



# Legal Beat

By MICHAEL SEAN QUINN

## It's a Dog's Life...And an Agent's Lot

What is the most authoritative source of truthful information in the whole universe? No question about it. It's Southwest Airlines' *Spirit* magazine. You know. The magazine found in the seat pocket right in front of you. Yes! The one that frequently has the crossword puzzle already done—often illegibly by an illiterate.

In any case, in the July 2000 issue of this venerable rag there is an article by John MacIntyre entitled Facts of Life. It contains the following: "1, 2, 3: Rank of car salesmen, telemarketers and insurance salesmen as the professions considered least honest."

There are two problems with this insulting passage. First, it can't be right. Lawyers surely head the list. Second, it is unclear whether insurance agents are considered absolutely the least honest, or whether there are two occupations considered less honest than they. MacIntyre can't tell the head from the bottom.

If MacIntyre's report were not contained in *Spirit* magazine, the world's most authoritative source of information, I would call it both misleading and libelous. He's on to something, though. People as a whole distrust the insurance industry, and they take it out on the poor agent. Maybe people distrust insurance-intermediaries because the public is so frequently tempted to lie to them.

In any case, this distrust has led to two national pastimes in insurance litigation. One of them is to try to wangle coverage for injuries from toxic chemicals, even in the face of the pollution exclusion. The other one is to sue agents for fun and profit.

The strategy in suing agents is two-fold. First, if the insurance contract does not say what the insured wishes it said, then the insured sues the agent and claims that the agent said something false to him in the process of selling the policy. The legal theories here are fraud and negligent misrepresenta-

tion. Second, the underlying point to this tactic is to have citizens of the same state on both the plaintiff's side and the defendant's side and thereby guarantee that the case cannot be in federal court.

### The blast that started it all

The destruction of federal diversity jurisdiction is not always the goal, however, as the case of *Amoco Production Company v. Hydroblast Corporation* proves. This case was decided recently in the federal district court for the Northern District of Texas, Lubbock Division, and then affirmed by the Fifth Circuit in July 2000.

Amoco hired Hydroblast to conduct pressure tests on certain heat exchangers. To do this, they were filled with a toxic chemical that can cause defatting of tissue, vomiting, dizziness and weakness. Sure enough, the tanks leaked suddenly, and the toxic substance drenched Hydroblast workers.

The workers sued Amoco. (The immunity set up by the workers' compensation statute prevented their suing Hydroblast.) But Hydroblast had indemnified and agreed to hold Amoco harmless from any suit filed against it by Hydroblast employees working at the Amoco plant. (The comp bar does not restrict recoveries on indemnity agreements.)

