit misunderstood the timing of the notice given to the insurer in *SCSC*, it concluded that we had implicitly decided notice was not enough. *Id.* at 178. In fact, SCSC did not inform its insurer of the claim until it asked for indemnification, so there was no period in which the insurer had notice but no request for coverage. *SCSC Corp.*, 536 N.W.2d at 317.

As there is no Minnesota decision regarding what constitutes tender, it is instructive to review what other states have done. While there are relatively few state supreme courts that have directly addressed the issue, of the three state supreme courts that have, all have ruled that notice of suit is sufficient to tender a defense. In 1998, the Illinois Supreme Court held that an insured's notice to the insurer of the lawsuit was enough to constitute tender. *Cincinnati Cos. v. West Am. Ins. Co.*, 183 Ill.2d 317, 233 Ill.Dec. 649, 701 N.E.2d 499, 504 (1998) (holding "the better rule is one which allows actual notice of a claim to trigger the insurer's duty to defend, irrespective of the level of the insured's sophistication, except where the insured has knowingly forgone the insurer's assistance").[FN4] New Hampshire and Wisconsin have also determined that putting an insurer on notice of a claim constitutes tender. *White Mountain Constr. Co. v. Transamerica Ins. Co.*, 137 N.H. 478, 631 A.2d 907, 910 (1993) (holding that "in order for an insured to tender the defense to the insurer, it need only put the insurer on notice of the claim"); *Towne Realty, Inc. v. Zurich Ins. Co.*, 201 Wis.2d

260, 548 N.W.2d 64, 67 (1996) (holding that "[a] tender of defense occurs once an insured has been put on notice of a claim against the insurer").[FN5]

FN4. Cases from the Seventh Circuit are frequently cited as adopting a rule that notice is not sufficient to constitute tender of defense. *See, e.g., Aetna Cas. & Sur. Co. v. Chicago Ins. Co.,* 994 F.2d 1254, 1261 (7th Cir.1993); *Hartford Accident & Indem. Co. v. Gulf Ins. Co.,* 776 F.2d 1380, 1383 (7th Cir.1985). These cases, however, were decided before the Illinois Supreme Court held in *Cincinnati Cos. v. West American Ins. Co.,* 183 Ill.2d 317, 233 Ill.Dec. 649, 701 N.E.2d 499, 504 (1998), that actual notice may trigger the duty to defend.

FN5. Intermediate courts in Louisiana and Pennsylvania appear to have reached the same result. *See Cobb v. Empire Fire & Marine Ins. Co.,* 488 So.2d 349, 350 (La.Ct.App.1986); *Widener Univ. v. Fred S. James & Co.,* 371 Pa.Super. 79, 537 A.2d 829, 833 (1988). *But see Litton Systems, Inc. v. Shaw's Sales & Serv., Ltd.,* 119 Ariz. 10, 579 P.2d 48, 52 (Ct.App.1978) (stating that notice must "contain full and fair information concerning the pending action and an unequivocal, certain and explicit demand to undertake the defense thereof"); *Unigard Ins. Co. v. Leven,* 97 Wash.App. 417, 983 P.2d 1155, 1160 (1999), *rev. denied,* 140 Wash.2d 1009, 999 P.2d 1263 (2000) (holding an "insured must affirmatively inform the insurer that its participation is desired").

[11] We agree with the supreme courts of Illinois, New Hampshire, and Wisconsin that sound public policy does not support a rule that requires insureds to expressly request a defense in order to trigger the duty to defend. Three broad reasons support defining "tender" as giving the insurer notice and opportunity to defend a covered lawsuit: first, it clarifies the duties of the parties early in the litigation; second, it acknowledges the greater knowledge and sophistication of the insurer; and third, it places no significant burden on insurers.

A rule that defines tender as an insured's actions in giving the insurer notice of a lawsuit and the opportunity to defend ***533** clarifies the roles and responsibilities of interested parties as early as possible. By disallowing the formation of a potential loophole for insurers around what constitutes an express request for defense, we clarify the duties of insurers and protect the bargain struck by the parties in the insurance policy. The insured paid for the insurer's promise to defend the insured for covered claims, and the insured's ignorance regarding the language the insured must use to invoke that coverage should not negate the bargain. *See Cincinnati Cos.,* 233 Ill.Dec. 649, 701 N.E.2d at 505; *White Mountain,* 631 A.2d at 910.

Our holding encourages the prompt resolution of coverage disputes we extolled in *Jostens* by clarifying when an insurer's duty to defend is triggered. *Jostens,* 387 N.W.2d at 167. Once the insurer's duty to defend is triggered, it must begin defending the suit or bring a declaratory action if it believes the policy does not cover the claim. *See id.* Forcing the insurer to take one of these two steps as soon as it receives notice of a claim helps the parties move on with the underlying suit. Once an insurer receives notice of a suit, it is responsible for defending the insured unless the insured explicitly refuses the insurer an opportunity to defend.

The relationship of an insured to its insurer is not one of equals, and a rule defining tender as notice and opportunity to defend reflects that disparity. Both primary and umbrella insurers are typically more sophisticated than the insured-they know their policies intimately, including their duties under the contract and how courts have interpreted language in the policies. *See Cincinnati Cos.*, 233 Ill.Dec. 649, 701 N.E.2d at 504-05. We will not create a legal rule that presumes an insured, whether a company or an individual, is equally sophisticated, knowing its contractual right to coverage and when and how to invoke it. Nor will we create a rule that "interpret[s] an insured's silence as a statement of intent to forgo the insurer's assistance." *Id.* at 505. Indeed, insurers are better able to "facilitate clear communication between the parties." *Towne Realty,* 548 N.W.2d at 67; *see also White Mountain,* 631 A.2d at 910.

The inequities inherent in the insurance relationship are not as manifest in this case as in an average coverage dispute. Most companies facing a multi-million dollar lawsuit will not have a parent company with deep enough pockets to ensure they have quality legal representation after their insurers abandon them. Nor would most companies have an experienced, in-house insurance department at their disposal. Instead, a smaller company left stranded by its insurer might be unable to afford a defense. And the average insured *individual* is likely to be even less knowledgeable about its contractual rights than a company, making the disparity between the insurer and insured even greater.

[12] Once notice is given, even without an express request for a defense, it should be the responsibility of the insurer to contact the insured to determine whether the insurer's assistance in the suit is required. The burden we are placing on the insurer with this rule is not onerous, as the Illinois and Wisconsin courts have noted. *Cincinnati Cos.*, 233 Ill.Dec. 649, 701 N.E.2d at 505; *Towne Realty,* 548 N.W.2d at 67. When notified of the insured's potential liability under the suit, the insurer "can simply ask the insured if the insurer's involvement is desired, thus eliminating any uncertainty on the question." *Cincinnati Cos.* at 504. While in *SCSC Corporation,* 536 N.W.2d at 316-17, we wanted to make sure that insurers could not be saddled with defense costs over which they had no control, this is not a concern here. The "notice and opportunity to defend" ***534** rule we adopt ensures insurers will not be surprised when defense costs are foisted on them.

We hold that once an insured provides its primary or umbrella insurer with notice of a suit and opportunity to defend, it has tendered the defense as required by *SCSC Corporation.* On the record before us, therefore, we conclude that Cargill legally tendered its defense to National Union as required by Insuring Agreement II.

V.

[13] Home seeks to enforce the provisions of Cargill's defense cost endorsement with National Union in which National Union agrees to repay the primary insurer for defense costs exceeding $750,000 as long as the insured notifies National Union that costs are approaching that level and obtains consent. Application of the endorsement would greatly benefit Home: the defense costs in the suit exceeded two million dollars, entitling Home to recover over one million. Under the contract, the insured is obligated to communicate with National Union as follows:

> The company shall indemnify the particular underlying insurer(s) of the Insured on a per occurrence basis for all costs of defending the Insured in excess of $750,000.
>
> The Insured shall notify the company when it is reasonably apparent to the Insured that "defense costs" will reach $750,000 and shall obtain the written consent of the company before incurring additional fees, costs or expenses, such consent not to be unreasonably withheld.
>
> * * * *
>
> With regard to an occurrence, failure of the Insured to obtain the written consent of the company set forth above, shall render this endorsement without effect as to that occurrence.

The district court determined that Cargill's failure to notify National Union that defense costs had reached $750,000 resulted in complete forfeiture of Home's indemnification rights. The court of appeals did not reach the notice issue, concluding instead that "National Union breached its insurance contract prior to implication of the notice requirement." *Home Ins.*, 643 N.W.2d at 325. The court of appeals held that because National Union breached the insurance contract by not defending Cargill in the Life Point action, and the breach occurred prior to implication of the notice requirement, Cargill was excused from providing notice under the contract.

We agree that National Union's failure to defend Cargill in the Life Point action breached its insurance contract. *See Domtar, Inc. v. Niagara Fire Ins. Co.*, 563 N.W.2d 724, 740 (Minn.1997) (treating the insurer's failure to defend as a breach of contract). And because we agree that National Union's breach suspended performance under the contract by Cargill, Cargill's failure to provide notice that defense costs were reaching $750,000 is excused. *See Space Center, Inc. v. 451 Corp.*, 298 N.W.2d 443, 451 (Minn.1980) (noting that "a repudiating party cannot set up the other party's subsequent nonperformance or a breach to avoid liability for its own prior total breach"). *Accord* Restatement (Second) of Contracts § 237 (1981) ("it is a condition of each party's remaining duties to render performances to be exchanged under an exchange of promises that there be no uncured material failure by the other party to render any such performance due at an earlier time"). While the remedy for breach is generally to grant the nonbreaching party the benefit of the bargain, *Domtar*, 563 N.W.2d at 739, it is another matter to extend the benefit of the bargain to Home, a third party to the contract.

***535** [14][15] When a third party to the contract seeks to enforce an indemnification right that runs to the benefit of that third party, equitable principles must be applied. *See Hermeling v. Minnesota Fire & Cas. Co.*, 548 N.W.2d 270, 273 n. 1 (Minn.1996) (noting that indemnity and contribution are both remedies based on equitable principles), *overruled on other grounds by Oanes v. Allstate Ins. Co.*, 617 N.W.2d 401 (Minn.2000). It is a well-established principle that "one who comes into equity must come with clean hands." *Fred O. Watson Co. v. U.S. Life Ins. Co.*, 258 N.W.2d 776, 778 (Minn.1977). While it is true that National Union failed to provide a defense in the Life Point action, neither did Home, the primary insurer, provide such a defense. Indeed, if Home had honored its policies it would have defended Cargill beginning

in June of 1993. Hypothetically, if Home had provided Cargill's defense, it seems likely that Home would have, in the normal course of providing that defense, alerted National Union as defense costs approached $750,000. Instead, Home nominally agreed to defend and then never paid any defense costs until it faced an enforcement action six years later. Therefore, because this case reaches us on appeal from summary judgment with very little information in the record, we remand to the district court to determine whether Home has the requisite "clean hands" to enforce this indemnification provision against National Union. In particular, the district court is to focus on Home's knowledge and action with respect to the Life Point action from 1993 onward.

VI.

[16] We turn now to answer whether Travelers owes reimbursement for defense costs incurred. Travelers is implicated because it provided primary insurance coverage for Waycrosse, Inc. (one of Cargill's subsidiary companies) from June 1991 through June 1993, a period of time covered by the Life Point complaint. Waycrosse, Inc. (Waycrosse I) was a Minnesota corporation until June 1991 and insured under Home's policy. A new entity was then formed with the same name, but incorporated in Delaware (Waycrosse II), with the Minnesota entity merging into Cargill. Both Waycrosse companies operated out of Cargill's offices in Minnesota with the same employees and conducted the same business operations. When Waycrosse was sued in the Life Point action, it sent notice to Travelers of the Life Point complaint, and Travelers responded by refusing to defend and denying coverage under a joint venture exclusion. Later, Travelers refused to defend and claimed that the Life Point complaint only implicated Waycrosse I and none of the claims even arguably implicated Waycrosse II.

The district court granted Travelers' motion for summary judgment and determined that the Waycrosse company named in the Life Point complaint was not Travelers' insured. The court of appeals disagreed. The court of appeals applied the summary judgment principle that facts must be construed in the light most favorable to the nonmoving party and held that the Life Point complaint implicated Waycrosse II, which Travelers insured.

[17][18] In addition to the summary judgment principle favoring the nonmoving party, two rules of construction weigh against granting summary judgment to Travelers in this case. First, courts are to construe pleadings liberally. *L.K. v. Gregg*, 425 N.W.2d 813, 819 (Minn.1988). Second, "[a] duty to defend an insured on a claim arises when any part of the claim is 'arguably' within the scope of the policy's coverage, and an insurer who wishes to escape that duty has the burden of ***536** showing that all parts of the cause of action fall clearly outside the scope of coverage." *Jostens*, 387 N.W.2d at 165. When we construe the complaint liberally, a claim is arguably made against Travelers' insured, Waycrosse II, bringing the suit within Travelers' duty to defend.

The Life Point complaint does not appear cognizant of the two Waycrosse corporations. In the caption it names "Waycrosse Inc., now merged into Cargill, Inc., a Delaware corporation." That description implicates both Waycrosse entities-Waycrosse I because it had merged into Cargill, and Waycrosse II because it is a Delaware corporation (while Waycrosse I was not). Thereafter, the Life Point plaintiffs continually refer to Cargill, naming Waycrosse as a

member, even when describing activities after Waycrosse I ceased to exist in June 1991. The complaint also seeks injunctive relief against Waycrosse, which was only possible from Waycrosse II, since Waycrosse I was no longer in existence. The complaint was sufficiently unclear that Travelers did not even raise this defense to coverage originally. Given that we are to construe pleadings broadly, and a duty to defend arises when any claim is arguably covered, we affirm the court of appeals' ruling and hold that Travelers had a duty to defend its insured, Waycrosse, Inc.

We affirm in part, reverse in part, and remand to the district court for further proceedings in accordance with this opinion.

HANSON, J., took no part in the consideration or decision of this case.

Minn.,2003.
Home Ins. Co. v. National Union Fire Ins. of Pittsburgh
658 N.W.2d 522

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728 F.3d 491, 2013 A.M.C. 2429
(Cite as: 728 F.3d 491)

United States Court of Appeals,
Fifth Circuit.
In re DEEPWATER HORIZON.
Ranger Insurance, Limited, Plaintiff–Appellee
v.
Transocean Offshore Deepwater Drilling, Incorporated; Transocean Holdings, L.L.C.; Transocean Deepwater, Incorporated; Triton Asset Leasing GMBH, Intervenor Plaintiffs–Appellees
v.
BP P.L.C.; BP Exploration & Production, Incorporated; BP American Production Company; BP Corporation North America, Incorporated; BP Company North America, Incorporated; BP Products North America, Incorporated; BP America, Incorporated; BP Holdings North America, Limited, Defendants–Intervenor Defendants–Appellants.
Certain Underwriters at Lloyd's London, Plaintiff–Appellee
v.
Transocean Offshore Deepwater Drilling, Incorporated; Transocean Holdings, L.L.C.; Transocean Deepwater, Incorporated; Triton Asset Leasing GMBH, Intervenor Plaintiffs–Appellees
v.
BP P.L.C.; BP Exploration & Production, Incorporated; BP American Production Company; BP Corporation North America, Incorporated; BP Company North America, Incorporated; BP Products North America, Incorporated; BP America, Incorporated; BP Holdings North America, Limited, Defendants–Intervenor Defendants–Appellants.

No. 12–30230.
Aug. 29, 2013.

Background: Primary liability and excess liability insurers for insured owner of mobile offshore drilling unit called *Deepwater Horizon* filed suit seeking declaratory judgment that insurers had no additional-insured obligation to oil company, that entered drilling contract with owner, with respect to underlying pollution claims arising from oil spill due to onboard explosion causing drilling unit to sink into Gulf of Mexico. After insured intervened, the United States District Court for the Eastern District of Louisiana, Carl J. Barbier, J., 2011 WL 5547259, denied oil company's motion for judgment on the pleadings, and entered partial final judgment in favor of insurers. Oil company appealed.

Holdings: The Court of Appeals, E. Grady Jolly, Circuit Judge, held that:
(1) question would be certified as to whether umbrella policies alone determined scope of oil company's coverage as additional insured, and
(2) question would be certified as to application of doctrine of contra proferentem.

Questions certified.

West Headnotes

[1] Insurance 217 ⚿1832(1)

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1832 Ambiguity, Uncertainty or Conflict
217k1832(1) k. In general. Most Cited Cases

Under Texas law, if an insurance coverage provision is susceptible to more than one reasonable interpretation, the court must interpret that provision in favor of the insured, so long as that interpretation is reasonable; the court must do so even if the insurer's interpretation is more reasonable than the insured's interpretation.

[2] Insurance 217 ⚿1835(2)

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1835 Particular Portions or Provisions of Policies
217k1835(2) k. Exclusions, exceptions or limitations. Most Cited Cases

Insurance 217 ⚿2098

217 Insurance
217XV Coverage—in General
217k2096 Risks Covered and Exclusions
217k2098 k. Exclusions and limitations in general. Most Cited Cases

Under Texas law, if an insurance coverage provision is susceptible to more than one reasonable interpretation, in particular, exceptions or limitations on liability are strictly construed against the insurer and in favor of the insured, and an intent to exclude coverage must be expressed in clear and unambiguous language.

[3] Federal Courts 170B ⚿3107

170B Federal Courts
170BXV State or Federal Laws as Rules of Decision; Erie Doctrine
170BXV(C) Unsettled or Undecided Questions
170Bk3105 Withholding Decision; Certifying Questions
170Bk3107 k. Particular questions. Most Cited Cases
(Formerly 170Bk392, 217k2396)

Question would be certified as to whether oil company was covered for damages, arising from oil spill due to explosion on insured's mobile offshore drilling unit that sank in Gulf of Mexico, because language of umbrella liability policies alone determined extent of company's

coverage as additional insured if, and so long as, the additional insured and indemnity provisions of drilling contract were separate and independent.

[4] Federal Courts 170B 3107

170B Federal Courts
170BXV State or Federal Laws as Rules of Decision; Erie Doctrine
170BXV(C) Unsettled or Undecided Questions
170Bk3105 Withholding Decision; Certifying Questions
170Bk3107 k. Particular questions. Most Cited Cases
(Formerly 170Bk392, 217k1832(1))

Question would be certified as to whether doctrine of contra proferentem applied to interpretation of liability insurance coverage provision of drilling contract between oil company and insured owner of mobile offshore drilling unit that exploded and sank in Gulf of Mexico.

***493** Michael John Maloney, Maloney, Martin & Associates, David Wallace Holman, Esq., Holman Law Firm, P.C., Byron Charles Keeling, Keeling & Downes, P.C., Houston, TX, for Plaintiff–Appellee.

Steven Lynn Roberts, Rachel Giesber Clingman, Attorney, Sutherland Asbill & Brennan, L.L.P., John Michael Elsley, Esq., Attorney, Royston, Rayzor, Vickery & Williams, L.L.P., Daniel O. Goforth, Goforth Geren Easterling, L.L.P., Houston, TX, Brad D. Brian, Esq., Daniel Benjamin Levin, Munger, Tolles & Olson, L.L.P., Los Angeles, CA, Edward F. Kohnke, IV, Esq., Edwin G. Preis, Jr., Esq., Preis & Roy, A.P.L.C., Kerry J. Miller, Frilot, L.L.C., New Orleans, LA, Kent C. Sullivan, Sutherland, Asbill & Brennan, L.L.P., Austin, TX, for Intervenor Plaintiffs–Appellees.

David B. Goodwin, Allan Baron Moore, Covington & Burling, L.L.P., San Francisco, CA, for Defendants–Intervenor Defendants–Appellants.

Richard N. Dicharry, Evans Martin McLeod, Esq., Phelps Dunbar, L.L.P., New Orleans, LA, Kyle S. Moran, Esq., Attorney, Phelps Dunbar, L.L.P., Gulfport, MS, for Plaintiff–Appellee.

Appeal from the United States District Court for the Eastern District of Louisiana.

Before JOLLY, BENAVIDES, and HIGGINSON, Circuit Judges.

E. GRADY JOLLY, Circuit Judge:

The original opinion in this case was filed on March 1, 2013.[FN1] Because this case involves important and determinative questions of Texas law as to which there is no controlling Texas Supreme Court precedent, the panel, upon the petition for rehearing, unanimously withdraws the previous opinion and substitutes the following certified questions to the Supreme Court of Texas.

FN1. *In re Deepwater Horizon*, 710 F.3d 338 (5th Cir.2013).

CERTIFICATION FROM THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT TO THE SUPREME COURT OF TEXAS, PURSUANT TO THE TEXAS CONSTITUTION ART. 5 § 3–C AND TEXAS RULE OF APPELLATE PROCEDURE 58.1.

TO THE SUPREME COURT OF TEXAS AND THE HONORABLE JUSTICES THEREOF:

I. Style of the Case: Parties and Counsel

The style of the case is In re: Deepwater Horizon: Ranger Insurance, Limited, Plaintiff–Appellee v. Transocean Offshore Deepwater Drilling, Incorporated; Transocean Holdings, L.L.C.; Transocean Deepwater, Incorporated; Triton Asset Leasing GMBH, Intervenor Plaintiffs–Appellees v. BP P.L.C.; BP Exploration & Production, Incorporated; BP American Production Company; BP Corporation North America, Incorporated; BP Company North America, Incorporated; BP Products North America, Incorporated; BP America, Incorporated; BP Holdings North America, Limited Defendants–Intervenor Defendants–Appellants; Certain Underwriters at Lloyd's London, Plaintiff–Appellee,***494** Transocean Offshore Deepwater Drilling, Incorporated; Transocean Holdings, L.L.C.; Transocean Deepwater, Incorporated; Triton Asset Leasing GMBH, Intervenor Plaintiffs–Appellees v. BP P.L.C.; BP Exploration & Production, Incorporated; BP America Production Company; BP Corporation North America, Incorporated; BP Company North America, Incorporated; BP Products North America, Incorporated; BP America, Incorporated; BP Holdings North America, Limited, Defendants–Intervenor Defendants–Appellants. This is Case No. 12–30230, in the United States Court of Appeals for the Fifth Circuit, on appeal from the judgment of the United States District Court for the Eastern District of Louisiana. Federal jurisdiction is premised upon 28 U.S.C. § 1333.

The names of all the parties to the case, each of whom is represented by counsel, and the respective names, addresses, and telephone numbers of their counsel, are as follows:

• Ranger Insurance, Limited, plaintiff in the district court and appellee in this court, represented by Michael John Maloney of Maloney, Martin & Associates, Suite 100, 3401 Allen Parkway, Houston, TX 77019–0000, Tel. 713–759–1600;

• Transocean Offshore Deepwater Drilling, Incorporated; Transocean Holdings, L.L.C.; Transocean Deepwater, Incorporated; and Triton Asset Leasing GMBH, intervenor—plaintiffs in the district court and appellees in this court, represented by Steven Lynn Roberts, of Sutherland Asbill & Brennan, L.L.P., Suite 3700, 1001 Fannin Street, Houston, TX 77002–6760, Tel. 713–470–6192;

• BP, P.L.C.; BP Exploration & Production, Incorporated; BP American Production Company; BP Corporation North America, Incorporated; BP Company North America, Incorporated; BP Products North America, Incorporated; BP America, Incorporated; BP Holdings North America Limited, defendants and defendant-intervenors in the district court and appellants in this court, represented by David B. Goodwin of Covington & Burling, L.L.P., 35th Floor, 1 Front Street, San Francisco, CA 94111–5356, Tel. 415–591–6000; and

• Certain Underwriters at Lloyds London, plaintiff in the district court and appellee in this court, represented by Richard N. Dicharry of Phelps Dunbar, L.L.P., Suite 2000, 365 Canal Street, 1 Canal Place, New Orleans, LA 70130, Tel. 504–556–1311.

II. Statement of the Case

Transocean Holdings, Inc. ("Transocean") owned the *Deepwater Horizon*, a semi-submersible, mobile offshore drilling unit. In April 2010, the *Deepwater Horizon* sank into the Gulf of Mexico after burning for two days following an onboard explosion ("Incident" or " *Deepwater Horizon* Incident"). At the time of the Incident, the *Deepwater Horizon* was engaged in exploratory drilling activities at the Macondo Well under a Drilling Contract between the Appellant BP American Production Company's (together with its affiliates, "BP") predecessor and Transocean's predecessor. This Contract required Transocean to maintain certain minimum insurance coverages for the benefit of BP. The extent to which these policies covered BP's pollution-related liabilities arising from the *Deepwater Horizon* Incident is the subject of this appeal.

The Insurance Contracts

Transocean held insurance policies with a primary liability insurer, Ranger Insurance Ltd. ("Ranger"), as well as several excess liability insurers led by London market syndicates ("Excess Insurers;" together with Ranger, "Insurers"). Transocean's insurance policy with Ranger provided at least $50 million of general liability coverage, and its policies with ***495** the Excess Insurers formed four layers of excess coverage directly above the Ranger Policy that provided at least $700 million of additional general liability coverage. The Ranger and Excess Policies contain materially identical provisions. [FN2] The Policy terms that are important to this case are "Insured" and "Insured Contract." The Policies define "Insured" as including the Named Insured, other parties, and

> FN2. As the district court noted (and the Insurers have not disputed), this similarity allows the court to treat all of the Insurers as one for purposes of analysis in this case.

> (c) any person or entity to whom the "Insured" is obliged by any oral or written "Insured Contract" (including contracts which are in agreement but have not been formally concluded in writing) entered into before any relevant "Occurrence", to provide insurance such as is afforded by this Policy....

The Policies define "Insured Contract" as follows:

> The words "Insured Contract", whenever used in this Policy, shall mean any written or oral contract or agreement entered into by the "Insured" (including contracts which are in agreement but have not been formally concluded in writing) and pertaining to business under which the "Insured" assumes the tort liability of another party to pay for "Bodily Injury", "Property Damage", "Personal Injury" or "Advertising Injury" to a "Third Party" or organization. Tort Liability means a liability that would be imposed by law in the absence of any contract or agreement.[FN3]

> FN3. The Policies contain further provisions addressing other insureds. Endorsement 1 provides a general condition that additional insureds are automatically included where

> required by written contract. Condition D.1 to Section I coverage limits the coverage of additional insureds: Transocean has the privilege to name additional insureds only to the extent as is required under contract or agreement.

The Drilling Contract

The Drilling Contract defines BP's and Transocean's obligations to one another, separately identifying the liabilities each party assumes. Article 20 of the Contract is a singular provision that imposes upon Transocean an insurance requirement:

> 20.1 *INSURANCE*
>
> Without limiting the indemnity obligations or liabilities of CONTRACTOR [Transocean] or its insurer, at all times during the term of this CONTRACT, CONTRACTOR **shall maintain insurance covering the operations to be performed under this CONTRACT as set forth in Exhibit C.**

(Emphasis added.) Exhibit C to the Drilling Contract is titled "Insurance Requirements" and establishes the types and minimum level of coverage that Transocean is obligated to maintain. This Exhibit provides that Transocean shall carry all insurance at its own expense and that the policies "shall be endorsed to provide that there will be no recourse against [BP] for payment of premium." Further, Exhibit C states:

> [BP], its subsidiaries and affiliated companies, co-owners, and joint venturers, if any, and their employees, officers and agents **shall be named as additional insureds in each of [Transocean's] policies, except Workers' Compensation for liabilities assumed by [Transocean] under the terms of this Contract.**
>
> (Emphasis added.)

The Procedural History

Following the Incident, BP notified the Insurers of its *Deepwater Horizon*-related ***496** losses. The Excess Insurers and Ranger each filed a one-count declaratory judgment action against BP.[FN4] The Insurers' complaints are substantively identical—both request a declaration that the Insurers have "no additional-insured obligation to BP with respect to pollution claims against BP for oil emanating from BP's well" as a result of the *Deepwater Horizon* Incident. The Insurers acknowledge that "the [D]rilling Contract requires additional insured protection in favor of certain BP entities." Thus, all parties concede that the Drilling Contract is an "insured contract" under the policies and that the policies provide some insurance coverage to BP as an additional insured. The issue in contention is the scope of BP's insurance coverage.

> FN4. In February 2011, the Judicial Panel on Multidistrict Litigation transferred both cases to the United States District Court for the Eastern District of Louisiana for coordinated pretrial proceedings with the other *Deepwater Horizon*-related litigation pending in that court. In March 2011, Transocean moved for leave to intervene in the consolidated actions, which motion the court granted.

In July 2011, BP moved for judgment on the pleadings, under Rule 12(c) of the Federal

Rules of Civil Procedure, against the Insurers. Relying upon Texas and Fifth Circuit precedent as developed in *Evanston Ins. Co. v. ATOFINA Petrochems., Inc.*, 256 S.W.3d 660 (Tex.2008), and in *Aubris Resources LP v. St. Paul Fire & Marine Ins. Co.*, 566 F.3d 483 (5th Cir.2009), BP argued (1) it was an "additional insured" under the insurance policies at issue and (2) the insurance policies alone—and not the indemnities detailed in the Drilling Contract—govern the scope of BP's coverage rights as an "additional insured." FN5

FN5. BP argues this motion did not require a determination of any rights or obligations of BP or Transocean to one another under any provisions of the Drilling Contract.

The district court found *ATOFINA* and *Aubris* are distinguishable from the case at hand and denied BP's Rule 12(c) motion in November 2011. In particular, the court read Transocean's insurance obligation in Exhibit C to the Drilling Contract to be to name BP as an "additional insured[ ] in each of [Transocean's] policies ... for liabilities assumed by [Transocean] under the terms of the contract." That is, the district court found BP's proffered reading of this clause unreasonable, and read the clause as if there were a comma following the phrase "except Workers' Compensation;" this reading rendered those three words their own discrete carve out from liability. Reasoning further that this interpretation required Transocean to name BP as an insured only for liabilities Transocean explicitly assumed under the contract, the court then looked to Article 24 of the Drilling Contract to conclude that BP was not covered under Transocean's policy for the pollution-related liabilities deriving from the *Deepwater Horizon* Incident (as the spill originated below the surface of the water). FN6

FN6. With respect to pollution-related liabilities, Article 24.1 of the Contract provides:

> CONTRACTOR [Transocean] shall assume full responsibility for and shall protect, release, defend, indemnify, and hold COMPANY [BP] and its joint owners harmless from and against any loss, damage, expense, claim, fine, penalty, demand, or liability **for pollution or contamination,** including control and removal thereof, **originating on or above the surface of the land or water,** from spills, leaks, or discharges of fuels, lubricants, motor oils, pipe dope, paints, solvents, ballast, air emissions, bilge sludge, garbage, or any other liquid or solid whatsoever in possession and control of CONTRACTOR....
>
> (Emphasis added.) Article 24.2 then provides:
>
> COMPANY [BP] shall assume full responsibility for and shall protect, release, defend, indemnify, and hold CONTRACTOR [Transocean] harmless from and against any loss, damage, expense, claim, fine, penalty, demand, or liability **for pollution or contamination,** including control and removal thereof, **arising out of or connected with operations under this CONTRACT hereunder and not assumed by CONTRACTOR in Article 24.1 above**....
>
> (Emphasis added.)

***497** Following further submissions of the parties, the district court then entered a partial final judgment on the Insurers' complaints under Rule 54(b). Effective March 1, 2012, the

court held "by its terms, the Court's Order and Reasons [on BP's motion for judgment on the pleadings] not only denied BP's motion but also granted judgment on the pleadings against [BP] and in favor of the Plaintiff Insurers on the Plaintiff Insurers' complaints." FN7 BP timely appealed. A unanimous panel of this court initially reversed the district court's judgment. *In re Deepwater Horizon,* 710 F.3d 338 (5th Cir.2013). The Insurers and Transocean petitioned for rehearing, and we withdrew that ruling to certify the following question to the Texas Supreme Court.

> FN7. In its brief, BP notes that this partial final judgment was entered in favor of the Insurers "and Transocean" and argues that Transocean is not a proper party to this order. BP's Rule 12(c) motion was directed only to the Insurers' complaints and claims—not against Transocean.

III. Legal Issues

BP appeals the district court's conclusion that it is not entitled to coverage under the policies, because Transocean was only required to name BP as an additional insured as to the risks Transocean assumed in the indemnities provisions of the Drilling Contract.

A.

The first issue is the scope of BP's coverage as an additional insured, and whether the umbrella policy itself determines the extent of coverage, or the indemnity clauses in the Drilling Contract effectively limit BP's coverage.

In 2008, the Texas Supreme Court addressed "whether a commercial umbrella insurance policy that was purchased to secure the insured's indemnity obligation in a service contract with a third party also provides direct liability coverage for the third party." *ATOFINA,* 256 S.W.3d at 662. Both the appellants and the appellees agree this case is instructive, but they proffer different applications of its holding to the facts of the case at issue. Uncertainty regarding the outcome under *ATOFINA* ultimately triggered this certification.

In *ATOFINA,* ATOFINA owned an oil refinery at which it hired Triple S to perform maintenance functions. *Id.* at 662. ATOFINA and Triple S entered a services contract which stipulated that ATOFINA was to be named an additional insured in each of Triple S's policies. Specifically, this provision stated:

> [ATOFINA], its parents, subsidiaries and affiliated companies, and their respective employees, officers and agents shall be named as additional insured in each of [Triple S's] policies, except Workers' Compensation; however, such extension of coverage shall not apply with respect to any obligations for which [ATOFINA] has specifically agreed to indemnify [Triple S]. FN8

> FN8. Petitioner's Br. on the Merits, *Evanston Ins. Co. v. ATOFINA Petrochemicals, Inc.,* 256 S.W.3d 660 (Tex.2008) (No. 03–0647), 2004 WL 1047377, at *4. Triple S also agreed to indemnify ATOFINA from all personal injuries and property losses sustained during the performance of the contract, "except to the extent that any such loss is attributable to the concurrent or sole negligence, misconduct, or strict liability

of [ATOFINA].” 256 S.W.3d at 662.

***498** After a Triple S employee drowned while servicing the ATOFINA refinery, his estate sued ATOFINA and Triple S for wrongful death. *Id.* at 663. Triple S's insurer, Evanston, and ATOFINA disagreed over who was required to pay for the litigation; ATOFINA contended it was an additional insured and thus covered, while Evanston argued ATOFINA's agreement to indemnify Triple S for ATOFINA's sole negligence precluded coverage. *Id.*

The Texas Supreme Court began by noting that ATOFINA sought coverage from Evanston on the basis that it was Triple S's additional insured—and had not sought indemnity directly from Triple S. *Id.* at 663–64. The court next looked to Section III.B.6 of the policy, which defined who is an insured as

> A person or organization for whom you have agreed to provide insurance as is afforded by this policy; but that person or organization is an insured only with respect to operations performed by you or on your behalf, or facilities owned or used by you.

Id. at 664. Because, by its own terms, this Section covered ATOFINA “with respect to operations performed by” Triple S, the court found this Section provided ATOFINA direct coverage even for its sole negligence.[FN9] *Id.* at 667. The court reached this conclusion, in part, because it found “it ... unmistakable that the agreement in this case to extend *direct* insured status to ATOFINA as an additional insured is separate and independent from ATOFINA's agreement to forego *contractual* indemnity for its own negligence.”[FN10] *Id.* at 670.

> FN9. Moreover, the court stated that “had the parties intended to insure ATOFINA for vicarious liability only, ‘language clearly embodying that intention was available.’ ” *Id.* at 666 (citing *McIntosh v. Scottsdale Ins. Co.*, 992 F.2d 251, 255 (10th Cir.1993)).

> FN10. The court further “disapprove[d] of the view that this kind of additional insured requirement fails to establish a separate and independent obligation for insuring liability.” 256 S.W.3d at 670.

In this appeal, BP focuses upon the *ATOFINA* court's statement that, “[i]nstead of looking, as the court of appeals did, to the indemnity agreement in the service contract to determine the scope of coverage, we base our decision on the terms of the umbrella insurance policy itself.” 256 S.W.3d at 664. And it further highlights that, as in *ATOFINA*, it is seeking insurance coverage from the Insurers, not indemnification from Transocean, and that the umbrella policy itself does not limit coverage for additional insureds.[FN11] Because the additional insured provision and the indemnities provisions in the Drilling Contract are separate and independent, because the Policy provides coverage to additional insureds “such as is afforded by this Policy,” and because Transocean would be covered for the injuries at issue, BP contends it, too, is entitled to coverage.

> FN11. For example, that policy does not say coverage for additional insureds is “limited to the liabilities assumed by the Named Insured in the agreement between the

Named Insured and Additional Insured."

The Insurers and Transocean, to the contrary, highlight the differences between the additional insured provisions at issue in *ATOFINA* and here. The *ATOFINA* clause, they proffer, imposed a broad requirement to list ATOFINA as an additional insured, whereas the analogous clause in the Drilling Contract creates a far more limited obligation, namely, to name BP as an additional insured only for liabilities Transocean specifically assumed in the contract. Furthermore, they contend ***499** that this language renders the additional insured provision inextricable from the indemnities provisions of the Drilling Contract; unlike in *ATOFINA*, the additional insured requirement is not separate and independent. They argue further the umbrella policy requires an "Insured Contract" exist between the named insured and the third party, while in *ATOFINA* no contract was required. In combination, the appellees contend, these factors allow the court to consider the indemnities clauses in the Drilling Contract in discerning the extent to which BP is covered as an additional insured.

Because there are potentially important distinctions between the facts of the instant case and *ATOFINA*, the outcome is not entirely clear.

B.

In the event the court must consider whether the Drilling Contract imposes limitations upon BP's coverage as an additional insured, an issue then arises of how to interpret the additional insured provision of that Contract. The parties offer competing interpretations, and which party prevails may depend upon whether the doctrine of *contra proferentem* applies.

[1][2] Texas law has consistently held that, if an insurance coverage provision is susceptible to more than one reasonable interpretation, the court must interpret that provision in favor of the insured, so long as that interpretation is reasonable. *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Hudson Energy Co.*, 811 S.W.2d 552, 555 (Tex.1991). The court must do so even if the insurer's interpretation is *more* reasonable than the insured's—"[i]n particular, exceptions or limitations on liability are strictly construed against the insurer and in favor of the insured," *id.*, and "[a]n intent to exclude coverage must be expressed in clear and unambiguous language." *ATOFINA*, 256 S.W.3d at 668, 668 n. 27 (citing *Hudson Energy*, 811 S.W.2d at 555); *see also Certain Underwriters at Lloyds, London v. Law*, 570 F.3d 574, 577 (5th Cir.2009) ("If ... ambiguity is found, the contractual language will be 'liberally' construed in favor of the insured." (citing *Barnett v. Aetna Life Ins. Co.*, 723 S.W.2d 663, 666 (Tex.1987))).

This rule favoring the insured derives, in part, from the "special relationship between insurers and insureds arising from the parties' unequal bargaining power." *Balandran v. Safeco Ins. Co. of America*, 972 S.W.2d 738, 741 n. 1 (Tex.1998). This aspect of the rule's foundation hearkens to the doctrine of *contra proferentem*, which construes any ambiguities against the drafter, and the "sophisticated insured" exception, which may apply when the policy is in some way negotiable (i.e., it is not a contract of adhesion) and the insured is as capable as the insurer of interpreting the contract.

