

TEXAS LEGAL LIABILITY ADVISOR



INFORMATION TO AVOID LIABILITY

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RECENT DEVELOPMENTS IN CGL INSURANCE COVERAGE

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For many businesses, the commercial general liability “CGL” insurance policy is the central component of liability protection. Yet, the CGL policy is not written or intended to provide protection against every claim made against a business. Accordingly, businesses with only CGL protection should routinely evaluate liability risks not covered by the CGL policy to determine what liability risks it may have to bear on its own, whether special CGL endorsements are necessary, and whether different insurance coverage should be considered. For example, construction defect claims in Texas are often plead under multiple causes of action including negligence, breach of express or implied warranties, breach of contract, and violations of the Deceptive Trade Practices Act. Some of these claims may be covered under the CGL, others are not. Businesses that assess and plan for risks not

covered by the CGL policy are better prepared to handle non-covered claims that may arise from time to time. This article explores some recent, significant

Texas appellate court decisions involving CGL policy coverage issues. These cases illustrate some of the issues insurers and insured businesses encounter when responding to complex liability claims.

BASIC COVERAGES UNDER THE CGL POLICY

The typical CGL policy purchased by a business is an occurrence-based policy, as opposed to a claims-made policy. In an occurrence-based policy, the insured is protected against covered claims occurring during the policy period, regardless of whether the claim or occurrence is brought to the attention of the insured or made known to the insurer during the policy period.²

The claims-made policy, on the other hand, covers only injuries or damages that are made known to the insurer during the policy period.³ The basic purpose

The insuring agreement of the standard Commercial General Liability Coverage Form¹ provides in part:

SECTION I - COVERAGES

COVERAGE A BODILY INJURY AND PROPERTY DAMAGE LIABILITY

1. Insuring Agreement

a. We 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. We will have the right and duty to defend any “suit” seeking those damages...

b. This insurance applies to “bodily injury” and “property damage” only if:

(1) The “bodily injury” or “property damage” is caused by an “occurrence” that takes place in the “coverage territory”; and

(2) The “bodily injury” or “property damage” occurs during the policy period.

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behind the CGL policy is to provide coverage for damages arising from the insured's own tortious conduct, as opposed to non-tort claims, such as breach of contract.⁴ The tort coverage offered under the CGL policy is identified under two basic types of liabilities: A) bodily injury and property damage, and B) personal injury and advertising injury. Coverage for bodily injury and property damage liability protects against "bodily injury" and "property damage" caused by an occurrence during the policy period. Coverage for personal injury and advertising injury, on the other hand, covers the specific torts or offenses found in the policy definitions of "personal injury" and "advertising injury." Coverage for bodily injury and property damage tends to give rise to more coverage litigation, including the recent decisions discussed herein.

WHAT IS AN "OCCURRENCE"

While the term "occurrence" as used in insurance policies has been construed by Texas courts for several decades,⁵ courts still face questions about whether a particular claim against an insured amounts to an occurrence. An "occurrence" under the standard CGL policy is defined as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." While the definition of occurrence uses the word accident, accident is not defined in the policy. Many Texas courts have construed the meaning of "accident" and have generally found it to mean negligently caused losses.⁶ The Texas Supreme Court has held that an injury is accidental *if, from the viewpoint of the insured, it is not the natural and probable consequence of the action or occurrence which produced the injury; or in other words, if the injury could not reasonably be anticipated by the insured, or would not ordinarily follow from the action or occurrence which caused the injury, it is accidental.*⁷ The mere fact that an actor intended to engage in conduct that gives rise to the injury does not mean that the injury was not accidental.⁸ But, an injury which is caused by voluntary and intentional conduct, is not accidental just because the result or injury may have been unexpected, unforeseen, and unintended.⁹ Therefore, the determination of whether an occurrence is accidental requires consideration of both

the actor's intent, and the reasonably foreseeable effect of the actor's conduct.¹⁰ One court recently considered these factors in a two step process.¹¹ First, a determination was made of the specific acts alleged to be the cause of the plaintiff's damages, and whether those acts were voluntary and unintentional.¹² If the acts were committed involuntarily and unintentionally, the acts were accidental, and no further analysis is necessary.¹³ If the acts were committed voluntarily and intentionally, step two asks whether those acts naturally resulted in the claimed injuries.¹⁴ The natural result of an act is the result that ordinarily follows, may be reasonably anticipated, and ought to be expected.¹⁵ If the result is not the natural and probable consequence of the act or course of action, then it is produced by accidental means.¹⁶

BREACH OF IMPLIED WARRANTY - NOT A CGL "OCCURRENCE"

