

# The Defense Chronicles

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## Highlights

*New Developments in  
Insurance Law..... 2*

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for the most recent  
significant changes in  
the law that affect  
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## Texas Supreme Court Eliminates Diminished-Value Element of Damage For Repaired Vehicles

*American Manufacturers Mutual Insurance Company, et al. v. Schaefer, et al., 124 S.W.3d 154 (Tex.2003).*

In a case of first impression, the Texas Supreme Court has held that the Texas Standard Personal Auto Policy does not obligate an insurer to compensate a policyholder for a vehicle's diminished market value when the car has been damaged but adequately repaired.

Gary Schaefer purchased a standard automobile insurance Policy from American Manufacturers Mutual Insurance Company ("AMM"). Part D of the Policy, entitled "Coverage for Damage to Your Auto", provided that AMM will pay for "direct and accidental loss to your covered auto..." The payment obligation was subject to a contractual limitation of liability that read, in pertinent part, as follows:

### Limit of Liability

Our limit of liability for loss will be the lesser of the:

1. Actual cash value of the stolen or damaged property; or
2. Amount necessary to repair or replace the property with other of like kind and quality; or
3. Amount stated in the Declarations of this policy.

The Policy also provided for the method of paying the loss:

### Payment of Loss


We may pay for loss in money or repair or replace the damaged or stolen property.

Schaefer's vehicle was involved in an accident. It was inspected by an AMM adjuster, and the insurance company elected to repair the vehicle. Schaefer did not dispute the quality or adequacy of the repairs. Instead, he maintained that the value of the vehicle decreased by \$2,600.00 due to market perceptions that a damaged and subsequently repaired vehicle is worth less than one that has never been damaged. Schaefer claimed that his Policy obligated AMM to compensate him for that diminished value.

In interpreting the Policy, the Supreme Court applied the rules of contract construction. If Policy language is worded so that it can be given a definite or certain legal meaning,

it is not ambiguous, and the court will construe it as a matter of law. An ambiguity does not arise simply because the parties offer conflicting interpretations. An ambiguity exists only if the contract language is susceptible to two or more reasonable interpretations. When construing the Policy's language, the court must give effect to all contractual provisions so that none will be rendered meaningless.

In applying the rules of contract construction to the Policy, the Supreme Court found that the Policy was unambiguous and did not require a payment for diminished value when a vehicle had been fully and adequately repaired. The Policy limited liability to the damaged vehicle's "actual cash value" or the amount needed "to repair or replace" the vehicle, whichever was less. Inserting the concept of diminished value into the repair provision would render the Policy's "Payment of Loss" section meaningless.

The Supreme Court acknowledged that Schaefer's repaired vehicle may be worth less when sold because it had been involved in an automobile accident and repaired, and that awarding Schaefer diminished value in addition to repair would go further to make him whole. Nevertheless, the Court refused to rewrite the parties' contract nor add to its language. 

### **Sole Proprietorship One and the Same as Individual for Insurance Purposes**

*CU Lloyds of Texas v. Hatfield, Houston [14<sup>th</sup> Dist.] Court of Appeals, No. 14-02-01251-CV (2004).*

In a case of apparent first impression under Texas law, the Houston Fourteenth Court of Appeals held that a CGL Policy provision excluding coverage for automobiles owned by the named insured, excluded coverage as to an automobile owned by that individual in his own name where the named insured was that individual doing business under another name. Gary May was driving on a highway near Angleton, Texas when he came upon a truck traveling in his lane at a very slow speed. He swerved in a belated attempt to avoid hitting the truck. The passenger side of the vehicle struck the truck's trailer, resulting in serious injuries to a passenger in May's vehicle. The vehicle May was driving was titled in the name of his father, Benjamin