The Texas Supreme Court has never recognized a sophisticated insured exception to the

general rule of interpreting insurance coverage clauses, nor has it ever indicated *contra proferentem* would not apply in construing these clauses. *See, e.g., ATOFINA*, 256 S.W.3d at 668 (stating the traditional rule construing coverage clauses in favor of the insured). Given that Texas has long recognized its rules regarding interpretation of insurance coverage clauses are partially derivative of the unequal bargaining power typical in many negotiations over insurance contracts, however, it is possible that such an exception may be deemed appropriate in a case like this, where all the parties involved are highly capable contractors.[FN12] ***500** On the one hand, the facts here indicate Insurers were not involved in drafting the Drilling Contract, and thus construing ambiguities in that contract against them might be inappropriate. But on the other, the Insurers were involved in drafting the umbrella policy language at issue, and the failure of that policy language to limit coverage in underlying "Insured Contracts" to the liabilities assumed by the named insured in those contracts is part of what ails the Insurers now.

FN12. One federal district court in Texas has found that the sophisticated insured exception might apply under Texas law, given the right circumstances. *Vought Aircraft Indus., Inc. v. Falvey Cargo Underwriting, Ltd.*, 729 F.Supp.2d 814, 824–25 (N.D.Tex.2010).

C.

Each party contends that its interpretation and application of *ATOFINA* better advances the goals of Texas insurance law and is more aligned with the intent of the parties. Their arguments illuminate the magnitude and wide ramifications, both throughout the oil and gas industry and for insurance law, of this case. Where state law governs such an issue, these policy factors are better gauged by the state high court than by a federal court.

IV. Questions Certified

[3][4] For the reasons discussed above, we hereby certify the following determinative questions of Texas law to the Supreme Court of Texas.

1. Whether *Evanston Ins. Co. v. ATOFINA Petrochems., Inc.*, 256 S.W.3d 660 (Tex.2008), compels a finding that BP is covered for the damages at issue, because the language of the umbrella policies alone determines the extent of BP's coverage as an additional insured if, and so long as, the additional insured and indemnity provisions of the Drilling Contract are "separate and independent"?

2. Whether the doctrine of *contra proferentem* applies to the interpretation of the insurance coverage provision of the Drilling Contract under the *ATOFINA* case, 256 S.W.3d at 668, given the facts of this case?

We disclaim any intention or desire that the Supreme Court of Texas confine its reply to the precise form or scope of the questions certified.

C.A.5 (La.),2013.
In re Deepwater Horizon
728 F.3d 491, 2013 A.M.C. 2429

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113 S.W.3d 37
(Cite as: 113 S.W.3d 37)

Court of Appeals of Texas,
Houston (1st Dist.).
PHILLIPS PETROLEUM COMPANY, Appellant,
v.
ST. PAUL FIRE & MARINE INSURANCE COMPANY and St. Paul Insurance Company, Appellees.

No. 01–01–00462–CV.
May 21, 2003.
Rehearing Overruled July 11, 2003.

Site owner sought declaratory judgment that contractors' insurers owed duty to defend and indemnify site owner, as additional insured, against personal injury actions brought by contractors' employees arising from fire at site. Insurers removed action based on diversity jurisdiction. Site owner moved to remand. The District Court, Kent, J., 99 F.Supp.2d 787, granted motion. On remand, the 149th District Court, Brazoria County, Robert May, J., entered summary judgment for the insurer. Producer appealed. The Court of Appeals, Terry Jennings, J., held that the insurer owed no further obligation to the site owner under the "fronting" policy once the insurer expended $1 million in defending the site owner in the underlying lawsuit.

Affirmed.

West Headnotes

[1] Appeal and Error 30 ⚿856(1)

30 Appeal and Error
30XVI Review
30XVI(A) Scope, Standards, and Extent, in General
30k851 Theory and Grounds of Decision of Lower Court
30k856 Grounds for Sustaining Decision Not Considered
30k856(1) k. In General. Most Cited Cases

When a motion for summary judgment raises multiple grounds, the Court of Appeals may affirm to the extent that any ground is meritorious.

[2] Insurance 217 ⚿1806

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1806 k. Application of Rules of Contract Construction. Most Cited Cases

Insurance contracts are subject to the same rules of construction as ordinary contracts.

[3] Insurance 217 ⚿1809

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1809 k. Construction or Enforcement as Written. Most Cited Cases

Insurance 217 ⚿1863

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1863 k. Questions of Law or Fact. Most Cited Cases

When an insurance contract permits only one interpretation, the Court of Appeals construes it as a matter of law and enforces it as written.

[4] Insurance 217 ⚿1810

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1810 k. Construction as a Whole. Most Cited Cases

Insurance 217 ⚿1813

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1811 Intention
217k1813 k. Language of Policies. Most Cited Cases

Insurance 217 ⚿1814

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1811 Intention
217k1814 k. Entire Contract. Most Cited Cases

The Court of Appeals must strive to effectuate an insurance contract as the written expression of the parties' intent and must attempt to give effect to all contract provisions, so that none will be rendered meaningless.

[5] Insurance 217 ⚿1810

217 Insurance
217XIII Contracts and Policies

217XIII(G) Rules of Construction
217k1810 k. Construction as a Whole. Most Cited Cases

The Court of Appeals construes the terms of the an insurance contract as a whole and considers all of its terms, not in isolation, but within the context of the contract.

[6] Insurance 217 ⚿1808

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1808 k. Ambiguity in General. Most Cited Cases

Insurance 217 ⚿1863

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1863 k. Questions of Law or Fact. Most Cited Cases

Whether an insurance contract is ambiguous is a question of law for the court to decide by looking at the contract as a whole in light of the circumstances present when the contract was entered.

[7] Insurance 217 ⚿1808

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1808 k. Ambiguity in General. Most Cited Cases

An ambiguity in an insurance contract does not arise merely because the parties advance conflicting contract interpretations; only when, after applying the applicable rules of construction, an insurance contract term is susceptible of two or more reasonable interpretations will the term be considered ambiguous.

[8] Insurance 217 ⚿1837

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1837 k. Matters Extrinsic to Policies in General. Most Cited Cases

The Court of Appeals' review of the terms of an insurance policy may under certain circumstances require review of the terms of a contract between the insured and a third party.

[9] Insurance 217 ⚿2926

217 Insurance
217XXIII Duty to Defend
217k2925 Fulfillment of Duty and Conduct of Defense
217k2926 k. In General. Most Cited Cases

Insurance 217 ⚿3506(2)

217 Insurance
217XXX Recovery of Payments by Insurer
217k3501 Reimbursement of Payments
217k3506 Liability Insurance
217k3506(2) k. Defense Costs. Most Cited Cases

Commercial general liability insurance carrier for insured contractor owed no further obligation to the site owner as an "additional insured" under the policy once the insurer expended $1 million in defending the site owner in the underlying lawsuit for damages sustained by insured's employee's from an explosion at the site; the insurer did not owe contractor an unlimited defense against the underlying lawsuits until insurer exhausted its policy liability limits by indemnifying the owner for damage payments, given that the policy was a "fronting" policy that obligated the insured to reimburse the insurer for all claims expenses, including attorney's fees, incurred in defense of the underlying lawsuits.

[10] Insurance 217 ⚿1810

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1810 k. Construction as a Whole. Most Cited Cases

The Court of Appeals is bound to construe the terms of an insurance policy as a whole, considering all of its terms in context, and to give effect to all provisions of the policy, so that none will be rendered meaningless.

[11] Insurance 217 ⚿1808

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1808 k. Ambiguity in General. Most Cited Cases

An ambiguity does not arise in an insurance contract merely because the parties advance conflicting contractual interpretations.

[12] Insurance 217 ⚿1721

217 Insurance
217XIII Contracts and Policies
217XIII(A) In General

217k1720 Validity and Enforceability
217k1721 k. In General. Most Cited Cases

An insurance contract, to be legally binding, must be sufficiently definite in its terms so that a court can understand the parties' obligations.

***38** Andrew Patrick Tower,Howrey Simon Arnold & White, Ronald D. Krist, Houston, Mark I. Levy, Robert Jacobs, Howrey Simon Arnold & White LLP, Washington, D.C., for Appellant.

David E. Chamberlain, Chamberlain & McHaney, J. Hampton Skelton, Skelton, Woody, Arnold & Placek, Austin, for Appellees.

Panel consists of Chief Justice RADACK and Justices NUCHIA and JENNINGS.

OPINION

TERRY JENNINGS, Justice.

In this insurance-coverage dispute, appellant, Phillips Petroleum Company (Phillips), challenges the trial court's rendition of summary judgment in favor of appellees, St. Paul Fire & Marine Insurance Company and St. Paul Insurance Company (together, St.Paul).[FN1] In two issues, Phillips contends that the trial court erred in granting summary judgment in favor of St. Paul and in denying Phillips's motion for reconsideration.

FN1. Appellees contend that St. Paul Insurance Company was incorrectly named as a defendant below and is not a proper party to this lawsuit. We do not address this contention because it is not relevant to the disposition of this appeal.

We affirm.

Facts and Procedural Background

In July 1997, representatives of Phillips and H.B. Zachry Company (Zachry) executed***39** a Preferred Service Provider Alliance and Master Service Agreement (MSA), under which Phillips contracted to hire Zachry to perform maintenance and construction work at several Phillips facilities in Texas, Oklahoma, Utah, and Puerto Rico. As part of the terms of the MSA, Zachry agreed to obtain and maintain certain types of insurance coverage and to name Phillips as an additional insured on such policies. Zachry also agreed that any insurance policies that it obtained as required by the M.S.A. § would be written or endorsed to be primary to any other coverage available to Phillips. Zachry subsequently purchased a policy of insurance from St. Paul (the policy),[FN2] which provided several types of coverage and carried a bodily-injury liability limit of $1 million per event.

FN2. We will refer to St. Paul's policy, numbered KK09100847, as “the policy.” For purposes of this appeal, the parties do not dispute that Phillips is an additional insured under this policy and that the coverage provided by the policy is primary to other coverage available to Phillips.

Following a June 1999 explosion at Phillips's Houston facility, injured Zachry employees and the estates of deceased Zachry employees sued Phillips, seeking, among other things, recovery of damages for injuries sustained in and deaths resulting from the explosion. Phillips subsequently demanded that Zachry's insurer, St. Paul, provide Phillips with a defense to these underlying lawsuits. St. Paul did so, subject to a reservation of its rights under the policy.[FN3] Phillips then sued St. Paul for breach of contract and sought a declaratory judgment that St. Paul owed Phillips an unlimited defense to the underlying lawsuits and indemnity up to the liability limits of the policy.[FN4]

FN3. The parties do not dispute that the policy was in effect at the time of the explosion.

FN4. Phillips also asserted separate claims against Zachry's excess insurance carriers, who are not parties to this appeal.

St. Paul answered Phillips's suit with a general denial and filed a motion for summary judgment. St. Paul argued that, because the policy purchased by Zachry was a "fronting" policy (i.e., the amount of the deductible payable by the insured equaled the amount of the liability limits), and because Zachry was obligated to reimburse St. Paul for all claim expenses, including attorneys' fees, incurred in the defense of a claim under the policy, St. Paul owed no further obligation to Phillips once St. Paul expended $1 million in defending Phillips in the underlying lawsuits.[FN5]

FN5. St. Paul presented summary judgment evidence to show, and the parties do not dispute, that St. Paul expended $1 million in its defense of Phillips in the underlying lawsuits.

The trial court granted an interlocutory summary judgment in favor of St. Paul and subsequently denied Phillips's motion for reconsideration. The court then severed its summary judgment into a separate cause, making its judgment final.

Standard of Review

[1] A party moving for summary judgment has the burden of proving that there is no genuine issue of material fact and that the movant is entitled to judgment as a matter of law. TEX.R. CIV. P. 166a(c); *Nixon v. Mr. Prop. Mgmt.,* 690 S.W.2d 546, 548 (Tex.1985); *Farah v. Mafrige & Kormanik,* 927 S.W.2d 663, 670 (Tex.App.-Houston [1st Dist.] 1996, no writ). When a motion for summary judgment raises multiple grounds, we may affirm to the extent that any ground is meritorious. *Cincinnati Life Ins. Co. v. Cates,* 927 S.W.2d 623, 625 (Tex.1996). These standards apply in insurance-coverage cases. *See e.g., State Farm Fire & Cas. Co. v. ***40** Vaughan,* 968 S.W.2d 931, 933 (Tex.1998); *Hanson v. Republic Ins. Co.,* 5 S.W.3d 324, 327 (Tex.App.-Houston [1st Dist.] 1999, pet. denied).

Contract Interpretation

In its two issues, Phillips argues that the trial court erred in granting summary judgment for St. Paul and in denying Phillips's motion for reconsideration because Phillips, as an additional insured under the policy purchased by Zachry, was owed an unlimited defense by St. Paul against the underlying lawsuits until St. Paul "exhausted its policy's liability limits by

indemnifying Phillips for damage payments." Phillips argues that the plain language of the policy is subject to this one, and only, reasonable interpretation. Alternatively, Phillips argues that any ambiguity in the policy with respect to the scope of St. Paul's defense obligations must be construed in Phillips's favor.

[2][3][4][5] Insurance contracts are subject to the same rules of construction as ordinary contracts. *Trinity Universal Ins. Co. v. Cowan,* 945 S.W.2d 819, 823 (Tex.1997); *Hanson,* 5 S.W.3d at 328. Accordingly, when a contract permits only one interpretation, we construe it as a matter of law and enforce it as written. *Upshaw v. Trinity Cos.,* 842 S.W.2d 631, 633 (Tex.1992); *Hanson,* 5 S.W.3d at 328. We must strive to effectuate the contract as the written expression of the parties' intent and must attempt to give effect to all contract provisions, so that none will be rendered meaningless. *Kelley–Coppedge, Inc. v. Highlands Ins. Co.,* 980 S.W.2d 462, 464 (Tex.1998); *State Farm Life Ins. Co. v. Beaston,* 907 S.W.2d 430, 433 (Tex.1995). To this end, we construe the terms of the contract as a whole and consider all of its terms, not in isolation, but within the context of the contract. *Beaston,* 907 S.W.2d at 433; *Forbau v. Aetna Life Ins. Co.,* 876 S.W.2d 132, 133–34 (Tex.1994); *Hartrick v. Great Am. Lloyds Ins. Co.,* 62 S.W.3d 270, 274 (Tex.App.-Houston [1st Dist.] 2001, no pet.).

[6][7] Whether a contract is ambiguous is a question of law for the court to decide by looking at the contract as a whole in light of the circumstances present when the contract was entered. *Kelley–Coppedge,* 980 S.W.2d at 464 (citing *Nat'l Union Fire Ins. Co. v. CBI Indus., Inc.,* 907 S.W.2d 517, 520 (Tex.1995)). An ambiguity does not arise merely because the parties advance conflicting contract interpretations. *Kelley–Coppedge,* 980 S.W.2d at 465. Only when, after applying the applicable rules of construction, a contract term is susceptible of two or more reasonable interpretations will the term be considered ambiguous. *Id.*

[8] Our review of the terms of an insurance policy may also, under certain circumstances, require review of the terms of a contract between the insured and a third party. As the Texas Supreme Court noted in *Urrutia v. Decker,* "Texas law has long provided that a separate contract can be incorporated into an insurance policy by an explicit reference clearly indicating the parties' intention to include that contract as part of their agreement." 992 S.W.2d 440, 442 (Tex.1999) (citing *Goddard v. East Tex. Fire Ins. Co.,* 67 Tex. 69, 1 S.W. 906, 907 (1886)).

A thorough review of the relevant provisions of the M.S.A. and the policy is necessary to determine whether the trial court erred in deciding the coverage dispute in favor of St. Paul.

MSA Provisions

As noted above, under the MSA, Zachry was required to purchase insurance coverage naming Phillips as an additional insured. Exhibit "M" of the MSA, entitled ***41** "Insurance Requirements," provides, in part, as follows:

> Zachry shall, at a minimum, maintain the following types and amounts of insurance and shall keep such insurance in force during the term of this Agreement.
>
> ....

> 3. Commercial General Liability Insurance on an occurrence form with a combined single limit of $1,000,000 per occurrence....
>
> ....
>
> As a separate and additional obligation independent of the indemnities contained in the Agreement, all of the required insurance policies named above, shall be written or endorsed to name [Phillips], its subsidiaries and affiliates as additional insureds to the extent of Zachry's indemnity and other obligations under this Agreement.
>
> ....
>
> All of the required insurance policies named above shall be written or endorsed to be primary, with respect to Zachry's obligations, to any other coverage available to cover the loss.

The parties do not dispute that, as a result of the foregoing provisions, Zachry was contractually obligated to obtain a commercial general liability insurance policy that (1) named Phillips as an additional insured and (2) was written to be primary to any other coverage available to Phillips to cover the losses concerned in the underlying lawsuit.

Policy Provisions

In its introductory section, the commercial general liability policy purchased by Zachry from St. Paul defines "you, your and yours" as the named insured, Zachry. In a section entitled "Who Is Protected Under This Agreement," the policy explains that, "[i]f you are named in the Introduction as a corporation or other organization, you are a protected person." In a section entitled "What This Agreement Covers," the policy provides that St. Paul agrees to "pay amounts any protected person is legally required to pay as damages for covered bodily injury, property damage or premises damage" caused by an "event" [FN6] during the term of the policy.

> FN6. "Event" is defined to mean an accident.

The policy sets forth St. Paul's duty to defend its insureds as follows:

> **Right and duty to defend.** We'll have the right and duty to defend any claim or suit for covered injury or damage ... made against any protected person.... [O]ur duty to defend claims or suits ends when we have used up the limits of coverage that apply with the payment of judgments, settlements or medical expenses.

The policy also contains numerous endorsements modifying the coverage provisions of the policy, including an Additional Protected Person Endorsement ("additional insured endorsement"), which reads, in part, as follows:

> This Endorsement changes your Contractors General Liability Protection.
>
> How Coverage Is Changed

There are two changes which are explained below.

1. The following is added to the Who Is Protected Under this Agreement section. This change adds certain protected persons and limits their protection.

Additional Protected Person. The person or organization shown below is an additional protected person *as required by contract with you.* But only for covered injury or damage arising out of: ***42** ... your work for that person or organization....

ADDITIONAL PROTECTED PERSON(S): Any Person or Organization required to be made an additional protected person in a written contract executed prior to a loss.

....

2. The following is added to the Other primary insurance section. This change broadens coverage.

....

[W]e will consider this insurance to be primary to and non-contributory with the insurance issued directly to the additional protected person listed above if ... your contract specifically requires that we consider this insurance to be primary....

(Emphasis added.)

The parties do not dispute that the effect of the foregoing provisions of the policy was to make Phillips an additional insured under the policy and to make the coverage available under the policy primary to any other insurance coverage available to Phillips. Rather, their dispute focuses on the *type* of insurance coverage that St. Paul was obligated to provide Phillips as an additional insured.

As noted above, the policy issued by St. Paul carried a bodily-injury liability limit of $1 million per event. The policy also contains a Contractors Commercial General Liability Deductible Endorsement ("deductible endorsement"), which reads, in part, as follows:

Deductibles Apply To Damages And Claims Expenses—Limits Are Reduced By The Deductible Amounts

This endorsement changes your Contractors Commercial General Liability Protection.

IMPORTANT NOTE: This endorsement makes you responsible for paying damages and claims expenses within the deductibles that apply.

....

Bodily injury and property damage each event deductible—other than products and completed work. $1,000,000.

....

There are two changes which are explained below.

1. The following section is added. This change adds deductibles to be paid by you.

DEDUCTIBLES

The deductibles shown in the Deductible Table and the information contained in this section fix the amount of damage and claim expenses that you'll be responsible fo[r] paying. Only those deductibles for which amounts are shown in the Deductible Table apply.

We will pay all or part of the deductible for you, unless we agree to do otherwise. WHEN WE DO MAKE PAYMENT, YOU AGREE TO REPAY THAT AMOUNT TO U.S. PROMPTLY AFTER WE NOTIFY YOU OF THE PAYMENT.

Also, *if we pay claim expenses that's [sic] subject to the applicable deductible, YOU AGREE TO REPAY THAT AMOUNT TO U.S. PROMPTLY AFTER WE NOTIFY YOU OF THE PAYMENT.*

Claim expenses includes [sic] the following fees, costs and expenses that result directly from the investigation, defense, or settlement of a specific claim or suit:

* *fees, costs or expenses of attorneys.*

....

Bodily injury and property damage each event deductible—other than products and completed work. You'll be responsible for the amount of damage and ***43** claim expenses within this deductible....

....

2. The following is added to the Limits of Coverage section. This section explains how the limits of coverage apply when a deductible applies.

The limits shown in the Coverage Summary, other than the General Total Limit and the Products and Completed Work total limit, *are reduced by the deductible amount that applies.*

(Emphasis added.)

Application

Phillips notes that the “plain language” of the policy expressly states that St. Paul's duty to defend continues until St. Paul has “used up the limits of coverage that apply with the payment of judgments, settlements or medical expresses.” Thus, Phillips argues that, because St. Paul did not indemnify Phillips for any “judgments, settlements, or medical expenses,” the policy's duty to defend language obligates St. Paul to continue to pay Phillips's defense costs. However, we may not construe this term of the policy in isolation; rather, we must consider all of the terms of the policy within the context of the entire policy. *Forbau,* 876 S.W.2d at

133–34; *Hartrick,* 62 S.W.3d at 274.

St. Paul contends that the effect of the policy's deductible endorsement, which sets Zachry's deductible at an amount equal to the bodily-injury liability limit, is to reduce St. Paul's net liability under the policy to zero. Further, St. Paul contends that, because the deductible endorsement specifies that "claim expenses," including attorney's fees, are subject to the deductible, St. Paul's contractual obligation to defend Phillips in the underlying lawsuits ceased once St. Paul had expended $1 million in attorney's fees on behalf of Phillips, regardless of whether a settlement or judgment had been paid.

Phillips argues that the effect of the policy's deductible endorsement to make the policy a "fronting" policy is relevant only to St. Paul's contractual obligations to Zachry. Phillips asserts that, regardless of the terms of the policy actually obtained by Zachry, Zachry was contractually obligated by a "plain reading" of the terms of the M.S.A. § to obtain "traditional" commercial general liability coverage, i.e., a policy whose limits of liability were not eroded by an insurer's "fronting" of "claim expenses" on behalf of its insured, but whose limits were exhausted only upon the payment of settlements or judgments equal to the liability limits. Phillips also argues that, because the policy's additional insured endorsement provided that Phillips was an additional insured under the policy "as required by contract with [Zachry]," the terms of the M.S.A. § requiring Zachry to purchase "traditional" commercial general liability insurance coverage govern and are to be read into or along with the coverage provisions of the policy. Finally, Phillips argues that, because the deductible endorsement uses the term "you," which is defined by the policy as "Zachry," instead of the term "protected persons," the provisions of that endorsement apply only to St. Paul's obligations to its insured, Zachry, and do not apply to the coverage that St. Paul was obligated to provide Phillips as Zachry's additional insured.

[9] However, other than the limits of coverage required, the M.S.A. § does not expressly specify the type of commercial general liability coverage that Zachry was required to purchase. Phillips's argument that the terms of the M.S.A. § obligated Zachry to purchase a "traditional" commercial general liability policy—one with an unlimited duty to defend until liability ***44** limits are exhausted by settlements or judgments—requires the insertion of terms into the policy which are not contained in the M.S.A. § itself. This we may not do. *See Kelley–Coppedge,* 980 S.W.2d at 464 (citing *CBI,* 907 S.W.2d at 520) (noting that parol evidence may not be relied on for purpose of creating ambiguity in contract).

Moreover, the policy's additional insured endorsement language, set out above, naming Phillips as an additional insured under the policy "as required by contract with you [Zachry]," is not, as argued by Phillips, "an explicit reference clearly indicating the parties' intention" to include the terms and provisions of the M.S.A. § as part of the policy. *See Urrutia,* 992 S.W.2d at 442. This language merely clarifies which persons or entities are to be additional insureds under the policy, namely, those persons "required to be made an additional protected person in a written contract executed prior to a loss."

[10] Finally, the policy's deductible endorsement is not applicable only to St. Paul's obligations to its insured, Zachry. The terms of the endorsement do not limit its application

only to named insureds. We are bound to construe the terms of the policy as a whole, considering all of its terms in context, and to give effect to all provisions of the policy, so that none will be rendered meaningless. *Kelley–Coppedge,* 980 S.W.2d at 464; *Beaston,* 907 S.W.2d at 433; *Hartrick,* 62 S.W.3d at 274. To apply the construction of the terms of the policy as urged by Phillips would have the effect of rendering the terms of the deductible endorsement meaningless with regard to St. Paul's obligations to Zachry's named insured, Phillips, while simultaneously leaving them valid and enforceable with regard to St. Paul's obligations to its named insured, Zachry.

[11][12] As noted above, an ambiguity does not arise in a contract merely because the parties advance conflicting contractual interpretations. *Kelley–Coppedge,* 980 S.W.2d at 465. We find no ambiguity in the policy with respect to the scope of St. Paul's defense obligation to Phillips. Additionally, a contract, to be legally binding, must be sufficiently definite in its terms so that a court can understand the parties' obligations. *T.O. Stanley Boot Co., Inc. v. Bank of El Paso,* 847 S.W.2d 218, 221 (Tex.1992). Here, the policy in question does not demonstrate that Phillips, as an additional insured, was owed an unlimited defense by St. Paul against the underlying lawsuits until St. Paul, in the words of Phillips, “exhausted its policy liability limits by indemnifying Phillips for damage payments.” On the contrary, because the policy purchased by Zachary was, in fact, a “fronting” policy and Zachary was obligated to reimburse St. Paul for all claims expenses, including attorney's fees, incurred in defense of the underlying lawsuits, St. Paul owed no further obligation to Phillips once St. Paul expended $1 million in defending Phillips.

Accordingly, we hold that the trial court did not err in granting summary judgment in favor of St. Paul and in denying Phillips's motion for reconsideration. We overrule both of Phillips's issues.

Conclusion

We affirm the judgment of the trial court.

Tex.App.–Houston [1 Dist.],2003.
Phillips Petroleum Co. v. St. Paul Fire & Marine Ins. Co.
113 S.W.3d 37

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280 F.3d 532
(Cite as: 280 F.3d 532)

United States Court of Appeals,
Fifth Circuit.
SCHNEIDER NATIONAL TRANSPORT, Etc., Plaintiff,
v.
FORD MOTOR COMPANY; et al., Defendants.
Schneider National Transport, as successor in interest to Builders Transport, Inc.,
Plaintiff–Appellee,
v.
Alexander and Alexander of New York Inc.; et al., Defendants,
Insurance Company of the State of Pennsylvania, Defendant–Appellant.

No. 00–41322.
Jan. 18, 2002.

Insured trucking company brought suit against its primary and excess insurers, seeking to recover costs incurred in defense of actions arising from multi-vehicle collision involving one of insured's trucks. The United States District Court for the Eastern District of Texas, Joe J. Fisher, J., granted summary judgment to insured, and denied excess insurer's cross-motion for summary judgment. Excess insurer appealed. The Court of Appeals, Limbaugh, District Judge, sitting by designation, held that: (1) Texas law, rather than law of Pennsylvania, where excess insurer was incorporated, governed action, and (2) excess insurer was not required to contribute to cost of defending insured until primary insurers had exhausted their underlying policy limits.

Reversed and remanded.

West Headnotes

[1] Federal Courts 170B 776

170B Federal Courts
170BVIII Courts of Appeals
170BVIII(K) Scope, Standards, and Extent
170BVIII(K)1 In General
170Bk776 k. Trial de novo. Most Cited Cases

Court of Appeals reviews district court's grant of summary judgment *de novo*.

[2] Federal Courts 170B 776

170B Federal Courts
170BVIII Courts of Appeals
170BVIII(K) Scope, Standards, and Extent
170BVIII(K)1 In General

170Bk776 k. Trial de novo. Most Cited Cases

Court of Appeals reviews district court's interpretation of an insurance policy *de novo*.

[3] Action 13 ⚿17

13 Action
13II Nature and Form
13k17 k. What law governs. Most Cited Cases

If the laws of the states do not conflict, then no choice-of-law analysis is necessary.

[4] Insurance 217 ⚿1091(10)

217 Insurance
217III What Law Governs
217III(A) Choice of Law
217k1086 Choice of Law Rules
217k1091 Particular Applications of Rules
217k1091(9) Automobile Insurance
217k1091(10) k. In general. Most Cited Cases

Law of Texas, as forum state, would be applied in interpreting automobile liability insurance policy, where no substantive difference existed between Texas law and law of Pennsylvania, which potentially applied.

[5] Insurance 217 ⚿1822

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1822 k. Plain, ordinary or popular sense of language. Most Cited Cases

Under both Texas and Pennsylvania law, insurance contracts, like other contracts, should be interpreted according to their plain meaning.

[6] Contracts 95 ⚿2

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k2 k. What law governs. Most Cited Cases

Under Texas choice-of-law principles, contract disputes are governed by the law of the state with the most significant relationship to the particular substantive issue.

[7] Insurance 217 ⚿1091(10)

217 Insurance

217III What Law Governs
217III(A) Choice of Law
217k1086 Choice of Law Rules
217k1091 Particular Applications of Rules
217k1091(9) Automobile Insurance
217k1091(10) k. In general. Most Cited Cases

Under Texas choice-of-law principles, Texas law, rather than Pennsylvania law, applied in determining obligation of excess insurer of insured trucking company to pay costs of defending lawsuit against insured, even though excess insurer was incorporated in Pennsylvania, where all litigation giving rise to case occurred in Texas, and all defense costs which were subject of litigation were incurred in Texas and involved Texas attorneys.

[8] Insurance 217 ⚿2917

217 Insurance
217XXIII Duty to Defend
217k2916 Commencement of Duty; Conditions Precedent
217k2917 k. In general. Most Cited Cases

Under Texas law, insured trucking company's excess insurer was not required to contribute to cost of defending insured in lawsuits arising from multi-vehicle collision involving one of insured's trucks until insured's primary insurers had exhausted their underlying policy limits, where excess policy provided that, if underlying insurance was exhausted, excess insurance would "continue in force as underlying insurance" and defend any suit arising from a covered occurrence, and that excess insurer would not be called upon to investigate or defend any suit "except for exhaustion of underlying limits by payment of covered claims."

[9] Insurance 217 ⚿1806

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1806 k. Application of rules of contract construction. Most Cited Cases

Under Texas law, the same rules that apply to contracts in general govern the interpretation of insurance contracts.

[10] Contracts 95 ⚿147(3)

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k147 Intention of Parties
95k147(3) k. Construing whole contract together. Most Cited Cases

Under Texas law, when interpreting a contract, court's primary concern is to ascertain and to give effect to the intentions of the parties as expressed in the instrument, and to achieve this objective, court considers the contract as a whole.

[11] Insurance 217 ⚿1822

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1822 k. Plain, ordinary or popular sense of language. Most Cited Cases

Under Texas law, a court must consider the terms of an insurance policy according to their plain and ordinary meaning.

[12] Insurance 217 ⚿2396

217 Insurance
217XVII Coverage—Liability Insurance
217XVII(B) Coverage for Particular Liabilities
217k2394 Excess and Umbrella Liability Coverage
217k2396 k. Scope of coverage. Most Cited Cases

Insurance 217 ⚿2917

217 Insurance
217XXIII Duty to Defend
217k2916 Commencement of Duty; Conditions Precedent
217k2917 k. In general. Most Cited Cases

Under Texas law, defense costs provision of insured trucking company's excess insurance policy, which stated that if underlying insurance was exhausted, excess insurance would "continue in force as underlying insurance" and defend any suit arising from a covered occurrence, and that excess insurer would not be called upon to investigate or defend any suit "except for exhaustion of underlying limits by payment of covered claims," meant that excess insurance would come into play, and provide coverage including defense costs, only when underlying insurance had been exhausted, and that duty to defend would not arise until underlying coverage was exhausted.

[13] Insurance 217 ⚿2917

217 Insurance
217XXIII Duty to Defend
217k2916 Commencement of Duty; Conditions Precedent
217k2917 k. In general. Most Cited Cases

Under Texas law, where the insured maintains both primary and excess policies, the excess liability insurer is not obligated to participate in the defense until the primary policy limits are exhausted.

[14] Insurance 217 ⚿1839

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1838 Materials Related or Attached to Policies
217k1839 k. In general. Most Cited Cases

Under Texas law, an incorporation by reference into an insurance policy must be sufficiently clear for court to conclude the parties intended the incorporation.

***534** Joseph M. Nicks (argued), Godfrey & Kahn, Green Bay, WI, Jude Thaddeus Heartfield, Heartfield & McGinnis, Beaumont, TX, for Plaintiff–Appellee.

Thomas C. Wright (argued), Julia Leigh Kurtz, Campbell, Harrison & Wright, Frank G. Jones, Fulbright & Jaworski, Houston, TX, for Defendant–Appellant.

Appeal from the United States District Court for the Eastern District of Texas.

Before JONES and DeMOSS, Circuit Judges, and LIMBAUGH,[FN1] District Judge.

FN1. District Judge of the Eastern District of Missouri, sitting by designation.

LIMBAUGH, District Judge:

This diversity case involves a dispute between primary and excess coverage insurance carriers as to the obligation to pay the cost of defending a lawsuit of the insured. The case was submitted to the district court on cross-motions for summary judgment. Appellee's motion for summary judgment was granted and appellant's denied. In so ruling, the district court determined that appellant, the excess insurance carrier, was required to contribute to the cost of the primary carrier of defending the lawsuit of the insured. This court reverses that decision, finding that the excess carrier was not required to contribute to the cost of defending its insured's lawsuit until the primary carriers had exhausted their underlying policy limits.

BACKGROUND

Builders Transport, Inc. (“Builders”) was a national freight company which operated a fleet of trucks throughout the United States.[FN2]

FN2. At a time following the events leading to this litigation, Builders was adjudicated a bankrupt and appellee Schneider National Transport bought Builders assets and was substituted as the plaintiff on March 17, 2000.

Builders, one of the largest truckers in the country, maintained a three-tiered structure to cover any loss resulting from a motor vehicle accident involving its fleet. Any loss not exceeding $1,000,000 arising from a collision was covered by Builders self-insured retention (“SIR”). Builders would pay all claims, including fees and expenses, for losses under

$1,000,000.

Planet Insurance Co. ("Planet") provided coverage for Builders for losses between $1,000,000 and $2,000,000. As to the payment of expenses and fees, the Planet policy provided that "in the event that any claim(s), exceed the Named Insured's self-insured retention and involve the liability of the Company, then, solely as respects each such claim the Company and the Named Insured shall prorate all costs and expenses in direct proportion to the amount of damages applicable to and payable by each of them ...."

In order to protect itself against a catastrophic loss, Builders purchased from appellant a $13,000,000 excess coverage, or umbrella, policy. Thus, appellant in its policy agreed to pay all losses between $2,000,000 and $15,000,000. Appellant's policy contained the following language relevant to defense costs:

> "*Insuring Agreements*
> II. *Defense, Settlement and Supplementary Payments:*
>
> Should applicable underlying insurance(s) become exhausted by payment of covered claims, this insurance will continue in force as underlying insurance ***535** and shall defend any suit arising out of a covered occurrence ...
>
> Except for exhaustion of underlying limits by payment of covered claims, and occurrences not covered by the underlying policies, but covered by this policy, the company shall not be called upon to investigate or defend any suit brought against the insured, but the company shall have the option to associate in the investigation and/or defense of suits covered under this policy ...."

On November 25, 1993 when the policies of Planet and appellant were in force, a truck driver employed by Builders was involved in a multi-vehicle collision. Two people died and several others suffered catastrophic permanent injuries as a result of the collision. Suit for personal injuries was brought in the district court of Jefferson County, Texas, captioned *Clancy, et al. and Chandler v. Builders Transport, Inc.*, Cause No. B–144, 840–B. Trial was set for the first part of June 1995 and the case was settled shortly before trial. The first portion of the settlement, occurring on June 9, 1995, was in the sum of $13,800,000. Of this sum, Builders paid $838,834, Planet paid $1,000,000 and appellant paid $11,961,166.

On June 27, 1995 the remainder of the case was settled for $2,200,000. Of this sum, appellant paid $1,038,834 and Builders paid $1,161,166 as uninsured exposure.[FN3]

> FN3. The district court found that the second portion of the settlement was for $2,500,000 with Builders contributing an additional $1,300,000 as its uninsured exposure. The precise settlement does not affect the outcome of this case as the parties all agree that Builders not only exhausted its initial $1,000,000 coverage, but contributed, in addition, a substantial sum as uninsured exposure and that both Planet and appellant paid their policy limits.

Builders claim that approximately $1,400,000 was incurred in costs and fees by it in

defending the claims. The great portion of this amount was incurred before the first settlement on June 9, 1995. About $50,000 was incurred between the first settlement on June 9, 1995 and the final settlement on June 27, 1995.

Builders assert that appellant and Planet should participate in the payment of the defense costs.[FN4] The Planet policy provided for a *pro rata* sharing of defense costs by all contributors to the settlement of a claim. Appellant's policy provided that once underlying coverages are exhausted, its insurance will continue in force as underlying insurance and appellant shall defend any suit arising out of a covered occurrence.

> FN4. Apparently, Builders has settled its claim for an apportionment of these costs with Planet.

In its decision, the district court reasoned that the phrase "as underlying insurance" when used in the context chosen by appellant in the defense portion of its own policy can only mean that upon the exhaustion of underlying coverages, appellant's policy will defend in the same manner as, or according to the way the underlying Planet policy operated, and that it will provide coverage for expenses to the same degree in which that policy did. *See Builders Transport, Inc. v. Ford Motor Co.,* 25 F.Supp.2d 739, 744 (E.D.Tex.1998). The costs were then apportioned and appellant was ordered to pay $627,866.72 for its proportionate *pro rata* share of the costs and fees incurred by Builders. Appellants were also ordered to pay Builders $522,422.14 for reasonable costs and attorneys' fees incurred in connection with this action.

Appellant urges this Court to reverse the finding of the district court and determine that it erred in applying Pennsylvania***536** law as opposed to Texas law, and erred in failing to find that appellant had no duty to its insured to provide costs and expenses incurred prior to exhaustion of all underlying insurance; that is, appellant should have no obligation to pay for costs and expenses incurred until after the payout of the first settlement on June 9, 1995.

DISCUSSION

Standard of review.

[1][2] We review the district court's grant of summary judgment and its interpretation of the insurance policies involved *de novo. American Guar. and Liability Ins. Co. v. 1906 Co.,* 129 F.3d 802, 805 (5th Cir.1997); *Matador Petroleum v. St. Paul Surplus Lines Ins.,* 174 F.3d 653, 656 (5th Cir.1999).

The issue as to whether the law of Pennsylvania or Texas should apply.

In an attempt to resolve this problem, the district court conducted a conflicts analysis and determined that the law of Pennsylvania should apply. This analysis was undertaken even though the district court found, and the parties agreed, that the laws of Pennsylvania and Texas are all in accord insofar as the issues before the Court are concerned. *Builders Transport, Inc.,* 25 F.Supp.2d at 743. Appellee also concedes this in its brief.

[3][4][5] However, "If the laws of the states do not conflict, then no choice-of-law analysis is necessary." *W.R. Grace and Co. v. Continental Cas. Co.,* 896 F.2d 865, 874 (5th Cir.1990); *National Union Fire Ins. v. CNA Ins. Companies,* 28 F.3d 29, 32, n. 3 (5th Cir.1994). Thus, the law of the forum state, Texas, should apply here as there is no conflict

between the substantive state law of Texas and Pennsylvania as each requires that insurance contracts, like other contracts, be interpreted according to their plain meaning. *Puckett v. United States Fire Insurance Co.,* 678 S.W.2d 936, 938 (Tex.1984), *Ranieli v. Mutual Life Ins. Co.,* 271 Pa.Super. 261, 413 A.2d 396 (1979).