Recently, the Houston First District Court of Appeals, in *Hartrick v. Great American Lloyds Insurance Co.*, was asked to make this type of determination, specifically, whether liability for breach of warranty is an occurrence under the CGL



policy.¹⁷ In the underlying liability suit at issue in *Hartrick*, Clairmont Building Corp. was sued for negligence, violations of the Texas DTPA, and breach of implied warranties of good and workmanlike construction and suitability for habitation arising out of the defective

construction of a house foundation.¹⁸ The plaintiffs claimed damage to the house and loss of market value because of pitching and heaving in the foundation. When the case went to trial, the jury found Clairmont liable only for the breach of warranty claims. Following the turnover of Clairmont's insurance coverage claim to the Plaintiffs, the Plaintiffs brought suit against Clairmont's insurance company arguing

that Clairmont's CGL policy provided coverage for the Plaintiffs' judgment. At issue in the coverage lawsuit was whether the liability judgment for breach of warranty was covered under the CGL policy, that is, whether it was an "occurrence." Initially, the Houston First Court of Appeals noted that the broad form CGL policy does not insure a contractor because of faulty workmanship, but rather, provides coverage for damages that result from the contractor's performance, other than damage to the work itself.¹⁹ The Court then held, that when an injury results from voluntary and intentional conduct, such as not preparing the soil and not constructing the foundation in keeping with the promises the law implies to the contractor, the injury is not "an accident."²⁰ Even though the insured contractor did not intend the result, breach of an implied warranty is not an "occurrence" covered under the CGL policy.²¹ The court found that the Plaintiffs' claimed damages were the reasonably foreseeable results that would ordinarily flow from a contractor's work not complying with its implied warranty to prepare the soil and clear the land properly, and its implied warranty to build a house on a foundation that is strong enough to support a house. The Court held that lack of compliance with implied warranties is not accidental, but results from one not doing what one what one must do.²²

The *Hartrick* opinion is consistent with the increasing number of Texas appellate decisions which have considered the meaning of "occurrence" in connection with non-negligent, intentional causes of action, holding that such claims as fraudulent promises, misrepresentation, and untrue statements do not fall within the plain meaning of the policy definition of an occurrence, and therefore, are not covered under the CGL policy.²³ The narrowing of the policy definition of occurrence has also extended to negligence claims that are related to and interdependent on claims of intentional conduct.²⁴ For example, in *Folsom Investments, Inc. v. American Motorists Ins. Co.*, the Dallas Court of Appeals determined that claims of negligent hiring, training, supervision, and retention against an employer, for an employee's unwelcome sexual advances against another employee, did not allege an occurrence under the employer's CGL policy.²⁵ When negligence claims, such as these, are related to and interdependent

on intentional misconduct of an employee, the coverage issue is determined by whether the employee's intentional misconduct falls within the policy definition of "occurrence," which in this case the court held, did not.²⁶ For businesses, these recent court decisions signify that the policy term "occurrence" is construed narrowly by Texas courts, and that claims reasonably related to intentional and voluntary conduct, even those claims alleging negligence, stand a strong chance of being denied by insurers on the grounds that no occurrence is alleged sufficient to trigger an insurer's duty under the CGL policy.

EXPOSURE TRIGGERS COVERAGE

Another area of recent development with respect to coverage issues and the CGL policy relates to the issue of what it means to have a bodily injury or property damage occur *during the policy period*. The problem arises because the standard CGL policy does not specify when an occurrence takes place, only that an insurer has a duty to defend when bodily injury or property damage is caused by an occurrence during the policy period.²⁷ One difficulty with this issue is the fact that the CGL policy language "occurrence during the policy period" requires an actual injury or damage during the policy period, and not merely the occurrence of the negligent act or omission that is the ultimate cause of the injury during the policy period.²⁸ Despite some prior Texas appellate decisions on the subject, the issue of when a specific damage or injury "occur(s) during the policy period" has been subject to debate since the Texas Supreme Court discussed, but declined to resolve, the issue in the 1994 case of *American Physicians Insurance Exchange v. Garcia*.²⁹ In *Garcia*, the Texas Supreme Court noted at least five different tests that could be applied to determine when a harm occurs that triggers coverage under an insurance policy.³⁰ The three primary theories applied to determine whether coverage has been triggered are the manifestation, exposure, and injury-in-fact theories. The *Garcia* court declined to resolve the issue because it was not required for that particular case.³¹ Prior to *Garcia*, there were only two decisions by Texas' appellate courts on the subject, and both of those cases applied some form of the "manifestation rule," which holds that coverage under the CGL policy

is not triggered unless the damage or injury manifests itself or becomes apparent during the policy period.³²