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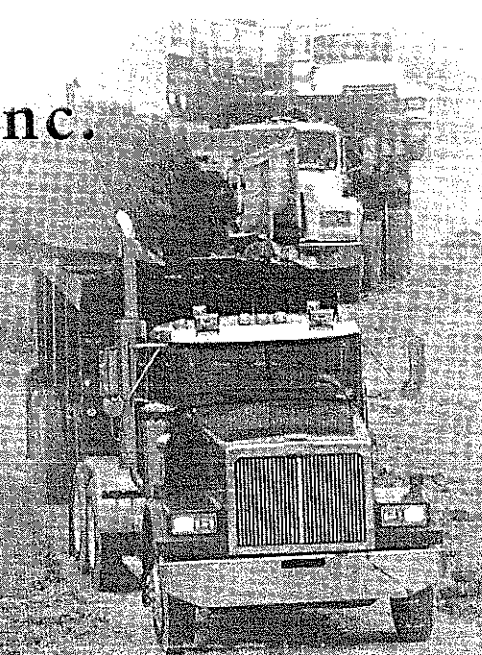
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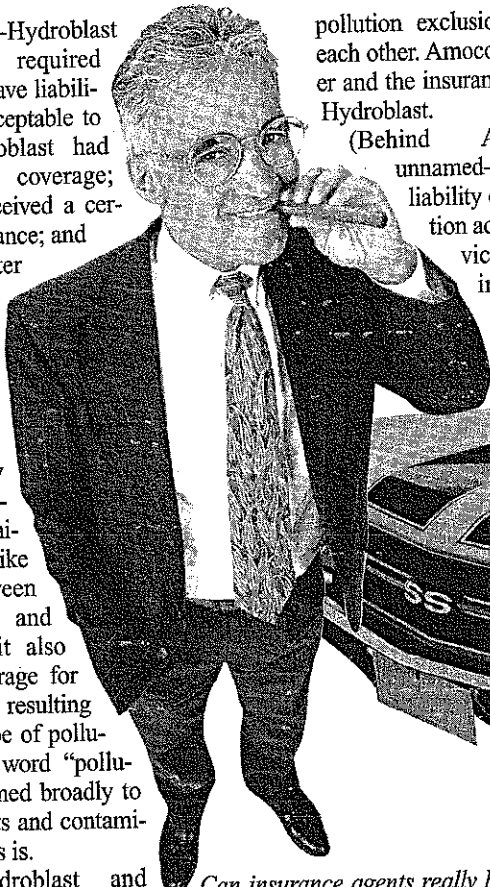
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The Amoco-Hydroblast contract required Hydroblast to have liability insurance acceptable to Amoco. Hydroblast had obtained CGL coverage; Amoco had received a certificate of insurance; and there the matter rested until the Hydroblast employees sued Amoco. The problem was that the CGL policy provided coverage for indemnity agreements like the one between Hydroblast and Amoco, but it also excluded coverage for bodily injuries resulting from the escape of pollution, and the word "pollutant" was defined broadly to include irritants and contaminants. It always is.

Both Hydroblast and Amoco were (or feigned) outraged at this application of the

pollution exclusion, so they settled with each other. Amoco then sued both the insurer and the insurance agency in the name of Hydroblast.

(Behind Amoco—silently and unnamed—may even have been its liability carrier pressing a subrogation action.) Hydroblast was serviced by a New Mexico insurance agency,



*Can insurance agents really be ranked alongside car salespersons as the least honest professionals? Say it isn't so.*

and virtually all of the insurance negotiations were handled in New Mexico.

In any case, the plaintiff, who ever it really was, alleged that the insurance agent, and his company, breached express or implied agreements by failing to procure the right kind of insurance and by failing to make sure that Amoco was listed as an additional insured. On top of that, Hydroblast asserted that the insurance agent violated the Texas

Deceptive Trade Practices Act and the Texas Insurance Code.

The pollution exclusion? The court held it applied. It reasoned that the pollution exclusion is quite broad, and that there is no language in it restricting its scope to environmental cases, as opposed to workplace accidents involving toxic chemicals. Consequently, held the court, the insurer had neither a duty to defend nor a duty to indemnify either Amoco or Hydroblast.

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The case against intermediaries? There was hardly any evidence as to what agreements there might have been between the insurance agency and Hydroblast. Given that dearth, the court destroyed Hydroblast's case by assuming a relatively-bad-but-plausible (though not worst-case) scenario. Suppose, said the court, the insurance agency and Hydroblast had agreed that the agency would obtain a policy of insurance for Hydroblast acceptable to Amoco. This is not an unreasonable assumption. What happened was that the agency procured a policy, sent a certificate of insurance to Amoco, and Amoco did nothing negative.

The only available inference, therefore, is that Amoco was satisfied with the policy. Consequently, the agency complied with the requirements of the relatively-bad-but-plausible scenario posited by the court.

Moreover, the DTPA and Insurance Code claims must fail, said the court. Hydroblast and the agency did their business in New Mexico. Consequently, DTPA and the Insurance Code, both of which are Texas statutes, have no applicability to the case. New Mexico law applied.

#### Agents and paradoxes

The law governing misrepresentations by insurance intermediary contains some internal tensions. On the one hand, if A makes a representation to B about a physical object, like a product, and what A says is false, B may have claims for fraud, negligent misrepresentation, breach of express warranty, product defect, and so forth. On the other hand, if A makes a representation about what is contained in a printed document, then—at least in theory—B cannot complain that what A says is false, because B has an obligation to read the document.