[6][7] Even if a choice of law analysis was required to be made, the Court determines that Texas probably has the most significant relationship to the substantive issues to be resolved. "Under Texas choice-of-law principles, contract disputes are governed by 'the law of the state with the most significant relationship to the particular substantive issue.' " *W.R. Grace & Co.,* 896 F.2d at 873 citing *Duncan v. Cessna Aircraft Co.,* 665 S.W.2d 414, 421 (Tex.1984). *See also Hughes Wood Products, Inc. v. Wagner,* 18 S.W.3d 202, 205 (Tex.2000). The only relationship that Pennsylvania has to this case is that appellant was incorporated there, but had its headquarters in New York. Builders had its headquarters in South Carolina. All of the litigation giving rise to this case occurred in Texas. All of the defense costs, which are the subject of this litigation were incurred in Texas and involved Texas attorneys. The mere fact of appellant's incorporation in Pennsylvania does not lead this Court to believe that that state has the most significant relationship to the substantive issue to be resolved here. The Court finds, therefore, that the law of Texas is the proper choice of law and the district court erred in determining that the law of Pennsylvania was the proper choice.

The dispute between the primary and excess insurance carriers as to the payment of defense costs.

[8] In considering this issue, the district court first examined the policy of Planet, an underlying carrier. No party takes exception to the finding that Planet's policy provided for a pro rata sharing of ***537** defense costs by all contributors to the settlement of a claim. The claim of error is made to the district court's finding that the excess coverage policy of appellant must be construed to require it to provide coverage for expenses to the same degree provided for by Planet's policy.

In reaching its conclusion, the district court relied heavily on the holding in *General Accident Insurance Company of America v. Safety National Casualty Corporation,* 825 F.Supp. 705 (E.D.Pa.1993). In that case, General Accident wrote a policy for a law firm providing primary lawyer's professional liability insurance. Safety National provided excess coverage. The law firm was involved with suits over a failed Savings & Loan association and General Accident provided the defense for the firm. The cases were settled with each company paying its policy limits. General Accident sought contribution from Safety National for a pro rata share of the defense costs upon common law principles of equitable contribution. The court entered summary judgment for General Accident holding that Safety National "has an equitable duty to contribute on a pro rata basis toward the costs of defending its insured." *General Accident,* 825 F.Supp. at 706.[FN5]

FN5. General Accident had also asserted a claim for breach of contract, but later conceded that its action could only lie in equity, not contract, so the court dismissed the breach of contract claim. *See General Accident,* 825 F.Supp. at 707, n. 6.

The reliance on the case of *General Accident* by the district court here is inappropriate for

two reasons: first, *General Accident* applied Pennsylvania law, not Texas law. Second, and most important, that case was decided on equitable principles, not contractual interpretation; here, the suit is founded on breach of contract involving contract interpretation. No claim was made by appellee for equitable relief.[FN6]

> FN6. The decision in *General Accident* does not suggest, and we do not infer that Pennsylvania law is different from Texas law, thereby requiring a choice of law analysis. *General Accident* was decided on equitable principles, not contract interpretation. In fact, *General Accident* conceded it had no claim in contract assuming had it continued to urge that claim, it would not have been entitled to contribution from Safety National. Thus, on applying contract interpretation to these types of problems, it would appear the laws of Texas and Pennsylvania are not dissimilar.

[9][10][11][12] The parties have agreed and the court concurs that appellants' policy is not ambiguous. Thus, "Under Texas law, the same rules that apply to contracts in general govern the interpretation of insurance contracts." *Matador Petroleum,* 174 F.3d at 656 *citing National Union Fire Ins. Co. v. CBI Indus., Inc.,* 907 S.W.2d 517, 520 (Tex.1995). "When interpreting a contract, our primary concern 'is to ascertain and to give effect to the intentions of the parties as expressed in the instrument.' *R&P Enter. v. LaGuarta, Gavrel & Kirk, Inc.,* 596 S.W.2d 517, 518 (Tex.1980). To achieve this objective, we consider the contract as a whole." *Matador Petroleum,* 174 F.3d at 656. This Court must consider the policy terms according to their plain and ordinary meaning. *Puckett,* 678 S.W.2d at 938.

The provision at issue in appellant's policy provides:

> "*Insuring Agreements*
> II. *Defense, Settlement and Supplementary Payments:*
>
> Should applicable underlying insurance(s) become exhausted by payment of covered claims, this insurance will continue in force as underlying insurance ***538** and shall defend any suit arising out of a covered occurrence ...
>
> Except for exhaustion of underlying limits by payment of covered claims, and occurrences not covered by the underlying policies, but covered by this policy, the company shall not be called upon to investigate or defend any suit brought against the insured, but the company shall have the option to associate in the investigation and/or defense of suits covered under this policy ...."

The plain and ordinary meaning of these policy provisions is that when underlying insurance has become exhausted, that is, when the company providing underlying insurance has paid on one or more claims to the maximum required under that policy, this insurance, the excess coverage, will come into play. Coverage under the excess policy will then be furnished including the defense costs. The excess carrier's duty to defend does not arise until the underlying insurance has been exhausted, i.e. when that insurance coverage has been paid out. This interpretation is supported by Texas law and the holding in the majority of other jurisdictions. *See Texas Employers Ins. v. Underwriting Members,* 836 F.Supp. 398, 404, 405, 407 and cases cited at 404 (S.D.Tex.1993).

[13] "The majority rule is that '[w]here the insured maintains both primary and excess policies, ... the excess liability insurer is not obligated to participate in the defense until the primary policy limits are exhausted.' " *Keck, Mahin and Cate v. Nat'l. Union Fire Ins. Co. of Pittsburgh Pa.*, 20 S.W.3d 692, 700 (Tex.2000) citing *Texas Employers Ins.*, 836 F.Supp., at 404.

Appellee urges the court to follow the reasoning of the district court, that the phrase in appellant's policy "as underlying insurance" means the excess carrier must provide coverage for expenses to the same degree in which the underlying insurance policy did; that is, a pro rata sharing. A plain reading of the policy does not support this reasoning. Even though the excess coverage policy is to continue "as underlying insurance" after the primary policy limits are exhausted does not mean the provisions of a primary policy providing for defense costs are incorporated into the terms of the excess policy.

[14] An incorporation by reference must be sufficiently clear for this court to conclude the parties intended the incorporation. *Juntunen v. Sea–Con Services, Inc.*, 879 F.2d 154, 156 (5th Cir.1989) (holding that the incorporation was intended when the excess liability policy provided that this policy shall follow the terms, conditions, definitions and exclusions of the controlling underlying insurance policy); *King v. Employers Nat'l. Ins. Co.*, 928 F.2d 1438, 1444 (5th Cir.1991) (in a liability dispute the excess coverage policy provided that the provisions of the immediate underlying policy of the primary carrier are incorporated as a part of the excess policy except for certain inconsistent provisions). *See also 20th Century Ins. Co. v. Liberty Mut. Ins. Co.*, 965 F.2d 747, 750, 751 (9th Cir.1992).

There is nothing in appellants' policy here that uses the term "incorporation" or "incorporation by reference" or "follow form" language. Nor is there any other express terminology stating that the provisions of the underlying policy are in some way to be a part of the terms of the excess policy, or that the parties intended this result. Absent such language, this Court is unable to hold that the parties intended, much less inferred, the defense cost burden be pro rated between all carriers as was provided for in the policy of Planet, ***539** one of the underlying carriers.[FN7]

> FN7. This case would be fraught with considerable unnecessary difficulties if it ruled the term "as underlying insurance" was intended to incorporate terms of the underlying insurance policies into the excess policy. There are two underlying insurance policies; one written by Tenant and the other, SIR, the insured's self-insured retentions. Does "as underlying insurance" refer to both or only one of the underlying policies and if only one, which one? The record is silent as to prorating of costs that might be attributable to the SIR policy. The creation of such an ambiguity, in and of itself, would be highly improper and confusing.

In addition, the thrust of appellee's argument following the reasoning of the district court does not take into consideration that portion of appellant's policy that serves virtually as a disclaimer. The policy states that appellant "shall not be called upon to investigate or defend any suit brought against the insured" except for exhaustion of underlying limits by payment of covered claims. The plain meaning of this provision is that appellant disclaims any obligation

to pay defense costs until the underlying policies have been exhausted or paid out. Only then will appellant have a contractual obligation to defend and pay costs.[FN8]

FN8. Although appellants' policy gives it “the option to associate in the investigation and/or defense of suits covered under this policy ...,” there is nothing in the record to suggest the option was ever exercised. In any event, the availability of the option does not require appellant to share in the defense costs if the option is not exercised.

CONCLUSION

As the laws of the states of Texas and Pennsylvania do not conflict as to relevant issues in this case, the law of Texas, the forum state, should apply and the district court erred in following the law of Pennsylvania.

As the insured, Builders, maintained both primary and excess liability policies, the excess insurer, appellant, is not obligated to participate in the defense of suits against the insured until the primary policy limits are exhausted. Summary judgment, therefore, should have been granted to appellant rather than respondent and the district court erred in failing to so rule.

On review of the record, and the briefs of the parties, and for the reasons set forth in this opinion, we reverse the district court's decision and direct that summary judgment be entered for appellant. In so ruling, we hold that appellant shall have no obligation to pay for costs and expenses incurred until after the payout of the first settlement on June 9, 1995, nor will appellant be required to pay any sum to Builders for costs and attorney fees incurred in connection with this action.

REVERSED AND REMANDED.

C.A.5 (Tex.),2002.
Schneider Nat. Transport v. Ford Motor Co.
280 F.3d 532

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754 A.2d 742, 50 ERC 2065, 89 A.L.R.5th 677
(Cite as: 754 A.2d 742)

Supreme Court of Rhode Island.
TEXTRON, INC.
v.
AETNA CASUALTY AND SURETY COMPANY et al.

No. 98-357-Appeal.
June 22, 2000.

Insured brought action against liability insurers to recover cleanup costs. The Superior Court, Providence County, Gagnon, J., granted partial summary judgment in favor of insurers on the basis of the trigger of coverage. Insured appealed. The Supreme Court, Goldberg, J., 723 A.2d 1138, vacated and remanded. On remand, the Superior Court, Gagnon, J., entered partial summary judgment in favor of comprehensive general liability (CGL) insurer. Insured appealed. The Supreme Court, Flanders, J., held that: (1) as a matter of first impression, the word "sudden" in the "sudden and accidental" exception to the pollution exclusion can mean "unexpected" and provides coverage to the insured that makes a good-faith effort to contain and to neutralize toxic waste; (2) drafting history of the exclusion could be considered; (3) discoverability in the exercise of reasonable diligence was applicable as a trigger of coverage for groundwater contamination; and (4) factual issues precluded summary judgment.

Reversed and remanded.

West Headnotes

[1] Appeal and Error 30 ⚿893(1)

30 Appeal and Error
30XVI Review
30XVI(F) Trial De Novo
30k892 Trial De Novo
30k893 Cases Triable in Appellate Court
30k893(1) k. In General. Most Cited Cases

Summary judgment is reviewed de novo.

[2] Judgment 228 ⚿185(6)

228 Judgment
228V On Motion or Summary Proceeding
228k182 Motion or Other Application
228k185 Evidence in General
228k185(6) k. Existence or Non-Existence of Fact Issue. Most Cited Cases

The superior court should grant summary judgments sparingly and only when a review of all pleadings, affidavits, and discovery materials properly before the court demonstrates that

no issue of fact material to the determination of the lawsuit is in genuine dispute.

[3] Appeal and Error 30 ⚿934(1)

30 Appeal and Error
30XVI Review
30XVI(G) Presumptions
30k934 Judgment
30k934(1) k. In General. Most Cited Cases

In reviewing a grant of summary judgment, the Supreme Court views the evidence in the light most favorable to the nonmoving party.

[4] Insurance 217 ⚿2265

217 Insurance
217XVII Coverage--Liability Insurance
217XVII(A) In General
217k2263 Commencement and Duration of Coverage
217k2265 k. Continuous Acts and Injuries; Trigger. Most Cited Cases

Discoverability in the exercise of reasonable diligence was applicable as a trigger of liability coverage for groundwater contamination.

[5] Insurance 217 ⚿2265

217 Insurance
217XVII Coverage--Liability Insurance
217XVII(A) In General
217k2263 Commencement and Duration of Coverage
217k2265 k. Continuous Acts and Injuries; Trigger. Most Cited Cases

Property damage triggers coverage under comprehensive general liability (CGL) insurance policy when the damage (1) manifests itself, (2) is discovered or, (3) in the exercise of reasonable diligence is discoverable.

[6] Judgment 228 ⚿181(23)

228 Judgment
228V On Motion or Summary Proceeding
228k181 Grounds for Summary Judgment
228k181(15) Particular Cases
228k181(23) k. Insurance Cases. Most Cited Cases

Genuine issue of material fact concerning whether the insured could have discovered groundwater contamination by reasonable diligence precluded summary judgment on whether coverage was triggered under comprehensive general liability (CGL) insurance policy.

[7] Insurance 217 ⚿1810

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1810 k. Construction as a Whole. Most Cited Cases

Insurance 217 ⚿1822

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1822 k. Plain, Ordinary or Popular Sense of Language. Most Cited Cases

A policy must be examined in its entirety, and the words used must be given their plain everyday meaning, if the meaning of the terms is contested.

[8] Insurance 217 ⚿1832(1)

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1832 Ambiguity, Uncertainty or Conflict
217k1832(1) k. In General. Most Cited Cases

Any ambiguous policy language is strictly construed in favor of the insured.

[9] Insurance 217 ⚿2278(17)

217 Insurance
217XVII Coverage--Liability Insurance
217XVII(A) In General
217k2273 Risks and Losses
217k2278 Common Exclusions
217k2278(17) k. Pollution. Most Cited Cases

The word “sudden” is ambiguous in the “sudden and accidental” exception to the pollution exclusion of a comprehensive general liability (CGL) insurance policy.

[10] Insurance 217 ⚿1832(1)

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1832 Ambiguity, Uncertainty or Conflict
217k1832(1) k. In General. Most Cited Cases

Insurance 217 ⚿1836

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1836 k. Favoring Coverage or Indemnity; Disfavoring Forfeiture. Most Cited Cases

An ambiguous policy term should be construed in favor of coverage and against the insurer.

[11] Insurance 217 ⚿2278(17)

217 Insurance
217XVII Coverage--Liability Insurance
217XVII(A) In General
217k2273 Risks and Losses
217k2278 Common Exclusions
217k2278(17) k. Pollution. Most Cited Cases

The word "sudden" in the "sudden and accidental" exception to the pollution exclusion of a comprehensive general liability (CGL) insurance policy bars coverage for the intentional or reckless polluter, but provides coverage to the insured that makes a good-faith effort to contain and to neutralize toxic waste but, nonetheless, still experiences unexpected and unintended releases of toxic chemicals that cause damage; thus, coverage will be provided when the contamination was unexpected from the insured's standpoint, that is, the insured reasonably believed that the waste-disposal methods in question were safe.

[12] Judgment 228 ⚿181(23)

228 Judgment
228V On Motion or Summary Proceeding
228k181 Grounds for Summary Judgment
228k181(15) Particular Cases
228k181(23) k. Insurance Cases. Most Cited Cases

The question whether a manufacturer was an intentional or reckless polluter with respect to waste disposal or with respect to selecting a waste-disposal system is usually a matter for fact-finding at trial on the applicability of the "sudden and accidental" exception to the pollution exclusion of a comprehensive general liability (CGL) insurance policy, and not a matter for summary judgment.

[13] Judgment 228 ⚿181(23)

228 Judgment
228V On Motion or Summary Proceeding
228k181 Grounds for Summary Judgment

228k181(15) Particular Cases
228k181(23) k. Insurance Cases. Most Cited Cases

Genuine issue of material fact concerning whether the insured tried to contain the contaminants safely in the neutralization pond or indiscriminately dumped them precluded summary judgment on whether release was "sudden" within the meaning of the "sudden and accidental" exception to the pollution exclusion of a comprehensive general liability (CGL) and umbrella insurance policies.

[14] Insurance 217 ⚿2278(17)

217 Insurance
217XVII Coverage--Liability Insurance
217XVII(A) In General
217k2273 Risks and Losses
217k2278 Common Exclusions
217k2278(17) k. Pollution. Most Cited Cases

The word "sudden" in the "sudden and accidental" exception to the pollution exclusion of a comprehensive general liability (CGL) insurance policy can mean "unexpected."

[15] Insurance 217 ⚿2278(17)

217 Insurance
217XVII Coverage--Liability Insurance
217XVII(A) In General
217k2273 Risks and Losses
217k2278 Common Exclusions
217k2278(17) k. Pollution. Most Cited Cases

Drafting history of the "sudden and accidental" exception to the pollution exclusion of a comprehensive general liability (CGL) insurance policy could be considered as supporting an interpretation of "sudden" to included unexpected; it was reasonable to hold insurers to the representations they made to regulators when seeking approval for an ambiguous pollution exclusion.

[16] Judgment 228 ⚿185.3(12)

228 Judgment
228V On Motion or Summary Proceeding
228k182 Motion or Other Application
228k185.3 Evidence and Affidavits in Particular Cases
228k185.3(12) k. Insurance. Most Cited Cases

Evidence that discharges other than those from the insured's containment pond could have been responsible for at least some of the environmental damage at issue precluded summary judgment on applicability of pollution exclusion of comprehensive general liability (CGL) and

umbrella insurance policies.

***743** John Tarantino,James W. McKay, Providence, Eugene R. Anderson, Robert M. Horkovich, Edward J. Stein, Anderson Kill & Olick, P.C., New York City, for plaintiff.

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Mark T. Reynolds, Providence, P. McNamara, for Allstate.

Michael A. Kelly, Gerald John Petros, Providence, for Cumberland Farms.

Alan Shoer, Providence, for D.E.M.

Michael P. Duffy, Boston, MA, Laura Foggan, Daniel Troy, Washington, DC, for Insurance Environmental Litigation.

John W. Kershaw, Providence, for John R. Ludbrooke & London Market.

***744** Present WEISBERGER, C.J., and LEDERBERG, BOURCIER, FLANDERS, and GOLDBERG, JJ.

O P I N I O N

FLANDERS, Justice.

Insurance coverage for a manufacturer's pollution-cleanup costs forms the declaration page of this appeal. A Superior Court motion justice granted partial summary judgment in favor of the defendant-insurer, Insurance Company of North America (INA), and against the plaintiff-insured, Textron, Inc. (Textron), ruling that no insurance coverage existed under the circumstances of this case. Textron argues on appeal that the motion justice: (1) incorrectly applied the trigger-of-coverage doctrine that we formulated in *CPC International*, *Inc. v. Northbrook Excess & Surplus Insurance Co.*, 668 A.2d 647 (R.I.1995) (*CPC I*) and (2) erred in holding that the pollution-exclusion clauses in the insurance polices at issue precluded coverage for the type of gradually occurring damage in question (namely, the eventual contamination of groundwater as a result of chemical seepage from a so-called neutralization pond that Textron maintained at its Wheatfield, New York, plant site). For the reasons unearthed below, we reverse, vacate the summary judgment, and remand for further proceedings consistent with this opinion.

Facts and Travel

From 1960 to 1973, Textron, a manufacturer of aerospace equipment, leased an eighty-acre manufacturing site in Wheatfield, New York from Bell Aircraft Corporation (Bell). In 1973 it bought the property from Bell and, until 1987, it continued to use this site for manufacturing a wide range of aerospace-related equipment, including helicopter components,

aircraft prototypes, and rocket-propulsion hardware. During its long-term use of the site, Textron's manufacturing processes generated toxic chemical wastes. To capture, contain, treat, and neutralize these wastes, it employed an artificial holding pond at the site as a waste receptacle and depository. After treating these wastes, Textron would release them into the site's sanitary-drainage system. However, unbeknownst to Textron, some of this toxic waste gradually seeped from the pond and, over the years, contaminated or contributed to the contamination of the surrounding groundwater.

During the 1980s the Environmental Protection Agency (EPA) charged Textron with polluting dozens of sites across the United States, including Wheatfield. As a result, the EPA sued Textron under the Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. §§ 9601 to 9675 (CERCLA), a strict-liability statute that allows the EPA either to demand that responsible parties voluntarily clean up polluted sites or else reimburse the EPA for its costs in conducting the cleanup operations. Textron, in turn, filed suit in August 1987 against approximately thirty of its own comprehensive general-liability insurers and excess-insurance carriers, including the present defendant, INA, seeking coverage for the site-cleanup costs. Because Textron has settled its claims with all of its other insurers that moved for summary judgment, INA is the only remaining defendant on this appeal.

The policies INA sold to Textron for 1979-81 and 1984-86 contained the following so-called pollution-exclusion clause:

> "This insurance does not apply to bodily injury or property damage arising out of the discharge, dispersal, release or escape of smoke, vapors, soots, fumes, acids, alkalis, toxic chemicals, liquids or gases, waste materials or other irritants, contaminants or pollutants into or upon land, the atmosphere or any water course or body of water, but this exclusion does not apply *if such discharge, dispersal, release or escape is sudden and accidental*." (Emphasis added.)

***745** The policy INA provided to Textron for the period 1982-84 stated as follows:

> "This insurance does not cover liability for: (1) Personal Injury or Bodily Injury or loss of, damage to, or loss of use of property directly or indirectly caused by seepage, pollution or contamination, provided always that this paragraph (1) shall not apply to liability for Personal Injury or Bodily Injury or loss of or physical damage to or destruction of tangible property, or loss of use of such property damaged or destroyed *where such seepage, pollution or contamination is caused by a sudden, unintended and unexpected happening during the period of this Insurance.*"
>
> "(2) The cost of removing, nullifying or cleaning-up seeping, polluting or contaminating substances *unless the seepage, pollution or contamination is caused by a sudden, unintended and unexpected happening* during the period of this Insurance." (Emphases added.)

For the period from 1963 to 1966, INA also issued to Textron an umbrella policy (that is, a policy that offered protection for losses in excess of the amounts covered by Textron's other liability insurance and that filled certain other gaps in coverage, *see Fratus v. Republic*

Western Insurance Co., 147 F.3d 25, 27 (1st Cir.1998)). This policy did not contain a pollution-exclusion clause.

The Superior Court granted partial summary judgment in favor of INA on Textron's claim for cleanup costs at the Wheatfield site based upon its determination that (1) these costs did not trigger coverage under the three-part test that this Court set forth in *CPC I,* and (2) for INA policies issued from 1979 to 1981, 1982 to 1984, and from 1984 to 1986, the incorporated pollution-exclusion clauses barred coverage because no temporally sudden event at the site caused the damage. Textron has appealed from that judgment.

Standard of Review

[1][2][3] This Court reviews the grant of a summary judgment motion de novo. *See Marr Scaffolding Co. v. Fairground Forms, Inc.,* 682 A.2d 455, 457 (R.I.1996). The Superior Court should grant summary judgments " 'sparingly [and] only when a review of all pleadings, affidavits, and discovery materials properly before the court demonstrates that no issue of fact material to the determination of the lawsuit is in genuine dispute.' " *Doe v. Gelineau,* 732 A.2d 43, 47-48 (R.I.1999). In reviewing a grant of summary judgment, we view the evidence in the light most favorable to the nonmoving party. *See Nichols v. R.R. Beaufort & Associates, Inc.,* 727 A.2d 174, 176 (R.I.1999).

Analysis

I

Trigger of Coverage

[4] Textron argues that the Superior Court erroneously granted partial summary judgment in favor of INA because it misread this Court's *CPC I* decision. According to Textron, the Superior Court wrongly construed *CPC I* as delineating only a single trigger of coverage for environmental property damage: namely, whether the insured discovered the damage during the policy period. In fact, Textron asserts, the holding in that case provided for three alternative triggers, one of which was a discoverability trigger: that is, whether by exercising reasonable diligence the insured could have discovered the environmental damage during the policy period. We later clarified this particular coverage trigger in *Textron, Inc. v. Aetna Casualty and Surety Co.,* 723 A.2d 1138 (R.I.1999) (*Textron-Gastonia*). There, we held that "discoverable in the underlying exercise of reasonable diligence" meant that (1) the property damage occurred during the policy period, (2) the property damage was capable of being detected, and (3) the insured had reason to test for the property damage. *See id.* at ***746** 1144. Nonetheless, the motion justice chose not to apply the discoverability trigger in this case because, he concluded, its reasonable-diligence standard was "inappropriate in this kind of a case." INA, on the other hand, asserts that, whether the motion justice misapplied the *CPC I* test was irrelevant because Textron failed to meet its burden of proving that, by exercising reasonable diligence, it would have discovered the damage during INA's policy period. We disagree.

[5] Property damage triggers coverage under this type of comprehensive general-liability-insurance policy when the damage (1) manifests itself, (2) is discovered or, (3) in the exercise of reasonable diligence is discoverable. *See CPC I,* 668 A.2d at 649. We agree with Textron that the motion justice's refusal to apply the third trigger of the *CPC I* test did indeed

misconstrue that holding, as amplified by our later ruling in *Textron-Gastonia*, 723 A.2d at 1143-44. The third trigger of the *CPC I* test does not force a manufacturer to "go around looking to find out if he's contaminating anything," as the motion justice supposed. Instead, it simply addresses the problem of latent injury (such as asbestos poisoning) or latent damage (such as groundwater contamination), when the injury or damage, although covered by the policy, is not immediately discernible or occurs after an unexpected event sets in motion a series of incidents that eventually results in the manifestation of the damage. Moreover, the "discoverability" trigger in *CPC I* descends from a long and venerable line of insurance cases. *See, e.g., American Home Assurance Co. v. Libbey-Owens-Ford Co.,* 786 F.2d 22, 30 (1st Cir.1986) (holding that the trigger event for damages resulting from falling windows occurred when the architect informed the owner of the building that the windows were defective and that they posed a "clear and present danger to the public," because this disclosure would have put a reasonable person on notice that this problem existed). Thus, contrary to the motion justice's belief, applying the "discoverability" trigger to cases like this one is not anomalous.

In *CPC I,* the First Circuit certified to this Court a question about triggers of insurance coverage under Rhode Island law. See *CPC I,* 668 A.2d at 647. In *CPC I,* a plaintiff-manufacturer that routinely dumped toxic chemicals into the drains and septic system of its plant sued its insurer for recovery of cleanup costs under a policy that ran from 1979 to 1980. *See id.* at 648. In 1979, during the period covered by the defendant's policy, state investigators discovered that the chemicals had contaminated municipal water supplies. *See id.* The insurer argued that the coverage-triggering "occurrence" was either the plaintiff-manufacturer's routine dumping, or a 1974 massive toxic spill. The insurer argued that the massive spill occurred outside the policy period. *See id.* The manufacturer, however, contended that the 1979 discovery of the contamination should have been the "occurrence" that triggered coverage. *See id.*

Unsure of and yet bound to apply Rhode Island law to the controversy before it, the First Circuit asked this Court to determine when there has been "an 'occurrence' sufficient to trigger coverage under a general liability policy when the insured sustains a chemical spill that results in a property loss that is not discovered until years after the spill took place." *Id.* at 649. This Court answered that "an 'occurrence' under a general liability policy takes place when property damage * * * manifests itself or is discovered or in the exercise of reasonable diligence, is discoverable." *Id.*

[6] Here, the evidence on summary judgment indicated that a genuine issue of material fact existed concerning whether Textron could meet the "discoverable by reasonable diligence" aspect of *CPC I* and *Textron-Gastonia*. First, the record contains evidence that damage not only existed but also was capable of being detected during the policy periods, 1979-81, 1984-86, ***747** 1982-84, and perhaps even during the 1963-66 period covered by the umbrella policy. P. Michael Terlecky, Jr. (Terlecky), the hydrogeologist who supervised environmental investigations at Textron's Wheatfield site, stated in his affidavit that "the groundwater, soil, sediments, and other materials such as bedrock became contaminated at the Wheatfield Site and such contamination was discoverable as early as 1960, [and that] new property damage arose in each and every year thereafter." Florin Gheorghiu, a geoscientist who worked at Textron's Wheatfield site from 1989 through 1992, stated in an affidavit that it

would take contaminated water about fifty-four days to seep downward through soil and reach bedrock. This expert also indicated that, using simple analysis of groundwater samples, Textron could have discovered contamination at the neutralization pond from the time it first began using it in 1960.

Finally, with respect to the question of whether Textron had reason to test for environmental damage during the policy period, expert affidavits suggested that it did. For example, Terlecky asserted that there were "small leaks and spills during transfer of metal parts and leakage through cracks in the concrete" of a building used since 1956 for solvent degreasing and for acid treatment of metal parts. *See Textron-Gastonia,* 723 A.2d at 1144 (holding that knowledge of overflow and other leaks of solvents at the site provided the insured with reasons to test for contamination). Another Textron employee testified that sudden and accidental spills of the chemicals that later ended up in the groundwater "certainly" occurred. Employees also testified that Textron used concrete "pads" from the rocket cell-testing area into the neutralization pond to catch accidental spills and leaks, and that these ramps themselves had cracks that allowed toxic chemicals to leak from them onto the ground. Thus, the same toxic chemicals that later turned up in the groundwater had spilled or leaked accidentally at various times, arguably giving Textron's engineers reasons to test for contamination. Indeed, according to their affidavits, they did, in fact, regularly conduct certain limited types of testing for contamination at the site.

In conclusion, Textron's specific allegations of site contamination amount to more than a mere assertion that it disposed of waste at the site. *See Truk-Away of Rhode Island, Inc. v. Aetna Casualty & Surety Co.,* 723 A.2d 309, 313 (R.I.1999) (holding that such a showing was inadequate to prove a triggering event). "Where a plaintiff can show through credible evidence, such as the affidavit of an expert witness, that property damage occurred sometime during the relevant policy period, the court should accept this as dispositive," *Textron-Gastonia,* 723 A.2d at 1143, at least for the purpose of creating a genuine issue of material fact on summary judgment. Textron introduced not only evidence of discoverable damage at the site during the policy period but also that it had reason to test for it. Thus, a genuine issue of material fact existed concerning whether this evidence met *Textron-Gastonia* 's three-prong test for whether the damage was discoverable in the exercise of reasonable diligence. Hence, the Superior Court erred in granting summary judgment when it declined to apply the discoverability trigger of coverage to the facts of this case.

II
The Pollution-Exclusion Clause

Textron also argues that genuine issues of material fact exist concerning the application of the policies' exceptions to the pollution-exclusion clause, particularly the "sudden and accidental" language used therein. First, it asserts that the word "sudden" in this exception can mean "unexpected," as opposed to "abrupt," and thus the policy can be construed to cover damages resulting from a gradual seepage of toxic chemicals from the containment pond. Textron also suggests that insurance-industry***748** records concerning the clause and its drafting history support a finding of coverage when the contamination was "unintended and unexpected," although not temporally abrupt. Textron maintains that it should have the opportunity to prove this theory at trial through the submission of pertinent insurance-industry

documents. It further contends that a genuine issue of material fact exists concerning whether the artificial containment pond was intended to be a safe container for toxic waste or merely a convenient dumping slough. If, as Textron posits, the previous owner had built and enhanced the pond as a safe receptacle for contaminants, then the relevant discharges for purposes of this litigation may be the subsequent accidental discharges from the pond, rather than the initial placements of wastes in it. If Textron establishes that this was a true containment pond for toxic wastes, then the relevant seepage could prove to be "unintended and unexpected," thus falling under the "sudden and accidental" exception in the pollution-exclusion clause as Textron interprets it. Finally, Textron insists that even if the word "sudden" in the pollution-exclusion clause means only "abrupt," it has presented ample evidence of releases at the site other than those emanating from the neutralization pond that were abrupt and that could have contaminated the groundwater.

INA, on the other hand, asserts that the word "sudden" necessarily contains a temporal element, and thus it can apply only to events that happened abruptly, but not to gradual ones that are merely "unintended or unexpected," as Textron asserts. It adds that Textron has presented no evidence of temporally "sudden" discharges of waste at the Wheatfield site.

The meaning of the word "sudden" in this kind of pollution-exclusion clause is a matter of first impression in Rhode Island. Moreover, our examination of the relevant cases from other jurisdictions reveals no clear majority among state or federal courts concerning whether this word entails a temporal element. (Both sides claim to hold the majority view, but the numbers are close enough that any slight preponderance of one position over the other is not particularly meaningful.) As one court has colorfully described it,

> "The cases swim [in] the reporters like fish in a lake. The Defendants would have this Court pull up its line with a trout on the hook, and argue that the lake is full of trout only, when in fact the water is full of bass, salmon and sunfish too." *Pepper's Steel & Alloys, Inc. v. United States Fidelity and Guaranty Co.,* 668 F.Supp. 1541, 1549-50 (S.D.Fla.1987).

[7][8] When we are asked to interpret contested terms in an insurance policy, "[t]he policy must be examined in its entirety and the words used must be given their plain everyday meaning." *McGowan v. Connecticut General Life Insurance Co.,* 110 R.I. 17, 19, 289 A.2d 428, 429 (1972). Moreover, we strictly construe any ambiguous policy language in favor of the insured. *See Bartlett v. Amica Mutual Insurance Co.,* 593 A.2d 45, 47 (R.I.1991).

A. Ambiguity of the Word "Sudden"

[9] Giving the word "sudden" its "plain everyday meaning" is no easy task. Both sides muster dictionary support of their respective positions, half of which accord a temporal meaning to the word and the other half of which give it the meaning of unexpected.[FN1] This diversity proves only ***749** that the word's meaning is legitimately subject to different interpretations-in other words, that it is ambiguous. Moreover, this Court has also held that "diversity of judicial thought [as to the meaning of terms in an insurance contract] is proof positive" of ambiguity. *Zanfagna v. Providence Washington Insurance Co.,* 415 A.2d 1049, 1051 (R.I.1980). Here, a multitude of cases exists on both sides. Furthermore, a slim but

persuasive majority of other jurisdictions holds that the word "sudden" in this type of clause is ambiguous; that is, it is susceptible to more than one reasonable interpretation, as Textron argues. *See Alabama Plating Co. v. United States Fidelity and Guaranty Co.,* 690 So.2d 331, 334 (Ala.1996) (per curiam) (noting that "[a] narrow majority of state supreme courts that have considered the meaning of the 'pollution exclusion,' * * * have held that the 'sudden and accidental' exception is ambiguous and must be construed in favor of the policyholder to provide coverage where migration of contaminants into the soil or groundwater was 'unexpected and unintended' "). *See also Queen City Farms, Inc. v. Central National Insurance Co. of Omaha,* 126 Wash.2d 50, 882 P.2d 703, 727 (1994) (concluding that "these exclusions are ambiguous, and therefore should be construed against the drafter-insurer, to mean that if the polluting event is unexpected and unintended, coverage is provided").

> FN1. Because the parties cumulatively cite eight dictionaries in their briefs, we take the liberty of indulging in a brief etymological foray of our own. First, we note that the American Heritage Dictionary offers three meanings for the word "sudden:" "[h]appening without warning; unforeseen;" "[c]haracterized by hastiness; abrupt or rash;" and "[c]haracterized by rapidity; quick and swift." American Heritage Dictionary of the English Language, 1794 (3d ed.1996). Black's Law Dictionary defines "sudden" as "[h]appening without previous notice or with very brief notice; coming or occurring unexpectedly; unforeseen; unprepared for." Black's Law Dictionary, 1432 (6th ed.1990) (citing *Hagaman v. Manley,* 141 Kan. 647, 42 P.2d 946, 949 (1935)). The Seventh Edition of Black's Law Dictionary does not define "sudden" but does describe "pollution exclusion." *See* Black's Law Dictionary, 586 (7th ed.1999). The first meaning of the word "sudden" in the American Heritage Dictionary is "[h]appening without warning, unforeseen[,]" and its second and third denote a temporal element. In fact, the modern English word "sudden" is derived from the Latin verb "subire" meaning "to approach stealthily [or secretly]." American Heritage, 1794. The Oxford English Dictionary gives this example: "A sudden little river crossed my path As unexpected as a serpent comes." *Claussen v. Aetna Casualty & Surety Co.,* 259 Ga. 333, 380 S.E.2d 686, 688 (1989) (quoting Oxford English Dictionary, 96 (1933)). While the modern word certainly has acquired a secondary, temporal meaning, the original and still perfectly functional meaning of the word is happening without warning or anticipation. Thus, reading the word "sudden" in the context of insurance policies to mean "unexpected" not only harmonizes with its context but also remains true to the word's original meaning. Our present interpretive problems with this word may arise from our modern forgetfulness that it is often used to describe a subjective state, that is, the mental state of the person visited by the event. In other words, even though a snake may have been slowly slithering toward a person, that person may still experience its appearance as temporally abrupt *because* it is unexpected. Thus, the temporal connotation given to "sudden" can arise from the subjective perception of an event and it does not denote necessarily any *objectively* temporal element.

[10] Under Rhode Island law, an ambiguous policy term should be construed in favor of coverage and against the insurer. *See Campbell v. Norfolk & Dedham Mutual Fire Insurance*

Co., 682 A.2d 933, 935 (R.I.1996) (holding that "[i]f the terms of an insurance contract are subject to more than one reasonable interpretation, the policy will be construed in favor of the insured to avoid forfeiture"); *Zanfagna,* 415 A.2d at 1051 (charging the fault for any ambiguity "to the insurer who selected the language"). Other jurisdictions have noted that this principle holds not only when the insured is an unsophisticated consumer, but also when, as here, the insured is a corporation that might presumably have more business acumen and bargaining power. *See Queen City,* 882 P.2d at 726.[FN2]

> FN2. To apply this principle to large corporations such as Textron makes more sense in the insurance-policy context than it might in other settings: while business customers of insurance companies may at first glance appear to have more power in negotiating an insurance contract, in fact the only negotiation that typically occurs over the policy language is that between state regulators and the insurers. *See Morton International, Inc. v. General Accident Insurance Co. of America,* 134 N.J. 1, 629 A.2d 831, 851 (1993). Often the commercial insured such as Textron does not even view the policy's language until after it pays the premiums. *See generally,* Nancer Ballard and Peter M. Manus, *Clearing Muddy Waters: Anatomy of the Comprehensive General Liability Pollution Exclusion,* 75 Cornell L.Rev. 610, 621 (1990).

[11][12] ***750** When used in the context of an insurance policy's pollution-exclusion clause, the word "sudden," we hold, bars coverage for the intentional or reckless polluter but provides coverage to the insured that makes a good-faith effort to contain and to neutralize toxic waste but, nonetheless, still experiences unexpected and unintended releases of toxic chemicals that cause damage. Thus, coverage will be provided when the contamination was unexpected from the insured's standpoint: that is, when the insured reasonably believed that the waste-disposal methods in question were safe. The insured must show that it had no reason to expect the unintended damage and that it undertook reasonable efforts to contain the waste safely. In other words, a manufacturer that uses state-of-the-art technology, adheres to state and federal environmental regulations, and regularly inspects, evaluates, and upgrades its waste-containment system in accordance with advances in available technology should reap the benefits of coverage under our construction of this type of pollution-exclusion clause. But one that knowingly or recklessly disposes of waste without the necessary and advisable precautions will forfeit coverage under this clause. Thus, coverage will exist "[w]here the facts establish that materials were placed into a waste disposal site which was believed would contain or safely filter them, but, in fact, the materials unexpectedly and unintentionally are discharged or released into the environment, or disperse or escape into the environment * * *." *Queen City,* 882 P.2d at 726. Whether a manufacturer was an intentional or reckless polluter with respect to waste disposal or with respect to selecting a waste-disposal system, is, as here, usually a matter for fact-finding at trial and not for summary judgment.