The most recent decision in this area was made in June of this year in *Pilgrim Enterprises, Inc. v. Maryland Casualty Company*.³³ The underlying liability lawsuits at issue in this coverage case involved personal injury and property damage claims against Pilgrim arising out of the use, spillage, and leakage of perchloroethylene, a chemical used in the dry cleaning process at several Pilgrim Cleaners, and which apparently over the course of many years contaminated soil and groundwater.³⁴ Pilgrim sought a defense from Maryland Casualty under its occurrence-based CGL policies spanning a four year period of time, approximately 9 years prior to the discovery of the soil contamination. After initially providing a defense, Maryland withdrew the defense provided to Pilgrim on the grounds that the claimed injuries were not alleged to have occurred, i.e. manifested, during any of Maryland's policy periods.³⁵ Pilgrim argued that coverage was triggered by harm sustained from *exposure* to continuous pollution, even if the harm remained undiscovered when it initially occurred.³⁶ The trial court agreed with Maryland that the CGL language "which occurs during the policy period" means that coverage is triggered only when the injury or damage is discovered or manifests during the policy period, and held that Maryland had no duty to defend Pilgrim in the subject liability lawsuits.³⁷

On appeal, the Houston First District Court of Appeals found that the issue had been considered by other Texas courts, but that it was still an unresolved question in Texas jurisprudence. Looking at the policy language itself, the court noted that the CGL policies at issue did not use the word "manifest" with respect to occurrence, nor did they state that an injury must be discovered during the policy period. Rather, the policies contemplate that harm caused by continuous and repeated exposure during a policy period will be covered.³⁸ The court held that with respect to a CGL policy that defines an occurrence to include continuous or repeated exposure to conditions, ***injury or damage can occur as the exposure takes place***.³⁹ In the Pilgrim case, the court found that Maryland's CGL policies provided coverage for the Plaintiff's allegations of physical

injury and property damage caused by any exposure to PCE during the policy periods at issue.⁴⁰ The court also noted that this "exposure rule" is equally applicable to both physical injury and property damage.⁴¹ This is a significant decision because it decides an issue that has been unsettled in Texas for years, and expands the scope of coverage for an insured by applying the exposure test to determine an occurrence as opposed to the more insurer-friendly manifestation test. For businesses with consecutive CGL coverage, this means that there is greater likelihood that multiple policies will be involved when dealing with a continuing occurrence claim which causes an indivisible injury. Because of the continued proliferation of toxic tort cases, and other specialized torts, these types of claims are now common.

RECOMMENDATIONS



Businesses should: 1) conduct annual risk audits in consultation with your attorney; 2) review all insurance policies, including endorsements; 3) review insurance coverages on an annual basis with your insurance agent; 4) consider special CGL endorsements, such as a

blanket additional insured endorsement; 5) conduct a cost/benefit analysis of specialty insurance products that may provide greater protection for your specific business than a CGL policy; 6) implement risk reduction strategies targeted at the specific types of risk that are not covered by the CGL policy; 7) when significant claims arise with coverage issues, consult a qualified attorney to provide advice on coverage issues and appropriate defense strategies; and 8) forward all reservation of rights letters to your attorney for consultation and response. Insurers should continue to: 1) carefully review all claims that are in any way related to an insured's defective work or service for coverage defenses; 2) for claims involving injury or damage caused by exposure to a condition over a period of time, remember that multiple policy periods may be invoked and that any exposure during

your policy period will be an occurrence under the policy; 3) when coverage issues are apparent, timely send out a thorough reservation of rights letter to the insured that addresses all coverage defenses; 4) include in reservation of rights letter notice of any intent to seek reimbursement of defense costs for uncovered claims; 5) advise the insured to put all carriers on notice when dealing with a continuing tort over multiple policy periods; 6) engage and consult coverage counsel when significant claims arise.

Notes

¹ Excerpt taken from Commercial General Liability Coverage Form (occurrence version) CG 00 01 07 98, copyrighted material of Insurance Services office, Inc. used with permission. Copyright, Insurance Services Office, Inc. 1998 (2000).

² See *Yancey v. Floyd West & Co.*, 755 S.W.2d 914, 925 (Tex. App.-Fort Worth 1988, writ denied).

³ See *id.*

⁴ See *Data Specialties, Inc. v. Transcontinental Ins. Co.*, 125 F.3d 909, 913 (5th Cir. 1997).

⁵ See *Parker v. Gulf Ins. Co.*, 486 S.W.2d 610, 615 (Tex. Civ. App.-Fort Worth 1972), *affirmed*, 498 S.W.2d 676 (Tex. 1973).