F. May, Jr. who, at the time of the accident, did business under the name of "May's Younglandia," a sole proprietorship.

CU Lloyds had issued an insurance policy that provided commercial general liability coverage (the "CGL Policy") for Benjamin F. May, Jr.'s business. The policy listed the named insured as "May's Younglandia." The passenger in the vehicle filed suit against Gary May and Benjamin F. May, Jr., individually and d/b/a May's Younglandia. The Mays requested a defense and indemnity from CU Lloyds under the CGL Policy. Although another insurer provided a defense and indemnity up to its limits, CU Lloyds denied coverage under the CGL Policy. The trial court found that Gary May drove negligently in the course and scope of his employment with May's Younglandia at the time of the accident. The trial court also held Benjamin F. May, Jr. d/b/a May's Younglandia liable both under the doctrine of respondeat superior and under Jason Hatfield's negligent - entrustment claim.


CU Lloyds filed a petition for declaratory judgment in Harris County seeking an interpretation of coverage under the CGL Policy. CU Lloyds moved for summary judgment, alleging it had no duty to defend or indemnify because the named insured owned the automobile involved in the accident and the CGL Policy excluded coverage for such a casualty. CU Lloyds further contended that it had no contractual duty to indemnify under the CGL Policy because a sole proprietorship, May's Younglandia, and its proprietor, Benjamin F. May, Jr., are legally the same person and, as a consequence, an exclusion in the CGL Policy precluded coverage for the accident.

The CGL Policy excluded coverage for the following:

"g. "Bodily Injury" or "Property Damage" arising out of the ownership, maintenance, use or entrustment to others of any aircraft, "auto" or watercraft owned or operated by or rented or loaned to any insured. Use includes operation and "loading or unloading."

The CGL Policy then listed several exceptions to this exclusion, namely: (6) a "non-owned auto" used in your business by any person other than you.

The CGL Policy defined "non-owned auto" in pertinent part, as "any auto you do not own, lease, hire or borrow

which is used in connection with your business.” The definition of “you” under the CGL Policy included the named insured—Benjamin F. May, Jr. d/b/a May’s Younglandia. The appellate court found that the critical issue on appeal was whether Benjamin F. May, Jr. and May’s Younglandia were one and the same for the purposes of the CGL Policy. A sole proprietorship is defined as “[a] business in which one person owns all the assets, owes all the liabilities, and operates in his or her personal capacity.” Under Texas law, a sole proprietorship has no separate legal existence apart from the sole proprietor. The appellate court, in reversing the trial court’s decision, held that May’s Younglandia, a sole proprietorship, and its proprietor, Benjamin F. May, Jr., were one and the same for purposes of the CGL Policy. Consequently, the coverage exclusion in the CGL Policy for vehicles owned by the named insured applied. Thus, CU Lloyds had no duty to defend or indemnify Benjamin F. May, Jr. d/b/a May’s Younglandia against the claims. 

### Check Your Spouse’s Life Insurance Policies After Saying “I Do”


*Frazier v. Frazier, Houston [1<sup>st</sup> Dist.] Court of Appeals, No. 10-02-01089-CV (2003).*

Eddie Frazier designated Earlene Frazier, who was his wife, the beneficiary of a life insurance policy issued by John Hancock Life Insurance Company. Frazier divorced Earlene in July of 2000, and soon thereafter, married Janice Frazier. Twenty days after the marriage, Frazier, suffering from “respiratory arrest,” was admitted to the hospital. He had previously been diagnosed with progressive squamous cell carcinoma of the lung. Following his admission to the hospital, he was intubated and placed on a ventilator machine.

During Frazier’s thirteen-day stay at the hospital, the doctors and Frazier’s children were in favor of removing him from the ventilator machine. Janice, his new wife, was against it because “she had some business she had to take care of.” She later changed her mind, and Frazier was winged off the ventilator machine and died shortly thereafter.

Following Frazier’s death, Janice filed a beneficiary designation form showing that she was the designated

beneficiary of Frazier’s life insurance policy. Frazier allegedly signed this form on November 2, 2000. Thereafter, Janice and Earlene both asserted claims to the proceeds from the life insurance policy. Faced with these competing claims, John Hancock filed its petition and interpleaded the policy proceeds.