Of course, we recognize that the two policies at issue here have slightly different language in their respective pollution-exclusion clauses. While the 1979-81 and 1984-86 policies bar coverage unless the event is "sudden and accidental," the 1982-84 policy bars coverage for discharges unless they are caused by a "sudden, unintended and unexpected happening." However, we construe the language of the second policy to have the same legal meaning and effect as that of the first under the analysis we have employed above. *See Public Service Co.*

of Colorado v. Wallis and Companies, 986 P.2d 924, 933 (Colo.1999) (holding that "the phrase 'sudden, unintended and unexpected' [in the London pollution-exclusion clause] means 'unprepared for, unintended and unexpected' "). The language of the later policy follows the form of certain underlying insurance policies issued by Lloyd's of London. Courts have held that the language of pollution-exclusion clauses in Lloyd's policies is legally synonymous with the standard pollution-exclusion language. *See Olin Corp. v. Insurance Co. of North America,* 762 F.Supp. 548, 563 (S.D.N.Y.1991) (finding "no meaningful difference" between the standard pollution-exclusion clause and the one at issue here). Though Lloyd's has argued that it never misrepresented the meaning of its clause to American insurance regulators, courts have held nonetheless that such clauses should not benefit from the misleading explanation of the standard pollution exclusion submitted to state regulators by American insurance companies. *Chemical Leaman Tank Lines, Inc. v. Aetna Casualty and Surety Co.,* 89 F.3d 976, 991 (3d Cir.1996).

[13] Here, a genuine issue of material fact exists concerning whether Textron tried, albeit unsuccessfully, to contain the contaminants safely in the neutralization pond. Textron has offered evidence that it had established a "neutralization system," and had introduced chemicals into the pond to treat them. Textron's engineers ***751** regularly tested the pond's waters to measure their pH level, and to monitor the neutralization process. Only after Textron deemed the toxins harmless did it release them from the pond. While Textron's engineers did not line the pond artificially, they testified that clay lining constituted the state-of-the-art sealant at that time, and that no existing regulation required or even recommended further lining. Engineering reports indicated that Bell, Textron's predecessor at the site, dug out the pond as a waste-containment strategy. And Textron's engineers assert that it enhanced the pond on the site to a "state of the art" toxic-containment level, while INA insists Textron merely used the pond "as is" to dump waste.[FN3] Therefore, competent evidence exists in this record, which, if credited by the factfinder, could support the conclusion that Textron was not a deliberate or reckless polluter. Hence, summary judgment was inappropriate.

> FN3. While it is technically true, as INA argues, that the pond preexisted Textron's presence at the site, this is because Bell, which occupied the Wheatfield site before Textron, had constructed the pond as a receptacle for waste. Whether Textron was reckless in failing to test and/or to check out the pond's alleged containment features and how well they worked in practice remains a subject for further fact-finding.

B. "Sudden" as Meaning Unexpected and Unintended in Light of Drafting History and Public Policy

[14][15] Construing "sudden" as capable of meaning "unexpected" constitutes both a defensible reading of the pollution-exclusion clause's drafting history and sound public policy. First, we note that most courts that have examined the drafting history of the pollution-exclusion clause as an aid in its construction have found the word "sudden" to mean unexpected. The most thorough of these, and the one with the most dramatic result, is *Morton International, Inc. v. General Accident Insurance Co. of America,* 134 N.J. 1, 629 A.2d 831 (1993). In *Morton,* the New Jersey Supreme Court examined the history of the pollution-exclusion clause's incorporation into insurance contracts and found that, despite its literal terms, the clause should be taken as precluding coverage to " 'the reckless polluter as well as

the intentional polluter.' " *Id.* at 851. Despite arguments about the insurance industry's intent in drafting the pollution-exclusion clause, the *Morton* court held insurers to the meaning of the word "sudden" as the court deemed they had represented it to insurance regulators-that is, as a clarification of the insurers' intention to exclude only intentional polluters from coverage-rather than as a word having a strictly temporal meaning. *See id.* at 875-76.

Similarly, in *Alabama Plating Co.,* the Alabama Supreme Court found that the phrase "sudden and accidental" in the pollution-exclusion clause was sufficiently ambiguous to require an inquiry into the drafters' intent, and found that this history demonstrated that the drafters of the clause meant to provide coverage when environmental contamination was "unexpected and unintended." *Alabama Plating Co.,* 690 So.2d at 335-36. The court described its historical reasoning as follows:

> "Before the addition of the so-called 'pollution exclusion' to 'occurrence'-based * * * policies * * * it was clear that the policies provided coverage for gradually occurring environmental contamination. The evidence of the intent of the drafter of the 'pollution exclusion' clause, an insurance industry group that represented [many insurers], reveals that when the clause was added * * * it was * * * with an expressed intent that there would be *no reduction in coverage,* but that the addition of the exclusion was merely a 'clarification' that the policies did not provide coverage for intentional polluters." *Id.* at 335; see also *Claussen v. Aetna Casualty & Surety Co.,* 259 Ga. 333, 380 S.E.2d 686, 689 (1989) (holding that "[d]ocuments presented by ***752** the Insurance Rating Board * * * to the Insurance Commissioner when the 'pollution exclusion' was first adopted suggest that the clause was intended to exclude only intentional polluters").

The *Alabama Plating* court also noted that the phrase had undergone years of judicial construction before insurers used it in property-damage policies and that "[c]ourts had uniformly interpreted [it] to mean that the damage had to be unexpected and unintended for the insurance to apply, so that the phrase provided coverage for gradual events." *Alabama Plating Co.,* 690 So.2d at 336. The court defended its historical reasoning by noting that the "judicial construction placed upon particular words or phrases made prior to the issuance of a policy employing them will be presumed to have been the construction intended to be adopted by the parties." *See id.* (quoting *Couch on Insurance 2d* § 15:20 (1984)).

The Washington Supreme Court has perhaps best articulated the rationale for according the word "sudden" the meaning of unexpected rather than temporally abrupt in the context of insurance-liability policies. *See Anderson & Middleton Lumber Co. v. Lumbermen's Mutual Casualty Co.,* 53 Wash.2d 404, 333 P.2d 938 (1959). The *Anderson* court explained that "the risk to the insurer would be the same, whether a break was instantaneous or began with a crack which developed over a period of time until the final cleavage occurred, as long as its progress was undetectable." *Id.* at 940. It reasoned that construing "sudden" as unforeseen effectuated the purpose of the liability policy at issue, and, impliedly, insurance contracts in general: namely, to protect the policyholder in case of accidental occurrences, but to prevent the insured from "proceed[ing] recklessly and hold[ing] the insurer liable for damage if [the policyholder] had been forewarned * * * and could have taken steps to forestall it * * *." *Id.* at 940-41.

In *Hudson v. Farm Family Mutual Insurance Co.,* 142 N.H. 144, 697 A.2d 501, 502-03 (1997), the insured was a farmer who made a claim against his insurer for injury to his cows caused by stray voltage. The farmer asserted that his insurance contract covered losses involving "Sudden and Accidental Damage from * * * Electrical Current." *See id.* The insurer countered that the long-term exposure at issue was not "sudden and accidental." *Id.* at 503. The court held that, in this context, the word "sudden" meant unexpected. *See id.* at 504. In support of this holding, it cited a leading insurance manual to the effect that " 'sudden' is not to be construed as synonymous with instantaneous." *See id.* The *Hudson* court also noted that construing "sudden" to mean "unexpected" as in the above cases did not, as INA argues, create a redundancy with respect to the succeeding word accidental. *See id.* Rather, "the joint use of the words 'sudden and accidental' serves distinct purposes not accomplished by either word standing alone." *Id.* "Simply put, sudden means unexpected, and accidental means unintended." *Id.* (quoting *New Castle County v. Hartford Acc. and Indem. Co.,* 933 F.2d 1162, 1194 (3d Cir.1991)).

Based upon the above authorities, we conclude that INA's proposed reading of the word "sudden" as necessarily including a temporal element breaks with the history of the word as courts have construed it in other standard insurance policies. Our examination of the pollution-exclusion clause's drafting history similarly suggests that its original purpose-at least as the industry represented it to regulators-was to deny coverage to reckless or intentional polluters. We note first that the President of INA himself announced his company's intention to adopt the pollution-exclusion clause with these comments:

> "INA will continue to cover pollution which results from an accidental discharge of effluents-the sort of thing that can occur when equipment breaks down. We will no longer insure the ***753** company which knowingly dumps its wastes. In our opinion, such repeated actions-especially in violation of specific laws-are not insurable exposures. * * * We at INA hope that our anti-pollution exclusion may help encourage many companies to take the first, crucial steps toward improving their manufacturing processes-the steps that will lead eventually to a cleaner, healthier and, we hope, happier life for all." *Morton,* 629 A.2d at 850 (quoting Charles K. Cox, *Liability Insurance in an Era of the Consumer,* Address Before the Annual Conference of the American Society of Insurance Management, (Apr. 9, 1970), quoted in Robert S. Soderstrom, *The Role of Insurance in Environmental Litigation,* 11 *Forum* 762, 767 (1976)).

The Insurance Rating Board represents the insurance industry before state regulators. When seeking approval from the Rhode Island Department of Business Regulation (Insurance Division) for the policy language at issue, it submitted a circular containing an explanatory memorandum that read in part:

> "Coverage for pollution or contamination is not provided in most cases under present policies because the damages can be said to be expected or intended and thus are excluded by the definition of occurrence. The above exclusion clarifies this situation so as to avoid any question of intent. *Coverage is continued for pollution or contamination caused injuries when the pollution or contamination results from an accident * * *.*" (Emphasis added.)

Moreover, the above representations are consistent with those the insurance industry made to other states when seeking approval of the pollution-exclusion clause. For example, the secretary of Travelers Insurance Company's Product Management Division, in a letter to New York State's associate insurance examiner dated January 13, 1982, assured that state's Insurance Division that "there is nothing in the term 'sudden and accidental' which *requires* the elimination of gradually occurring events from the collective. A number of court decisions in many jurisdictions have essentially reached the same conclusion: there is nothing which prevents gradually occurring events from being construed to be 'sudden and accidental' as long as there is no intent to cause injury or damages."

As these cases suggest, state regulators as a practical matter often are the only parties who are in a position to negotiate language changes in proposed commercial insurance contracts. Under these circumstances, it is reasonable to hold insurers to the representations they made to regulators when seeking approval for a pollution-exclusion clause like this one, which is susceptible to more than one plausible interpretation.

Many of the cases INA cites in support of its position deal with manufacturers who entrusted the disposal of their waste to third-party waste haulers. *See, e.g., Stamford Wallpaper Co. v. TIG Insurance,* 138 F.3d 75, 80 (2nd Cir.1998) (holding that the mere fact that the manufacturer had handed its waste over to a third party did not automatically cause the release of waste to fall within the "sudden and accidental" exception to the pollution exclusion); *St. Paul Fire and Marine Insurance Co. v. Warwick Dyeing Corp.,* 26 F.3d 1195, 1204 (1st Cir.1994) (holding that a manufacturer's use of a waste disposal company did not allow it to obtain coverage under the exception to the pollution-exclusion clause because the discharge that caused the damage was the hauler's deposit of the waste in the landfill, not an intervening, unexpected event such as a sudden leak). And one of these cases employs the same standard for determining whether coverage applies in cases of third-party waste disposal that we have enunciated above. *See A. Johnson & Co. v. Aetna Casualty and Surety Co.,* 933 F.2d 66 (1st Cir.1991). ***754** In *A. Johnson,* the plaintiff's predecessor had "arranged for the handling or transport of a pollutant which arrived at the Site and which has been discharged to ground water or other waters of the State." *Id.* at 67. Even though the First Circuit predicted that the Maine Supreme Judicial Court would construe the word "sudden" as having a temporal meaning, it held that the exclusion applied because "leakage from multiple storage tanks" at the disposal site constituted " 'common place events which occurred in the course of daily business' " and thus did not fall under the heading of sudden and accidental. *Id.* at 75-76 (quoting *Industrial Indemnity Insurance Co. v. Crown Auto Dealerships,* 731 F.Supp. 1517, 1520-21 (M.D.Fla.1990)). Whether the leaks in *A. Johnson* were temporally sudden was irrelevant; rather, their visible occurrence as part of the manufacturer's daily operations precluded their classification as sudden and accidental. Because the discharges were obvious and ongoing, the plaintiff-manufacturer could not have claimed they were unexpected. *See id.* at 75.

Similarly, in *Northern Insurance Co. of New York v. Aardvark Associates, Inc.,* 942 F.2d 189, 195 (3d Cir.1991), also cited by INA, the Third Circuit predicted that the Supreme Court of Pennsylvania would find a transporter of waste could not invoke the "sudden and accidental" exemption because the leakage had been occurring for some time and that

"inspectors had 'noted approximately 1200 industrial waste drums in various stages of deterioration' and that * * * 'hazardous drum contents were leaking onto the soil * * *.' " A reading of "sudden" as meaning unexpected or unintended would not have changed the outcome of this case: again, the court used the clause to deny coverage to a knowing or reckless polluter whose contamination arose directly from its regular course-of-business activity without the aid of an intervening, unexpected event. *Id.* at 196.

Whether Textron's deposition of waste into the neutralization pond amounted to indiscriminate dumping of toxic chemicals conducted as part of its regular business activity, as in the above cases, or whether its regular practice was to contain the waste, neutralize it, and thereby try to prevent it from contaminating the environment, is a disputed question of material fact in this case. Unlike the manufacturer in *Warwick Dyeing*, Textron does allege-and may be able to prove at trial-that an intervening, unexpected event (namely, the unexpected leakage from the pond) caused the damage. *Cf. Warwick Dyeing*, 26 F.3d at 1204 (finding "no evidence of any intervening discharge between the disposal of waste on the landfill and the actual damage that eventually resulted"). Even though a separate line of cases refuses to absolve manufacturers from liability for toxic-waste cleanup costs simply because they turned the waste over to a third party whose actions caused environmental damage, this is not Textron's situation. Textron contends that its initial discharge into the pond did not cause the harm, but instead an intervening event, namely an unexpected leak, did so. The *Warwick Dyeing* court, as noted above, suggested that such an assertion would raise questions about the manufacturer's culpability for the leak. Thus, fact-finding is in order concerning whether these discharges were in fact unexpected and unintended, as Textron has alleged.

Construing the word "sudden" as meaning unexpected in pollution-exclusion clauses also represents sound public policy. Read this way, the clause rewards manufacturers with coverage if they undertake a good-faith effort to dispose of contaminants safely yet suffer an unexpected discharge despite these efforts, thus providing them with an incentive to arrange for the disposal of toxic waste with great care. In the case of manufacturers who independently contract for their waste disposal, this holding requires them to take reasonable steps to ascertain whether their hauler or carter complies with the highest ***755** standards for waste disposal. A contrary interpretation of the clause would fail to distinguish between intentional and unintentional discharges, between waste dumped onto or into the ground in the middle of the night, and waste that has been carefully sealed in lined, state-of-the-art containers but nonetheless accidentally escapes into the environment. As a matter of interpreting this ambiguous clause, it seems prudent to follow a path that affords companies that use toxins in their work the incentive to handle them carefully, but that still affords coverage for truly unexpected and unintended releases of toxic materials.

III
Concurrent Causation

Textron next argues that the so-called "concurrent causation doctrine" also should have precluded summary judgment because a genuine issue of material fact exists concerning whether INA can prove that the sole cause of the damage at issue fell within the pollution-exclusion clause. INA counters that Textron's operations at this site were simply "pollution-prone" and that the motion justice correctly refused to "microanalyze the facts."

Although no Rhode Island case addresses this issue, the First Circuit has held that a jury should determine which event among several alternate possibilities "primarily caused" alleged environmental damage. *See CPC International, Inc. v. Northbrook Excess and Surplus Insurance Co.,* 144 F.3d 35, 48 (1st Cir.1998). In cases involving multiple discharges of pollutants, other courts have held that if property damage results from at least one covered cause, the fact that other non-covered causes also contributed to the property damage does not eliminate coverage. *E.g., SCSC Corp. v. Allied Mutual Insurance Co.,* 536 N.W.2d 305, 314 (Minn.1995). In *SCSC,* the insurers of a business that allegedly contaminated groundwater beneath its property argued that they did not have to provide coverage. *See id.* at 309. They relied upon the same pollution-exclusion clause that is at issue in this case. *See id.* at 313. The jury found that multiple events caused the damage, yet it was unable to find that a covered event was the overriding cause. *See id.* at 314. In affirming the trial court's findings of liability on the part of the insurer, the Minnesota Supreme Court held that

> "Coverage is not defeated simply because a separate excluded cause contributes to the damages. * * * If the insurer asserts that a noncovered or excluded cause was the true cause, the insurer cannot simply show that this noncovered or excluded cause is a direct cause; it must show something more than that. It is consistent, therefore, to require the insurer to show that the noncovered or excluded cause is the overriding cause-so much so that it overrides the insured's showing of a direct, covered cause. To allow any less of a showing would conflict with the principle that the insured need show only one direct, covered cause." *Id.*

Similarly, in *Continental Casualty Co. v. Rapid-American Corp.,* 80 N.Y.2d 640, 593 N.Y.S.2d 966, 609 N.E.2d 506, 508 (1993), New York's highest court found that the insurer of a company that used asbestos was liable to defend against suits arising out of asbestos exposure even though the policy precluded coverage for any discharges into the atmosphere. The court held that even though some contamination may have occurred from ingestion through discharges into the air, some of it may also have occurred through direct contact with hands or clothing. See id. 593 N.Y.S.2d 966, 609 N.E.2d at 513. Hence, "[w]here contamination could occur in a variety of ways, only one of which is potentially excluded, [the insurer] cannot meet the heavy burden of showing that the exclusion applies * * *." *Id.*

Moreover, when, as here, an insured has offered "specific evidence creating a genuine ***756** issue as to whether the incidents at the sites were sudden and accidental and caused more than a de minimis release of pollutants into the environment," summary judgment is inappropriate. *Millipore Corp. v. Travelers Indemnity Co.,* 115 F.3d 21, 34 (1st Cir.1997). (Emphasis added.) Similarly, the Massachusetts Supreme Judicial Court has held that a grant of summary judgment in favor of an insurance company on the basis of the pollution-exclusion clause was error when, notwithstanding the fact that "most of the releases resulted from * * * routine business practices, * * * some of the releases were indeed 'sudden and accidental.' " *Nashua Corp. v. First State Insurance Co.,* 420 Mass. 196, 648 N.E.2d 1272, 1276 (1995).

[16] The reasoning in the above-cited cases persuades us that summary judgment was inappropriate here. Textron offered evidence of discharges other than those from the

containment pond that could have been responsible for at least some of the environmental damage at issue. For example, the intermittent releases of steam from the rocket-cell testing waters and the accidental leaks of chemicals from the rocket-cell testing area and from the blade-bonding facility could have caused at least some of the damage in question. This evidence requires fact-finding on the part of the jury to apportion the damages between covered and noncovered damages or to determine that no such apportionment is possible.

Conclusion

In sum, then, we hold that the Superior Court erred in granting summary judgment because genuine issues of material fact exist that require resolution by the fact-finder. For these reasons we sustain Textron's appeal, vacate the Superior Court's judgment, and remand this case for further proceedings consistent with this opinion.

R.I.,2000.
Textron, Inc. v. Aetna Cas. and Sur. Co.
754 A.2d 742, 50 ERC 2065, 89 A.L.R.5th 677

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992 S.W.2d 440, 42 Tex. Sup. Ct. J. 521
(Cite as: 992 S.W.2d 440)

Supreme Court of Texas.
Emilio URRUTIA and Penske Truck Leasing Co., L.P., Petitioners,
v.
Ferol DECKER, Respondent.

No. 98–0554.
Argued Jan. 13, 1999.
Decided April 8, 1999.

Victim of automobile accident brought action against driver and insured lessor to avoid settlement on ground of fraud or mutual mistake about amount of liability insurance. The 234th District Court, Harris County, Scott Brister, J., entered summary judgment in favor of driver and insured. Victim appealed. The Court of Appeals, Mirabel, J., 965 S.W.2d 26, reversed and remanded. Review was granted. The Supreme Court, Phillips, C.J., held that: (1) rental agreement was sufficiently written into lessor's policy and did not need to be attached to it; (2) the liability insurance provided by the agreement was made voidable, not void, by lack of approval by the State Board of Insurance; and (3) victim was bound by terms of the insurance since he had accepted it.

Reversed and rendered.

West Headnotes

[1] Insurance 217 ⚿1751

217 Insurance
217XIII Contracts and Policies
217XIII(B) Formation
217k1750 Attaching Documents to Policies
217k1751 k. In general. Most Cited Cases

Rental agreement for motor vehicle did not need to be attached to lessor's automobile liability insurance policy to be effective as part of insurance contract under statute requiring contract or agreement to be written into the application and policy. V.A.T.S. Insurance Code, art. 5.06(2).

[2] Insurance 217 ⚿1751

217 Insurance
217XIII Contracts and Policies
217XIII(B) Formation
217k1750 Attaching Documents to Policies
217k1751 k. In general. Most Cited Cases

Insurance 217 ⚿1839

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1838 Materials Related or Attached to Policies
217k1839 k. In general. Most Cited Cases

A separate contract can be incorporated into an insurance policy by an explicit reference clearly indicating the parties' intention to include that contract as part of the agreement. V.A.T.S. Insurance Code, art. 5.06(2).

[3] Insurance 217 ⚿2660.5

217 Insurance
217XXII Coverage—Automobile Insurance
217XXII(A) In General
217k2660 Persons Covered
217k2660.5 k. In general. Most Cited Cases
(Formerly 217k2660)

Rental agreement extending liability insurance to motor vehicle lessee was sufficiently "written into" the lessor's automobile insurance policy through endorsement defining "insured" to include lessees to the extent provided in rental agreement, and, thus, the agreement was sufficiently incorporated into the policy to satisfy statute requiring contract or agreement to be written into the application and policy. V.A.T.S. Insurance Code, art. 5.06(2).

[4] Insurance 217 ⚿2100

217 Insurance
217XV Coverage—in General
217k2096 Risks Covered and Exclusions
217k2100 k. Persons covered. Most Cited Cases

An insurer may validly agree to add as an additional insured any person or organization to which the named insured is obligated by virtue of a written contract to provide insurance.

[5] Insurance 217 ⚿2104

217 Insurance
217XV Coverage—in General
217k2104 k. Extent of loss or liability in general. Most Cited Cases

An endorsement adding an additional insured may provide lower coverage limits to the additional insured than to the named insured.

[6] Insurance 217 ⚿1774

217 Insurance
217XIII Contracts and Policies

217XIII(C) Formal Requisites
217k1774 k. Filing and approval. Most Cited Cases

Insurers may not be able to enforce agreements written on forms not approved by the State Board of Insurance. V.A.T.S. Insurance Code, art. 5.06(2).

[7] Insurance 217 ⚿1738

217 Insurance
217XIII Contracts and Policies
217XIII(B) Formation
217k1731 Offer and Acceptance; Applications
217k1738 k. Effect of acceptance and approval. Most Cited Cases

Insurance 217 ⚿1969

217 Insurance
217XIII Contracts and Policies
217XIII(R) Rescission for Fraud or Mistake
217k1969 k. Rescission by insureds or beneficiaries. Most Cited Cases

Because insurance sold through a policy not approved by the State Board of Insurance is voidable, the insured may, upon learning that the insurance is unapproved, elect to rescind it; if the insured elects to accept the insurance, he or she must do so under the agreed terms. V.A.T.S. Insurance Code, art. 5.06(2).

[8] Insurance 217 ⚿2756(1)

217 Insurance
217XXII Coverage—Automobile Insurance
217XXII(C) Liability Coverage
217k2754 Amount of Coverage
217k2756 Limits of Liability
217k2756(1) k. In general. Most Cited Cases

Liability insurance provided to motor vehicle lessee in rental agreement was made voidable, not void, by lack of approval by the State Board of Insurance, and, thus, accident victim who accepted the insurance benefits provided by the agreement was bound by policy limits applicable to customer. V.A.T.S. Insurance Code, art. 5.06(2).

***441** Tim S. Leonard, David Scott Curcio, John B. Wallace, William Douglas Hammond, Mark D. Flanagan, Houston, for petitioners.

Dan Hennigan, Houston, for respondent.

Chief Justice PHILLIPS delivered the opinion for a unanimous Court.

This case requires us to determine the validity of liability insurance a truck leasing

company provided to its customer as part of a rental transaction. Based on representations that $20,000 was all the insurance available, the claimant settled his bodily injury claim for that amount. When he later discovered the nature of the leasing company's insurance arrangement, he sued the leasing company and its customer, seeking to set aside the previous settlement. The claimant urged that the settlement was obtained by fraud or resulted from the parties' mutual mistake about the insurance available to pay his claims.

The trial court granted summary judgment for the leasing company and its customer. The court of appeals reversed and remanded, holding that the claimant had raised a fact issue on mutual mistake because the rental agreement was not written on a form approved by the State Board of Insurance and was not written into the policy, as required by article 5.06(2) of the Texas Insurance Code. At a minimum, the court held, this failure raised a fact issue about whether the rental agreement was effective to limit the customer's liability insurance to $20,000 instead of the much larger sum available under the leasing company's master policy. 965 S.W.2d 26. Because we disagree with the court of appeals' conclusion about the effect of the rental agreement, we reverse the judgment of the court of appeals and render judgment that the claimant take nothing.

Old Republic Insurance Company insured Penske Truck Leasing Company under a commercial business auto policy. This policy, issued in the state of Pennsylvania, provided one million dollars of liability protection to Penske. An endorsement to the Old Republic policy [the "Pennsylvania endorsement"] enlarged the policy's definition of "insured" to include certain customers of Penske as follows:

> *WHO IS AN INSURED*
>
> It is agreed Section II. A. 1 of Business Auto Coverage Form CA0001 (12–93) is amended to include the following:
>
> C. Both lessees and rentees of covered autos as insureds, but only to the extent and for the limits of liability agreed to under contractual agreement with the named insured.
>
> This endorsement authorized Penske to add any rental customer as an insured under the Old Republic policy for the liability limits negotiated in a particular rental agreement.

Emilio Urrutia leased a truck from Penske in Houston. As part of the transaction, Penske agreed to provide liability protection to Urrutia. The rental agreement limited this insurance to the minimum coverage required by our state financial responsibility law.[FN1] The rental ***442** agreement accordingly provided Urrutia with liability coverage of $20,000 for bodily injury to a single third party. *See* TEX. TRANSP. CODEE § 601.072 (prescribing minimum liability protection of $20,000/$40,000/$15,000).

FN1. Paragraph 6 of the Rental Agreement provided in pertinent part:

> *6.LIABILITY PROTECTION (L.P.).* The party (either: Lessor or Customer) as indicated by the initials or signature of the person signing this Agreement on the reverse side shall, at its sole cost, provide liability protection for Customer and any operator authorized by Lessor, and no others, and for Lessor and its partners and

> their respective agents, servants and employees, in accordance with the standard provision of a Basic Automobile Liability Insurance Policy as required in the jurisdiction in which Vehicle is operated, against liability for bodily injury. including death and property damage arising out of the ownership, maintenance, use and operation of Vehicle as permitted by this Agreement, with limits as follows:
>
> (A) *IF "LESSOR PROVIDES L.P." IS INITIALED * * * LESSOR SHALL PROVIDE:*
>
> *IF A TRUCK,* primary coverage of $10,000 each person, $20,000 each accident for bodily injury, including death and $5000 each accident for property damage or with limits of liability up to the requirements of the Financial Responsibility Law or other applicable statute of the state or municipality in which the accident occurred whichever is greater.
>
> * * *

While operating the Penske truck, Urrutia collided with a car driven by Ferol Decker. Mr. Decker sustained serious injuries and incurred substantial medical expenses. He nevertheless agreed to settle his personal injury claims against Urrutia and Penske for $20,000 because he understood from an insurance adjuster calling on behalf of Urrutia that this was all the insurance available. As part of the settlement, Decker released both Urrutia and Penske. Later, Decker learned about Penske's million-dollar liability policy and filed this suit, seeking to reopen his personal injury claim.

Urrutia and Penske asserted the settlement agreement in defense and moved for summary judgment against Decker. Decker responded that the settlement was invalid because it was obtained by fraud or mutual mistake. The trial court disagreed and granted summary judgment.

The court of appeals reversed and remanded, concluding that the parties made a mutual mistake of fact by reading the rental agreement to limit Urrutia's liability coverage to $20,000. The court of appeals held that the rental agreement could not effectively limit coverage because the insurance provisions in that agreement were void under article 5.06(2) of the Texas Insurance Code. 965 S.W.2d at 29.

Article 5.06(2) provides that a "contract or agreement not written into the application and policy is void and of no effect." TEX. INS.CODE art. 5.06(2). Applying this statute, the court of appeals concluded that the rental agreement between Penske and Urrutia was void as insurance because the agreement was not "written into" the Old Republic policy. The court did not find a similar problem with the Pennsylvania endorsement, however, which allowed Penske to extend its insurance to Urrutia. The court of appeals did not explain why the Pennsylvania endorsement was valid to amend the policy while the Texas rental contract was not.

[1][2] Penske suggests that the court of appeals must have reasoned that the Texas rental agreement was not a part of the Old Republic policy because it was not attached to the policy like the Pennsylvania endorsement. But the rental agreement did not have to be attached to the Old Republic policy to be effective. In *Fidelity Union Life Ins. Co. v. Methven,* 162 Tex. 323,

346 S.W.2d 797, 800 (1961), we concluded that all endorsements "should be attached to insurance policies, but failure to attach them does not invalidate them." Texas law has long provided that a separate contract can be incorporated into an insurance policy by an explicit reference clearly indicating the parties' intention to include that contract as part of their agreement. *Goddard v. East Tex. Fire Ins. Co.,* 67 Tex. 69, 1 S.W. 906, 907 (1886).

Moreover, although the court of appeals held that the rental agreement was void for insurance purposes, it nevertheless relied on the agreement to identify Urrutia as an insured. The court did not explain why the rental contract was void for the purpose of defining Urrutia's coverage but valid for the purpose of making Urrutia an insured in the first place. We find no ***443** justification for this selective application of the rental contract.

[3][4][5] Urrutia's coverage under the Old Republic policy depended on both the Texas rental contract and the Pennsylvania endorsement. The Pennsylvania endorsement enlarged the policy's definition of "insured," authorizing the named insured, Penske, to add its rental customers as additional insureds. The endorsement, however, allowed Penske to determine in the rental contracts themselves which customers would be insured and the amount of their respective coverage. An insurer may validly agree to add as an additional insured "any person or organization to which the named insured is obligated by virtue of a written contract to provide insurance." 21 DORSANEO, TEXAS LITIGATION GUIDE § 341.07[2][h] at 341–57 (July 1998), *citing Forest Oil Corp. v. Strata Energy, Inc.,* 929 F.2d 1039, 1044–45 (5th Cir.1991). Such an endorsement also "may provide lower coverage limits to the additional insured than to the named insured," as the rental contract did here. *See id.,* DORSANEO at 341–57–58. The Texas rental contract was thus also an endorsement to the Old Republic policy, supplying the limits of coverage and extending those benefits to the customer identified therein as accepting Penske's offer of insurance.

Furthermore, the Pennsylvania endorsement clearly referred to the rental agreements between Penske and its rental customers as the basis for extending and limiting insurance coverage to these customers. Accordingly, Penske's rental agreement with Urrutia was sufficiently "written into" the Old Republic policy through the Pennsylvania endorsement. The insurance provisions in the rental agreement were therefore not void by reason of inadequate incorporation into the policy.

The court of appeals also held that the Texas rental contract was void as an endorsement to the Old Republic policy because it was not in a form approved by our State Board of Insurance. While we agree that the rental agreement did not have board approval for use as an insurance contract, we do not agree that this rendered the insurance provisions of the rental agreement void.

[6] Insurers doing business in this state are required to use policies and endorsements approved by our State Board of Insurance. TEX. INS.CODE art. 5.06(2). Insurers who do not use board-approved policies and endorsements may be subject to penalty. TEX. INS.CODE art. 5.06(2); *Springfield v. Aetna Cas. & Sur. Ins. Co.,* 620 S.W.2d 557, 558 (Tex.1981). Furthermore, these insurers may not be able to enforce agreements written on unapproved forms. This Court has said that an unapproved endorsement or clause that conflicts with an

approved provision in a standard form policy is unenforceable. *Commercial Union Assurance Co. v. Preston,* 115 Tex. 351, 282 S.W. 563, 565 (1926).

[7] But this case is different from *Commercial Union.* Here the insurance provisions in the Texas rental contract, while lacking board-approval, do not conflict with any approved standard form policy or provision. In fact, the unapproved Texas rental endorsement to the Old Republic policy is the only basis for extending insurance benefits to Urrutia. To void the insurance provisions in the Texas rental agreement under these circumstances would penalize the innocent insured, not provide him more protection. *See Travelers Ins. Co. v. Chicago Bridge & Iron Co.,* 442 S.W.2d 888, 893 (Tex.Civ.App.—Houston [1st Dist.] 1969, writ ref'd n.r.e.) (insured is not deprived of coverage merely because the insurer did not use the approved policy form). Because insurance sold through an unapproved policy is voidable, the insured may, upon learning that the insurance is unapproved, elect to rescind it. If the insured elects to accept the insurance, however, he or she must do so under the agreed terms. *See Imperial Premium Fin., Inc. v. Khoury,* 129 F.3d ***444** 347, 350 (5th Cir.1997)(insured cannot select the good and discard the bad); *Hertz Corp. v. Pap,* 923 F.Supp. 914, 922 (N.D.Tex.1995)(insured cannot chose to void unfavorable language and retain remainder of unapproved policy), *aff'd,* 98 F.3d 1339 (5th Cir.1996); *McLaren v. Imperial Cas. & Indem. Co.,* 767 F.Supp. 1364, 1376 (N.D.Tex.1991)(insured must take or leave the policy in its entirety), *aff'd* 968 F.2d 17 (5th Cir.1992), *cert. denied,* 507 U.S. 915, 113 S.Ct. 1269, 122 L.Ed.2d 665 (1993); *cf. Mutual Life Ins. Co. of N.Y. v. Daddy$ Money, Inc.,* 646 S.W.2d 255, 257 (Tex.App.—Dallas 1982, writ ref'd n.r.e.)(when policy has board approval but conflicting endorsement does not, insurer cannot enforce endorsement).

[8] In this case, Urrutia has accepted the insurance benefits extended to him through the Texas rental agreement. Accordingly, the court of appeals erred in voiding the insurance provisions in the rental agreement merely because they were not written on forms prescribed by the State Board of Insurance.[FN2]

> FN2. Since the accident in this case, the Legislature has enacted new legislation, clarifying the application of insurance laws to car rental companies. *See* TEX. INS.CODE art. 21.07 § 21(Rental Car Companies); *see* also Tex. S.B. 522, 76th Leg., R.S. (1999)(proposing to amend section 21 to include trailers and trucks). The Commissioner of Insurance has, in turn, adopted new policy forms and rules to implement the new statute. *See* Commissioner of Insurance Order No. 98–0513, 23 Tex. Reg. 4927 (May 15, 1998)("Adoption of a Texas Automobile Rental Liability Policy and a Texas Automobile Rental Liability Excess Policy and Amendments to the Texas Automobile Rules and Rating Manual to Provide Rules and Rates Governing Such Policies").

In summary, the liability insurance Penske sold Urrutia was voidable because it did not have board approval. It was not void, however. Furthermore, the Texas rental agreement was sufficiently incorporated into the Old Republic policy to satisfy the requirements of article 5.06(2). Finally, the rental agreement clearly limited the liability protection extended to Urrutia to $20,000 for bodily injury. Accordingly, we reverse the judgment of the court of appeals and render judgment that Decker take nothing.

Tex.,1999.
Urrutia v. Decker
992 S.W.2d 440, 42 Tex. Sup. Ct. J. 521

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729 F.Supp.2d 814
(Cite as: 729 F.Supp.2d 814)

United States District Court,
N.D. Texas,
Dallas Division.
VOUGHT AIRCRAFT INDUSTRIES, INC., Plaintiff,
v.
FALVEY CARGO UNDERWRITING, LTD., et al., Defendants.

Civil Action No. 3:08–CV–0727–D.
June 25, 2010.

Background: Shipper brought action against insurer, agent, and underwriters to recover under marine cargo insurance policy for costs it incurred in repairing horizontal stabilizer damaged while being shipped on rail. Parties filed cross-motions for summary judgment.

Holdings: The District Court, Sidney A. Fitzwater, Chief Judge, held that:
(1) policy did not afford coverage for replacing resources on insured's main production line or building or shipping additional items;
(2) policy did not cover costs insured incurred in manufacturing and shipping subsequent items on expedited basis;
(3) policy was ambiguous as to whether it covered cost of shipping newly-constructed replacement;
(4) policy was ambiguous as to whether it covered insured's overhead costs;
(5) insurer did not breach its common law duty of good faith and fair dealing;
(6) insurer did not engage in unfair or deceptive insurance practice;
(7) insurer was not liable in quantum meruit;
(8) insurer was not unjustly enriched; and
(9) fact issues remained as to whether managing agent for lead underwriter disclosed identity of its principal.

Motions granted in part and denied in part.

West Headnotes

[1] Insurance 217 ⚿1806

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1806 k. Application of rules of contract construction. Most Cited Cases

Texas courts interpret insurance policies according to rules of contract interpretation.

[2] Contracts 95 ⚿143(2)

95 Contracts

95II Construction and Operation
95II(A) General Rules of Construction
95k143 Application to Contracts in General
95k143(2) k. Existence of ambiguity. Most Cited Cases

Contracts 95 ⚿176(2)

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k176 Questions for Jury
95k176(2) k. Ambiguity in general. Most Cited Cases

Under Texas law, when contract is worded so that it can be given definite meaning, it is unambiguous and judge must construe it as matter of law.

[3] Insurance 217 ⚿1810

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1810 k. Construction as a whole. Most Cited Cases

Under Texas law, when interpreting insurance policy, court must give effect to all of policy's provisions so that none is rendered meaningless.

[4] Insurance 217 ⚿1808

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1808 k. Ambiguity in general. Most Cited Cases

Insurance 217 ⚿1810

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1810 k. Construction as a whole. Most Cited Cases

Insurance 217 ⚿1863

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1863 k. Questions of law or fact. Most Cited Cases

Under Texas law, whether insurance contract is ambiguous is question of law for court to

decide by looking at contract as a whole in light of circumstances present when contract was entered.

[5] Insurance 217 ⚿1809

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1809 k. Construction or enforcement as written. Most Cited Cases

Insurance 217 ⚿1836

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1836 k. Favoring coverage or indemnity; disfavoring forfeiture. Most Cited Cases

Under Texas law, if insurance contract uses unambiguous language, court must enforce it as written; if, however, contract is susceptible to more than one reasonable interpretation, court will resolve any ambiguity in favor of coverage.

[6] Insurance 217 ⚿1833

217 Insurance
217XIII Contracts and Policies
217XIII(G) Rules of Construction
217k1830 Favoring Insureds or Beneficiaries; Disfavoring Insurers
217k1833 k. Status or bargaining power of insureds. Most Cited Cases

Under Texas law, as predicted by district court, exception to general rule in favor of coverage may be made when corporate insureds with bargaining power equal to insurer participate in drafting insurance coverage, insured contributes to drafting of agreement rather than adopting contract of adhesion, contents of policy are in some way negotiable, and insured is as capable as insurer of interpreting contract.