⁶ See *Glover v. National Ins. Underwriters*, 545 S.W.2d 755, 763 (Tex. 1997); *Argonaut Southwest Ins. Co. v. Maupin*, 500 S.W.2d 633, 635 (Tex. 1973); *Data Specialties, Inc. v. Transcontinental Ins. Co.*, 125 F.3d 909, 912 (5th Cir. 1997).

⁷ See *Mid-Century Ins. Co. v. Lindsey*, 997 S.W.2d 153, 155 (Tex. 1999).

⁸ See *Trinity Universal Ins. Co. v. Cowan*, 945 S.W.2d 819, 828 (Tex. 1997).

⁹ See *Argonaut Southwest Ins. Co. v. Maupin*, 500 S.W.2d 633, 635 (Tex. 1973); see also *Trinity Universal Ins. Co. v. Cowan*, 945 S.W.2d 819, 826-28 (Tex. 1997); *Wessinger v. Fire Insurance Exch.*, 949 S.W.2d 834, 837 (Tex. App.-Dallas 1997, no writ).

¹⁰ See *Mid-Century Ins. Co. v. Lindsey*, 997 S.W.2d 153, 155 (Tex. 1999).

¹¹ See *Folsom Invest., Inc. v. Amer. Motorists Ins. Co.*, 2000 WL 1239998, p.2 (Tex. App.-Dallas, Aug. 31, 2000, n.w.h.).

¹² See *id.*

¹³ See *id.*

¹⁴ See *id.*

¹⁵ See *Wessinger v. Fire Ins. Exch.*, 949 S.W.2d 834, 837 (Tex. App.-Dallas 1997, no writ).

¹⁶ See *id.*; see also *McKinney Builders II, Ltd v. Nationwide Mut. Ins. Co.*, 1999 WL 608851, pg 6. (N.D. Tex., 1999)(Builder's reliance on incorrect survey resulting in builder's construction of house which encroached on neighbor's property was not the natural and probable consequences of the builder's reliance on survey which builder believed was correct, therefore, an occurrence under the CGL policy).

¹⁷ See *Hartrick v. Great American Lloyds Ins. Co.*, 2000 WL 1159603, p.3 (Tex. App.-Houston [1st Dist.] 2000, n.w.h.).

¹⁸ See *id.* at 1.

¹⁹ See *id.* at 4.

²⁰ See *id.* at 5.

²¹ See *id.*

²² See *id.*

²³ See *Freedman v. CIGNA Ins. Co.*, 976 S.W.2d 776, 778 (Tex. App.-Houston [1st Dist.] 1998, no writ); *Houston Petroleum Co. v. Highlands Ins. Co.*, 830 S.W.2d 153, 156 (Tex. App.--Houston [1st Dist.] 1990, writ denied); see also *State Farm Lloyds v. Kessler*, 932 S.W.2d 732, 738 (Tex. App.--Fort Worth 1996, writ denied) (misrepresentations and failures to disclose are intentional acts, not accidents).

²⁴ See *Folsom Invest., Inc. v. Amer. Motorists Ins. Co.*, 2000 WL 1239998, p.3.; *American States Ins. Co. v. Bailey*, 133 F.3d 363 (5th Cir. 1998); *Cornhill Ins. PLC v. Valsamis, Inc.*, 106 F.3d 80 (5th Cir. 1997).

²⁵ See *Folsom Invest., Inc. v. Amer. Motorists Ins. Co.*, 2000 WL 1239998, p.2.

²⁶ See *id.* at 4.

²⁷ See Commercial General Liability Coverage Form, Coverage A.

²⁸ See *Guaranty Nat'l Ins. co. v. Azrock Industries, Inc.*, 211 F.3d 239, 244 (5th Cir. 2000).

²⁹ See *American Physicians Insurance Exchange v. Garcia*, 876 S.W.2d 842, 853 n. 20 (Tex. 1994).

³⁰ See *id.*

³¹ See *id.*

³² See *Dorchester Development Corp. v. Safeco Ins., Co.*, 737 S.W.2d 380, 383 (Tex. App.-Dallas 1987, no writ); *Cullen/Frost Bank v. Commonwealth Lloyd's Ins., Co.*, 852 S.W.2d 252, 257 (Tex. App.- Dallas

19993, writ denied).

^{33.} *See* Pilgrim Enterprises, Inc. v. Maryland Cas. Co., 24 S.W.3d 488 (Tex. App.-Houston [1st. Dist.] 2000, n.w.h.).

^{34.} *See id.* at 490.

^{35.} *See id.* at 491.

^{36.} *See id.* at 493.

^{37.} *See id.* at 491-2.

^{38.} *See id.* at 497.

^{39.} *See id.* at 497.

^{40.} *See id.* at 498.

^{41.} *See id.* at 497.



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