At trial, Earlene contested whether Frazier actually signed the “beneficiary designation form.” She testified that she had seen Frazier’s signature on many occasions and that the signature on the form was not his signature. Moreover, Frazier’s children testified that Frazier did not have the capacity to sign the form on November 2, 2000. After a bench trial, the trial court ruled that at the time of Frazier’s death, Earlene was the beneficiary under the policy, and that Frazier did not sign the change in beneficiary designation form submitted by Janice. Because of that fact, Janice never became the beneficiary under the policy, and the proceeds of the policy were awarded to Earlene. The court of appeals, in holding in favor of Frazier’s first wife, Earlene, held that the evidence was sufficient to support the trial court’s finding that Frazier did not sign the beneficiary designation form. Janice did not introduce any evidence to contradict the finding that Frazier was unable to sign the beneficiary designation form. Janice also never produced an authenticated copy of the divorce decree, and thus there was no evidence in the record showing that Earlene waived her status as the designated beneficiary. 

### Second Court of Appeals Grants *En Banc* Rehearing on Insurance Coverage for Punitive Damages

*Westchester Fire Insurance Company v. Admiral Insurance Company, Fort Worth Court of Appeals, No. 02-01-227-CV (orig. order June 26, 2003).*

The Second Court of Appeals has granted an *en banc* rehearing on whether insurance coverage for punitive damages is void as against public policy. As previously reported in the Summer of 2003 edition of *The Defense Chronicles*, a three-judge panel, in a controversial 2-1 decision held that absent a clear indication from the Legislature or the Supreme Court to the contrary, insurance coverage for punitive damages under the facts of the case was not against public policy. Some courts,

in analyzing coverage in a standard form liability policy providing coverage for “sums” or “all sums” an insured becomes required to pay as a result of bodily injury or property damage, have held that the policy covers punitive damages if not otherwise excluded. The public policy argument against such coverage is that if an insured is able to insure against losses from punitive damage awards, punishment and deterrence are not achieved against the wrongdoer.

Once the *en banc* Second Court of Appeals issues an opinion on this important issue, it will be reported in The Defense Chronicles. 


### Texas Supreme Court to Revisit Insurance Reimbursement Ruling

*Excess Underwriters at Lloyds, et al. v. Frank’s Casing Crew and Rental Tools, No. 02-730 (2003).*

The Texas Supreme Court has heard oral argument in a case that may allow the Supreme Court to revisit its 2000 decision in *Texas Association of County Government Risk Pool v. Matagorda County* in which a divided Supreme Court held that an insurer cannot seek reimbursement from its insured for the insurer’s settlement of what proves to be an uncovered claim.

In the *Excess Underwriters* case, *Excess Underwriters* is seeking reimbursement of approximately \$7 million which it paid to settle a claim relating to the collapse of a drilling rig in the Gulf of Mexico. Although *Excess Underwriters* had issued reservation of rights letters contesting coverage of some of the claims made against its insured, due to the risk of a larger judgment, *Excess Underwriters* decided to fund the entire settlement and then seek reimbursement from its insured as to claims found to be uncovered by its policy. The court of appeals, citing the *Matagorda County* case, held that *Excess Underwriters* was not entitled to reimbursement from its insured because the insured did not expressly agree that the insurance company could seek reimbursement.

The case illustrates the dilemma faced by insurers and insureds in situations where the insurer contends that claims may not be covered by its insurance policy, but a demand has been made for settlement within policy limits. In that situation, the insurer is faced with the possibility of paying

a claim which may not be covered under its policy. Because of the changes in the make-up of the Supreme Court since 2000, there is a chance that the Supreme Court could seek a resolution that is more equitable to both the insurer and the insured than the effect of the Court’s decision in the *Matagorda County* case. 