[7] Insurance 217 ⚿2185

217 Insurance
217XVI Coverage—Property Insurance
217XVI(A) In General
217k2184 Repair or Replacement
217k2185 k. In general. Most Cited Cases

Under Texas law, provision of marine cargo insurance policy covering costs of “replacing or repairing the lost or damaged part so that the machine or article is restored to its condition at the time of shipment” did not afford coverage for replacing resources on insured manufacturer's main production line or building or shipping additional items, even if it was

necessary for manufacturer to replace resources committed to repair in order to maintain normal production schedule, where damaged item would have been repaired even had other items not been completed, and expediting expenses were incurred to meet separate, preexisting obligations.

[8] Insurance 217 ⚿2185

217 Insurance
217XVI Coverage—Property Insurance
217XVI(A) In General
217k2184 Repair or Replacement
217k2185 k. In general. Most Cited Cases

Under Texas law, provisions of marine cargo insurance policy covering "expediting costs involved [with the forwarding of a replacement and/or replacement parts]" and "any overtime repair costs and/or other additional expenses including duties, taxes and destination charges" did not cover costs insured manufacturer incurred in manufacturing and shipping on expedited basis five subsequent horizontal stabilizers after it commenced repairs on stabilizer damaged during transport, where only one stabilizer was damaged, and subsequent stabilizers met separate contractual demands.

[9] Insurance 217 ⚿2185

217 Insurance
217XVI Coverage—Property Insurance
217XVI(A) In General
217k2184 Repair or Replacement
217k2185 k. In general. Most Cited Cases

Under Texas law, provisions of marine cargo insurance policy covering "expediting costs involved [with the forwarding of a replacement and/or replacement parts]" and "any overtime repair costs and/or other additional expenses including duties, taxes and destination charges" did not cover cost of labor required to complete construction of initial replacement item, but rather included only costs associated with replacement's shipment.

[10] Federal Civil Procedure 170A ⚿2501

170A Federal Civil Procedure
170AXVII Judgment
170AXVII(C) Summary Judgment
170AXVII(C)2 Particular Cases
170Ak2501 k. Insurance cases. Most Cited Cases

Under Texas law, provisions of marine cargo insurance policy covering "expediting costs involved [with the forwarding of a replacement and/or replacement parts]" and "any overtime repair costs and/or other additional expenses including duties, taxes and destination charges" was ambiguous as to whether it covered component manufacturer's cost of shipping newly-

constructed replacement horizontal stabilizer to aircraft manufacturer after its original stabilizer was damaged during transport, and thus summary judgment was not warranted on component manufacturer's claim against insurer for expenses incurred in shipping replacement stabilizer, where component manufacturer chose to repair damaged stabilizer, and made claim and was paid for costs associated with repair.

[11] Insurance 217 ⚿2185

217 Insurance
217XVI Coverage—Property Insurance
217XVI(A) In General
217k2184 Repair or Replacement
217k2185 k. In general. Most Cited Cases

Under Texas law, where insurance policy provides cash value for repair, whether cash value includes contractor's overhead and profit depends on whether repair is so complex that hiring contractor is likely.

[12] Federal Civil Procedure 170A ⚿2501

170A Federal Civil Procedure
170AXVII Judgment
170AXVII(C) Summary Judgment
170AXVII(C)2 Particular Cases
170Ak2501 k. Insurance cases. Most Cited Cases

Under Texas law, provision of marine cargo insurance policy requiring insurer to pay cost and expense of repairing damaged part and “all other necessary charges” to restore item to its condition at time of shipment was ambiguous as to whether it covered overhead costs incurred by insured manufacturer in repairing item damaged during transport or was limited to direct labor and material costs, and thus summary judgment was not warranted on issue in insured's action to recover under policy.

[13] Insurance 217 ⚿3335

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3334 In General
217k3335 k. In general. Most Cited Cases

Insurance 217 ⚿3336

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3334 In General

217k3336 k. Reasonableness of insurer's conduct in general. Most Cited Cases

Under Texas law, common law duty of good faith and fair dealing is breached when insurer denies or delays payment of claim after its liability has become reasonably clear.

[14] Insurance 217 ⚿3336

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3334 In General
217k3336 k. Reasonableness of insurer's conduct in general. Most Cited Cases

Under Texas law, in reviewing bad faith claim against insurer, objective standard is employed to determine whether reasonable insurer under similar circumstances would have delayed or denied claimant's benefits.

[15] Insurance 217 ⚿3335

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3334 In General
217k3335 k. In general. Most Cited Cases

Under Texas law, insurer does not breach its duty of good faith and fair dealing by denying questionable claim.

[16] Insurance 217 ⚿3336

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3334 In General
217k3336 k. Reasonableness of insurer's conduct in general. Most Cited Cases

Under Texas law, as long as insurer has reasonable basis to deny or delay payment of claim, even if that basis is eventually determined by fact-finder to be erroneous, insurer is not liable for tort of bad faith.

[17] Insurance 217 ⚿3361

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3358 Settlement by First-Party Insurer
217k3361 k. Investigations and inspections. Most Cited Cases

Under Texas law, insurer cannot insulate itself from bad faith liability by investigating claim in manner calculated to construct pretextual basis for denial.

[18] Insurance 217 ⚿3361

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3358 Settlement by First-Party Insurer
217k3361 k. Investigations and inspections. Most Cited Cases

Under Texas law, insurer cannot escape liability for breach of its duty of good faith and fair dealing by failing to investigate claim so that it can contend that liability was never reasonably clear.

[19] Insurance 217 ⚿3360

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3358 Settlement by First-Party Insurer
217k3360 k. Duty to settle or pay. Most Cited Cases

Under Texas law, insurer did not breach its common law duty of good faith and fair dealing by instructing accounting firm that it retained to analyze claim to exclude overhead costs from its calculation of amounts payable under marine cargo insurance policy, even though insured disputed whether it was entitled to recover its overhead costs, where insurer did not dispute coverage or contend that insured's expenses were excessive, but reasonably concluded that insured's recovery under policy did not include overhead expenses related to repair of damaged item.

[20] Insurance 217 ⚿3417

217 Insurance
217XXVIII Miscellaneous Duties and Liabilities
217k3416 Of Insurers
217k3417 k. In general. Most Cited Cases

Under Texas law, insurer's defense to insured's claim for breach of common law duty of good faith and fair dealing also serves to defeat insured's other extracontractual causes of action only if each cause was nothing more than recharacterization of bad faith claim. V.T.C.A., Insurance Code §§ 541.051 et seq., 541.151.

[21] Insurance 217 ⚿3362

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith

217k3358 Settlement by First-Party Insurer
217k3362 k. Fraud or misrepresentation. Most Cited Cases

Insurance 217 ⚿3363

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3358 Settlement by First-Party Insurer
217k3363 k. Communications and explanations. Most Cited Cases

Under Texas law, insurer's successful defense to insured's claim that it violated its common law duty of good faith and fair dealing did not bar insured's claims that insurer engaged in unfair insurance practices, where common law breach claim was based on insurer's instructions to accounting firm that calculated damages payable under marine cargo insurance policy, but statutory claims were based on its alleged misrepresentation of benefits under policy, its misrepresentation of policy provisions during settlement, its failure to promptly explain its denial of claim, its attempt to obtain full and final release when only partial payment had been made, its failure to affirm or deny coverage within reasonable time, its misrepresentation of quality of its services, and its failure to disclose material information at sale of policy. V.T.C.A., Insurance Code §§ 541.051 et seq., 541.151.

[22] Insurance 217 ⚿3363

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(C) Settlement Duties; Bad Faith
217k3358 Settlement by First-Party Insurer
217k3363 k. Communications and explanations. Most Cited Cases

Under Texas law, statement by insurer's adjuster that he would “await the results of the repairs and the ensuing repair cost calculations in order to proceed with the claim settlement” after insured cargo was damaged during transport could not have reasonably been interpreted by insured as implying that insurer would reimburse it for its overhead in making repairs, and thus did not amount to unfair or deceptive insurance practice. V.T.C.A., Insurance Code § 541.061.

[23] Contracts 95 ⚿16

95 Contracts
95I Requisites and Validity
95I(B) Parties, Proposals, and Acceptance
95k16 k. Offer and acceptance in general. Most Cited Cases

Under Texas law, valid and enforceable contract requires offer by one party and acceptance by other party, in strict compliance with terms of offer.

[24] Insurance 217 ⚿1735

217 Insurance
217XIII Contracts and Policies
217XIII(B) Formation
217k1731 Offer and Acceptance; Applications
217k1735 k. What constitutes acceptance. Most Cited Cases

Insurance 217 ⚿3383

217 Insurance
217XXVII Claims and Settlement Practices
217XXVII(D) Requisites and Validity of Settlement or Release
217k3383 k. In general. Most Cited Cases

Under Texas law, statement by insurer's adjuster that he would "await the results of the repairs and the ensuing repair cost calculations in order to proceed with the claim settlement" after insured cargo was damaged during transport did not amount to acceptance of new contract between insurer and insured requiring insurer to pay insured's overhead in connection with repair of damaged item, rather than direct labor and material costs allegedly called for by policy.

[25] Estoppel 156 ⚿85

156 Estoppel
156III Equitable Estoppel
156III(B) Grounds of Estoppel
156k82 Representations
156k85 k. Future events; promissory estoppel. Most Cited Cases

Under Texas law, statement by insurer's adjuster that he would "await the results of the repairs and the ensuing repair cost calculations in order to proceed with the claim settlement" after insured cargo was damaged during transport did not amount to promise by insurer to pay insured's overhead in connection with repair of damaged item, rather than direct labor and material costs allegedly called for by policy, and thus could not form basis for insured's promissory estoppel claim.

[26] Implied and Constructive Contracts 205H ⚿30

205H Implied and Constructive Contracts
205HI Nature and Grounds of Obligation
205HI(C) Services Rendered
205Hk30 k. Work and labor in general; quantum meruit. Most Cited Cases

Implied and Constructive Contracts 205H ⚿34

205H Implied and Constructive Contracts
205HI Nature and Grounds of Obligation

205HI(C) Services Rendered
205Hk33 Rendition and Acceptance of Services in General
205Hk34 k. Implication of request or promise to pay. Most Cited Cases

Under Texas law, to prevail on quantum meruit claim, plaintiff must prove that: (1) valuable services were rendered; (2) to party sought to be charged; (3) which services were accepted by party sought to be charged; (4) under such circumstances as reasonably notified recipient that plaintiff, in performing such services, expected to be paid by recipient.

[27] Implied and Constructive Contracts 205H 55

205H Implied and Constructive Contracts
205HI Nature and Grounds of Obligation
205HI(D) Effect of Express Contract
205Hk55 k. In general. Most Cited Cases

Under Texas law, insurer was not liable in quantum meruit for expediting or overhead costs incurred by insured in repairing insured item that was damaged during transit, where parties' relationship was based on written policy, and insured did not notify insurer that it expected to be paid overhead or expediting costs.

[28] Implied and Constructive Contracts 205H 3

205H Implied and Constructive Contracts
205HI Nature and Grounds of Obligation
205HI(A) In General
205Hk2 Constructive or Quasi Contracts
205Hk3 k. Unjust enrichment. Most Cited Cases

Under Texas law, party may recover under unjust enrichment theory when one person has obtained benefit from another by fraud, duress, or taking of undue advantage.

[29] Implied and Constructive Contracts 205H 3

205H Implied and Constructive Contracts
205HI Nature and Grounds of Obligation
205HI(A) In General
205Hk2 Constructive or Quasi Contracts
205Hk3 k. Unjust enrichment. Most Cited Cases

Under Texas law, insurer did not induce insured component manufacturer to repair, rather than replace, specialized item, and thus was not unjustly enriched by decision, even though decision to repair greatly reduced insurer's liability, where item was highly specialized and only insured could have made repair, and insured did not inform insurer of its intent to repair item until after it had conferred with its clients.

[30] Contracts 95 175(1)

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k175 Evidence to Aid Construction
95k175(1) k. Presumptions and burden of proof. Most Cited Cases

Under Texas law, party forming contract is presumed to be party to that contract.

[31] Principal and Agent 308 ⚿138

308 Principal and Agent
308III Rights and Liabilities as to Third Persons
308III(B) Undisclosed Agency
308k138 k. Duty to disclose agency. Most Cited Cases

Under Texas law, to avoid liability, agent must disclose both that it is acting in representative capacity and identity of its principal.

[32] Federal Civil Procedure 170A ⚿2501

170A Federal Civil Procedure
170AXVII Judgment
170AXVII(C) Summary Judgment
170AXVII(C)2 Particular Cases
170Ak2501 k. Insurance cases. Most Cited Cases

Genuine issue of material fact as to whether managing agent for syndicate that served as lead underwriter for marine cargo insurance policy disclosed identity of its principal precluded summary judgment in agent's favor in insured's action to recover under policy.

[33] Contracts 95 ⚿338(1)

95 Contracts
95VI Actions for Breach
95k331 Pleading
95k338 Plea, Answer, or Affidavit of Defense in General
95k338(1) k. In general. Most Cited Cases

Under Texas law, ambiguity is affirmative defense that must be pleaded in breach of contract action.

[34] Contracts 95 ⚿143(2)

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k143 Application to Contracts in General
95k143(2) k. Existence of ambiguity. Most Cited Cases

Contracts 95 ⚿176(2)

95 Contracts
95II Construction and Operation
95II(A) General Rules of Construction
95k176 Questions for Jury
95k176(2) k. Ambiguity in general. Most Cited Cases

Under Texas law, interpretation of contract is matter of law, and court can conclude that contract is ambiguous even when no party pleads ambiguity.

[35] Federal Civil Procedure 170A ⚿751

170A Federal Civil Procedure
170AVII Pleadings
170AVII(C) Answer
170AVII(C)2 Affirmative Defense or Avoidance
170Ak751 k. In general. Most Cited Cases

Insurer's failure to specifically plead that marine cargo insurance policy was ambiguous as to expenses for which insured could seek reimbursement if it decided to repair, rather than replace, damaged item did not preclude introduction of parol evidence to interpret policy in insured's action to recover under policy, where court ruled that policy was ambiguous as matter of law. Fed.Rules Civ.Proc.Rule 8(c), 28 U.S.C.A.

[36] Evidence 157 ⚿448

157 Evidence
157XI Parol or Extrinsic Evidence Affecting Writings
157XI(D) Construction or Application of Language of Written Instrument
157k448 k. Grounds for admission of extrinsic evidence. Most Cited Cases

Under Texas law parol evidence is admissible after concluding that contract is ambiguous, but such evidence cannot be admitted to determine whether contract is ambiguous.

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MEMORANDUM OPINION AND ORDER

SIDNEY A. FITZWATER, Chief Judge.

The parties' cross-motions for summary judgment present questions concerning the interpretation of a marine cargo insurance policy, the insurer's liability for its handling of the insured's claim, and the validity of related common law claims. The court must also address questions concerning the admissibility of certain summary judgment evidence and the

availability of an affirmative defense of ambiguity.

I

A

This is an action by plaintiff Vought Aircraft Industries, Inc. ("Vought") against Falvey Cargo Underwriting, Ltd. ("Falvey"); XL London Market, Limited, acting on its own behalf, and on behalf of the underwriting members of Lloyd's Syndicate 1209, and all other Lloyd's Syndicates participating on the policy ("XL"); and Dornoch Limited, for and on behalf of the underwriting members of Lloyd's Syndicate 1209 and all other Lloyd's Syndicates participating on marine cargo policy No. M–20108, WC–20108 ("Dornoch").[FN1] Vought sues to recover for breach of a Marine Cargo Policy No. M–20108, WC–20108 (the "Policy") and on other claims arising from its repair of a horizontal stabilizer[FN2] that was damaged while being shipped by rail to Vought's customer, The Boeing Company ("Boeing"). Vought manufactured the horizontal stabilizer for installation on a C–17 Globemaster III aircraft being built by Boeing for the United States Air Force ("Air Force"). It is undisputed that the damage to a horizontal stabilizer in shipment is a covered peril under the Policy.

FN1. Vought originally sued Lloyd's of London, but it voluntarily dismissed this defendant by Fed. R. Civ. 41(a)(1)(A)(i) notice of dismissal on June 2, 2008.

FN2. The stabilizer is a horizontal wing atop the tail fin that helps the plane maintain level flight.

Vought is the named insured in the Policy. According to Vought,[FN3] Falvey is the ***820** insurer, and it placed the risk with certain Underwriters in the Lloyd's, London insurance market; Dornoch is the lead underwriter; and XL is liable for Vought's claim because it is an insurer on the Policy and serves as managing agent for all underwriters of Syndicate 1209, including Dornoch.

FN3. Both sides have moved for summary judgment. As the court has stated in cases like *AMX Corp. v. Pilote Films*,

> [b]ecause both parties have filed motions for summary judgment, the court will principally recount only the evidence that is undisputed. If it is necessary to set out evidence that is contested, the court will do so favorably to the party who is the summary judgment nonmovant in the context of that evidence. In this way it will comply with the standard that governs resolution of summary judgment motions.

AMX Corp. v. Pilote Films, 2007 WL 1695120, at *1 n. 2 (N.D.Tex. June 5) (Fitzwater, J.) (citing *U.S. Bank Nat'l Ass'n v. Safeguard Ins. Co.*, 422 F.Supp.2d 698, 701 n. 2 (N.D.Tex.2006) (Fitzwater, J.)), *modified in part on other grounds*, 2007 WL 2254943 (N.D.Tex. Aug. 7, 2007) (Fitzwater, J.).

After the horizontal stabilizer was damaged, Vought conferred with Boeing and the Air Force. The three agreed that Vought should repair the stabilizer due to its highly-specialized design, which made it infeasible for another company to repair it. Vought informed Falvey of the repair plan and that it intended to make a claim for reimbursement of the repair costs.[FN4]

FN4. Although the court assumes that Vought informed Falvey of the repair plan, the court holds below, *see infra* § VIII, that a reasonable jury could not find that Falvey and Vought entered into a binding contract regarding the repair of the stabilizer. Therefore, Vought cannot recover on its independent claim for breach of a contract to repair the stabilizer.

The damaged horizontal stabilizer was returned to Vought's Dallas facility. Because Vought does not maintain a dedicated repair facility, it was placed on the factory floor with other C–17 stabilizers, adjacent to the regular production line. To maintain its normal production schedule, it was necessary for Vought to repair the stabilizer while simultaneously continuing with normal production. Vought was required to deliver horizontal stabilizers to Boeing on a specific schedule. When the damaged stabilizer was returned to Vought, it did not have a completed stabilizer to provide Boeing as a replacement. To fill this gap, Vought expedited production and shipment of the next available stabilizer on the assembly line, which it shipped to Boeing as a replacement for the damaged stabilizer. This, in turn, created another gap in the production schedule, requiring Vought to expedite the production and shipment of successive stabilizers. Six stabilizers were completed on an expedited basis before the damaged stabilizer was repaired and inserted back into the production schedule and the normal delivery schedule was restored.

Vought submitted a claim to Falvey for $1,658,056.00, which consisted of $136,748.00 in direct labor costs, $71,552.00 in fringe benefits, and $15,306.00 in direct materials to repair the damaged stabilizer, totaling $223,606.00. Vought also requested reimbursement for $284,509.00 in overhead expenses incurred in repairing the damaged stabilizer. This sum was composed of $206,920.00 in “Direct Overhead,” which included depreciation of facilities, equipment, and tools; some supervisor salaries; and all other costs that did not result from direct labor charges but that could be assessed to a particular manufacturing process. The balance of this request consisted of $77,589.00 in “General and Administrative Costs” composed of overhead that could not be associated with a particular manufacturing task, such as executive salaries or benefits for retired workers. These costs were spread equally across all of Vought's manufacturing operations as a percentage above actual cost.

The final component of Vought's reimbursement request was for costs incurred by diverting resources to the repair of the damaged stabilizer and expediting production and shipment of the stabilizer that was completed and shipped as a replacement for the damaged stabilizer and the next five that were completed and shipped to cover the production gap until the original damaged stabilizer was reinserted into ***821** the production line and normal production and delivery resumed. This claim consisted of $663,854.00 in expedited repair costs, $313,730.00 of direct overhead associated with these expediting costs, and $172,357.00 of general and administrative costs associated with these expediting costs.

After Falvey received Vought's claim, it engaged the accounting firm of Matson, Driscoll & Damico, LLP (“Matson”) to evaluate the claim. Falvey instructed Matson not to consider Vought's overhead costs as part of the claim. Matson determined that Falvey was obligated to pay $236,274.00, minus a $100,000.00 deductible, for direct labor repair costs, fringe benefits on such repair costs, and direct material costs that Vought had incurred in repairing the

damaged horizontal stabilizer. Falvey later tendered this amount and also reimbursed Vought $11,205.00 for the cost of shipping the repaired stabilizer back to Boeing. Falvey refused Vought's demand for the full amount of its claim.

B

The Policy "cover[s] all shipments of goods and/or merchandise and/or property," Ds. Oct. 10, 2009 App. 5, including by rail, *id.* at 6. Vought's aircraft parts are insured "[a]gainst all risks of physical loss or damage from any external cause, except those risks as may be excluded by [two specific warranties] or other warranties or exclusions specified in this policy, unless covered elsewhere [in the Policy] [.]" *Id.* at 10. The Policy provides in § 16.2.5 that "the insurer is to pay for ... any physical loss or damage to ... goods ... during land transportation, from ... collision." *Id.* at 11. It covers the transportation of goods from the time they leave Vought's facility until they are delivered to Boeing and unloaded. *See id.* at 11 and 13.

Vought relies primarily on two clauses in the Policy to establish its right to reimbursement for its entire claim: § 24, the Policy's "Machinery" clause ("Machinery Clause"), and § 38, captioned "Expediting Cost" ("Expediting Cost Clause"). Where the covered item is a machine or an article consisting of multiple parts, the Machinery Clause limits Vought's liability under § 16.2 to the damaged parts:

> When the goods and/or merchandise and/or property insured under this policy include a machine or other article consisting, when complete for sale or use, of several parts, then in case of loss or damage covered by this insurance to any part of such machine or other article, This Insurer shall be liable only for the proportion of the insured value applicable to the part or parts lost or damaged, or at The Insured's option, for the cost and expense of replacing or repairing, assembling or duplicating the lost or damaged part or parts (including any and all expediting, labor and installation charges) and all other necessary charges so that the machine or article is restored to its condition at the time of shipment.

Id. at 15.[FN5] The Expediting Cost Clause states:

> FN5. Vought characterizes the stabilizer both as an article consisting, when complete for sale, of separate parts and as a "damaged part" that can itself be declared a total loss, thus allowing Vought to recover the full value of the stabilizer. *See* P. Oct. 9, 2009 Br. 7. By characterizing the damaged stabilizer as one part, Vought essentially treats the Machinery Clause as a coverage provision rather than as a limitation on the coverage provided by § 16.2. This approach affects its interpretation of the Expediting Clause. *See infra* § IV(C)(3)(c).

> Where there is loss [or] damage ... which [is], or will be, the subject of a claim under this policy, and The Insured considers it necessary to forward replacements and/or replacement parts ***822** by means other than the means by which the original shipment was dispatched, The Insurer will pay the expediting costs so involved and any overtime repair costs and/or other additional expenses including duties, taxes and destination charges, in addition to the underlying claim.

Id. at 20. Additionally, § 54, captioned "Constructive Total Loss," provides:

> No recovery for a constructive total loss shall be had under this policy unless (i) the insured goods ... are reasonably abandoned on account of their actual total loss appearing to be unavoidable, or (ii) because they cannot be preserved from actual total loss without incurring an expenditure which, if incurred, The Insured reasonably believes would exceed the expected value of the goods[.]

Id. at 26. And § 45 states that the Policy "shall not cover loss [ ] of market or loss, damage, or expense arising from delay, ... unless such risks are expressly assumed elsewhere in this policy." *Id.* at 22.

C

Vought filed this lawsuit in state court, and defendants removed it based on diversity of citizenship. Vought alleges claims for breach of contract (breach of the Policy), breach of the duty of good faith and fair dealing, unfair insurance practices under Chapter 541 of the Texas Insurance Code, breach of contract (breach of the repair agreement), promissory estoppel, quantum meruit, and unjust enrichment. Besides its noncontractual claims, Vought seeks to recover the sum of $1,410,577.00 for the balance of its claim under the Policy that defendants have not already covered.

Vought moves for partial summary judgment on its breach of contract claim, contending that it is entitled to judgment for the unpaid balance of its claim. Falvey, XL, and Dornoch move for summary judgment on all of Vought's claims. XL moves in the alternative for summary judgment on the ground that it cannot be held liable because it was acting as an agent for Dornoch, a disclosed principal.

II

The parties' summary judgment burdens depend on whether they will have the burden of proof at trial on the particular claim or defense to which the motion is addressed. To be entitled to summary judgment on a claim or defense for which it will have the burden of proof at trial, a party "must establish 'beyond peradventure all of the essential elements of the claim or defense.' " *Bank One, Tex., N.A. v. Prudential Ins. Co. of Am.*, 878 F.Supp. 943, 962 (N.D.Tex.1995) (Fitzwater, J.) (quoting *Fontenot v. Upjohn Co.*, 780 F.2d 1190, 1194 (5th Cir.1986)). This means that the party must demonstrate that there are no genuine and material fact disputes and that it is entitled to summary judgment as a matter of law. *See Martin v. Alamo Cmty. Coll. Dist.*, 353 F.3d 409, 412 (5th Cir.2003). "The court has noted that the 'beyond peradventure' standard is 'heavy.' " *Carolina Cas. Ins. Co. v. Sowell*, 603 F.Supp.2d 914, 923 (N.D.Tex.2009) (Fitzwater, C.J.) (quoting *Cont'l Cas. Co. v. St. Paul Fire & Marine Ins. Co.*, 2007 WL 2403656, at *10 (N.D.Tex. Aug. 23, 2007) (Fitzwater, J.)).

Concerning a claim or defense for which the party will not have the burden of proof at trial, the party can meet its summary judgment obligation by pointing the court to the absence of evidence to support the claim or defense. *See Celotex Corp. v. Catrett*, 477 U.S. 317, 325, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986). Once it does so, the nonmovant must go beyond its pleadings and designate specific facts showing that there is a genuine issue for trial. *See id.* at

324; *Little v. Liquid Air Corp.*, 37 ***823** F.3d 1069, 1075 (5th Cir.1994) (en banc) (per curiam). An issue is genuine if the evidence is such that a reasonable jury could return a verdict in favor of the party with the burden of proof. *See Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986). The failure of the party with the burden of proof to produce evidence as to any essential element renders all other facts immaterial. *See Trugreen Landcare, L.L.C. v. Scott*, 512 F.Supp.2d 613, 623 (N.D.Tex.2007) (Fitzwater, J.). Summary judgment is mandatory if that party fails to meet this burden. *See Little*, 37 F.3d at 1076.

III

The court begins by addressing together Vought's motion for partial summary judgment and the part of defendants' motion for summary judgment that seeks dismissal of Vought's claim for breach of the Policy.[FN6]

FN6. Although defendants did not plead ambiguity, the court can consider whether the Policy is ambiguous. *See infra* § XIII(B).

A

[1][2][3] As a threshold question, the court must address the legal standards that govern its interpretation of the Policy. Texas courts interpret insurance policies according to the rules of contract interpretation. *Int'l Ins. Co. v. RSR Corp.*, 426 F.3d 281, 291 (5th Cir.2005) (citing *Kelley–Coppedge, Inc. v. Highlands Ins. Co.*, 980 S.W.2d 462, 464 (Tex.1998)); *Forbau v. Aetna Life Ins. Co.*, 876 S.W.2d 132, 133 (Tex.1994) ("Interpretation of insurance contracts in Texas is governed by the same rules as the interpretation of other contracts."). When a "contract is worded so that it can be given a definite meaning, it is unambiguous and a judge must construe it as a matter of law." *Int'l Ins.*, 426 F.3d at 291; *see also Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Hudson Energy Co.*, 811 S.W.2d 552, 555 (Tex.1991). "In applying these rules, a court's primary concern is to ascertain the parties' intent as expressed in the language of the policy." *Int'l Ins.*, 426 F.3d at 291; *see also Forbau*, 876 S.W.2d at 133 ("[T]he court's primary concern is to give effect to the written expression of the parties' intent."). The court must give effect to all of a policy's provisions so that none is rendered meaningless. *Int'l Ins.*, 426 F.3d at 291.

[4][5] "Whether an insurance contract is ambiguous is a question of law for the court to decide by looking at the contract as a whole in light of the circumstances present when the contract was entered." *Int'l Ins.*, 426 F.3d at 291 (citing *Kelley–Coppedge*, 980 S.W.2d at 464). "If an insurance contract uses unambiguous language, [the court] must enforce it as written. If, however, a contract is susceptible to more than one reasonable interpretation, [the court] will resolve any ambiguity in favor of coverage." *Don's Bldg. Supply, Inc. v. OneBeacon Ins. Co.*, 267 S.W.3d 20, 23 (Tex.2008) (footnotes omitted); *see also Nat'l Union Fire Ins. Co. v. Hudson Energy Co.*, 811 S.W.2d 552, 555 (Tex.1991).

An exception to the general rule in favor of coverage is often made when corporate insureds with bargaining power equal to the insurer participate in drafting the insurance coverage.

> One of the frequently cited reasons for interpreting language in favor of the insured is that insurance policies are generally contracts of adhesion, which offer little choice to the purchaser. This justification, though, has little application [where], as is often the situation with large, knowledgeable business firms, the contracts were manuscript ***824** policies negotiated and drafted by the insured.

Port Auth. of N.Y. & N.J. v. Affiliated FM Ins. Co., 311 F.3d 226, 235 (3d Cir.2002).[FN7] The exception is justified where the insured contributes to the drafting of the agreement rather than adopting a contract of adhesion,[FN8] the contents of the policy are in some way negotiable, and the insured is as capable as the insurer of interpreting the contract. *See Newport Assocs. Dev. Co. v. Travelers Indem. Co. of Ill.*, 162 F.3d 789, 794 (3d Cir.1998) ("The doctrine of *contra preferentum* is based on the fact that insurance contracts are in most instances 'nonnegotiable' since they tend to be drafted solely by the insurance industry. When a contract is drafted by the insured or jointly negotiated, the doctrine does not apply.") (internal quotation marks and citation omitted).[FN9] The exception also applies where the contract is prepared by a broker acting for the insured. *See Newport*, 162 F.3d at 794–95 (applying exception where "the insurance policy was drafted by an independent broker who was hired by [plaintiff] and acted in consultation with [plaintiff's] employees").[FN10]

FN7. *See also Northbrook Excess & Surplus Ins. Co. v. Procter & Gamble Co.*, 924 F.2d 633, 638 (7th Cir.1991) ("However, it is clear that the rule is grounded in the need to protect an insured from an insurer who has had exclusive control of the drafting process. That concern is not implicated here."); *E. Associated Coal Corp. v. Aetna Cas. & Sur. Co.*, 632 F.2d 1068, 1075 (3d Cir.1980) ("[T]he principle that ambiguities in policies should be strictly construed against the insurer does not control the situation where large corporations, advised by counsel and having equal bargaining power, are the parties to a negotiated policy."); *AIU Ins. Co. v. Superior Court*, 51 Cal.3d 807, 274 Cal.Rptr. 820, 799 P.2d 1253, 1265 (1990) ("[W]here the policyholder does not suffer from lack of legal sophistication or a relative lack of bargaining power, and where it is clear that an insurance policy was actually negotiated and jointly drafted, we need not go so far in protecting the insured from ambiguous or highly technical drafting.") (construing ambiguity in favor of insured because policy was drafted by insurer); *Benjamin Moore & Co. v. Aetna Cas. & Sur. Co.*, 179 N.J. 87, 843 A.2d 1094, 1103 (2004) ("An exception to [the rule] exists for sophisticated commercial entities that do not suffer from the same inadequacies as the ordinary unschooled policyholder and that have participated in the drafting of the insurance contract.").

FN8. Vought also contends that allowing an exception to the traditional rule of interpretation for large corporations would mean an identical policy could be interpreted differently, depending on whether it was purchased by an individual or a corporation. But because the exception is limited to policies drafted at least in part by corporations, this concern is unfounded.

FN9. *See also Six Flags, Inc. v. Westchester Surplus Lines Ins. Co.*, 565 F.3d 948, 958 (5th Cir.2009) (applying Louisiana law) ("[T]he presumption [in favor of coverage]

does not apply where the insured is a sophisticated commercial entity that itself drafts or utilizes its agent to secure desired policy provisions."); *Eagle Leasing Corp. v. Hartford Fire Ins. Co.,* 540 F.2d 1257, 1261 (5th Cir.1976) ("There is no purpose in following a legal platitude that has no realistic application to a contract confected by a large corporation and a large insurance company each advised by competent counsel and informed experts.") (applying Missouri law).

FN10. *See also Travelers Indem. Co. v. United States,* 543 F.2d 71, 74 (9th Cir.1976) ("[T]he rule of strict construction has no applicability when the language is supplied by the insured, his agent or his broker."); *Marine Trans. Corp. v. Nw. Fire & Marine Ins. Co.,* 2 F.Supp. 489, 492 (E.D.N.Y.) ("The contract was prepared by brokers acting for the assured, and consequently is not to be most strongly construed against the company."), *modified on other grounds,* 67 F.2d 544 (2d Cir.1933).

[6] Neither the court nor the parties are aware of a Texas case that addresses the sophisticated insureds exception. But Texas courts have made clear that the traditional rule of construction is based on an insured's unequal bargaining power, the ***825** special relationship between the insured and the insurer, and the general principle that contracts are construed against the drafting party. *See Balandran v. Safeco Ins. Co. of Am.,* 972 S.W.2d 738, 741 n. 1 (Tex.1998).[FN11] Where the sophisticated insureds exception applies, these concerns are not in play. Such insureds draft the policy, or at least play a role in drafting it. They are not presented a policy that contains non-negotiable terms; rather, they can bargain for coverage. And they are able to interpret the policy on their own, lessening the likelihood that the insurer will take advantage of them. Accordingly, considering that Texas applies principles that are congruous with the sophisticated insureds exception, the court holds that Texas courts would apply the exception where the facts warrant.

FN11. Vought argues that Texas courts (and courts from other states) have applied the traditional rule in favor of corporate insureds, and it cites *Pioneer Chlor Alkali Co. v. Royal Indemnity Co.,* 879 S.W.2d 920 (Tex.App.1994, no writ), as an example. But the sophisticated insureds exception is not based on the corporate nature of the insured. It rests instead on the insured's role in drafting the policy. This is because, as the court in *Pioneer Chlor* observed, the traditional rule of construction is based on the insured's lack of participation in the drafting process. "Generally, in the insurance context, the language and terms of the policy are chosen by the insurance company. Therefore, if the language chosen is ambiguous or inconsistent, and susceptible of more than one reasonable interpretation, the court must resolve the uncertainty by adopting the construction that most favors the insured." *Id.* at 929 (citations omitted).

Vought also argues that the sophisticated insureds exception has been rejected more often than it has been accepted. But most of the cases Vought cites concern corporate insureds who did not participate in drafting the policy; these cases merely hold that the exception is not based on the insured's corporate status alone. *E.g., St. Paul Mercury Ins. Co. v. Grand Chapter of Phi Sigma Kappa, Inc.,* 651 F.Supp. 1042, 1045 (E.D.Pa.1987) ("Pennsylvania principles of construction require the Court to resolve an ambiguity of this kind in favor of the insured unless the parties possess equal bargaining power, such as when a large corporation,

advised by counsel, is the insured.”).[FN12] They do not involve instances where the insured participated in drafting the policy.[FN13] *Ogden Corp. v. Travelers Indemnity Co.,* 681 F.Supp. 169, 173–174 (S.D.N.Y.1988), did hold under New York law that a sophisticated insured who drafted a policy through its insurance broker was entitled to the benefit of the general rule because it did not draft the policy in its entirety. But this court has found no other case that cites *Ogden* for this principle. Rather, other New York cases indicate that there is an exception to the general rule when sophisticated insureds participate in policy drafting.

> FN12. Vought also cites *Outboard Marine Corp. v. Liberty Mut. Ins. Co.*, 154 Ill.2d 90, 180 Ill.Dec. 691, 607 N.E.2d 1204, 1218 (1992), and *CPS Chemical Co. v. Continental Insurance Co.*, 222 N.J.Super. 175, 536 A.2d 311, 318 (1988).
>
> FN13. Vought also cites another case involving a corporate insured. In that case, the court did not resolve an ambiguity, but rather determined whether a legal interpretation or the ordinary meaning of a word should be used. *See Boeing Co. v. Aetna Cas. & Sur. Co.*, 113 Wash.2d 869, 784 P.2d 507, 513 (1990). The court held that unless the insurer could prove that the insurer and the insured intended a specific legal meaning of contract terms, the rule that policy terms were given their ordinary meaning would apply. *Id.* The court determined that the mere fact that the insured was a corporation aided by counsel did not mean that it intended the specific legal definitions to apply. *Id.* at 514. The court reasoned that the policy was still a standard form policy drafted by the insurer. *Id.*

***826** The doctrine of *contra proferentem* does not apply as the evidence submitted on the motions shows that while defendant prepared the drafts of the agreement, the basic concept and terms originated with plaintiff, that plaintiff is sophisticated and was instrumental in crafting various parts of the agreement, and that plaintiff, while not an insurance company, had equal bargaining power and acted like an insurance company by maintaining a self-insured retention.
Cummins, Inc. v. Atl. Mut. Ins. Co., 56 A.D.3d 288, 290, 867 N.Y.S.2d 81 (N.Y.App.Div.2008); *see also In re Sept. 11th Liab. Ins. Coverage Cases*, 458 F.Supp.2d 104, 118 (S.D.N.Y.2006) (“[A]pplication of this rule [favoring insureds] is generally inappropriate if both parties are sophisticated.”) (citation and internal quotation marks omitted).

Vought also cites *Eli Lilly & Co. v. Home Insurance Co.*, 794 F.2d 710 (D.C.Cir.1986) (“*Eli Lilly II* ”). *Eli Lilly II* applied the Indiana Supreme Court's answer to certified questions in *Eli Lilly & Co. v. Home Insurance Co.*, 482 N.E.2d 467 (Ind.1985) (“*Eli Lilly I* ”). In *Eli Lilly I* the Indiana Supreme Court held that the traditional rule of interpretation applied in favor of a major pharmaceutical company because, although the company may have been involved in drafting the policies, it was state policy to promote indemnity. *Eli Lilly I*, 482 N.E.2d at 471. But assuming that *Eli Lilly I* supports Vought's position, it is not binding on this court, the case has not been extensively followed outside Indiana, and there is no indication that Texas would follow it.

Accordingly, the court holds that the sophisticated insureds exception can conceivably

apply in this case.

B

The summary judgment evidence does not permit the court to conclude at the summary judgment stage that the traditional rule or the sophisticated insureds exception applies.

Defendants will have the burden at trial of negating the application of the traditional rule by proving that Vought participated in drafting the Policy.[FN14] *See First Nat'l Bank of Fort Walton Beach v. U.S. Fid. & Guar. Co.*, 416 F.2d 52, 56 (5th Cir.1969) ("[I]t is incumbent upon the insurer to bear the burden of showing that the Bank was instrumental in drafting the [insurance] agreement[.]"). But Vought bears the burden of proof as to its claim for breach of the Policy, and must therefore prove the claim beyond peradventure to obtain summary judgment. It cannot, therefore, obtain summary judgment on that claim based on the application of the traditional rule of interpretation if defendants present evidence that the sophisticated insureds exception applies.[FN15] As explained below, defendants have presented evidence creating a genuine question of fact about the application of the traditional rule of interpretation.

