



Pay and Chase Allocation: Considerations for Settling in Preparation of Chasing

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*Satterfield and Pontikes Construction, Inc. v.
United States Fire Insurance Company*
898 F.3d 574 (5th Cir. 2018)



Zapata County retained Satterfield and Pontikes Construction, Inc. (“Contractor”) to serve as the general contractor for its courthouse building project

Contractor's Insurance for the Project

First Tier

AGLIC
(2006-2007):
\$1,000,000 per
occurrence

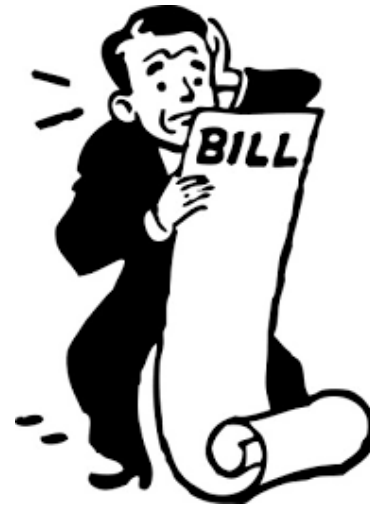
Amerisure
(2007-2011)

Second Tier

U.S. Fire: \$25,000,000 limit
Kicked in only when first tier was depleted

Limitations on U.S. Fire Policy

- Barred coverage for any “property damage” resulting from exposure to fungi, including mold, or bacteria
- Did not cover attorney’s fees or other legal costs.



Arbitration

Issues arose and
Zapata County
terminated
Contractor

Zapata County
sued Contractor

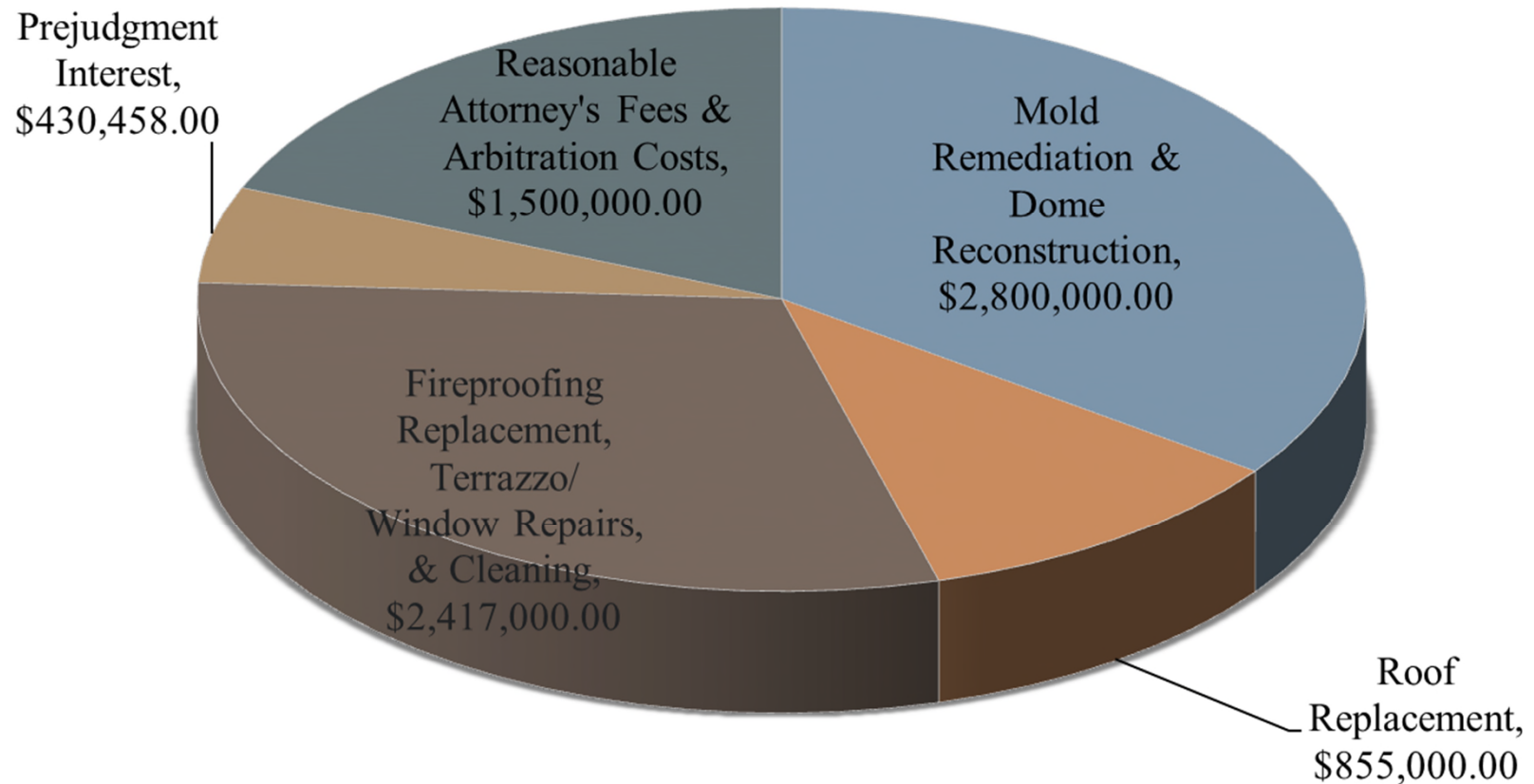
The parties
arbitrated their
dispute

Arbitration panel found:

- Contractor failed to build the courthouse in a good and workmanlike manner
- Contractor failed to properly supervise its subcontractors
- The courthouse suffered physical harm and damage because of Contractor's failures

Zapata County's Arbitration Award

(\$8,063,641.78 including post judgment interest)



Contractor Joined Its Subcontractors

- Contractor sought money pursuant to the indemnification clauses in the subcontracts
- Contractor informed U.S. Fire of its efforts to settle with the subcontractors
- U.S. Fire stated it would not object to any “reasonable settlement”
- Contractor settled with 17 parties for \$4,492,500

The settlement agreements did not allocate the proceeds of the settlements to the damages or liabilities they covered

Contractor Sought Payment from Carriers

$ \begin{array}{r} \$8,063,641.78 \\ - \$4,492,500.00 \\ \hline \$3,571,141.78 \end{array} $	The subcontractors' settlement money did not cover the entire arbitration award.
$ \begin{array}{r} \$3,571,141.78 \\ - \$1,985,604.63 \\ \hline \$1,585,537.15 \end{array} $	AGLIC paid \$1,985,604.63 to help satisfy the award.
$ \begin{array}{r} \$1,585,537.15 \\ - \$0 \\ \hline \$1,585,537.15 \end{array} $	U.S. Fire paid \$0, arguing that the first layer of insurance for covered damages had not been completely exhausted.
$ \begin{array}{r} \$1,585,537.15 \\ - \$1,146,405.10 \\ \hline \$439,132.05 \end{array} $	Amerisure paid \$1,146,405.10 towards the arbitration award.
Contractor paid the balance of the award.	

Contractor paid.



Then, Contractor chased.

Contractor Sued U.S. Fire

Contractor's Position:

- U.S. Fire, as its second layer insurance provider, was required to make up the shortfall after the first layer of insurance was exhausted
- After the \$4.5 million from the subcontractors and \$1.5 million from AGLIC, U.S. Fire should have paid the \$2 million shortfall

U.S. Fire's Rebuttal:


- Contractor's argument ignored that not all of the damages were covered under its insurance policy.
- Once the excluded items and AGLIC's \$1 million first layer were removed, then no more than \$2,500,000 was *potentially* recoverable from U.S. Fire

Double Recovery and Unjust Enrichment

- U.S. Fire argued that allowing Contractor to recover from both it and the subcontractors for the same damages would result in double recovery and unjust enrichment for Contractor
- It agreed the \$1.75 million from the Contractor's waterproofing sub could be allocated as uninsured mold damages but contended the remaining \$2.74 million of the settlement money applied to the covered damages Contractor sought to recover from U.S. Fire
- That amount was greater than the \$2,531,411.51 of potentially covered damages and, therefore, there was no shortfall for U.S. Fire to pay

District Court Decision

- Granted summary judgment in favor of U.S. Fire relying upon the 5th Circuit's decision in *RSR Corporation v. International Insurance Company*
- Placed a burden on Contractor to demonstrate the settlement proceeds could be allocated to the noncovered portions of U.S. Fire's policy.
 - Contractor could not/did not meet this burden.



“[Contractor] cannot unilaterally allocate all of its settlement proceeds to uncovered losses in order to manufacture a covered loss.”

Contractor's Arguments on Appeal

FIRST:

The subcontractor settlements were not the product of insurance coverage and, therefore, U.S. Fire was not entitled to use them to offset amounts covered by its own policy to prevent double recovery.

SECOND:

District court erred when it placed the burden on Contractor to show that the subcontractor settlements were allocated to either covered or noncovered damages under the U.S. Fire policy.

Decision on Contractor's First Argument

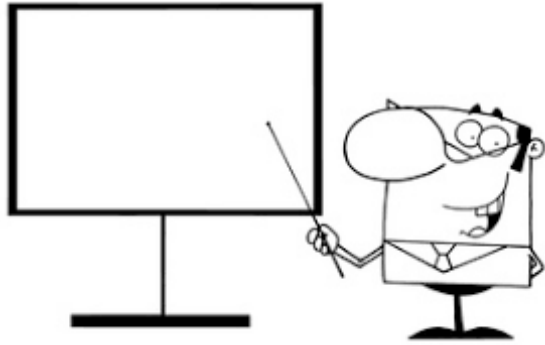
“An indemnity agreement falls under the plain language of the ‘Other Insurance’ provision of U.S. Fire’s policy – which is very broad – because it is a ‘mechanism by which an Insured arranges for funding of legal liabilities for which [U.S. Fire’s] policy also provides coverage.”

- Plain language of the policy determined the subcontractor settlement money was the product of insurance coverage
- U.S. Fire was entitled to use the subcontractor settlements to offset amounts covered by its policy

Decision on Contractor's Second Argument

- Texas law places the burden of proof on Contractor to show how it allocated the settlement proceeds between covered and noncovered damages
- If Contractor cannot meet that burden, the court must assume that all of the settlement proceeds went first to satisfy the covered damages under U.S. Fire's policy

Although U.S. Fire agreed Contractor could reasonably settle with the subcontractors, that did not equate to U.S. Fire agreeing to allocate all of those settlement proceeds to noncovered damages.



Lessons from Satterfield

- Prior to settling, retain expert witnesses to inspect the alleged defect(s) to determine the cause and cost of repair
- During settlement negotiations, review your client's CGL policies to understand what is covered and what is not
- In the settlement agreement, allocate the settlement proceeds to the damages or liabilities they represent
- During the chase, be ready to refute the potential argument you attempted to manufacture a covered loss