

Client Alert

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Texas Supreme Court Confirms Narrow Construction of Contractual Liability Exclusion

The Supreme Court of Texas confirmed in *Ewing Constr. Co. v. Amerisure Ins. Co.*, No. 12-0661 (Tex. Jan 17, 2014), that a promise to perform work in a “workmanlike manner” is not an assumption of liability within the meaning of a contractual liability exclusion, because the promise does not enlarge the scope of potential liability that would exist in the absence of the contractual promise. Rather, the promise merely restates a duty that the party already owed at common law.

FACTUAL BACKGROUND

Ewing Construction, Inc. (“Ewing”), a general contractor, was hired by Tuloso-Midway Independent School District (the “School District”) to, among other things, build new tennis courts at a school in Corpus Christi, Texas. Soon after their construction, the tennis courts began to crumble and crack and, according to the School District, became unusable for their intended purpose of hosting competitive tennis events. The School District sued Ewing, alleging negligence and breach of contract due to Ewing’s faulty construction.

Ewing was insured under a general liability insurance policy issued by Amerisure Insurance Company (“Amerisure”). Ewing sought defense and indemnity against the School District’s claim, but Amerisure denied coverage based on, *inter alia*, the policy’s “contractual liability” exclusion, which purports to bar coverage for liabilities contractually assumed by the policyholder.

Ewing sued Amerisure in the US District Court for the Southern District of Texas to obtain a ruling that its claim was covered. Amerisure — though it conceded that the defective tennis courts constituted “property damage” caused by an “occurrence,” which triggered coverage under the policy — argued in defense that the School District’s claim was excluded from coverage by the policy’s contractual liability exclusion.

The district court agreed with Amerisure and granted summary judgment in its favor. The court, relying on *Gilbert Texas Constr., LP v. Underwriters at Lloyd’s of London*, 327 S.W.3d 118 (Tex. 2010), reasoned that Ewing had contractually assumed liability for its own construction work. The court further held that the exclusion’s exception for liabilities that otherwise exist at common law did not apply to the School District’s claim because the claim did not seek damages that Ewing would have in the absence of the contract.

On appeal, the Fifth Circuit initially affirmed the district court’s decision, but later withdrew its opinion, granted rehearing and certified the matter to the Texas Supreme Court.

THE TEXAS SUPREME COURT LIMITS THE SCOPE OF THE EXCLUSION

Answering the questions certified by the Fifth Circuit, the Texas Supreme Court held that the contractual liability exclusion must be construed narrowly to apply only to instances where a policyholder has contractually accepted liability that it would not otherwise be subject to at common law. In reaching its decision, the court distinguished *Gilbert*, 327 S.W.3d 118. In *Gilbert*, the contractor agreed contractually to accept responsibility for damage to the property of third parties. These liabilities, the court explained,

extended beyond Gilbert's obligations under general law. As the court reiterated, however, the contractual liability exclusion applies only if the contractually assumed liability was greater than the liabilities that otherwise exist under general law. The circumstances of *Gilbert* were just that, with Gilbert having accepted liabilities that it would not otherwise have been subject to under the law.

In contrast to *Gilbert*, Ewing merely contracted "to construct the courts in a good and workmanlike manner." This, the court explained, was something that Ewing was obligated to do even without the contractual promise. Ewing's contract, like any construction contract, required that Ewing exercise ordinary care; and Ewing would have owed that duty at common law even without the contractual provision. Thus, Ewing's "assumption of liability" did not fall within the ambit of the contractual liability exclusion.

Finally, the court rejected Amerisure's argument that the alleged "faulty workmanship" was not an "occurrence." Amerisure posited that general liability policies are not intended to supplant performance bonds, which are designed to cover an insured's own work. The court reaffirmed its holding from *Lamar Homes, Inc. v. Mid-Continent Cas. Co.*, 242 S.W.3d 1 (Tex. 2007), and ratified that "allegations of unintended construction defects may constitute an 'accident' or 'occurrence' " under typical general liability policies. Likewise, the court reiterated that damage to property built by contractors can be "property damage" under most general liability policies. Coverage, therefore, had indeed been triggered.

IMPLICATIONS

Amerisure clarifies the Texas Supreme Court's stance in *Gilbert*, making clear that the ruling in *Gilbert* is the exception, not the norm. In its ordinary application, the contractual liability exclusion is, like any exclusion, construed narrowly, with its application directed only at those liabilities that would not otherwise exist at general law. *Amerisure* also confirms that construction defects are indeed "accidents," sufficient to trigger coverage under typical general liability policies.

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