> FN14. Defendants must also show that Vought had equal bargaining power. If Vought shopped around the same policy to different brokers, defendants could apparently meet this burden even if Vought and its broker did not negotiate over the specific policy contents.
>
> FN15. Because the sophisticated insureds exception may apply, the court cannot grant summary judgment in favor of either party where it determines that the Policy is ambiguous. *See Recursion Software, Inc. v. Interactive Intelligence, Inc.*, 425 F.Supp.2d 756, 785 (N.D.Tex.2006) (Boyle, J.) ("Summary judgment is generally appropriate only if the language of the contract is wholly unambiguous.").

Defendants point to evidence that the footer contains the name of Vought's broker—Marsh USA, Inc. ("Marsh")—stating "0304 Marsh Form." *E.g.*, Ds. Oct. 10, 2009 ***827** App. 15. In a deposition, Cindy Woodruff ("Woodruff"), a Marsh adviser responsible for the Vought account, testified that the Policy was a manuscript policy form—i.e., a specially designed form rather than an insurer's standard form.[FN16] Concerning the production of the form, she stated: "Marsh will produce it and the carriers review it and either accept it or decline it." Ds. Oct. 10, 2009 App. 200. She indicated that Marsh's role as broker was to choose the proper coverage for its clients. "We [Marsh] actually assess [the clients'] operations, the coverages [they] may need; and then we go out and place the insurance with an insurance carrier." Ds. Oct. 10, 2009 App. 192. Woodruff testified, however, that she was unfamiliar with the particular form in question.

> FN16. *See Eagle Leasing*, 540 F.2d at 1260 ("[the policy is a] 'manuscript' policy, containing some standard printed clauses but confected especially for [the insured].").

Vought argues that it had no part in negotiating any provision of the Policy, it never instructed Marsh to negotiate any language in the Policy, Falvey drafted the Policy on its own form, and a Falvey executive, Robert E. Falvey, Esquire ("Robert"), testified to that effect.

But Robert's testimony does not indicate that Falvey drafted the Policy. Asked who drafted the Policy, Robert responded: "I don't know who drafted that. It is a policy that I—I believe [is] provided to us through the broker and from underwriters." P. Nov. 6, 2009 App. 377. In response to a question about whether Falvey had any role in approving the Policy language, Robert responded: "Yes, they will. For periodic revisions and reviews they will meet and present requests for clarifications or changes, etc., from time to time." *Id.* Vought also stresses that a high-ranking Marsh executive was unfamiliar with the Policy form. But it is not surprising that the executive in question was unaware of the Policy because he appears to have been involved in handling claims rather than placing policies. Finally, Vought argues that the Marsh broker who placed the Policy had seen the form only once and did not know who drafted the language. That broker agreed to the statement that the Policy "would have been issued by Falvey [from its home office]." P. Nov. 6, 2009 App. 429. He stated that he had used the policy once before, also with Falvey, and that he did not know who prepared the form. He then described the Policy as "a Marsh agreed form with Falvey." *Id.* at 430. And he stated that the Machinery Clause was a "standard clause in a broker's form," *id.*, explaining that brokers tended to draft more expansive terms than did insurers.

Based on the record evidence, the court holds that there is a genuine fact issue as to whether Marsh participated in drafting the Policy. Marsh's main representative to Vought indicated that the Policy was drafted by Marsh, which is in keeping with the insurer's role. And the Policy describes itself as a "manuscript policy." D. Nov. 6, 2009 App. 33. But Marsh's cargo insurance specialist stated that he did not know who wrote the Policy, and that he had seen it only once, and in connection with Falvey. If Marsh participated in the drafting of the form, it is likely that the specialist would have known of its origin. The remaining evidence is ambiguous and does not clearly show who drafted the Policy.

Accordingly, at the summary judgment stage, the court cannot say definitively that the traditional rule of interpretation does or does not apply. Although the court cannot determine whether the traditional rule of interpretation applies, it can still determine as a matter of law whether the Policy is ambiguous. If the Policy is ambiguous, then the trier of fact, in resolving the ambiguity as a factual matter, must ***828** first decide the predicate facts that dictate whether the traditional rule of interpretation or the sophisticated insureds exception applies. The trier of fact must then resolve the ambiguity under the controlling standard (i.e., under the traditional rule of interpretation or the sophisticated insureds exception). This conclusion is immaterial, of course, as to the Policy provisions that the court concludes below are unambiguous and can be interpreted as a matter of law.

IV

Having addressed this threshold question, the court considers the parties' motions for summary judgment regarding Vought's claim that defendants breached the Policy by failing to pay for "expediting charges" that Vought incurred.

A

When the damaged stabilizer was returned to Vought's facility, Vought modified the assignment of its workers. Some were tasked with finishing on an expedited basis the next stabilizer in line so that Vought could provide it to Boeing as a replacement for the damaged

stabilizer. Others were pulled from the main production line to repair the damaged stabilizer. Vought brought in other workers to replace reassigned members of the regular production line. By the time Vought finished repairing the damaged stabilizer, it had completed six other stabilizers and shipped them to Boeing. Vought asserts that the Policy covers three categories of expenses that defendants did not reimburse: (1) the cost of resources brought in to replace workers [FN17] pulled from Vought's normal production line, (2) the cost of completing and shipping the first stabilizer, and (3) the cost of completing and shipping the next five stabilizers.[FN18] The direct cost of completing and shipping the six stabilizers, including the cost of diverting workers from the normal production line, totals $663,854.00. Vought seeks an additional $313,730.00 for direct overhead and $172,357.00 for general and administrative costs related to its expedited production of the six stabilizers that preceded the reinsertion of the repaired stabilizer into the production line.

FN17. In its brief, Vought states that defendants should have reimbursed the costs of replacing "resources" they took from the main production line. P. Oct. 9, 2009 Br. 21. But for factual support, it refers to the affidavit of its benefits accounting manager, who discussed personnel costs exclusively. P. Oct. 9, 2009 App. 389.

FN18. Vought's briefing is unclear concerning how many stabilizers were completed and shipped before the damaged one was returned to Boeing. In describing coverage for expediting costs, Vought divides its claim into costs for the initial stabilizer and costs for the "completion and shipment of six other replacement stabilizers," i.e., seven new stabilizers total. P. Oct. 9, 2009 Br. 21 (citing P. Oct. 9, 2009 App. 389–90). But the affidavit Vought cites in support of this analysis describes one initial replacement stabilizer and five subsequently-completed stabilizers, i.e., six stabilizers in all. The affidavit comports with Vought's description of the expedited stabilizers elsewhere in its brief. *See id.* at 7 ("[The] repair required that six horizontal stabilizers be completed ... before the repaired stabilizer was reinserted into the production line[.]").

B

Vought contends that reimbursement for these expenses is covered by the Machinery Clause. The Machinery Clause provides, in relevant part, that, at Vought's election, defendants are liable for the cost and expense of replacing or repairing the damaged stabilizer parts [FN19] "and all other ***829** necessary charges so that the machine or article is restored to its condition at the time of shipment." Ds. Oct. 10, 2009 App. 15. Falvey reimbursed Vought for the direct labor costs and fringe benefits paid to workers who worked directly on the damaged stabilizer. Vought argues that defendants were also obligated to cover the costs of the replacement workers who were added to the normal production line to complete the ensuing six stabilizers. It posits that it was required to reassign its normal workforce to the repair because they, rather than temporary workers, were alone qualified to handle the repair; it was necessary to replace the resources committed to the repair in order to maintain a normal production schedule; it would have been practically impossible to conduct the repair had the main line been so deprived of resources that it could no longer function; and such replacement labor costs were literally necessary to repair the damaged stabilizer. Vought also argues that accelerating completion and shipment of the six replacement stabilizers was necessary for it to repair the damaged stabilizer. According to Vought, "[w]hen a complicated piece of equipment,

consisting of many parts, is damaged and in need of repair, it can create a gap in shipments, and the insureds' customers' supply line is threatened." P. Oct. 9, 2009 Br. 22.

> FN19. In considering defendants' liability under the Machinery Clause for expenses related to the six subsequent stabilizers, it is immaterial whether the clause covers the repair of the stabilizer or the repair of the damaged parts of the stabilizer.

[7] The court disagrees with Vought's contention that the Machinery Clause affords coverage for replacing resources on its main production line (the first category of expediting costs) or building or shipping the six stabilizers (the second and third categories of expediting costs). Under the clause, Vought had the option to recover the cost of replacing or repairing the damaged stabilizer parts. Regardless which option Vought chose, defendants became liable for any "cost [or] expense of replacing or repairing ... the lost or damaged part ... *so that the machine or article is restored* to its condition at the time of shipment." Ds. Oct. 10, 2009 App. 15 (emphasis added). Defendants' liability includes only the expenses necessary to restore a damaged machine or article to its condition at the time of shipment. The Machinery Clause does not provide that defendants would pay all expenses related to or occasioned by a covered loss. The expediting expenses that Vought seeks were not necessary to repair the damaged stabilizer. That stabilizer would have been repaired even had the other stabilizers not been completed. These expediting expenses were incurred to meet separate, preexisting obligations to Boeing.

Interpreting the Machinery Clause,[FN20] the court holds as a matter of law that defendants were only obligated to cover costs and expenses that Vought incurred to restore the damaged horizontal stabilizer to its condition at the time of shipment. The Machinery Clause does not allow for coverage of other expenses that Vought incurred for such reasons as the need to satisfy contractual obligations to customers (including Boeing) or the manner in which it operated its production line.

> FN20. Because the Machinery Clause is unambiguous in this respect, the court will not interpret it in favor of Vought. It is therefore immaterial whether the traditional rule of interpretation or the sophisticated insureds exception would apply in this respect. *See supra* § III(B) (noting this point).

If the Machinery Clause were interpreted as Vought contends, an insured could recover potentially significant costs and expenses that were not necessitated by the repair of the damaged part. If such potentially open-ended costs and expenses were covered, an insurer could not fairly evaluate the risk it was assuming in exchange for the premium paid. Its liability would depend, not on what it could reasonably***830** expect to pay for the replacement or repair of one lost or damaged machine or article, but on a host of ripple effects that the loss or damage caused the insured's business operations and perhaps on the insured's unilateral decisions concerning how to mitigate these effects. Here, defendants accepted the risk of insuring Vought for the cost and expense of replacing or repairing one damaged horizontal stabilizer, not one damaged horizontal stabilizer plus six other horizontal stabilizers that were moving through the production line. Accordingly, Vought cannot rely on the Machinery Clause to recover the expediting costs that it seeks.

C

Vought also relies on the Expediting Cost Clause to recover the costs incurred in completing and shipping the six stabilizers.[FN21] This clause provides that defendants must in certain circumstances pay "expediting costs involved [with the forwarding of a replacement and/or replacement parts]" and "any overtime repair costs and/or other additional expenses including duties, taxes and destination charges." Ds. Oct. 10, 2009 App. 20. This obligation arises only if the expenses concern a loss that is or will be the subject of a policy claim, and Vought "considers it necessary to forward replacements and/or replacement parts by means other than the means by which the original shipment was dispatched." *Id.*

> FN21. In its brief, Vought asserts that the Expediting Clause covers the expedited completion costs as well as the shipping costs. *See* P. Oct. 9, 2009 Br. 23. It apparently does not contend the clause covers the cost of replacing personnel on its regular production line. Regardless, Vought is not entitled to reimbursement for any expenses associated with the manufacturing of the six subsequent stabilizers, including the cost of replacing personnel.

1

Vought argues that this clause covers the shipping and manufacturing both of the initial replacement stabilizer and of the others shipped before the damaged stabilizer was repaired and reinserted into the production line. It posits that the clause covers "overtime repair costs" and "other additional expenses." Vought maintains that

> [u]nder the doctrine of *noscitur a sociis* ("a word is known by the company it keeps"), it is clear that "other additional expenses" must include expedited manufacturing costs, because similar costs, like costs of "repair" and "overtime" (which is actually associated with expediting production), are listed in the same provision and are specifically covered.

P. Oct. 9, 2009 Br. 23. Vought also asserts that because the Expediting Cost Clause uses the plural term "replacements" rather than the singular "replacement," all six stabilizers should be covered and that this interpretation provides coverage that meets the foreseeable needs of a supplier of complex machinery, since damage to one product will necessarily affect the insured's current and future obligations.

Defendants respond that Vought's claim fails because the Expediting Cost Clause only applies when the replacement part is sent by a different mode of transportation, such as by air instead of by ship; these expediting costs amount to delay and disruption costs[FN22] (pointing out that Vought's ***831** second amended complaint describes them as just that), *see* 2d Am. Compl. ¶ 41; expediting costs must be connected to the repair of the single damaged stabilizer; and Vought's costs of expediting are excluded from coverage because they were submitted to another insurer, not to Falvey. Defendants do not otherwise address the meaning of the Expediting Cost Clause and do not offer an alternative explanation for what could be considered "expediting costs" or "other additional expenses."[FN23]

> FN22. Section 45, captioned "Delay," provides:
>
> This insurance is warranted free from, and shall not cover, loss of market or loss,

> damage, or expense arising from delay, regardless of whether such delay is caused by a risk insured against or otherwise, unless such risks are expressly assumed elsewhere in this policy.
>
> Ds. Oct. 10, 2009 App. 22.

FN23. Defendants rely on deposition testimony consisting of opinions offered by employees of Falvey's and Vought's insurance brokers as to what the Policy covers and how it operates. Besides being parol evidence, the opinions lack foundation. Because the witnesses do not relate their opinions to the Policy, or otherwise explain how they arrived at those conclusions, the statements are of no use to the court in interpreting the clause. The interpretation of the Policy by others is of no consequence on a matter of interpretation that the court must conduct as a matter of law.

2

Defendants' initial argument, that the Expediting Cost Clause does not apply unless Vought used a different mode of transportation, is not supported by the language of the Expediting Cost Clause. The clause is designed to allow Vought to make an expedited shipment of replacements or replacement parts and thereby incur expediting costs for such a delivery. The "means other than the means by which the original shipment was dispatched" can include a faster version of the same mode of transportation (e.g., via a trucking company who, for an increased fee, guarantees delivery on an accelerated basis rather than on a standard schedule).

The court also disagrees with defendants that Vought is seeking delay and disruption costs. Section 45 of the Policy excludes coverage for "loss of market or loss, damage, or expense arising from delay" unless this risk is expressly assumed in the Policy. Vought faced possible fines or damages from Boeing, but it never actually incurred such expenses. Vought incurred the costs in question *to avoid* loss, damage, or expense arising from delay. The expenses were not themselves delay and disruption costs.

The court also declines to credit defendants' argument that the court cannot consider whether the Policy covers expediting expenses. Vought submitted the claim to both Falvey and another insurer so that the insurers could fully evaluate coverage. In the claim, it detailed the expenses making up the claim, differentiating between repair costs and expediting costs. Defendants appear to reason that, in doing so, Vought submitted the repair costs to Falvey and the expediting costs to the other insurer. But in submitting its claim, Vought offered no opinion as to which insurer ought to pay which expenses. The entire claim was submitted to Falvey in the first instance, and the court will consider it in its entirety.

3

The court agrees with defendants, however, that the Policy does not cover the costs Vought incurred in manufacturing and shipping on an expedited basis the five subsequent stabilizers. And the court agrees with defendants that the Expediting Cost Clause does not cover the cost of manufacturing, on an expedited basis, the initial replacement stabilizer. But the court concludes that the Expediting Cost Clause is ambiguous regarding whether it covers

the cost of shipping the initial replacement stabilizer where, as here, the insured chose to repair and ship the damaged stabilizer.

a

The Expediting Cost Clause must be read in the context of the Policy as a ***832** whole. *See Int'l Ins.*, 426 F.3d at 291. Section 16.2 obligates defendants to pay for any physical loss or damage from collision to covered goods during transportation. Where the good is a machine or an article consisting of multiple parts, the Machinery Clause limits defendants' liability to those parts that were damaged. But the clause allows Vought to file a claim either for the cost of repairing damaged parts or the cost of replacing them. The Expediting Cost Clause provides coverage, in addition to the underlying claim, for the insured's costs of expediting the shipment of a replacement and/or replacement part and any overtime repair costs and/or other additional expenses, including duties, taxes, and destination charges. The question becomes what goods or parts are included in "replacements and/or replacement parts." Vought asserts that the phrase refers to all six additional stabilizers and, presumably, to the repaired stabilizer (for which Falvey has already reimbursed Vought).

The intent of the Expediting Cost Clause is to allow Vought to meet quickly the need of a customer whose good was damaged or lost in shipment. A single good is replaced once another good meets the previous need; it is not replaced by multiple identical objects. Here, because only one stabilizer was damaged, only one stabilizer can be considered the replacement covered by the Expediting Cost Clause. Defendants are only responsible for the costs associated with that one replacement stabilizer.

[8] The court therefore rejects Vought's contention that, because the Expediting Cost Clause refers to "replacements," the Policy provides Vought reimbursement for the five subsequent stabilizers on the Vought production line. The Expediting Cost Clause provides coverage for the shipment of multiple replacement parts only if multiple parts are the subject of the claim. The five stabilizers completed after the first one did not replace the damaged stabilizer; they met separate contractual demands. The Policy does not cover any costs—including labor, other direct costs, overhead, or shipping—attributable to the five subsequent stabilizers. Defendants are therefore entitled to summary judgment dismissing this aspect of Vought's breach of Policy claim. Vought is not entitled to partial summary judgment in its favor as to this component of the claim.

b

[9] The Expediting Cost Clause also does not cover the cost of completing construction of the initial replacement stabilizer. The clause provides coverage for "expediting costs," "overtime repair costs," and "other additional expenses including duties, taxes and destination charges." The cost of constructing the initial stabilizer does not fall within any of these categories.

The meaning of "expediting costs" can be determined from the context of the clause. Expediting costs are expenses "involved" with "forward[ing] replacements and/or replacement parts by means other than the means by which the original shipment was dispatched." Ds. Oct. 10, 2009 App. 20. The clause relates the means of forwarding, and therefore expediting costs,

to the means of dispatching the original shipment. In other words, expediting costs are costs associated with the shipment of the replacement. They do not include labor for original construction.

"[O]vertime repair costs" refers to overtime costs incurred when Vought opts to ship a repaired replacement part. The costs of *completing* a new stabilizer are not *repair* costs at all, so they cannot qualify as "overtime repair costs."

***833** Nor can the costs of such new construction qualify as "other additional expenses." Vought argues that "other additional expenses" are mentioned alongside "overtime repair costs," so that the initial term must bear some similarity to the latter specific term. But the phrase "other additional expenses" comes *after* "overtime repair costs," indicating the additional expenses must be something different. Indeed, the clause specifies that coverage for "other additional expenses" "includ[es] duties, taxes and destination," indicating the other expenses must be like those stated to be included in the term. "[D]uties, taxes and destination charges," and the Expediting Cost Clause's focus on transportation-related costs, indicate the phrase "other additional expenses" cannot be read expansively to include such expenses as those incurred in constructing a new replacement part.

c

[10] The court holds that the clause is ambiguous regarding whether it covers Vought's cost of shipping the newly-constructed replacement stabilizer to Boeing (defendants reimbursed Vought for the cost of shipping the repaired stabilizer). From the perspective of Boeing, the newly-constructed stabilizer replaced the damaged stabilizer. And from the perspective of Vought, this stabilizer met the obligation that it intended to satisfy when it shipped the stabilizer that was damaged in transit. But the court cannot say as a matter of law that the Expediting Cost Clause covers the cost of shipping the entire wing. And it is also ambiguous whether, assuming the clause does cover the entire wing, the clause covers a newly-constructed replacement stabilizer when Vought opted to repair rather than replace the damaged stabilizer.

Where, as here, the covered article consists of multiple parts, the Machinery Clause limits coverage for the loss to the repair or replacement of the damaged part or parts. The Expediting Cost Clause provides coverage for expenses related to shipping "replacements and/or replacement parts." If the Machinery Clause limits Vought's entire claim to the repair or replacement of the damaged part or parts, it would also appear to limit the coverage provided by the Expediting Cost Clause to charges related to the expedited shipment of the covered replacement part or parts. It would not cover shipping costs related to the replacement of the entire machine or multipart article. Vought argues that the Expediting Cost Clause should not be read so narrowly because it provides coverage for replacements, replacement parts, or both. But this interpretation overlooks the fact that the expedited item must be a covered replacement. If the coverage of the underlying claim is limited to the damaged part or parts, the Expediting Cost Clause only covers costs of shipping the replacements for those parts.

But there is another reasonable interpretation of the Policy: that the Expediting Cost Clause is not limited by the Machinery Clause. Defendants' liability is ultimately created by §

16.2, which provides that defendants are to "pay for ... any physical loss of or damage to the [covered] goods." Ds. Oct. 10, 2009 App. 10–11. The covered good—the subject of Vought's claim—is the entire stabilizer. While the Machinery Clause limits defendants' liability for the repair of a multipart good such as the stabilizer, the Expediting Cost Clause may operate independently of the Machinery Clause to cover the cost of shipping the entire replacement good, even if only part needed repair.

But there is still another potential meaning. Even if the coverage of the Expediting Cost Clause is not limited by the Machinery***834** Clause (i.e., it covers the shipment of the entire stabilizer, not merely the repaired part), the clause may not cover the shipment of the initial replacement stabilizer. While the Expediting Cost Clause provides coverage for expenses "*in addition to* the underlying claim," Ds. Oct. 10, 2009 App. 20 (emphasis added), the clause does not provide for coverage *unrelated to* the underlying claim. In suing for costs associated with the initial stabilizer, Vought is essentially seeking the benefit of replacing the damaged stabilizer. But Vought elected to repair it, and it made a claim and was paid for costs associated with the repair. Vought's choice to expedite completion and ship a new stabilizer to Boeing is distinct from the underlying claim for costs of repairing the damaged stabilizer. The Expediting Cost Clause could therefore be reasonably interpreted to apply fully to the return shipment of the damaged stabilizer.

4

In sum, the court holds that the Policy does not cover the cost of replacing resources pulled from the normal production line, the cost of constructing the six stabilizers, or the cost of shipping the five subsequent stabilizers. The court grants defendants' motion for summary judgment and denies Vought's motion for summary judgment as to these costs. Because the Policy is ambiguous regarding coverage for the shipment of the initial replacement stabilizer, the court denies the motions for summary judgment of both Vought and defendants as they relate to shipping costs for this stabilizer. *See Recursion Software, Inc. v. Interactive Intelligence, Inc.*, 425 F.Supp.2d 756, 784 (N.D.Tex.2006) (Boyle, J.) ("Summary judgment is generally appropriate only if the language of the contract is wholly unambiguous.")

V

Vought also sues to recover overhead expenses related to the repair of the damaged stabilizer. These expenses consist of $206,920.00 in direct overhead and $77,589.00 in general and administrative costs.[FN24]

FN24. Vought's overhead expenses are comprised of its "direct overhead" and "general and administrative costs." Direct overhead includes depreciation on facilities, equipment and tools, certain supervisor salaries, and all other costs that do not result from direct labor charges, but that can still be assessed to a particular manufacturing process. General and administrative costs make up the balance of Vought's corporate expenses that cannot be attributed to specific manufacturing tasks. They include executives' salaries and benefits for retired workers. Vought does not assert that Falvey improperly considered direct expenses to be overhead expenses.

A

The Machinery Clause requires that defendants pay "the cost and expense of replacing or repairing ... the ... damaged part ... and all other necessary charges so that the machine or article is restored to its condition at the time of shipment." Ds. Oct. 10, 2009 App. 15. Vought argues that, as a government contractor, it must follow well-defined accounting procedures to allocate general corporate expenses—such as the depreciation of its facilities, lighting bills, and executives' salaries—among its various manufacturing activities, and that these expenses are a cost of repairing the damaged stabilizer. The court rejects this argument because Vought points to nothing in the Policy indicating that the Policy adopts government contracting regulations.

Vought also maintains that overhead costs are an inherent part of repair costs. It cites a number of cases in which courts construed insurance policies (usually homeowner policies) to pay an insured the ***835** cost of employing a general contractor. The single Texas case is representative of the others. In it, the plaintiff's hotel was damaged by wind and hail. *Ghoman v. N.H. Ins. Co.*, 159 F.Supp.2d 928, 930 (N.D.Tex.2001) (Kaplan, J.). The plaintiff's property was insured under a policy that required the insurer to reimburse the actual cash value of the damage. *Id.* at 932. That value was calculated by subtracting depreciation from the cost of replacement or repair. *Id.* at 934. The parties disagreed about whether the repair costs included a general contractor's overhead. *Id.* at 931. A general contractor is not paid a specified wage for coordinating a project; rather the contractor is paid "overhead and profit," a percentage of the cost of a project. *See Gilderman v. State Farm Ins. Co.*, 437 Pa.Super. 217, 649 A.2d 941, 943 (1994). Because the insurer was required to reimburse the cash value of a repair, rather than the actual costs of the repair, repair costs "include any cost an insured is reasonably likely to incur in repairing or replacing a covered loss." *Ghoman*, 159 F.Supp.2d at 934 (quoting *Salesin v. State Farm Fire & Cas. Co.*, 229 Mich.App. 346, 581 N.W.2d 781, 790 (1998)). Even though the plaintiff completed the repair himself, without hiring (or paying) a general contractor, he was entitled to these costs because they were of a sort reasonably likely to be incurred by an insured. *Id.* In other words, the insured was entitled to the amount required to hire an outside professional to complete the repair, even though he performed the repair himself. Vought thus argues that its overhead costs should be included as a cost of repair.

Vought's argument relies on two assumptions: first, that the cases on which it relies are relevant because the general contractors' "overhead and profits" are essentially equivalent to Vought's "overhead" expenses; and, second, that the Policy requires defendants to pay something akin to the cash value of a repair rather than the actual costs and expenses of making the repair. In effect, Vought reasons that its costs should include any type of costs and expenses that a third-party would charge for the repair, including overhead expenses. But the overhead expenses that Vought seeks to recover and the overhead at issue in cases like *Ghoman* are not necessarily identical, despite coincidental names. A general contractor's overhead is part of the fee for his services. Rather than charge an hourly or per-job fee, he charges a fee tied to the expense of the project. The fee reimburses him for his own expenses and provides a profit. For Vought, however, overhead consists of fixed costs that it incurs at a more general level. To be profitable, Vought must factor a share of these costs into each product that it sells. The two types of overhead do, however, have one key common aspect: an

insured will incur either cost if he hires a third party to perform the repair work. Just as a third-party contractor would charge "overhead and profit," another contractor would pass along its fixed "overhead" as a cost of repairing the stabilizer. They are both expenses an insured is reasonably likely to incur.

[11] Defendants argue that another contractor would not have charged overhead for this repair. Where a policy provides cash value for a repair, whether cash value includes a contractor's overhead and profit depends on whether the repair is so complex that hiring a contractor is likely. *See Mee v. Safeco Ins. Co. of Am.*, 908 A.2d 344, 350 (Pa.Super.Ct.2006). In the case of home repair, if damage is so severe that a number of different trades would be necessary to complete the repair, a general contractor likely would be necessary. Conversely, if the repair were so simple that it could be completed by one tradesman, no general contractor would be needed. Defendants argue that the damage to ***836** the stabilizer was minimal—"more of a scrape where lamination was taken off"—as evidenced by the fact that only about $15,000 in materials were necessary to repair it. Ds. Nov. 6, 2009 Br. 11. Further, they contend that it was not necessary for Vought to hire multiple trades; in fact, the stabilizer was a specialized product, and no one other than Vought could perform the work. But defendants' analysis ignores the central point of *Ghoman* and like decisions. The rule is not that overhead is allowable if a contractor is reasonably necessary to perform the work; instead, it is the rule that, in a cash value policy, an expense is available to an insured, even though he performs the work himself, where he would be reasonably likely to incur that expense if a third party performed the repair. *See Ghoman*, 159 F.Supp.2d at 934. If another contractor performed the same repair work on the stabilizer, it would pass along fixed overhead to Vought.

The question, then, is whether the Policy entitles Vought to recover the actual cash value of the repair or only the cost of the repair. Vought argues that the Policy need not be an actual cash value policy for the rule to apply. It maintains that, in *Ghoman*, the court held that "actual cash value" meant repair costs less depreciation, and that repair costs included any cost an insured would likely incur. Therefore, Vought reasons, the court was really defining "repair costs." But Vought's interpretation isolates that phrase from the rest of *Ghoman.*

In *Ghoman* the policy "provide[d] that the insurance company 'will determine the value of Covered Property in the event of loss or damage ... [a]t actual cash value as of the time of loss or damage[.]' " *Ghoman*, 159 F.Supp.2d at 931–32 (alterations and ellipses in original). *Ghoman* essentially held that where an insured had purchased cash value coverage, he was entitled to the value of repairing his property, i.e., all expenses he could foreseeably incur in repairing it. *See id.* at 934 ("The court concludes that 'actual cash value' under the policy means repair or replacement costs less depreciation. Repair or replacement costs include any cost that an insured is reasonably likely to incur in repairing or replacing a covered loss.") (alteration and internal quotation marks omitted). The *Ghoman* court thus defined repair or replacement costs, in light of the nature of the policy, to provide the value of the damage.

But the provision under which Vought seeks coverage is different.[FN25] It provides for costs and expenses, not value: defendants will pay the "cost and expense of ... repairing ... [the] damaged part or parts ... and all other necessary charges ... so that the machine or article

is restored to its condition at the time of shipment." Ds. Oct. 10, 2009 App. 15. Defendants thus did not agree to pay Vought foreseeable expenses of repair, but rather to cover the costs and expenses necessary to restore the damaged stabilizer parts to their condition at the time the stabilizer was shipped.[FN26] Vought is therefore owed its ***837** costs, not the value of its repair. Vought's reliance on *Ghoman* and related cases is accordingly misplaced.

> FN25. The Machinery Clause states: "This Insurer shall be liable only for the proportion of the insured value applicable to the part or parts lost or damaged, or at the Insured's option, for the cost and expense of replacing or repairing ... [the] damaged part[.]" Ds. Oct. 10, 2009 App. 15. Vought opted to seek the cost of repair. A Vought executive informed Falvey that "Vought has formulated a repair plan for the subject damaged C–17 component part .... [It] has, therefore, begun to repair the part accordingly and will aggregate its costs and will subsequently file a claim with each of your companies for reimbursement of those costs[.]" P. Nov. 6, 2009 App. 55.
>
> FN26. In other words, while "value" should be determined by looking to the market price, "cost" should be determined by looking at actual receipts.

B

Vought also relies on the indemnity nature of the Policy to seek the overhead costs. Citing several cases in which courts awarded overhead costs as part of damages, Vought argues that overhead costs are necessary to make it whole. *Dillingham Shipyard v. Associated Insulation Co.*, 649 F.2d 1322 (9th Cir.1981), is representative of these cases, and the only one that involves a contract.

In *Dillingham* a shipyard contracted to install a sonar system in a United States Coast Guard cutter. *Id.* at 1323. To perform the work, it subcontracted with a company to install a tile dampening system in an ammunition handling room. *Id.* The subcontractor left a leaky gas tank in the room, causing an explosion. *Id.* Per its contract with the Coast Guard, the shipyard repaired the damage to the cutter. *Id.* The shipyard then sued the subcontractor based on a provision in the subcontract in which the subcontractor promised to indemnify and hold harmless the shipyard for any damages, costs, and expenses paid by the shipyard as a result of the subcontractor's negligence. *Id.* at 1324. The court determined that the indemnification award should include the shipyard's overhead (including overhead attributed to its home office) "because such expenses must be included in the judgment in order to compensate [the shipyard] fully for its costs and expenses in making the repairs." *Id.* at 1326.

But *Dillingham* and the other cases Vought cites do not apply in the insurance policy context. In *Dillingham* the court was attempting to award all costs resulting from a particular event. "It is [a] fundamental principle that reasonable expenses, including overhead expenses, incurred as a result of a breach of contract or a tortious act are proper items of recoverable damages." *William Wrigley Jr. Co. v. Waters*, 890 F.2d 594, 604 (2d Cir.1989). In the tort or contractual damages context, the court's intent is to make the injured party whole. Because the court's assessment comes after the damage is sustained, the full amount of injury can be accurately assessed. In the insurance context, however, the insurer and the insured bargain for a specific level of reimbursement. In advance of any loss, the insurer calculates the premium

to be charged based on the risk it is assuming. Vought and defendants contracted for a specific level of coverage, so the Policy's terms dictate whether Vought is entitled to recover the overhead expenses related to repairing the damaged stabilizer.

C

Vought asserts that its overhead costs should be reimbursed because "[i]n each instance in which the Policy provides that Vought should receive compensation, the Policy itself makes clear that Vought should be fully compensated[.]" P. Oct. 9, 2009 Br. 19. It points to § 9.1, which provides that insured goods should be valued at the invoice price; the invoice price, it argues, reflects Vought's overhead. But Vought ignores the effect of the Machinery Clause, which is to limit a claim for a damaged good consisting of multiple parts to the cost of repairing or replacing the damaged part. The effect on coverage of that clause is the subject of this dispute.

D

Vought maintains that the expense of operating its business is a necessary cost of repairing the damaged parts in the stabilizer. It reasons:

> ***838** Overhead resources that are devoted to a particular project or that occupy a business's time cannot be devoted to alternate income-generating projects. If overhead costs associated with a repair are not reimbursed, this opportunity cost further reduces the value of the business. While overhead costs may lack a certain tangible quality, this does not mean they do not exist, that they are not actually incurred in a repair, or that they are not somehow deserving of compensation.

P. Oct. 9, 2009 Br. 17. In other words, Vought's overall cost of operating its business is one aspect of the cost of everything it does. Moreover, the use of Vought's equipment, space, and personnel actually reduced the resources the company had available for other potential projects (i.e., imposed opportunity costs). Defendants contend, however, that to award Vought a portion of overhead expenses would unjustly enrich the insured. At bottom, they posit, the overhead expenses that Vought seeks would have been incurred in the same amount regardless of whether Vought had to repair the stabilizer parts.

Both positions have some merit, and the Policy does not clearly answer which position is correct. The Policy requires defendants to pay repair costs and expenses and "all other necessary charges" so that the stabilizer is restored to its condition at the time of shipment. On the one hand, Vought would have incurred the same costs of executives' salaries and depreciation on property if the repair had not been made. The expenses could thus be seen as general expenditures, not necessary charges for repairing the damaged stabilizer. On the other hand, Vought could not have made the repair were it not for the infrastructure of personnel, buildings, and equipment in place at Vought's facility. In this sense, the overhead charges were necessary so that the stabilizer could be repaired.

[12] The court therefore holds as a matter of law that the Machinery Clause is ambiguous in this respect. On the one hand, "other necessary charges" could include overhead of some type, including some or all of the overhead for which Vought sues in connection with its

repair of the damaged stabilizer.[FN27] On the other hand, costs and expenses and all other necessary charges could include only direct labor and material costs incurred in making the repair. Because the Policy is ambiguous in this respect, the court denies the motion for partial summary judgment of Vought,[FN28] and it denies defendants' motion for summary judgment to the extent it relates to Vought's claim for overhead costs incurred in connection with repairing the damaged stabilizer. *See Recursion Software,* 425 F.Supp.2d at 785.

FN27. This ambiguity does not affect the court's decision regarding the six stabilizers because, for the reasons explained, Vought cannot recover any costs, expenses, and charges for the completion of those stabilizers.

FN28. Ordinarily, an insured is entitled to have an ambiguity construed in its favor. But as the court explains *supra* at § III(B), it is possible that the sophisticated insureds exception may apply in this case. If it does, Vought will not be entitled to the benefit of the ambiguity.

VI

The court turns next to Vought's claim that defendants breached the duty of good faith and fair dealing. Defendants move for summary judgment dismissing this claim.

A

[13][14][15][16] The common law duty of good faith and fair dealing is breached when an insurer denies or delays payment of a claim after its liability has become reasonably***839** clear. *See Universe Life Ins. Co. v. Giles,* 950 S.W.2d 48, 56 (Tex.1997). "An objective standard is employed to determine 'whether a reasonable insurer under similar circumstances would have delayed or denied the claimant's benefits.' " *Vandeventer v. All Am. Life & Cas. Co.,* 101 S.W.3d 703, 722 (Tex.App.2003, no pet.) (quoting *Aranda v. Ins. Co. of N. Am.,* 748 S.W.2d 210, 213 (Tex.1988)). An insurer does not breach its duty by denying a questionable claim. *See Aranda,* 748 S.W.2d at 213. "[A] bona fide dispute about the insurer's liability on the contract does not rise to the level of bad faith." *Transp. Ins. Co. v. Moriel,* 879 S.W.2d 10, 17 (Tex.1994). In such instances, the insurer's liability is not reasonably clear. As long as the insurer has a reasonable basis to deny or delay payment of a claim—even if that basis is eventually determined by the fact-finder to be erroneous—the insurer is not liable for the tort of bad faith. *Lyons v. Millers Cas. Ins. Co. of Tex.,* 866 S.W.2d 597, 600 (Tex.1993).

[17][18] An insurer cannot escape liability, however, by performing an inadequate investigation. Within the duty of good faith is an insurer's obligation to conduct an adequate investigation of the claim. *United Serv. Auto. Ass'n v. Croft,* 175 S.W.3d 457, 469 (Tex.App.2005, no pet.). "[A]n insurer cannot insulate itself from bad faith liability by investigating a claim in a manner calculated to construct a pre-textual basis for denial." *State Farm Fire & Cas. Co. v. Simmons,* 963 S.W.2d 42, 44 (Tex.1998). Similarly, an insurer cannot escape liability by "failing to investigate a claim so that it can contend that liability was never reasonably clear." *Universe Life,* 950 S.W.2d at 56 n. 5.

B

Vought alleges that defendants breached the duty of good faith by failing to conduct a

proper investigation. According to Vought, Falvey's determination of which claims were covered was improper because Falvey instructed the accounting firm that it retained to analyze the claim to exclude overhead costs from its calculation. It also posits that the accounting was improper because the accountant relied on Falvey's interpretation of the Policy rather than on an independent reading. Vought does not argue that using an independent accountant to determine coverage was improper.

[19] A reasonable jury could not find in Vought's favor on this theory. It could only find that the examples of breach on which Vought relies are instances of Falvey's attempting to interpret what the Policy covers. The determinations Falvey made before employing the accounting firm are no different than the decisions it would have needed to make had it determined coverage without outside assistance. That Falvey decided some aspects of coverage before retaining the accounting firm to analyze Vought's claim in detail would not permit a reasonable jury to find that the accountants' report was a pretext to deny most of Vought's claim. Moreover, the accounting firm did not perform an investigation; instead, it analyzed the expenses that Vought submitted.[FN29] Falvey neither disputed that the damage to the stabilizer was an event covered under the Policy nor contended that Vought's expenses (to the extent categorically covered) were unreasonably high. In fact, the accounting firm recommended making a somewhat higher payment for the expenses it did approve. The dispute was ***840** not factual but interpretive: whether all of the expenses Vought sought to recover were covered by the Policy.

> FN29. In *Simmons,* for instance, the court faulted the insurer's investigation for unreasonably concluding that the insureds set the fire that led to the loss and for unreasonably failing to investigate whether others may have started the fire. *Simmons,* 963 S.W.2d at 45.