There are two problems here. First, the insurance industry thinks of insurance contracts as if they were products. Shouldn't something like the law governing products therefore govern insurance policies?

Second, insurance policies are complex written instruments that are contracts of adhesion. They are not negotiated much as to terms. Most insureds never read them. Most people and most businesses rely on their agents to say what's in them. Insurance policies, like many complex contracts, are not easy to understand. As a result, it seems unrealistic to give agents an absolute defense if they say something that isn't true about what's in the policy.

At the same time, this area of the law is beset by another tension. It is very easy for people to lie (or make mistakes) about what insurance intermediaries tell them. Hence, it is a bad idea to make it easy to sue insurance brokers for making false statements about what's in insurance policies.



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That would be just another way of making the E & O carriers for brokers insurers of last resort. (This point is particularly true if MacIntyre's claim in *Spirit* magazine is anything like true.)

Usually, these tensions work themselves out in a just and reasonable manner. Not always, however, and therein lies a rub.

The law's method for solving this problem is not very attractive. If A has probably told B something false about a contractual document B has an obligation to read, the law will reform the document in accordance with A's statements, if B can actually prove

them, and if A had authority to speak.

Often B's burden of proof is quite difficult to meet.

Insurance contracts often say, however, that they cannot be reformed in accordance with an agent's misstatements. Insurer's contracts with agents often say, this too. Many courts are inclined to honor this provision. Besides, courts reason, agents are not parties to the insurance contracts they sell. Of course, there is a paradox hidden here.

Suppose a contract recites, "This contract cannot be reformed." Now suppose A says to B, "Let's vary the terms of the con-

tract," and they both agree. Wouldn't there be something wrong with holding B to the written deal under these circumstances? Or suppose A tells B not to pay attention to the "This contract cannot be reformed" clause, and A looks like he is in charge. Or suppose B relies upon A to tell him what's in a complex, difficult instrument, and A says the contract can be reformed. Or B says nothing at all. Are these not conundrums?

### Pollution paradoxes

The Hydroblast case raises yet another problem. Consider its application of the pollution exclusion. In effect, it rules out coverage of all chemical-based bodily and property injuries. Even asbestos and sand-based injuries are excluded. Here lies another paradox. On the one hand, insurance contracts are to be given their plain meaning, and the language of the so-called pollution exclusion is quite broad. Courts are thus construing and applying the language correctly.

On the other hand, pollution exclusions—like almost all other exclusions—are standardized and drafted on an industry-wide basis. Original industry intent is therefore a sensible notion.

It is not clear that industry draftspersons originally thought they were excluding anything more than environmental degradation—Superfund liability and the like. There is a rule of law that prescribes that exclusions are to be understood narrowly, not broadly. Yet the courts say that pollution exclusions are broad. This fact disturbs many policyholders.

Perhaps it shouldn't. After all, if the plain meaning of an exclusion is broad, it must be understood broadly. The principle that exclusions are narrow is a rule of construction only. It applies only if language is ambiguous.

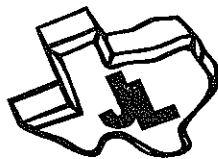
Policyholder frustration won't go away. Isn't all language ambiguous to some extent? Controversies over exclusions are an enduring feature of the litigation landscape. Arguments about the pollution exclusion linger. Obviously, there is a socio-political problem in the offing, not just an incidental economic/business dispute.

Before it is solved, dissolved, or defused, it will spill over and pollute the business lives of agents. This has been and will go on for years and years. For agents, the worst is yet to come. MacIntyre's cavalier observation has not served their interests well. ■

*Quinn is an Austin shareholder in the law firm of Sheinfeld, Maley & Kay. He litigates and testifies on insurance related problems and is currently the chair of the Insurance Section of the State Bar of Texas. He also is a Visiting Professor of Law at the University of Texas-Austin.*

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