UPDATES ON THE CONTRACTUAL LIABILITY EXCLUSION—WHERE WILL IT ALL LEAD?

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Gilbert Texas Construction, L.P. v Underwriters at Lloyd’s London, 327 SW3d 118 (Tex. 2010)
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.
Gilbert prevailed on its summary-judgment motion, leaving only RTR’s breach of contract claim.
Exclusion 2(b) This 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 only liability theory remaining at the time Gilbert settled arose from Gilbert’s undertaking in the contract with DART—an obligation Gilbert assumed by contract. And Gilbert does not claim there are facts that could result in its being liable under some other theory besides breach of contract.
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.*, 673 N.W.2d 65, 80-81 (Wis. 2004)
The exclusion applies when the insured is obligated to pay damages “by reason of the assumption of liability in a contract or agreement.”
Plain Language

Those terms are not defined, so we give them their “generally accepted or commonly understood meaning.”
Plain Language

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.
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.”
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.
RTR’s breach of contract claim was founded on an obligation or liability contractually assumed by Gilbert within the meaning of the policy exclusion.
Ewing Construction Co. v Amerisure Ins. Co., 2012 WL 2161134 (Fifth Cir. 2012)
In June 2008, Ewing Construction Company, Inc. ("Ewing") entered a contract with Tuloso–Midway Independent School District ("the School District"), in which Ewing agreed to construct tennis courts at a school in Corpus Christi, Texas. Soon after Ewing completed the tennis courts, the School District complained that the courts were cracking and flaking, rendering them unfit for playing tennis. On February 25, 2010, the School District filed a petition ("the underlying lawsuit") in Texas state court, seeking damages for defective construction, and naming Ewing as a defendant. Ewing tendered defense of the underlying lawsuit to Amerisure Insurance Company ("Amerisure"), its insurer under a CGL policy. Amerisure denied coverage.
Allegations in petition:

It alleges that Ewing breached its contract and performed negligently:

Defendant Ewing Construction has breached its contractual commitments, proximately causing damages to Plaintiff. On information and belief, Plaintiff says that Defendant Ewing and/or its subcontractors breached its contract in the following respects:

a) Failing to complete construction in accordance with the contract plans and specifications;
b) Failing to exercise ordinary care in the preparation, management and execution of construction;
c) Failing to perform in a good and workmanlike manner; and
d) Failing to properly retain and supervise subcontractors.
Furthermore, Defendant Ewing Construction and/or its subcontractors was/were guilty of negligence proximately causing damage to Plaintiff in the following respects:

a) Failing to properly prepare for and manage the construction;

b) Failing to properly retain and oversee subcontractors;

c) Failing to perform in a good and workmanlike manner; and

d) Failing to properly carry out the construction so that it was in [sic] completed in accordance with the plans and specifications.
2. Exclusions

This insurance does not apply to:

... 