Vought also alleges that Falvey breached this duty by refusing to pay the full claim. Defendants maintain that Falvey's denials were proper and that its liability for Vought's claimed overhead and expediting expenses was never clear, i.e., that there was a bona fide dispute about coverage. Indeed, the court has determined that defendants are not liable to Vought for most of the costs associated with the manufacture and shipment of the six stabilizers. And defendants' liability for Vought's overhead expenses related to the repair of the damaged stabilizer or for the cost of shipping the initial stabilizer is not reasonably clear even now.[FN30]

> FN30. Vought also asserts that defendants "flatly misstated the basis for denying Vought's claims by erroneously claiming they arise under the 'Sue and Labor' Clause, rather than the Machinery Clause." P. Nov. 6, 2009 Resp. 44. But Vought points to no authority that, where defendants did not deny a claim for which they were clearly liable, they breached the duty of good faith.

Accordingly, the court grants summary judgment dismissing Vought's claim for breach of the duty of good faith and fair dealing.

VII

Defendants also move for summary judgment dismissing Vought's claim for unfair insurance practices under the Texas Insurance Code.

A

[20] Vought alleges that defendants violated Tex. Ins.Code Ann. §§ 541.051 to 541.061 and 541.151. Defendants contend that because Vought's common law good faith claim fails, its statutory claim fails as a matter of law. But a "defense to an insured's common law bad faith claim also serves to defeat each of its other extracontractual causes of action *only* if 'each cause was nothing more than a recharacterization of the bad faith claim.' " *Mid–Continent Cas. Co. v. Eland Energy, Inc.,* 2009 WL 3074618, at *26 n. 28 (N.D.Tex. Mar. 30, 2009) (Fitzwater, C.J.) (emphasis in original) (quoting *Escajeda v. Cigna Ins. Co. of Tex.,* 934 S.W.2d 402, 408 (Tex.App.1996, no writ)). Two of Vought's statutory allegations are recharacterizations of the common law claim. Vought asserts that defendants failed to effectuate a prompt, fair, and equitable settlement once its liability became clear, and that defendants refused to pay the claim without a reasonable investigation. These claims fail for the same reason as do their common law analogues.

[21] But several other of Vought's statutory claims are not recharacterizations of its common law claim. Vought alleges that Falvey misrepresented the benefits of the Policy; misrepresented the Policy provisions during settlement; failed to promptly explain its denial of the claim; undertook to obtain a full and final release when only a partial payment had been made; failed to affirm or deny coverage within a reasonable time; misrepresented the quality of its services; and failed to disclose material information at the sale of the Policy with the intent to induce Vought to buy a Policy that it would not have otherwise bought. Defendants' defense to the common law claims therefore does not defeat these claims.

B

Defendants also argue that there is no evidence to support the remainder of Vought's statutory allegations. Vought responds by asserting only that Falvey misled it into repairing the stabilizer by withholding its decision not to cover overhead costs.[FN31] Vought argues that Falvey convinced***841** it to repair the stabilizer, rather than to declare it a total loss, thus saving defendants over $1 million; that Falvey had a duty as the insurer not to withhold such material information, and that it should not be allowed to profit by its conduct;[FN32] and that this omission violated Tex. Ins.Code Ann. § 541.061(2), (3), or (4).[FN33] Defendants reply that Vought could not have simply declared the stabilizer a loss if it was not cost effective to do so.[FN34]

FN31. Vought mentions in passing that Falvey initially stated that Vought's claim was excluded from coverage by the Sue and Labor Clause of the Policy. It points to a letter sent by Falvey explaining its refusal to pay some of Vought's claim. But contrary to Vought's contention, Falvey does not in this letter justify its denial on the Sue and Labor Clause; rather, it points to that clause to distinguish the Policy from the policy in *Ghoman.* And Vought does not further describe this conduct or explain how it is illegal. Assuming that Vought has preserved this as a basis for its claim, the court holds that a reasonable jury could not find in its favor on this basis.

FN32. In arguing for defendants' statutory liability, Vought mischaracterizes Falvey's role in its decision to repair the stabilizer. In describing the incident earlier in its summary judgment response brief, Vought explains:

> Under the Policy's terms, Vought had the right to decide whether to repair the damaged stabilizer or declare it a total loss. Vought engineers conferred with Boeing and the United States Air Force, and all agreed that repair was possible and that it could be done for significantly less than the stabilizer's $2.5 million invoice price. They also agreed that Vought would have to undertake the repairs itself, because the wing had a highly specialized design and could not feasibly be repaired by any other company.
>
> In a letter dated August 11, 2005, Vought informed Defendants of the repair plan, notified Falvey that Vought would make a claim for reimbursement of the repair costs, and stated its intention to perform the repairs itself[.]
>
> P. Nov. 6, 2009 Br. 4 (citations omitted).

FN33. Vought neither provides evidence of violations of its other statutory bases for bad faith nor argues for liability based on them. It has therefore failed to raise a genuine issue of material fact concerning these grounds.

FN34. They do not explain, however, why such a claim would have been impermissible. Instead, they cite various individuals' deposition testimony contained in an appendix to their reply. The court resolves the statutory bad faith claims on other grounds and need not consider this testimony or decide whether it is admissible at the summary judgment stage.

[22] The evidence to which Vought points would not enable a reasonable jury to find that Falvey violated § 541.061. Section 541.061 provides:

> It is an unfair method of competition or an unfair or deceptive act or practice in the business of insurance to misrepresent an insurance policy by:
>
> ...
>
> (2) failing to state a material fact necessary to make other statements made not misleading, considering the circumstances under which the statements were made;
>
> (3) making a statement in a manner that would mislead a reasonably prudent person to a false conclusion of a material fact; [or]
>
> (4) making a material misstatement of law[.]

Vought has not provided evidence that defendants could be liable under § 541.061(2) because it has not pointed to a statement that a reasonable jury could find was rendered misleading by Falvey's failure to disclose it would not cover overhead costs. Nor has Vought pointed to a statement that could be found to violate § 541.061(3). After Vought informed

Falvey that it intended to file a claim for repair expenses, a Falvey officer responded:

> I have received and reviewed the documents [related to the claim], as well as the Preliminary Repair Analysis ....
>
> ***842** At this point I shall await the results of the repairs and the ensuing repair cost calculations in order to proceed with the claim settlement.
>
> In the meantime, I would appreciate a copy of any contract Vought may have with [the railroad] so that we might evaluate the recovery potential.

P. Nov. 6, 2009 App. 59. A reasonable jury could not find that anything in this statement should have led Vought to believe it would be reimbursed for overhead. And Vought has not pointed to a misstatement of law.

In sum, Vought has pointed to no facts that would enable a reasonable jury to find that defendants violated any provision of the Texas Insurance Code. The court therefore grants summary judgment dismissing Vought's claim under Tex. Ins.Code Ann. §§ 541.051 to 541.061 and 541.151.

VIII

Defendants also move for summary judgment dismissing Vought's claim that defendants breached a contract formed when Vought offered, and defendants agreed, that Vought should perform the repairs on the horizontal stabilizer.

Vought alleges that when it and defendants reached this agreement, Vought became the equivalent of a third-party repair contractor who was entitled to full compensation. Defendants maintain that Vought chose to repair the stabilizer without discussing the matter with them, and that they never agreed to fund the repair. Vought reasons that the Policy provided that defendants would pay for the stabilizer repair, but did not specify that Vought was required to perform the repair itself. It maintains that, by informing defendants that it planned to repair the stabilizer itself, it was making an offer as a third-party contractor. And it contends that defendants accepted the offer.

[23] A valid and enforceable contract requires an offer by one party and an acceptance by the other party, in strict compliance with the terms of the offer. *See Searcy v. DDA, Inc.*, 201 S.W.3d 319, 322 (Tex.App.2006, no pet.). To obtain summary judgment, defendants can point the court to the absence of evidence to support the claim. *See Celotex Corp.*, 477 U.S. at 325, 106 S.Ct. 2548. Vought must then adduce evidence that would permit a reasonable jury to find in its favor.

[24] Regardless whether Vought's communication could be considered an offer, a reasonable jury could not find that defendants expressed an intention to accept the offer. In a response to the letter from Vought describing planned repairs, a Falvey executive referred to a claim under the Policy but stated only that the company would "await the results of the repairs and the ensuing repair cost calculations in order to proceed with the claim settlement." P. Nov. 6, 2009 App. 59. The executive's reference to a claim settlement indicates the correspondence was concerned with defendants' obligations under the existing contract, not

under a new contract.

Vought has failed to point to evidence that would permit a reasonable jury to find that defendants accepted Vought's offer in strict compliance with its terms. Defendants are therefore entitled to summary judgment dismissing Vought's claim (count four) that defendants breached the repair agreement.

IX

Defendants move for summary judgment dismissing Vought's promissory estoppel claim. They maintain that Vought cannot establish any of the elements of promissory estoppel, particularly the requirement that defendants promised to pay for the entire cost of the repair.

***843** [25] To be liable for promissory estoppel, defendants must have promised to pay for some portion of the repair that they did not cover. *See Miller v. Raytheon Aircraft Co.,* 229 S.W.3d 358, 378–79 (Tex.App.2007, no pet.) (holding that, to be liable for promissory estoppel, defendant must have made promise to perform subject of claim). Vought has failed to point to evidence that would permit a reasonable jury to find defendants made a promise to pay the entire cost of the repair. Defendants are therefore entitled to summary judgment dismissing Vought's claim for promissory estoppel.

X

Defendants move for summary judgment dismissing Vought's claim for quantum meruit.

[26] To prevail on this claim, Vought must prove that "(1) valuable services were rendered; (2) to the party sought to be charged; (3) which services were accepted by the party sought to be charged; (4) under such circumstances as reasonably notified the recipient that the plaintiff, in performing such services, expected to be paid by the recipient." *Collins & Aikman Floorcoverings, Inc. v. Thomason* 256 S.W.3d 402, 407–408 (Tex.App.2008, pet.denied). Vought posits that repairing the stabilizer was a valuable service rendered for defendants and that Vought could justifiably have expected to have been paid at least as much as a third-party contractor hired to make the repairs. Defendants counter that, before Vought undertook the repairs, it did not notify them that they were expected to pay expediting or overhead costs.

[27] Vought has failed to cite evidence that would enable a reasonable jury to find that Vought performed services under such circumstances as reasonably notified defendants that Vought expected to be paid overhead or expediting costs. Because a contract of insurance was in place, a reasonable jury could only find that defendants expected that they would be required to pay Vought as provided under the terms of the Policy. Accordingly, the court grants summary judgment dismissing Vought's quantum meruit claim.

XI

Defendants move for summary judgment dismissing Vought's claim for unjust enrichment. They point to the absence of evidence that they obtained a benefit by fraud, duress, or undue advantage.

[28] "A party may recover under the unjust enrichment theory when one person has

obtained a benefit from another by fraud, duress, or the taking of an undue advantage." *Heldenfels Bros., Inc. v. City of Corpus Christi*, 832 S.W.2d 39, 41 (Tex.1992). Vought argues that Falvey induced Vought to repair the stabilizer under circumstances that suggested that Vought would be fully compensated for its services; Falvey had already decided not to fully fund the repair, and it had a duty to disclose this fact to Vought; and this omission took undue advantage of Vought's willingness to make the repairs itself rather than obtain the services of a third party. Vought reasons that the undue benefit is the amount the third party would have charged to make the repairs, which includes both overhead and expediting charges, and that defendants received the additional benefit of not having to pay the replacement cost of the stabilizer, which Vought could have sought instead.

[29] A reasonable jury could not find in Vought's favor on this claim. Vought's reasoning is inconsistent with its explanation of the events leading up to the stabilizer's repair. According to Vought, the stabilizer is highly specialized, and only Vought could have made the repair. Vought decided to repair the stabilizer after***844** conferring with Boeing and the Air Force. It did not inform Falvey of its intent to repair the stabilizer until after it had made this decision.[FN35] Therefore, a reasonable jury could not find that defendants induced Vought to repair the stabilizer itself rather than obtain the services of a third party. Defendants are therefore entitled to summary judgment dismissing Vought's claim for unjust enrichment.

> FN35. As the court explains *supra* at § VIII, a reasonable jury could not find that Vought and Falvey entered into a separate contract that governed the repair of the stabilizer.

XII

XL moves for summary judgment on the alternative ground that it cannot be liable to Vought because it was at all times acting as an agent for a disclosed principal.

A

XL maintains that it acted as an agent for Dornoch, a disclosed principal who was the lead underwriter for Lloyd's Syndicate 1209, and that pursuant to basic principles of agency law, it cannot be held liable. Vought responds that XL never disclosed its agency, and, alternatively, never disclosed the existence or identity of the principal for which it was acting. Vought posits that there is a genuine issue of material fact about XL's liability because, in an answer to an interrogatory, defendants identified XL as an insurer.

B

To determine whether XL qualifies as an agent for a disclosed principal, the court must first analyze the Lloyd's of London ("Lloyd's") insurance market through which the Policy was placed. Lloyd's is not itself an insurance company, but a market in which members may buy and sell insurance. *See Corfield v. Dallas Glen Hills LP*, 355 F.3d 853, 857 (5th Cir.2003) (citing John M. Sylvester & Roberta D. Anderson, *Is It Still Possible To Litigate Against Lloyd's in Federal Court?*, 34 Tort & Ins. L.J. 1065, 1068 (1999)). Lloyd's members are individuals or corporations called "names"; these names are the parties who actually contract to insure a risk. *Id.* at 858. Lloyd's regulates membership, ensuring the solvency of its members. *Id.* Most names insure risks by forming "syndicates," an administrative entity with

no legal status apart from its names. *Id.* Names agree to underwrite a certain percentage of each risk to which the syndicate subscribes. On most policies, the risk is underwritten by several different syndicates, each of which agrees to be liable for a certain percentage of the risk. *Id.* FN36

> FN36. Liability for each name on a policy is several, not joint. Names may be liable for any amount, but only for the percentage of the loss that the name has agreed to cover. *See E.R. Squibb & Sons, Inc. v. Acc. & Cas. Ins. Co.,* 160 F.3d 925, 929 (2d Cir.1998).

Each syndicate appoints, by contract, a "managing agent," normally a business entity, to be responsible for the management of the risks underwritten by the syndicate. *Id.* The managing agent typically selects one of its employees to be the "active underwriter" for the syndicate, who can then buy and sell insurance on behalf of the syndicate. *Id.* "Each Managing Agent is responsible for its own syndicate's financial well-being; it tries to attract capital and underwriting business." *Roby v. Corp. of Lloyd's,* 996 F.2d 1353, 1357 (2d Cir.1993). Managing agents "among other things, accept or reject the risks submitted for underwriting, collect premiums, pay losses and disburse all funds." *Alexander & Alexander Servs., Inc. v. Lloyd's Syndicate 317,* 902 F.2d 165, 166 (2d Cir.1990). "Active underwriters and at least two principals of the managing agency are required to participate in the syndicates that they ***845** manage." *McAuslin v. Grinnell Corp.,* 2000 WL 1059850, at *2 (E.D.La. Aug. 1, 2000).

Any given policy typically involves multiple syndicates; the syndicates usually designate one of the active underwriters from one of the syndicates as the "lead" underwriter on the policy. *Corfield,* 355 F.3d at 858–59. This lead underwriter is typically the first underwriter to subscribe to a policy and the one to assume the greatest risk. *Id.* at 859. Usually, the lead underwriter is the only name disclosed; the others remain anonymous. *Id.* The insured need only sue the lead underwriter, however, because the typical policy allows one name on the policy to appear as a representative of the rest. *Id.* The typical policy also requires the other names to abide by the final judgment in the lead underwriter's case. *Id.*

Insurance policies must be placed through a Lloyd's approved broker. *Alexander & Alexander Servs.,* 902 F.2d at 166. The broker prepares a "slip" that sets out the insured risk, and it submits it to multiple managing agents. *Id.* A managing agent then indicates whether his syndicate will underwrite any of the risk, and, if so, in what percentage. *Id.* Once the entire risk is subscribed, the broker informs the insured that the insurance has been placed. *Id.* Then the Corporation of Lloyd's, which manages the Lloyd's market, issues the policy through its Policy Signing Office. *Id.* at 166–67. This policy lists the numbers of the subscribing syndicates and the percentage of the risk that each has underwritten. *See Landoil Resources Corp. v. Alexander & Alexander Servs. Inc.,* 720 F.Supp. 26, 27 (S.D.N.Y.1989).

C

[30][31] Having set out material aspects of how the Lloyd's insurance market functions, the court now determines whether XL is entitled to summary judgment on the ground that it was acting only as the agent for a disclosed principal. A party forming a contract is presumed

to be a party to that contract. *See, e.g., Lake v. Premier Transp.*, 246 S.W.3d 167, 171 (Tex.App.2007, no pet.). To avoid liability, the agent must disclose both that it is acting in a representative capacity and the identity of its principal. FN37 *Id.* Because XL has the burden of proving at trial that it was acting as the agent for a disclosed principal, *see, e.g., Southwestern Bell Media, Inc. v. Trepper*, 784 S.W.2d 68, 72 (Tex.App.1989, no writ), it can obtain summary judgment on this basis only by making this showing beyond peradventure.

FN37. XL does not assert that Vought has failed to provide evidence that it is liable for any risk under the Policy.

[32] XL points to what it describes as "managing agents' agreements" to demonstrate that it was acting as an agent for Syndicate 1209. One document states that a company called Brockbank Syndicate Management, Limited ("Brockbank") was to serve as agent for Dornoch; another states that Brockbank was to serve as agent for County Down, Limited; and the third states that XL was to serve as agent for Stonebridge Underwriting, Ltd. Even if this evidence establishes XL's actual agency, it does not establish that XL disclosed that agency, or the identity of its principal, to Vought prior to the contract. Nor does XL point to any other evidence that it disclosed its agency or its principal.

XL's role in insuring the risk is demonstrated by the "Binder for International Transportation Insurance" ("Binder") that was attached to the Policy. The Policy frequently refers to the liability of "the ***846** Insurer" without specifically identifying the insurer. Section 66, captioned "SIGNATURE OF THIS INSURER," states:

> This is to certify that this insurance has been arranged herein as specified 100% with Underwriters at Lloyd's, London, England as per authority granted FALVEY CARGO UNDERWRITING, LTD. With regard to all references in this policy to the "Company", it is understood and agreed that the Company shall be deemed to be Falvey Cargo Underwriting, Ltd. In WITNESS WHEREOF, This Insurer has executed, issued and delivered this policy at Wakefield, Rhode Island "As Per Declaration Page."

Ds. Oct. 10, 2009 App. 31 (bold font omitted). The attached Binder provides pertinent terms concerning the Policy, such as the identity of the insured, the interest insured, deductibles, and policy limits. The Binder includes the declaration that "[t]his is to certify that the undersigned have arranged insurance as hereinafter specified 100% with Underwriters at Lloyd's, London, England as per Covernote JC492803." *Id.* at 46. Page 2 of the Cover Note contains the heading, "UNDERWRITERS AT LLOYD'S LONDON BINDING AUTHORITY AGREEMENT," Ds. Oct. 10, 2009 App. 48, and appears to be a standard Lloyd's form. It grants Falvey the authority "to bind insurance for the Underwriters' account." *Id.* The final page lists a series of syndicates and the amount of the risk each assumes. *Id.* at 74. Following the name of each syndicate are a set of initials and "London." *Id.* Above the list are the words "*HEREON:* 100.0000% Being Order Hereon." *Id.* The next line reads, "36.3637% Lloyd's Underwriter Syndicate No. 1209 XL, London." *Id.* The other lines list different syndicates with percentages of their risk.

The document does not indicate the identity of "XL, London" or the nature of its

relationship to the Policy. This description suggests that XL is the active underwriter for Syndicate No. 1209 and, because Syndicate No. 1209 assumed the greatest risk on the Policy, that XL is also the lead underwriter on the policy. While Vought does not contend that XL is the active underwriter, the Binder does not show that XL was acting as an agent or that it disclosed its principal.

Moreover, in response to an interrogatory that asked that defendants "[i]dentify each Underwriting Entity on the Policy," they listed Syndicate 1209 and XL as a "Syndicate Owner." P. Oct. 9, 2009 App. 240. This response creates a genuine issue of material fact about whether XL was merely an agent acting for a disclosed principal, an agent acting for an undisclosed principal, or perhaps itself a principal. Accordingly, XL's alternative motion for summary judgment is denied.

XIII

Vought moves to exclude certain evidence on which defendants rely in support of their summary judgment motion and to strike defendant's affirmative defense of ambiguity.

A

The court turns first to Vought's motion to exclude evidence. Vought challenges evidence that consists of statements by various employees of Vought, Falvey, and Marsh directly or indirectly indicating their understanding of the Policy's coverage. Vought contends that this is parol evidence about the meaning of the Policy; the evidence is only admissible to support a defense of ambiguity; and defendants failed to plead this affirmative defense in their answer or elsewhere, as required by Texas law.[FN38] Vought maintains that, because***847** defendants' ambiguity argument must be stricken, the parol evidence must be excluded. Alternatively, Vought argues that if the court holds that the Policy is ambiguous, the meaning of the Policy is a fact issue, and the court cannot consider the parol evidence to grant summary judgment. Vought also contends that defendants' parol evidence is not properly authenticated, and that portions of it constitute evidence of subsequent remedial measures that is inadmissible under Fed.R.Evid. 407.

> FN38. Both sides maintain that the Policy is unambiguous. Defendants argue in the alternative that, if the Policy is ambiguous, the court should not employ the rule of construction favoring the insured, but should instead rely on parol evidence to interpret the Policy.

Defendants respond that whether a policy is ambiguous is a matter of law for the court to determine; they need not have previously pleaded ambiguity for the court to hold that the Policy is ambiguous; the evidence is relevant to Vought's bad faith and unjust enrichment claims; some of the evidence is admissible as a party admission; the evidence is properly authenticated (it consists of deposition testimony or documents attested to by deposition witnesses); and changes to Policy terms are only a subsequent remedial measure where the change is made by the insurer.

B

[33][34] Fed.R.Civ.P. 8(c) requires that a party specifically plead an affirmative defense.

Rule 8(c) contains a nonexclusive list of affirmative defenses that does not include ambiguity. Under Texas law, however, ambiguity is an affirmative defense that must be pleaded. *See Old Republic Sur. Co. v. Palmer,* 5 S.W.3d 357, 360 (Tex.App.1999, no pet.). Even in a diversity case, however, interpretation of a contract is a matter of law, and the court can conclude that a contract is ambiguous even when no party pleads ambiguity. *See Recursion Software,* 425 F.Supp.2d at 785 (quoting *In re Newell Indus., Inc.,* 336 F.3d 446, 449 n. 5 (5th Cir.2003)); *Dyll v. Adams,* No. 3:91–CV–2734–D, slip op. at 3 & n. 2 (N.D.Tex. Sept. 30, 1996) (Fitzwater, J.) ("This procedural requirement of Texas law does not preclude the court from concluding that the release is ambiguous. It is well-settled that state procedural law does not bind a federal court when it sits in a diversity case."), *aff'd in part, rev'd in part on other grounds,* 167 F.3d 945 (5th Cir.1999).

[35][36] The court has held above, *see supra* § V(C), that the Machinery Clause is ambiguous concerning whether covered "other necessary charges" include overhead of some type, including some or all of the overhead for which Vought sues in connection with repairing the damaged stabilizer, and is ambiguous concerning whether the Expediting Cost Clause covers expediting costs. Therefore, parol evidence is admissible to determine the meaning of the Policy. *See, e.g., Nautilus Ins. Co. v. Nicky & Claire's Day Care, Inc.,* 630 F.Supp.2d 727, 734 (W.D.Tex.2009).[FN39] The court accordingly denies Vought's motion to exclude based on the contention that defendants failed to plead the affirmative defense of ambiguity.

> FN39. Parol evidence is admissible after concluding that a contract is ambiguous, but such evidence cannot be admitted to determine whether the contract is ambiguous. *See Nautilus Ins.,* 630 F.Supp.2d at 734. In determining whether the Machinery Clause is ambiguous concerning overhead costs, the court has not considered parol evidence.

C

The court also declines to exclude the evidence as unauthenticated or as evidence of a subsequent remedial measure. The requirement of authentication is satisfied by evidence sufficient to support a finding that the evidence in question is what its ***848** proponent claims. *See* Fed.R.Evid. 901(a). The evidence in question meets the authentication standard. Rule 407 renders inadmissible evidence of remedial measures taken after an injury or harm allegedly caused by an event. Vought argues that this rule applies to changes Vought made to its insurance policies after Falvey denied Vought's claim. But here, the disputed proof is parol evidence about the meaning of the Policy. The court has not relied on parol evidence to determine whether the Policy is ambiguous. Although parol evidence can be relied on to interpret the Policy, the court has not attempted to resolve the ambiguity in the Policy. Therefore, the court denies the motion to exclude.[FN40]

> FN40. The court has not considered how Rule 407 affects, if it does, the admissibility of defendants' evidence at trial. That decision must await consideration of the evidence to be offered at trial.

XIV

Defendants move for leave to file a supplemental appendix. Because consideration of the

evidence in the appendix would not alter the reasoning or results of this memorandum opinion and order, the motion is denied as moot.

* * *

For the foregoing reasons, Vought's October 9, 2009 motion for partial summary judgment is denied. The October 10, 2009 motion for summary judgment of Falvey, Dornoch, and XL is granted in part and denied in part. Vought's November 6, 2009 motion to exclude evidence and to strike affirmative defense of ambiguity is denied. And defendants' December 7, 2009 motion for leave to file supplemental appendix is denied as moot.

SO ORDERED.

N.D.Tex.,2010.
Vought Aircraft Industries, Inc. v. Falvey Cargo Underwriting, LTD.
729 F.Supp.2d 814

END OF DOCUMENT

The Additional Insured Book

Seventh Edition

Donald S. Malecki, CPCU

Jack P. Gibson, CPCU, CRIS, ARM

International Risk Management Institute, Inc.
Dallas, Texas

COMMERCIAL GENERAL LIABILITY
CG 20 38 04 13

THIS ENDORSEMENT CHANGES THE POLICY. PLEASE READ IT CAREFULLY.

ADDITIONAL INSURED – OWNERS, LESSEES OR CONTRACTORS – AUTOMATIC STATUS FOR OTHER PARTIES WHEN REQUIRED IN WRITTEN CONSTRUCTION AGREEMENT

This endorsement modifies insurance provided under the following:

COMMERCIAL GENERAL LIABILITY COVERAGE PART

A. **Section II – Who Is An Insured** is amended to include as an additional insured:

1. Any person or organization for whom you are performing operations when you and such person or organization have agreed in writing in a contract or agreement that such person or organization be added as an additional insured on your policy; and
2. Any other person or organization you are required to add as an additional insured under the contract or agreement described in Paragraph **1.** above.

Such person(s) or organization(s) is an additional insured only with respect to liability for "bodily injury", "property damage" or "personal and advertising injury" caused, in whole or in part, by:

a. Your acts or omissions; or
b. The acts or omissions of those acting on your behalf;

in the performance of your ongoing operations for the additional insured.

However, the insurance afforded to such additional insured described above:

a. Only applies to the extent permitted by law; and
b. Will not be broader than that which you are required by the contract or agreement to provide for such additional insured.

A person's or organization's status as an additional insured under this endorsement ends when your operations for the person or organization described in Paragraph **1.** above are completed.

B. With respect to the insurance afforded to these additional insureds, the following additional exclusions apply:

This insurance does not apply to:

1. "Bodily injury", "property damage" or "personal and advertising injury" arising out of the rendering of, or the failure to render, any professional architectural, engineering or surveying services, including:
   a. The preparing, approving, or failing to prepare or approve, maps, shop drawings, opinions, reports, surveys, field orders, change orders or drawings and specifications; or
   b. Supervisory, inspection, architectural or engineering activities.

This exclusion applies even if the claims against any insured allege negligence or other wrongdoing in the supervision, hiring, employment, training or monitoring of others by that insured, if the "occurrence" which caused the "bodily injury" or "property damage", or the offense which caused the "personal and advertising injury", involved the rendering of, or the failure to render, any professional architectural, engineering or surveying services.

2. "Bodily injury" or "property damage" occurring after:
   a. All work, including materials, parts or equipment furnished in connection with such work, on the project (other than service, maintenance or repairs) to be performed by or on behalf of the additional insured(s) at the location of the covered operations has been completed; or

ADDITIONAL INSURED – OWNERS, LESSEES OR CONTRACTORS – AUTOMATIC STATUS FOR OTHER PARTIES WHEN REQUIRED IN WRITTEN CONSTRUCTION AGREEMENT (cont.)

b. That portion of "your work" out of which the injury or damage arises has been put to its intended use by any person or organization other than another contractor or subcontractor engaged in performing operations for a principal as a part of the same project.

C. With respect to the insurance afforded to these additional insureds, the following is added to **Section III – Limits Of Insurance:**

The most we will pay on behalf of the additional insured is the amount of insurance:

1. Required by the contract or agreement described in Paragraph **A.1.**; or

2. Available under the applicable Limits of Insurance shown in the Declarations;

whichever is less.

This endorsement shall not increase the applicable Limits of Insurance shown in the Declarations.

THE

LAW OF INSURANCE,

AS APPLIED TO

FIRE, LIFE, ACCIDENT, GUARANTEE,

AND

OTHER NON-MARITIME RISKS.

BY

JOHN WILDER MAY.

BOSTON:
LITTLE, BROWN, AND COMPANY.
1873.

explain their ambiguity, or unless the context evidently points out that they must, in the particular instance, and in order to effectuate the immediate intention of the parties, be understood in some special and peculiar sense.[1]

A policy of insurance is a contract, and is to be governed by the same principles as govern other contracts. When it is said that a contract of insurance is a contract *uberrimæ fidei*, this only means that the good faith, which is the basis of all contracts, is more especially required in that species of contract in which one of the parties to the contract is necessarily less acquainted with the details of the subject of the contract than the other.[2] Its language, says Nelson, C. J.,[3] "is to receive a reasonable interpretation; its intent and substance, as derived from the language used, should be regarded. There is no more reason for claiming a strict literal compliance with its terms than in ordinary contracts. Full legal effect should always be given to it for the purpose of guarding the company against fraud and imposture. Beyond this, we would be sacrificing substance to form, — following words rather than ideas." Indeed, a moment's reflection will render it apparent that there is nothing in an agreement about insurance intrinsically more sacred or inviolable than in an agreement about any other subject-matter.

§ 174. **The Contract will be construed liberally in favor of the Object to be accomplished.** — It was early held, with special reference to contracts of marine insurance, that the *strictum jus* or *apex juris* is not to be laid hold on, but they are to be construed largely for the benefit of trade and for the insured,[4] — a rule which, under different forms of expression, has obtained with reference to all kinds of insurance to the present day. Having indemnity for its object, the contract is to be construed

[1] Per Lord Ellenborough, Robertson *v.* French, 4 East, 135. And see *post*, § 179.

[2] Lord Abinger, C. B., in Cornfoot *v.* Fowke, 6 Mees. & Wels. 358, in reply to the suggestion of Sir Frederic Thesiger, *arguendo*, on a question of representation that a greater degree of good faith is required in contracts of insurance than in others.

[3] Turley *v.* North Am. Fire Ins. Co., 25 Wend. 374.

[4] Tiernay *v.* Ethrington, 1 Burr. 341.

liberally to that end, and it is presumably the intention of the insurer that the insured shall understand that in case of loss he is to be protected to the full extent which any fair interpretation will give.[1] The spirit of the rule is, that where two interpretations equally fair may be given, that which gives the greater indemnity shall prevail. And to the same spirit is due the rule that conditions and provisos will be strictly construed against the insurers because they have for their object to limit the scope and defeat the purpose of the principal contract;[2] and apparently contradictory clauses will be so construed if possible as to reconcile them with each other, and to give to each its due force in furtherance of the main purpose of the contract.[3] Of course the different provisions of the contract must be so construed, if possible, as to give effect to each. If, therefore, the natural and obvious interpretation of one would render it nugatory, or bring it into conflict with another, while a different interpretation would reconcile the two, and give force and effect to both, the latter is to be adopted. So if the natural interpretation, looking to the other provisions of the contract, and to its general object and scope, would lead to an absurd or unreasonable conclusion, as such a result cannot be presumed to have been within the intention of the parties, such interpretation must be abandoned, and that adopted which will be more consistent with reason and probability.

§ 175. **Language taken most strongly against those for whose Benefit it is.** — No rule, in the interpretation of a policy, is more fully established, or more imperative and controlling, than that which declares that, in all cases, it must be liberally construed in favor of the insured, so as not to defeat without a plain necessity his claim to the indemnity, which in making the insurance it was his object to secure. When the words are, without violence, susceptible of two interpretations, that which will sustain his claim and cover the loss must, in pref-

[1] Dow *v.* Hope Ins. Co., 1 Hall (N. Y. Superior Ct.), 174.
[2] Hoffman *v.* Ætna Fire Ins. Co., 32 N. Y. 405.
[3] Merchants' Ins. Co. *v.* Edmond, 17 Gratt. (Va.) 138.

erence, be adopted.[1] While courts will extend all reasonable protection to insurers, by allowing them to hedge themselves about by conditions intended to guard against fraud, carelessness, want of interest, and the like, they will nevertheless enforce the salutary rule of construction, that as the language of the conditions is theirs, and it is therefore in their power to provide for every proper care, it is to be construed most favorably to the insured.[2] Thus, if a stipulation be ambiguous, and no light can be thrown upon it in accordance with the received principles of law, from extrinsic evidence, the doubt is to be resolved against the party by whom and in whose favor the stipulation is made. The words of a promise, with its exceptions and qualifications, are to be considered as those of the promisor, while those of a representation on which the promise is founded are the words of the promisee. If a question be equivocal, so that it is susceptible of being answered in more than one way, and differently from different points of view, it will not be open to the company which prepares the question to object that it is not answered in the true sense.[3] Thus the question whether one has suffered any serious injury might be answered in the affirmative if regarded in the light of the severity of the suffering, and temporary inconvenience occasioned at the time. But looked at afterwards, and after a permanent and complete recovery, it may well be answered in the negative, so far as the injury is material to the question of the value of a life risk.[4] So an incidental communication from the insurer to the insured will be deemed to contain not only all the language expresses, but all that can be fairly deducible therefrom in the light of the circumstances under which it is made. Thus if notice of additional insurance and an approval in writing by the insurers be required, an acknowledgment in writing that notice has been received,

[1] Westfall *v.* Hudson River Fire Ins. Co., 2 Duer (N. Y. Superior Ct.), 490.

[2] Cropper *v.* Western Ins. Co., 32 Penn. St. 351.

[3] Cropper *v.* Western Ins. Co., 32 Penn. St. 351; Wilson *v.* Hampden Fire Ins. Co., 4 R. I. 150; Ætna Ins. Co. *v.* Jackson, 16 B. Mon. (Ky.) 242; Bartlett *v.* Union Mut. Fire Ins. Co., 46 Me. 500; Wilson *v.* Conway Ins. Co., 4 R. I. 141.

[4] Union Mut. Ins. Co. *v.* Wilkinson, 13 Wall. (U. S.) 222.

without more, will be deemed an approval.[1] So words of exception, if of doubtful import, are to be construed most strongly against the party in whose interest they are introduced.[2]

§ 176. An instance of the application of the doctrine that where there is any ambiguity in a policy it must be taken most strongly against the party who prepares it, is well illustrated in a comparatively recent case. The proposal or declaration is made the basis of the contract and part of the policy, affirms that its particular statements are "correct and true throughout," and stipulates that if it shall hereafter appear that any fraudulent concealment or designedly untrue statement is made, the policy shall be void. It was contended by the insurers that by this language the policy was to be void not only upon an untrue statement designedly made, but also upon an untrue statement honestly made. But the court replied that upon that construction the clause which relates to designedly untrue statements would be superfluous, because only a reiteration of that which is involved in the former clause requiring the particulars to be correct and true. But in construing an instrument prepared by the insurers, it ought to be read most strongly against the makers, and inasmuch as, upon the construction contended for, the latter clause would be wholly unnecessary, it should rather be construed as merely explanatory of what is meant by the terms "correct" and "true" in the former clause.[3]

§ 177. **Written over printed Words prevail.** — As in all contracts consisting partly of printed matter and partly of written, so with contracts of insurance, where any discrepancy or repugnancy exists, the written portion is to prevail over the printed, for the obvious reason that as the latter contains the more general and formal provisions applicable for the most part to all cases, there is more ground for supposing that these

[1] Potter *v.* Ontario and Liv. Mut. Ins. Co., 5 Hill (N. Y.), 147; Robertson *v.* French, 4 East, 135.

[2] Palmer *v.* Warren Ins. Co., 1 Story (U. S. C. Ct.), 360; Blackett *v.* Royal Ex. Ins. Co., 2 Cromp. & Jer. 244.

[3] Fowkes *v.* Manchester and London Life Ass. Association, 3 Best & Smith, Q. B. 917; s. c. E. C. L. 113, 917.

A TREATISE

ON

THE LAW OF FIRE INSURANCE

ADAPTED TO THE PRESENT STATE OF THE LAW,

ENGLISH AND AMERICAN.

WITH

COPIOUS NOTES AND ILLUSTRATIONS.

IN TWO VOLUMES.

VOL. I.

By H. G. WOOD,

AUTHOR OF "THE LAW OF NUISANCES," "THE LAW OF MASTER AND SERVANT," ETC., ETC.

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Construction of policies.

SEC. 58. The legal maxim *benignae faciende sunt interpretationes propter implicitatem laicorum ut res magis valeat quam pereat; et verba intentione, non e contra, debent insevire*, is as applicable in the interpretation of policies of insurance as of other written instruments, and the courts are inclined to construe them liberally, and so as to carry out and effectuate the real, true intention of the parties thereto.[1]

Every part of the instrument will be made operative and effective, if possible, but, if it is evident that one part of the instrument expresses *the real intent* of the parties, and another part of it *is inconsistent therewith*, the part which is inconsistent with the intention of the parties must be rejected and yield to that part of it which will effectuate their real purpose. Thus, where the written and printed portions of a policy conflict, effect is given to the *written* portion of it, because, being incorporated into the contract *at the time when it was made*, it is presumed that it expresses the actual agreement made, and that the parties intended thereby to override that portion of the contract expressed in type, which is inconsistent therewith.[2] The maxim, *quando res non valit ut ago, valeat quantum valere potest* applies, and the courts will look to the *intent* of the parties and effectuate it in some form, if possible, and, if necessary to do so, will reject that which is inconsistent.[3] But, if there is no *real* inconsistency, and the evident intent of the parties can be effectuated by interpreting the instrument as a whole, that is, by

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[1] *Riggin* v. *Patapsco Ins. Co.*, 7 H. & J. (Md.) 279; *Crauisllat* v. *Bull*, 8 Yeates (Penn.) 375. The rule that ambiguous language must be construed against the insurer, was applied to a clause in the policy of reinsurance as follows: "This insurance to be on the excess which the T. insurance company may have on all their policies on cotton, sugar, and molasses, issued at their office in New Orleans, or at their Shreveport agency, to wit, on the excess of $10,000 on boats from places on the Mississippi River, but said excess not to exceed $5,000 by any one boat;" and it was held that the words "on boats" indicated that more than the freight was included. *Teutonia Ins. Co.* v. *Boylston Mut. Ins. Co.*, 20 Fed. Rep. 148.

[2] *Nicoll* v. *American Ins. Co.*, 3 W. & M.(U. S.) 529.

