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FIFTH CIRCUIT COURT OF APPEALS ASKS TEXAS SUPREME COURT TO RESOLVE ISSUE OF “TRIGGER” RULE APPLICABLE TO LATENT PROPERTY DAMAGE CLAIMS

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On August 8, 2007, the Fifth Circuit Court of Appeals issued an opinion in No. 06-10727, *OneBeacon Insurance Company v. Don's Building Supply, Inc.*, certifying important questions of Texas insurance law to the Texas Supreme Court. Gene Creely of Cozen O'Connor's Houston office is representing OneBeacon in this significant appeal, and Tim Headley of Cozen O'Connor's Dallas office represented OneBeacon in the District Court below.

In its certification order, the Fifth Circuit Court of Appeals has asked the Texas Supreme Court to pronounce what “trigger” rule should be employed under Texas law for determining when latent property damage is deemed to occur for purposes of coverage under a commercial general liability policy. Prior to this time, the Texas Supreme Court has refrained from adopting any particular liability “trigger” rule in latent property damage cases. Most of the Texas Courts of Appeals (including the Dallas, San Antonio, and Austin Courts of Appeals), as well as most federal courts (including the Fifth Circuit Court of Appeals) that have dealt with the issue under Texas law, have applied a “manifestation trigger” rule in latent property damage cases. Under the “manifestation trigger” rule, property damage is deemed to occur when the property damage manifests itself or becomes apparent or is capable of being easily perceived, recognized and understood. However, the Houston Courts of Appeals in *Pilgrim* and *Pine Oak Builders* have recently rejected the “manifestation trigger” rule and instead applied an “exposure trigger” rule to latent property damage caused by continuous or repeated exposure to conditions during a policy period (even if the property damage did not manifest itself and was not discoverable until after the policy period).

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By its certification order, the Fifth Circuit Court of Appeals basically requests the Texas Supreme Court to resolve the “split of authority” on the issue of the “trigger” rule applicable to latent property damage claims.

In this case, OneBeacon sought a declaratory judgment that it had no duty to defend or indemnify Don’s Building Supply against claims asserted against it in underlying lawsuits under commercial general liability policies that afforded coverage for Don’s Building Supply from 1993 through 1996. The lawsuits were filed at various times in 2003 through 2005. The plaintiffs asserted claims arising from water intrusion that allegedly caused rot and deterioration of wooden structural members in the wall cavities of their respective homes resulting from allegedly defective Exterior Insulation and Finish Systems (“EIFS”) siding that was allegedly supplied by Don’s Building Supply and installed on their respective homes at various times during the policy period. In their pleadings, the plaintiffs also plead the “discovery rule” and other allegations, acknowledging that they did not know and could not have known about the damage to the respective homes until within two years before the filing of the respective lawsuits.

Relying on the “manifestation trigger” rule employed by the Fifth Circuit Court of Appeals in *Azrock* and *Unitramp*, as well as the majority of Texas Courts of Appeals, OneBeacon moved for summary judgment asserting that (1) the pleadings in underlying lawsuits did not allege any damage or injury that manifested itself during OneBeacon’s policy periods, but rather the pleadings alleged that the damage or injury did not become manifested until well after the policies expired and thus (2) OneBeacon had no duty to defend or indemnify Don’s Building Supply against the claims in the underlying lawsuits.

In response, Don’s Building Supply filed a cross motion for summary judgment seeking a declaration that OneBeacon had a duty to defend it against the claims in the underlying lawsuits. In its cross-motion for summary judgment, Don’s Building Supply argued that the Houston 1st Court of Appeals’ decision in *Pilgrim* (which was issued after *Azrock* and *Unitramp* and applied an “exposure trigger” rule to environmental property damage claims) was “controlling” and required the application of an “exposure trigger” rule. In doing so, Don’s Building Supply asked the District Court to disregard the Fifth Circuit Court of Appeals’ decisions in *Azrock* and *Unitramp*, as well as the other Texas state and federal decisions applying a “manifestation trigger” rule in latent property damage cases, and adopt an “exposure trigger” rule applicable to the EIFS-related claims in the underlying lawsuits. Don’s Building Supply further argued that, since the allegations suggested that the water intrusion began shortly after installation of the EIFS siding on the plaintiffs’ homes (which was installed at various time during the policy period) and that the resulting damage or injury was continuous or ongoing (although the damage did not manifest itself and was not discovered until many years after the expiration of the policies), OneBeacon had a duty to defend Don’s Building Supply against the EIFS-related claims in the underlying lawsuits.

After full briefing, the District Court entered an order granting OneBeacon's motion for summary judgment and denying Don's Building Supply's cross-motion for summary judgment. In its order, the District Court disagreed with Don's Building Supply's position that *Pilgrim* was "controlling," despite the fact that the Houston 1st Court of Appeals' decision in *Pilgrim* was issued after the Fifth Circuit Court of Appeals' decisions in *Azrock* and *Unitramp*. Rather, the District Court recognized that the Fifth Circuit Court of Appeals had long adopted and applied a "manifestation trigger" rule to property damage claims under its interpretation of Texas law in *Azrock* and *Unitramp* and that it was required to follow this precedent, unless it could be established that such precedent was "clearly wrong." After concluding that such precedent was not "clearly wrong," the District Court followed the Fifth Circuit Court of Appeals' decisions in *Azrock* and *Unitramp*, as well as numerous other Texas state and federal decisions, and applied a "manifestation trigger" rule to the latent property damage claims in the underlying lawsuits. The District Court further held that, in light of the "discovery rule" and other allegations, the pleadings in the underlying lawsuits failed to allege any property damage that manifested itself during the policy period; rather, the pleadings clearly alleged that the damage or injury did not manifest itself until well after the policies had expired. Accordingly, the District Court held that OneBeacon did not have a duty to defend or indemnify Don's Building Supply against the claims in the underlying lawsuits.

Don's Building Supply filed a motion for rehearing which was denied and it subsequently appealed to the Fifth Circuit Court of Appeals. While the case was pending on appeal, the parties learned about the Houston 14th Court of Appeals' decision in *Pine Oak Builders* which followed *Pilgrim* and applied an "exposure trigger" rule in the context of EIFS-related claims.

In addition to resolving the "trigger" issue presented, the Fifth Circuit Court of Appeals has asked the Texas Supreme Court in this case to advise on whether the "discovery rule" allegations and other allegations in the underlying lawsuits precluded a finding of any property damage that occurred during the OneBeacon policy periods (assuming that the Texas Supreme Court should conclude that a "manifestation trigger" rule applies in this case).

For a further analysis of this "trigger" issue, please contact Gene Creely of Cozen O'Connor's Houston office. Cozen O'Connor is a nationally recognized leader in representing the insurance industry in all coverage areas, including construction defect matters.