b. Contractual Liability

“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) That the insured would have in the absence of the contract or agreement....
“We acknowledge that Gilbert contains some rather opaque language, and that its particular facts make for imperfect comparisons to the instant case. Nonetheless, Gilbert furnishes the Texas Supreme Court's approach to the contractual liability exclusion, and that approach is straightforward: Apply the plain language of the exclusion, rather than grafting additional language to it. *Id.* at 131–32. Ewing's position, that the phrase, “assumption of liability in a contract” means “assumption of a duty to repair third party property, but not assumption of implied contractual duties,” is contrary to that approach.”
“Applying this plain meaning approach preserves the longstanding principle that a CGL policy is not protection for the insured's poor performance of a contract. See Lamar Homes, Inc. v. Mid–Continent Cas. Co., 242 S.W.3d 1, 10 (Tex.2007). Although other jurisdictions adopt this principle by holding that poor contractual performance is not, under a CGL policy, an occurrence causing property damage, Texas chooses to arrive at this holding through its interpretation of coverage exclusions. See id. at 5 n. 3, 10 (“More often, however, faulty workmanship will be excluded from coverage by specific exclusions because that is the CGL's structure.”). Our holding today respects this choice.”
“Having determined that the contractual liability exclusion applies, we now ask whether any exception to that exclusion restores coverage. The district court found inapplicable the exception that Ewing asserts, that is, the exception to the contractual liability exclusion that allows coverage for liability that “the insured would have in the absence of the contract or agreement.” Ewing contends that the district court erred because the petition in the underlying lawsuit uses the term “negligence,” and liability for negligence is liability that exists irrespective of a contract.”
“The School District's use of the term “negligence,” however, is not dispositive. See Century Sur. Co. v. Hardscape Constr. Specialties, Inc., 578 F.3d 262, 267–70 (5th Cir. 2009). We must assess the substance of the School District's petition and determine whether it alleges an action in contract, tort, or both. Id. at 267 (citing Jim Walter Homes, Inc. v. Reed, 711 S.W.2d 617, 617–18 (Tex. 1986)). To do this, we look to the “source of liability and the nature of the plaintiff's loss.... When the only loss or damage is to the subject matter of the contract, the plaintiff's action is ordinarily on the contract.” Id. (quoting Sw. Bell Tel. Co. v. DeLanney, 809 S.W.2d 493, 494–95 & n. 2 (Tex. 1991))."
“Ewing's contract with the School District is the source of its potential liability because Ewing's duty to construct usable tennis courts arose out of contractual undertakings. Further, the damage alleged in the School District's complaint is damage to the subject matter of the contract, the tennis courts, not to any other property. The school district's claim therefore sounds in contract, regardless of the other labels that may be attached to it. 3 Id. at 269–70. Because the liability Ewing faces is contractual, it is not liability that would arise in the absence of a contract. The exception, therefore, does not apply and coverage remains excluded. We hold that Amerisure owes no duty to defend Ewing in the underlying lawsuit.”
“Before resolving the remaining issues on appeal, we pause to acknowledge a somewhat troubling concern. If the contractual liability exclusion means what it says, then it will often exclude coverage under the same circumstances as another CGL exclusion: the “your work” exclusion. The “your work” exclusion excludes coverage for “property damage to [the insured's] work arising out of it or any part of it.” Because an insured ordinarily undertakes work through a contract, the contractual liability exclusion will ordinarily accomplish the same purpose, that is, exclude coverage for property damage to the insured's work.”
“The solution is premised on the least clear passage of Gilbert: a comparison of liability incurred under “general law principles” and liability incurred when promising to repair third party property. See Gilbert, 327 S.W.3d at 127. We view this passage as merely explaining why an obligation relating to third party property—which ordinarily would arise in tort—arose in contract under the unusual facts of the case. Whatever the passage means, it cannot call for a hyper-technical interpretation of the contractual liability exclusion, like the interpretation the dissent favors, without contradicting the rest of the Gilbert opinion.
The opinion's bottom line is that “assumption of liability in a contract” means to have “undertake[n]” the “quality or state of being legally obligated or accountable” in a contract. *Id.* There is no question but that Ewing has assumed liability in that sense, and we will not contradict what is clear by seizing on what is not.4 In fact, the dissent's interpretation—that only a promise to repair the property of another is an assumption of liability—looks strikingly like the interpretation that *Gilbert* expressly rejected, i.e., that only an assumption of the liability of another is an assumption of liability. *Id.* at 126–27.”
Dissent:

- Gilbert’s holding was narrow
- Every contractual obligation is not an assumption
- Business risks exclusion denies status as a performance bond
Motion for Rehearing
Motion for Rehearing en banc
Motion to Certify
Crownover v. Mid-Continent Casualty Co., 3:09-CV-02285 (N.D. Tex. 2011) appeal pending (argued the day after Ewing argued)
Arbitrator found home completed in November 2002. In the year following the completion of the home, both the HVAC system and the foundation began showing signs of problems. The HVAC system was not “installed property, did not perform as required, and exhibited numerous deficiencies” and “the foundation failed”. 
Arbitrator found a breach of the express warranty of good workmanship. Attorneys fees were awarded under ch. 38.
The arbitration award was clearly based on the Crownovers’ breach of contract claim against Arrow. The issue was whether Arrow would have liability “absent its contractual undertaking.”
“By its plain terms, the insurance agreement excludes damages the insured becomes legally obligated to pay by assumption of liability in a contract or agreement. As the Gilbert court explained, the plain meaning of the exclusion does not require the insured to assume the liability of another. The arbitrator based his award of damages on the express warranty to repair in Arrow’s contract with the Crownovers.”
“Plaintiffs’ contention that the arbitration award is somehow also based upon Arrow’s liability under their non-contractual claims contradicts the plain language of the award. The arbitrator explicitly declined to reach the Crownovers’ negligence and implied warranty claims. ..Mid-Continent has met its burden of establishing that the exclusion applies.”
“The burden then shifts to Plaintiffs to establish that an exception to the exclusion applies. . . Plaintiffs argue that since the implied-in-law warranty of good workmanship mirrors the express warranty relied upon by the arbitrator, the adjudicated facts prove that Arrow would have liability for the arbitration damages in the absence of the contract.”
“The court admits that, given the wording of the exclusion, Plaintiffs’ argument has intuitive appeal. . . The implied warranty of good workmanship only arises in the absence of an express contractual warranty. . . Once Arrow and the Crownovers entered into a contract with an express warranty of good workmanship, the “gap-filler” implied warranty ceased to be of any relevance.”
Conclusion:

- Ewing-Gilbert’s goes beyond facts
- Applies to the duty to defend
- Exc B has limits-
  - Limited to parties to the contract
  - Is limited to damage to the subject of the contract
- Liability arises out of contractual undertaking