[3] *Maugher* v. *Holyoke Ins. Co.*, 1 Holmes (U. S. C. C.) 289. In *Bowman* v. *Pacific Ins. Co.*, 27 Mo. 15, the policy contained stipulations that "if there shall be kept or stored therein any articles denominated hazardous or extra hazardous, or included in the memorandum of special rates, so long as the same shall be appropriated, these presents shall cease;" also: "No greater amount than 25 pounds of gunpowder shall be placed at any time in the building described in this policy." Insured kept from four to six pounds of powder in his store. Gunpowder was included in the memorandum of special rates. It was held that the two clauses will harmonize if one be understood as modifying the other; the general was to be controlled by the special clause, for, to give a preponderating importance to the general provision would interpolate a material qualification upon the special clause; that keeping less than 25 lbs of powder did not affect the right of the insured to recover.

retaining both the written and printed portions thereof, effect will be given to the whole.[1] One of the golden rules of interpretation was well expressed by Lord HALE.[2]: "*The judges*," said he, "*ought to be curious and subtle to invent reasons and means to make acts effectual according to the just intent of the parties; they will not therefore cavil about the propriety of words, when the intent of the parties appears, but will rather apply the words to fulfil the intent, than destroy the intent, by reason of the insufficiency of the words.*" The language of a policy is to be construed according to its natural meaning, its ordinary and usual signification, except where such construction would render the words used, senseless, or it is evident from the general scope and intent of the instrument that the words were used in some other sense. *In all cases the words of a policy are to be taken most strongly against the insurer.* The maxim *verba chartarum fortius accipintur contra proferentum*, is rigidly enforced in all cases where other rules of construction fail. This is upon the theory that, as the insurer makes the policy, and selects his own language, he is presumed to have employed that which expresses his real intention and the actual contract entered into, and has left nothing to be inferred or supplied by reference to extraneous matters.[3] But this does not permit either party to show how they understood the contract. The court is to construe the instrument *from the language used*, and so far as there is any inconsistency, give to it a construction most favorable to the assured. It was well said by the court in a Kentucky case,[4] "there is no principle of law which allows the understanding of one of the parties to determine the meaning of the contract. The rule is sometimes applied in cases of ambiguity, that words are to be construed most strongly against the party using them. That is founded upon a principal of common honesty and good faith, that, when a promise or stipulation is susceptible of two meanings, it should be construed and effectuated in that sense *in which the party making it knew, or had reason to believe it was understood and received by the other party.*" Thus, in a case in New York,[5] the defendants issued a

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[1] *Stacey* v. *Franklin Fire Ins. Co.*, 2 W. & S. (Penn.) 44.

[2] *Crossing* v. *Scudamore*, 2 Lev. 9; *Brink* v. *Merchants' Ins. Co.*, 49 Vt., 442.

[3] *Palmer* v. *Warren Ins. Co.*, 1 Story (U. S.) 360; *Nicoll* v. *The American Ins. Co.*, *ante*, *Ins. Co.* v. *Wright*, 1 Wall. (U. S.) 529.

[4] *Montgomery* v. *Fireman's Ins. Co.*, 16 B. Mon. (Ky. 427.

[5] *Marco* v. *Liv., Lon, & Globe Ins. Co.* 35 N. Y. 664.

policy to the plaintiff upon "a stock of goods" in a certain building. Subsequently the goods were removed to another building, and the insurer indorsed thereon, "*This policy is transferred to the frame building* owned by Marco on the east side of Whitehall street." The defendants claimed that thereby the policy was applied to the *frame building*, and did not cover the stock. But the court held that the indorsement must be construed in view of the circumstances, and according to the *intent* of the parties, and as the plaintiff had a right to understand it.

Where a policy referred to the goods as "stored in" a certain warehouse, but provided that "if the interest of the assured . . . be any other than the . . . sole ownership of the property . . . it must be so expressed in the policy," and there was no such expression, it was held, that the policy did not cover goods not the assured's own stored in the warehouse.[1]

But where the terms of a policy are susceptible, without violence, of two interpretations, that construction most favorable to the insured should be adopted. Thus in a Pennsylvania case the policy providing that, in case of loss, the company should pay to the mortgagee "such proportion of the sum insured as the damages by fire to the premises mortgaged or charged shall bear to the value immediately before the fire," it was held that the words "premises mortgaged" should be construed to mean so much of the mortgaged premises as was insured at the time of the fire; in this case, the value of the building insured, and not merely the proportion of the sum insured, which the value of the building bore to the value of the whole lot mortgaged, with the building thereon.[2]

So where a policy insured a stock of music and musical instruments, "his own or held by him in trust or on commission." It also provided that goods held on storage must be separately and specifically insured. The insured received a piano from the owner to be forwarded to another city for repairs. It was held, that the piano was covered by the policy to the extent of its value.[3]

So where a policy insured two barns and certain articles "contained therein," and also a horse "in barn or in fields," it was held that the horse was insured, though in a barn not one of those specified.[4]

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[1] *Fuller* v. *Phœnix Ins. Co.* 61 Iowa, 350.

[2] *Teutonia Fire Ins. Co.* v. *Mund*, 102 Pa. St. 89.

[3] *Lucas* v. *Liverpool & London & Globe Ins. Co.*, 23 W. Va. 258; 48. Am. Rep. 383.

[4] *Trade Ins. Co.* v. *Barrcliff*, 45 N. J. L. 543.

All the stipulations in a policy, both printed and written, are to be given effect, if it can be done without defeating the written stipulations. If it cannot be done, then the written stipulation is to prevail.[1] If the words written in the policy, have received a judicial construction, and also a peculiar commercial construction by usage, variant with such judicial construction, the judicial construction is to control,[2] but if no judicial construction has been given to them, and by usage they have acquired any meaning variant from that in which they are ordinarily used, such meaning by usage may be shown, unless from the whole instrument it is evident that they were used in their ordinary sense.[3] Thus, in the case cited from Massachusetts, to an inquiry in an application for insurance upon a manufactory, "are there casks of water in each loft kept *constantly* full?" the answer was, "there are casks of water in each room, kept constantly full," and the court held that evidence was admissible to show that, in the general use of language among manufacturers, the whole of a loft or story, appropriated to a particular department, was called "one room," although the same was divided by partitions with doors; and that the meaning of the word "room," and whether there was any such general use of language, were questions for the jury and not for the court; also, *that if such use of the word "room" was general among manufacturers, it need not be known and general among insurers, in order to effect a contract of insurance upon manufacturing property;* for the insurers must be presumed to have so understood it, when they insured such property."[4]

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[1] *Goss* v. *Citizen's Ins. Co.*, 18 La. An. 97; *Bargett* v. *Orient Ins. Co.*, 3 Bos. (N. Y.) 385. In *Lettiner* v. *Granite Ins. Co.*, 5 Duer (N. Y.) 394, the court says that no part of the words of a policy are to be rejected as insensible or inoperative, if a rational or intelligible meaning can be given to them consistent with the general design and object of the whole instrument.

[2] *Bargett* v. *Orient, etc., Ins. Co.*, 3 Bos. (N. Y.) 385.

[3] *Daniels* v. *Hud. Riv. Ins. Co.*, 12 Cush. (Mass.) 416; *Mobile, etc., Ins. Co.* v. *McMillan*, 27 Ala. 77.

[4] In *Whitmarsh* v. *Conway Ins. Co.*, 16 Gray (Mass.), 657 it was held that evidence of a well-settled custom, by which the words of a policy covering "store fixtures" are applied *to all furniture in the store*, whether fixed or movable, necessary or convenient for use in the course of trade, was admissible. "If," said CHAPMAN, J., "the term *store fixtures* is a term of trade, commonly used among traders and insurers, and is used in such a signification as to include any or all the articles mentioned as such in the report, those were insured by this policy. The parol evidence on this subject was proper and admissible."

In a case before the United States Circuit Court for New Hampshire in 1883 in *Thurston* v. *Union Ins. Co.*, 17 Fed. Rep. 127, 28. Alb. C. J., 490, the policy covering a building expressly excepted from its operation "store fixtures" and the question in the case was what articles under the head even outside the protection of the policy

In construing the language of a policy its ordinary and usual import will be given to it unless it is shown that certain words have as usage acquired a peculiar meaning, or unless its technical meaning is so universally understood that it may be presumed that it was intended in its technical sense. Thus in an action on an insurance policy upon "electrotype, stereotype and steel plates and cuts," belonging to plaintiffs, who were a firm of book publishers, there were certain brass plates which, it was claimed by plaintiffs, were included in the policy under the name "cuts," because they were embraced in the natural and ordinary meaning of that word, as defined in the dictionaries, and used in the common speech of people. The defendant contended that the word "cuts" was understood among book publishers, engravers and all other persons who used dies and cuts, to include only wood-cuts and steel-engravings and plates, and did not include the articles in question; and gave evidence to that effect. The defendant at the

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LOWELL, J., said: There is no doubt that an exception of fixtures out of a policy upon buildings refers to things which are, under some circumstances, removable, and not necessarily and always a part of the buildings. If we could suppose a printed exception in a policy to be intended to adapt itself to the various relations of landlord and tenant, mortgagor and mortgagee, heir and executor, so that fixtures refer to what may be removed in the particular case, all the disputed items in this case would be within the policies, because they are undoubtedly irremovable, as between the plaintiff and the mortgagee. But if these same things had been affixed by a tenant, there is no doubt that he might remove them during his term. Such a shifting construction would be unreasonable. We must look for a meaning of "store fixtures" which has a more general application. And I find it in the context and the popular meaning of the words. I hold it to mean, in this connection, store fittings or fixed furniture, which are peculiarly adapted to make a room a store, rather than something else. It is plain that "store fixtures" does not refer to the fixtures of the shoe factory, for the written part of the policies distinguishes the stores from the factory, and so does the common use of the words. Store is the American word for shop or warehouse, and is never applied to a factory. The words "store fixtures" are construed in *Whitmarsh* v. *Conway Fire Ins. Co.* 16 Gray, (Mass) 359, though that case is not of special importance in deciding this case.

For the convenience of counsel I number the items in a copy of the referee's report which I place on file. And first I will say what items I find to be covered by all the policies. These are items 1 and 2, which were admitted by the defendants' counsel to be within the contract; they are the walls, roofs, floors, partitions, doors, and windows, including the show windows which last had not plate-glass of the prohibited size. 11. Boiler fixtures in boiler-room. The boiler cannot be removed without taking down part of the boiler-house, and is used, among other things, to heat the building. 13. Elevator machinery, which in recent usage is as much a part of the house as are the stairs. 14. Steam piping, radiators, and iron tanks, which both from their mode of annexation and their use, which is equally applicable to a dwelling-house, a factory, or a shop, are part of the building. 16. Gas piping, for similar reasons. 10. Speaking tube, for similar reasons. I exclude from all the policies, items 6, wooden tank; 17, gas-fixtures, which are chattels—the former by its construction, the latter by usage. Also as "store fixtures," 3, 4, and 5—shelving and counters in the stores, and shelving and basin in the barber's shop.

For all items not above excluded the three companies are liable. The fourth, or Howard Company, by my construction, escapes by virtue of "or other" from the fixtures of the shoe factory, which are items 7, 8, 9, 12, 15, and 18.

I believe I have mentioned every item, and that the parties can assess the damages against each company without difficulty, in accordance with this opinion."

trial asked for this instruction, that if the jury should find that the word "cuts" had among book publishers a technical meaning universally so understood among book publishers and the makers and users of cuts and dies, they might presume that the word was used in that sense in the policy. The court refused to give this instruction, but instructed thus: "Words are to be understood in their plain, ordinary and popular sense, unless they have in respect to the subject-matter, as by the known usage of trade or the like, acquired a particular sense, distinct from the popular sense of the same words. Where a word has both a popular and a technical sense, or where it has several different meanings, it is a question of fact for the jury to determine, from the subject-matter, the contract, the character of the contracting parties, or the nature of the contract and all the surrounding circumstances, in which sense the word was used by the contracting parties." It was held that the defendant was entitled to the instruction asked.[1]

If there is any doubt, in view of the general tenor of an instrument of writing, whether the words used therein are to be taken in an enlarged or restricted sense, all other things being equal, that construction should be taken which is most beneficial to the promisee. This rule of construction is especially applicable to the construction of policies of insurance; the provisions and conditions of which are, as admitted in the argument, prepared by the assurers themselves, and their advisers, persons thoroughly conversant with the principles and practice of insurance, with the utmost deliberation, "every word being weighed, and every contingency debated," and thus prepared are executed and delivered to the assured, who ordinarily have no part in their preparation. If an exception in a policy be capable of two interpretations, equally reasonable, that must be adopted which is most favorable to the assured, for the language is that of the assurer.[2] No rule in the interpretation of a policy is more fully established, or more imperative and controlling, than that which declares, that in all cases it must be liberally

[1] *Houghton* v. *Watertown F. Ins. Co.* The rule of law in relation to the construction of contracts is correctly stated in *Daniel* v. *Hudson River Iron Co.*, 12 Cush. 499. See also *Whitmarsh* v. *Conway Ins., Co.*, 16 Gray (Mass) 359. Upon this subject, the decisions of courts in various, jurisdictions seem to be uniform, and to result in this. That the jury should be instructed that when words have acquired an exact and technical meaning in any trade or business, and are used in a contract relating to such trade or business, *prima facie* they are to be construed in the meaning or sense which they have acquired in that business.

[2] *Western Ins. Co.*, v. Cropper 32. Penn St. 357. *Ins. Co.* v. *Berger*, et. al. 42 Penn. St. 292; *Insurance Co.* v. *O'Malley*, 97 Penn. St. 400; *Hoffman* v. *Ætna Ins. Co.*, 32 N. Y 405.

construed in favor of the insured, so as not to defeat, without a plain necessity, his claim to the indemnity, which in making the insurance it was his object to secure. When the words are without violence susceptible of two interpretations, that which will sustain his claim and cover the loss must in preference be adopted. Another rule of construction equally well known, is that the words of an agreement are to be applied to the subject-matter, about which the parties are contracting at the time. The matter in hand is always presumed to be in the minds and thoughts of the speaker, though his words seem to admit of a larger sense, and therefore the generality of words used shall be restrained by the particular occasion. Words should not be taken in their broadest import when they are equally appropriate in a sense limited to the object the parties had in view. "All words," says LORD BACON, "whether they be in deeds or in statutes, or otherwise, if they be general, and not express and precise, shall be restrained unto the fitness of the matter and the person."[1] Indemnity is the real object and purpose of all insurance; that is what the assured bargains for, and what the assurer intends to provide. The predominant intention of the parties in a contract of insurance is indemnity, and this is to be kept in view and favored in putting a construction upon a policy.[2] Having indemnity for its object, the contract is to be construed liberally to that end, and it is presumedly the intention of the insurer that the insured shall understand, that in case of loss, he is to be protected to the full extent which any fair interpretation will give.[3] The spirit of the rule is, that when two interpretations, equally fair, may be given, that which gives the greater indemnity shall prevail. Therefore where there was a provision in a policy that in case of loss the company should pay to the mortgagee "such proportion of the sum insured as the damages by fire to the premises mortgaged or charged shall bear to the value immediately before the fire," it was held that the words "premises mortgaged" should be construed to mean so much of the mortgaged premises as was insured at the time of the fire. That is the value of the building insured, and not merely the proportion of the sum insured, which the value of the building

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[1] *Bacon Law Max.* Reg. 10.

[2] *Philips Ins.*, § 124.

[3] *Dow* v. *Hope Ins. Co.*, 1 Hall (N. Y.), 174; *Riggin* v. *Patapsco Ins. Co.*, 7 H. & J. (Md.) 279.

ore to the value of the whole lot mortgaged with the buildings hereon.[1]

An indorsement upon a policy, so far as it contravenes any provision of the policy itself, controls although the policy is under seal and the endorsement is not. Thus an endorsement not under seal signed by the proper officer of the company, "a permission is hereby granted to assured to remove the personal property insured within to the property now occupied by him, and insured to J. S. by policy No. 832." One of the conditions annexed to and made a part of the policy provided that "insurance on contents of buildings shall be taken to include every species of personal property therein." The assured having sued the company in covenant to recover for a loss; on demurrer, it was held that the risk which the policy covered as respects the property in question, continued only so long as it remained in the buildings in which it was at the time the policy was issued; and the plaintiff, therefore, had no cause of action against the company for this loss, except by virtue of the permission indorsed upon the policy. And that as there was no provision in the policy authorizing the indorsement of the permission to remove the property from the original buildings, said indorsement was a new and distinct contract by parol, upon which the action of covenant would not lie.[2] The consideration for the insurance named in the policy was single and entire. The amount of insurance was a gross sum, apportioned upon several distinct items of property, as specified in the policy. It was held that the contract of insurance was an entirety, the sole effect of the apportionment being to limit the extent of the insurer's risk, as to each item, to the sum so specified, and when such a policy contains a stipulation avoiding it in case the insured mortgages the property without notifying the secretary, a mortgage of a portion only of the property insured, without such notice, avoids the whole policy.[3]

In an application for a policy of fire-insurance were these questions and answers: "What is your title to the property? Contract." "How much insured in other companies? None." In an action upon the policy. It was held that the fair interpretation of the questions and answers was that plaintiff held the property by a contract for the purchase thereof, and had himself no other

[1] *Teutonia Ins. Co.*, v. Mund 102. Penn St. 89.
[2] *Shertzer* v. *Mut Fire Ins. Co.*, 46 Md. 506.
[3] *Plath* v. *Farmers, &c. F. Ins. Assoc.*, 23 Minn. 479.

insurance; and that the fact that plaintiff's vender had an insurance upon his interest did not constitute a breach of warranty. Plaintiff signed a blank form of application, which was filled up by the defendant's agent without any knowledge or dictation from plaintiff; there were false answers and statements therein occasioned by the carelessness, mistake, or inadvertence of the agent. The policy contained a clause that he who procured the insurance should be held by contract to be plaintiff's agent; also a condition that the application must be made out by defendant's authorized agent. It was held that there was no warranty binding upon plaintiff, and consequently no breach.[1]

Conditions in policies. Classification of hazards, effect of.

SEC. 58. As has previously been stated, it is competent for the insurer to prescribe the terms and conditions upon which he will assume a risk, and, so long as those conditions are not in violation of law, or contrary to public policy, they are binding and obligatory upon the assured, and any violation thereof by him, releases the insurer from liability, whether the loss resulted from such violation or not.[2] Thus, the insurer may decide what risks are *hazardous, extra hazardous or especially hazardous*, and what are not so, and if they are named and specified in the policy, and prohibited therein, a violation of the condition avoids the policy, even though in fact such articles or use are not hazardous. The question is not open, whether the hazards of the risk are increased thereby or not. The insurer, by electing to regard it so, and having so declared it in the policy, has precluded all inquiry in that direction, and, if the keeping of ice or water upon the premises was specified as hazardous, the keeping of either, without permission, would avoid the policy as much as the keeping of gunpowder or nitro-glycerine.[3]

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[1] *Sprague* v. *Holland Purchase Ins. Co.*, 69 N. Y. 128.

[2] *Wood* v. *Hartford Ins. Co.*, 13 Conn. 533.

[3] Mr. MARSHALL, in his work on Insurance, 249, says: "It is quite immaterial for what purpose or with what view it is made; or whether the assured had any view at all in making it; unless there has been a literal compliance, the assured can derive no benefit from the policy." On p. 251, he says: "It is also immaterial to what cause the non-compliance is attributable, *for if it be not in fact complied with, although perhaps for the best reasons*, the policy is void. In *Faulkner* v. *Central F. Ins. Co.*, 1 Kerr (N. B.) 279, the plaintiff took out a policy upon goods, which contained a provision that, if there should at any time be more than twenty-five pounds' weight of gunpowder on the premises insured, or where any goods are insured, such insurance should be void, and no benefit derived therefrom. To an action for a loss under the policy, the defendant plead a breach of this condition, and the plaintiff replied *that the powder was put there without his privity, because a vessel in which it was intended to ship it had sailed without it*; and that *he had used every exertion*

Ambiguous conditions. Repugnant stipulations, effect of.

SEC. 60. *It is the duty of the insurer to clothe the contract in language so plain and clear, that the insured cannot be mistaken or misled as to the burdens or duties thereby imposed upon him. Having the power to impose conditions, and being the party who draws the contract, he must see to it that all conditions are plain, easily understood, and free from ambiguity.* In the language of the court in an English case,[1] *it* "*ought to be so framed that he who runs can read. It ought to be framed with such deliberate care that no form of expression by which, on the one hand, the party assured can be caught, or by which, on the other, the company can be cheated, shall be found on its face.*" Failing to employ a clear and definite form of expression, the benefit of all doubts will be resolved in favor of the assured. The courts will not permit the assured to be misled, or cheated, where there is any sort of justification, from the language used, for the interpretation placed by him upon the instrument. A contract drawn by one party, who makes his own terms, and imposes his own conditions, will not be tolerated as a snare to the unwary, and if the words employed, of themselves, or in connection with other language used in the instrument, or in reference to the subject-matter to which they relate, are susceptible of the interpretation given them by the assured, although in fact intended otherwise by the insurer, the policy will be construed to favor the assured.[2] The courts will not favor cunningly devised

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those uses expressly permitted, belonged to the highest grade of hazards, and the language employed is capable of a construction permitting all other like uses we are bound to presume that the defendant intended such a construction, otherwise it must have acted in bad faith, which is never presumed. We are to suppose, if the language will permit it, that the defendant intended to protect the property of the assured according to the change which it knew had taken place. The distinction between this and the *Pindar case* is that in that case the language was held to be unambiguous, and, although the policy was claimed to be different from that called for, yet, having been issued, delivered and accepted, and sued upon, the assured was bound by its terms, and that extrinsic evidence of circumstances, or otherwise, was incompetent to change it. Such is the established law, but it does not apply to a case where the language is capable of different constructions. The defendant was defeated upon the issue of fact made in the court below, and that finding is conclusive upon this court, whether right or wrong, and the effect of it, upon what the defendant intended by the language used, is adverse to the construction put upon it by it. This construction of the contract renders the testimony offered, that distilleries are more hazardous than the establishments specified, immaterial. The assured having the right to use the premises for any specially hazardous purpose, it was not competent to prove any distinction of hazard in these premises."

[1] *Anderson* v. *Fitzgerald*, 4 H. L. Cas. 484.

[2] *Hoffman* v. *Ætna Ins. Co.* 32 N. Y. 405; *Reynolds* v. *Commerce Ins. Co.*, 47 Id. 597; *Chandler* v. *St. Paul F. & M. Ins Co.*, 21 Minn. 85; 18 Am. Rep. 385; *Blackett* v. *Assurance Co.*, 2 C. & J. 244; *Merrick* v. *Germania Fire Ins. Co.*, 54

policies which are intended to enable the company to reap the advantage and yet escape the risk, and, where there has been a fair contract, and a substantial compliance with its terms, it will be enforced, although there may be some trifling or technical laches.[1] And in construing conditions, it is proper, for the purpose of determining whether the insurer has misled the insured, to look at the *place* in the policy where the condition is printed, and the kind of type, as compared with the rest of the policy,[2] and, for the purpose of arriving at the real intention of the parties, reference may be had to matters *dehors* the policy, as to the location, situation and purposes of the risk, the uses to which it was devoted, the usages, if any, incident thereto, or, indeed, to any attending facts and circumstances that tend to show the real purpose and intention of the parties.[3]

Penn. St. 277; *Braunstein* v. *Accidental Death Ins. Co.*, 1 B. & S. 782; *Catlin* v. *Springfield Fire Ins. Co.*, 1 Sum. (U. S.) 434; *Bartlett* v. *Union M. & F. Ins Co.*, 46 Me. 500; *The Mayor of N. Y.* v. *Hamilton Fire Ins. Co.*, 39 N. Y. 45; *Phillips* v. *Putnam Ins. Co.*, 28 Wis. 427; *Wilson* v. *Conway Fire Ins. Co.*, 4 R. I. 141; *Palmer* v. *Warren Ins. Co.*, 1 Story (U. S.) 360.

[1] *Kentucky Mut. Ins. Co.*. v. *Jenks*, 5 Ind. 96; *Ind. Mut. F. Ins. Co.* v. *Conner*, id. 170.

[2] *Kingsley* v. *Mut. F. Ins. Co.*, *ante*.

[3] In *Mauger* v. *Holyoke Ins. Co.*, 1 Holmes (U. S.) 287, the assured took out a policy of insurance to the amount of $2,000, "on their new lithographic printing press, contained in the fourth story of brick building situate No. 13 Banker Street, Boston, Mass. It is understood that $300 of the amount shall attach on hand presses." Just before this insurance was affected, in April, 1872, the assured had purchased a new lithographic press worth $3,500, and of a smaller size than the one purchased afterwards and referred to in the policy. Permission was given July 3 for removal to fourth and fifth stories of stone and brick building corner of Milk and Devonshire streets, Boston. In June, 1873, the assured procured insurance to the amount of $4,000 "on their lithographic presses and ink-mill, with shafting and belting connected therewith, contained in the fourth and fifth stories of stone building 57 Milk street, corner of Devonshire street." At this time the assured had *two* lithographic presses and several hand presses. The press upon which the defendants' policy was issued was purchased in October, 1872, and was insured by the defendants in November, 1872, for one year in the sum of $4,300, as follows: "On their Hugh and Kimbler's No. 6 steam lithographic press, size 30 x 40, situate in chambers of granite and brick building, situate No. 57 Milk street, corner of Devonshire street," payable, in case of loss, to the plaintiff. The policy, by its terms, required the defendants to pay three-fourths of the value of the property in sixty days after proofs of loss had been made, unless the amount was to be reduced under the following provision of the policy: "In case of any other contract of insurance upon the property hereby insured, *whether such contract be valid or not*, as against the parties thereto, or either of them, the insured shall not, in case of loss or damage, be entitled to recover of this company any greater portion of the loss or damage sustained than the amount herein insured shall bear to the whole amount insured on said property." As previously stated, the assured, at the time of the loss, in November, 1872, had *three* lithographic presses at 57 Milk street, besides shafting and belting. The defendant contended that *all* the policies attached to the press specifically insured by its policy, and that the clause relating to double insurance applied in the adjustment of the loss. The court held that there was no double insurance, and that, in determining the question as to the *intention* of the parties, facts and circumstances *dehors* the policy might be shown. "Explaining the

Courts will not go outside the policy to ascertain its meaning, or the intention of the parties, *when it can be reasonably construed without*,[1] but that matters outside the policy may be resorted to for the purpose of arriving at the real intention of the parties, when there is any ambiguity in the policy, is established by numerous respectable authorities.[2] Thus, in a case in the Circuit Court of the United States,[3] the policy provided that the assured should keep a force pump on the premises. The court held that this included power to operate it, but no particular power. "If," said CURTIS, J., "the warranty was of a force pump in a dwelling-house at all times ready for use, I should hold it satisfied by the existence of a force pump *in a condition to be worked*," because, referring to

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policies in this case," said SHEPLEY, J,, "in the light of attending facts and circumstances at the time they were effected, the attention of the parties is arrived at without difficulty. The first policy was clearly on the *new* lithographic press, definitely described and located. The policy of June 28th was on the *two* lithographic presses then in the chambers, 57 Milk street, and was not intended to apply, *and did not apply*, to any *steam* lithographic presses to be subsequently placed therein. It was not a *floating* policy on a stock of merchandise in a store, bought for sale, and with the intention of replacing it as sold and keeping the stock good; but on specific machinery, intended for permanent use in the location described. It was not expected or intended to embrace, and the literal meaning of the words used does not embrace, any presses not then in the building. It could only embrace such presses subsequently placed in the building, if explained by facts and circumstances *dehors* the policy, and the facts and circumstances do not thus explain it or aid such a construction. The policy is specifically upon the third steam lithographic press, not in the building when the other insurances were effected, and not within the description in those policies. There was, therefore, no double insurance." *Stacey* v. *Franklin F. Ins. Co.*, 2 W. & S. (Penn.) 506, is a case involving similar questions, and holding a similar doctrine. See also *Younger* v. *Royal Exchange Ins. Co.*, 1 Burr. 341; *May* v. *Buckeye, etc., Ins. Co.*, 25 Wis. 291; 5 Ben. F. I. C. 295; *Bond* v. *Gonsales, post.*

[1] *Baltimore Ins. Co.* v. *Loney*, 20 Md. 36; *Astor* v. *Union Ins. Co.*, 7 Cow. (N. Y.) 202; *Murray* v. *Hatch*, 6 Mass. 465; *Levy* v. *Merrill*, 4 Me. 480. An insurance clause on a general stock of merchandise was in the written portion of the policy. The prohibitory clause was in the printed portion. The court below instructed the jury that the latter was repugnant to the former, and could not be interpreted so as to prevent a recovery if they found that "turpentine and benzine" were part of all kinds of merchandise usually kept in a country store. And this ruling was held to be correct. *Lancaster Fire Ins. Co.* v. *Lenheim*, 89 Pa. St. 497.

An exception that the insurer be not liable for any loss "occasioned by explosions of any kind, by means of invasion," &c, was held not to be limited to explosions occasioned by invasion. In such case, simple combustion is to be distinguished from explosion. Accordingly,—*Held*, that the contracting parties did not intend by the special premium to exempt from the printed exception the explosion risk, but did intend the special premium because of the extra hazard of fire risks, designated in the memorandum of special hazard, &c., *Smiley* v. *Citizens' Fire etc. Ins. Co.*, 14 W. Va. 33.

A policy of insurance covering wearing apparel subjects the company to liability upon the property, if in the course of its ordinary use it be destroyed elsewhere than on the premises described in the policy. *Longueville* v. *Western Assurance Co.*, 51 Iowa, 553.

[2] *Finney* v. *Bradford*, 8 Met. (Mass.) 348; *Sayles* v. *N. W. Ins. Co.*, 2 Curtis (U. S. C. C.) 610; *Stacey* v. *Franklin Fire Ins. Co., ante.*

[3] *Sayles* v. *N. W. Ins. Co. ante.*

the subject-matter of the contract, no inference could be drawn that *power* was to be provided therefor. "Considering," he added "the nature of the works and the notorious and uniform usage to have such a pump in such a position *driven by power*," it must be presumed that the parties contracted in reference thereto, and that power was included in the warranty. "*Policies are to be construed largely according to the intention of the parties, and for the indemnity of the assured, and the advancement of trade.*[1] *Facts and circumstances dehors the instrument, may be proved in order to discover the intention of the parties.*" The doctrine that, unless excluded by the fair interpretation of the words employed in the policy, reference will be had to the nature of the risks, its condition, situation and attending circumstances at the time when the policy was made, as well as to the ordinary incidents or usages relating to the risk, was well expressed and illustrated in an early English case.[2]

In that case, the policy covered the "body, tackle, apparel, ordinance, munition, artillery boat and other furniture of and in the said ship." The vessel sailed and arrived in Canton River, China, where she was to stay *to clean and refit*, and for other purposes. Upon her arrival there, the sails, yards, tackle, cables, rigging apparel, and other furniture, were, by the captain's orders, taken out of her and put into a warehouse built for that purpose, on a small sand bar, in order that the articles named might be kept dry and be preserved until the ship should be *heeled and cleaned*. While in the warehouse, *for this purpose*, they were destroyed by fire, and the insurers insisted that it was not a loss covered by the policy, as the articles were not destroyed *in the ship*. It was found that the course pursued by the captain was *necessary*, *prudent* and *usual*, and the court held that the loss was covered by the policy, and the rule established were, *that, that may be done which is usually done in reference to such risk, and that the ends or purposes for which the subject-matter of the risk is employed, may be obtained by any of the usual means or methods employed in such business or with such risks*. "The insurer," said LORD MANSFIELD, "in estimating the price at which he is willing to indemnify the trader, against all risks, must have under his consideration, *the nature of the voyage to be performed, and the usual course and manner of do-*

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[1] ROGERS, J., in *Stacey* v. *Franklin Ins. Co., ante.*

[2] *Younger* v. *Royal Exchange Assurance Co.*, 1 Burr. 341.

ing it. Everything done in the usual course must have been foreseen and in contemplation at the time he engaged. He took the risk upon the supposition *that, what was usual or necessary would be done.* It is absurd to suppose that the usual means of obtaining it, are meant to be excluded." " It is certain," said LEE, C. J., in the same case, " that in the construction of policies, the *strictum jus* or *apex juris* is not to be laid hold on; but they are to be construed largely for the benefit of trade. * * * *The construction should be according to the course of trade.*"[1]

Thus, where a policy contains repugnant, or conflicting conditions, the course pursued by the assured in attempting to comply with the requirements of the contract, will be sustained, *if the instrument is susceptible of such an interpretation*, although, in fact, contrary to the intention and meaning of the insurer. As, where the policy contained a condition, that " no suit for the recovery of any claim under this policy, shall be commenced after the end of one year after any claim shall occur, and in case such suit shall be commenced after the end of one year next after such loss or damage shall have occurred, the lapse of time shall be conclusive evidence against the validity of the claim," and also a condition that the company should not be liable to pay the loss until sixty days *after* the giving of notice, and proofs of loss were furnished, and an action was not commenced within one year after the loss occurred, but was commenced within one year after the lapse of sixty days from the filing of proof of loss, it was held that the action was seasonably commenced, because the terms of the condition were antagonistical, and the insured was justified in understanding that an action commenced within one year from the time *when the claim arose*, to wit: sixty days after proofs were furnished, was in conformity with the requirements of the policy. A similar doctrine has been held in several cases under similar provisions.[2]

In such cases, under such conditions, a claim against the company does not arise from the mere happening of the loss. No claim exists until all the conditions subsequent have been complied with; that is, until notice has been given, and proofs of loss duly furnished. These are essential elements to perfect the claim, and until so perfected no legal claim exists.[3]

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[1] *Bond* v. *Gonsales*, 2 Salk. 445; *McCluer* v. *Girard, etc., Ins. Co.*, 43 Iowa, 398.

[2] *Mix* v. *Andes Ins. Co.*, 9 Hun (N. Y.) 397; *Mayor, etc.*, v. *Hamilton Ins. Co.*, 39 N. Y. 45. *Ames* v. *N. Y. Union Ins. Co.*, 14 N. Y. 253; *Haward* v. *Franklin M. & F. Ins. Co.*, 9 How. Pr. (N. Y.) 45.

[3] YOUNG, J., in *Chandler* v. *St. Paul F. & M. Ins. Co., ante.* In *Mix* v. *Andes*

Insurers may impose any lawful conditions upon the insured, as a basis upon which the risk will be carried, but they must use language that leaves no doubt as to the meaning of the condition. If there is any doubt or ambiguity in the expressions employed, they will be construed most strongly against the insurer. This is upon the principle that a person who draws a contract must draw it with such certainty of expression, that the other party, following the ordinary and usual sense of the words employed, or the meaning which the party obviously intended to give them, in connection with the subject-matter to which they relate, will not be misled thereby, and if there is any ambiguity, the party is not bound to inquire of the other party what was intended, but is fully justified in following the ordinary and usual interpretation of the words used. But, if in connection with other parts of the contract, it is evident that the insurer intended to extend their meaning, and the

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Ins. Co. 9 Hun (N. Y.) 397, TALCOTT, J., said: "The condition of the policy on which the defendant relies for a defense in the action is as follows: 'It is, furthermore, hereby expressly provided, that no suit or action against said company for the recovery of any claim upon, under, or by virtue of the policy, shall be sustainable in any court of law or chancery, unless such suit or action shall be commenced within the term of twelve months next after any loss or damage shall occur; and in case any such suit or action shall be commenced against said company after the expiration of twelve months next after such loss or damage shall have occurred, the lapse of time shall be taken and deemed as conclusive evidence against the validity of the claim thereby so attempted to be enforced. The Court of Appeals has expressly decided in several cases, that such a condition in a policy of insurance is valid and binding, and that an action must fail unless commenced within the time limited. *Ripley* v. *The Ætna Ins. Co.* 30 N. Y. 136; *Roach* v. *The N. Y. & Erie Ins. Co.* 30 id. 546. But the same court has also held that according to the true and just interpretation of such a condition, the time therein specified within which an action must be commenced does not begin to run until the cause of action shall have accrued. *The Mayor of N. Y.* v. *The Hamilton Ins. Co.* 39 N. Y. 45. In the case cited, the condition was like the one in policy under consideration, limiting the time for the commencement of the action to a certain period after the loss or damage shall occur. But it was also provided that payment of losses should be made by the company within sixty days from the adjustment of the preliminary proofs of loss by the parties. In the case at bar the policy provides as follows: No. 11. 'Until proofs, declarations and certificates are produced, and examination submitted to, if required, the loss shall not be deemed payable.' No. 12. 'Payment of losses shall be made sixty days after the loss has been ascertained and proved.' According to the decision in the case last cited, the cause of action did not accrue on the policy in question, until sixty days after the preliminary proofs of loss had been served upon the defendant. The fire by which the insured property was destroyed occurred on the 7th day of July, in the year 1872. But the proofs of loss were not delivered to the defendant until the 24th day of August, 1872, at which date the loss upon the policy was settled and agreed upon by the defendant at the sum of $4,571.43. Consequently, according to the just interpretation of the condition, by which the time for commencing an action on the policy was limited to twelve months, that time did not commence to run until sixty days after the said 24th day of August, in the year 1872. The suit was actually commenced by service of the summons and complaint, upon the duly appointed agent of the defendant, appointed to receive service of process in the State of New York according to the laws thereof, on the 11th day of September in the year 1873, and within twelve months from the time within which the cause of action accrued. See also, *Ames* v. *The N. Y. Union Ins. Co.*, N. Y. 254."

insured acts upon that theory, the insurer is estopped from setting up in defence, that the insured has violated the conditions of the contract because he has acted upon the enlarged sense of the language employed, which was fully justified by the language used and the subject-matter to which it related.[1] Thus, in the case last referred to, the policy contained a provision as follows: "The above premises are privileged to be occupied as hide, fat-melting, slaughter and packing houses, and stores and dwellings, *and for other extra hazardous purposes.*" In the classification of hazards annexed to the policy, the occupations specially privileged were not embraced in the *extra hazardous* class, but came within a general clause under the head of *specially hazardous.* The insured let a portion of the building for a distillery and rectifying establishment, which also came under the specially hazardous class, and the insurers claimed that this use was not warranted by the terms of the policy, and consequently that they were not liable for the loss. But the court held that the words "hazardous" or "extra hazardous" must be taken to mean *purposes of the same class as those before specified, and that the assured had a right to use the premises for any specially hazardous purpose. If the insurer expressly puts a construction upon certain terms employed, and there is no doubt as to the meaning, the insured is bound thereby,*[2] but if he employs language in such a connection as to leave a doubt, the benefit of the doubt will be given to the assured.[3]

Words claimed to create condition must be set forth in proper place.

SEC. 61. Words purporting to be a condition upon which the policy was issued, must be set forth in such a place, and in such manner in the policy as leaves no doubt that they were so intended, and words inserted promiscuously therein, having no connection with other conditions of the policy, although the word condition is used, will not be treated as a condition of the policy. Thus where the words, "on condition that the applicants take all risk from cotton waste," inserted between the statement of the sum insured on the property, and the description of its location, were

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[1] *Reynolds* v. *Commercial F. Ins. Co.*, 47 N. Y. 597. The opinion of CHURCH, C.J., in this case will be found very instructive upon the question of construction of contracts.

[2] *Pindar* v. *Continental Ins. Co.*, 38 N. Y. 365.

[3] *Reynolds* v. *Commerce Ins. Co.*, *ante.*