



## Texas Supreme Court Clarifies Contractual Liability Exclusion



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The Texas Supreme Court issued its much-anticipated opinion in *Ewing Construction v. Amerisure Insurance* on January 17, resolving a simmering controversy about the scope of the “contractual liability” exclusion in a construction contractor’s general liability policy. The Supreme Court held that excluding coverage for damages the contractor is “obligated to pay . . . by reason of the assumption of liability in a contract” does not bar coverage for damages attributed to the contractor’s failure to perform construction in a “good and workmanlike manner.” The Court rejected a much broader interpretation of the standard exclusion that had been adopted by a federal district court and initially affirmed by the Fifth Circuit. The holding limited the effect of the Supreme Court’s 2010 decision in *Gilbert Texas Construction v. Underwriters at Lloyd’s London*, which the Southern District of Texas in *Ewing* had read to mean that the exclusion applied whenever “an insured has entered into a contract and, by doing so, assumed liability for its own performance under that contract.”

The case arose out of Ewing’s construction of tennis courts for the Tulo-so-Midway school district. When the district sued Ewing in state court for defective work, alleging breach of contract and negligence, Ewing tendered its defense to Amerisure under a CGL policy. Amerisure denied any duty to defend or indemnify, prompting Ewing to file suit in federal court. Ewing sought a declaration that Amerisure had breached its duty to defend and would be obligated to indemnify Ewing for any damages awarded to the district. Amerisure counterclaimed for contrary declarations that Amerisure had no duty to defend or indemnify Ewing against the district’s claims, and the parties filed cross-motions for summary judgment. Based on its interpretation of *Gilbert*, the district court denied Ewing’s motion, granted Amerisure’s motion on the contractual liability exclusion, and entered final judgment. The Fifth Circuit affirmed on the duty to defend and remanded other issues, but in response to Ewing’s motion for rehearing withdrew that opinion and certified two questions to the Texas Supreme Court:

1. Does a general contractor that enters into a contract in which it agrees to perform its construction work in a good and workmanlike manner, without more specific provisions enlarging this obligation, “assume liability” for damages arising out of the contractor’s defective work so as to trigger the Contractual Liability Exclusion.

2. If the answer to question one is “Yes” and the contractual liability exclusion is triggered, do the allegations in the underlying lawsuit alleging that the contractor violated its common law duty to perform the contract in a careful, workmanlike, and non-negligent manner fall within the exception to the contractual liability exclusion for “liability that would exist in the absence of contract.”

Because the Court answered the first question “no,” it did not address the second question.

*Gilbert* arose from a contract for construction of the DART light rail system. An owner of property adjacent to the work site sued Gilbert for flood damage. Gilbert’s liability insurer denied coverage and refused to defend, citing the contractual liability exclusion. Gilbert successfully asserted sovereign immunity in the underlying lawsuit, so all that remained was a claim for breach of contract. Gilbert settled that claim, and sought indemnity from Lloyds. When the case reached the Texas Supreme Court, it rejected Gilbert’s argument that the exclusion applies only where the insured “assumes *another’s* liability,” a position that had been accepted in other jurisdictions. The Court held the contractual liability exclusion was triggered by the general contractor’s contractual promise to repair and pay for damage to adjacent property caused by its failure to comply with the requirements of the contract, because it had thereby assumed obligations beyond its duties under common law. Under the unusual circumstances of that case, where Gilbert was immune to tort liability, its only potential liability was for the obligation assumed under the contract to repair or pay for damage to adjacent property, which triggered the exclusion.

In contrast, the Court held in *Ewing* that the contractor’s contractual promise to perform in a good and workmanlike manner did not exceed its obligations under common law, so it was not a liability “assumed” by contract. The allegations in the underlying lawsuit therefore did not trigger the contractual liability exclusion. This holding will be welcomed by all participants in the construction industry in Texas, which depends on insurance to spread the risk of liability arising out of alleged defects in construction.