### Texas Supreme Court Construes Definition of Total Disability

*Provident Life & Accident Insurance Company v. James Knott, M.D., No. 02-045 (Tex. 2003).*

The Texas Supreme Court, in this insurance coverage dispute, construed the definition of *total disability* written in two insurance policies. Interpreting the policies, the Court held that an insured is totally disabled when he is unable to perform all of the important and usual duties of his occupation.

The subject case was brought by a doctor who practiced obstetrics and gynecology full-time until he suffered a spine fracture in a plane crash and underwent surgery. Prior to the plane crash, the doctor had purchased two policies which, among other things, provided benefits for total disability and partial disability. The doctor was unable to return to work for several months, and then returned to work part-time performing limited medical procedures and examinations. He claimed that after the accident he was unable to perform operative obstetrics and other procedures because the bending and stress of these procedures aggravated his back injury. A few months after the doctor turned 65, he submitted a claim for total disability to Provident. No new event or accident precipitated the claim. Provident refused to pay lifetime benefits for total disability under the policies.

The court focused on the definition of total disability as defined in the policies. Both of the policies contained the following definition of total disability: “Total disability means that due to injuries or sickness, you are unable to perform the duties of your occupation.” Provident argued that under this provision, the doctor was totally disabled only when he was unable to perform *all* of the duties of his occupation. The doctor contended that whether he was totally disabled was a fact question that depended on whether he was unable to do any substantial portion of the work connected with his occupation.


The Supreme Court, in ruling in favor of Provident, held that in order for the doctor to receive lifetime benefits under the total disability provision, he had to show that he was unable to perform *all* of the important and usual duties of his occupation. Because he was able to perform *some of the important and usual duties of his occupation*, he was not totally disabled under the policies' terms. The Court further held that the policies constituted the allocation by market participants of risks and benefits regarding an insured's possible future disability. The Court's role was not to redistribute those risks and benefits, but to enforce the allocation that the parties previously agreed upon. 

### **Business Pursuits Exclusion Does Not Apply to Mining Lease**

*Hallman v. Allstate Insurance Company, Dallas Court of Appeals, No. 05-02-00962-CV (2003).*

Ruth Hallman owned property in Kaufman County, Texas. In 1995 she leased her property to certain companies to mine limestone. The following year, neighboring property owners sued Hallman and others for damages related to blasting and transporting the stone. Hallman made a claim to Allstate under her homeowner's insurance policy, requesting that Allstate defend and indemnify her in the mining litigation. Allstate agreed to defend Hallman, but then filed suit seeking a declaration of rights under the insurance

policy. Hallman filed a counterclaim for declaratory judgment on the defense and indemnity issues. Allstate took the position that the claims were not covered because those allegations did not state a claim for bodily injury or property damage caused by an "occurrence" as defined in the policy. Further, even if coverage were triggered, Allstate asserted coverage was barred by the "business pursuits exclusion."

The trial court ruled in favor of Allstate and found that the claim was not covered. The court of appeals reversed. In reaching its decision, the court of appeals looked at the policy, which provided that coverage for personal liability does not apply to bodily injury or property damage arising out of or in connection with "a 'business' engaged in by an 'insured'" but the exclusion did not apply to activities which were ordinarily incidental to non-business pursuits. The petition filed in the case alleged that Hallman entered into one lease agreement in 1995. The petition did not allege that Hallman regularly engaged in leasing her property as a means of earning a living or that her personal business was leasing property. Thus, the court could not conclude, by construing the language of the policy and the petition, that the petition alleged facts that came within the definition of the "business pursuits exclusion." An insurer's contractual duty to defend must be determined solely from the face of the pleadings, without reference to any facts outside the pleadings. 

- William T. Sullivan

***The contents of this newsletter are presented as general information only and are not intended as legal advice. The reader is invited and advised to consult with an attorney for more specific information regarding the matters and materials addressed herein, or for advice based on the individual circumstances of his or her specific situation.***

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