Case No. 11-10649

---

MID-CONTINENT CASUALTY COMPANY,

Plaintiff - Appellee

v.

ELAND ENERGY, INC., SUNDOWN ENERGY LP,

Defendants - Appellants

---

ELAND ENERGY, INC.; SUNDOWN ENERGY, L.P.,

Plaintiffs - Appellants

v.

MID-CONTINENT CASUALTY COMPANY,

Defendant - Appellee

---

# BRIEF OF APPELLEE MID-CONTINENT CASUALTY COMPANY

---

Bruce E. Ramage
Texas Bar No. 16492500
*ramage@mdjwlaw.com*
Levon G. Hovnatanian
Texas Bar No. 10059825
*hovnatanian@mdjwlaw.com*
MARTIN, DISIERE, JEFFERSON & WISDOM, L.L.P.
808 Travis, 20th Floor
Houston, Texas 77002
(713) 632-1700 – Telephone
(713) 222-0101 – Facsimile

## CERTIFICATE OF INTERESTED PERSONS

**Case No. 11-10649**

**MID-CONTINENT CASUALTY COMPANY,**

Plaintiff - Appellee

**v.**

**ELAND ENERGY, INC., SUNDOWN ENERGY LP,**

Defendants - Appellants

---

**ELAND ENERGY, INC.; SUNDOWN ENERGY, L.P.,**

Plaintiffs - Appellants

**v.**

**MID-CONTINENT CASUALTY COMPANY,**

Defendant - Appellee

The undersigned counsel of record certifies that the following listed persons and entities as described in the fourth sentence of Rule 28.2.1 have an interest in the outcome of this case. These representations are made in order that the Judges of this Court may evaluate possible disqualification or recusal.

Eland Energy, Inc., Appellant,

Sundown Energy LP, Appellant,
a Texas Domestic Limited Partnership

Appellate Counsel for Apellants
Carl D. Rosenblum
Madeleine Fischer
Alida C.Hainkel
Jones Walker,
Waechter, Poitevent, Carrère &

Denègre, L.L.P.
201 St. Charles Avenue, 49th Floor
New Orleans, Louisiana 70170-5100

Apellate Counsel for Appellee

Bruce E. Ramage
Levon G. Hovnatanian
Christopher W. Martin
Robert G. Dees
Ethan D. Carlyle
Martin, Disiere, Jefferson
& Wisdom, L.L.P.,
808 Travis, 20th Floor
Houston, Texas 77002

## STATEMENT REGARDING ORAL ARGUMENT

Mid-Continent respectfully asserts that oral argument will not be helpful. It believes that oral argument will not be helpful to the Court because Judge Fitzwater's analysis in four memorandum opinions covering approximately 299 pages resolves any complexity in the issues and facts.

## TABLE OF CONTENTS

## INDEX OF AUTHORITIES

**Cases** **Page**

**Other Authorities**



**Rules**

## STATEMENT OF FACTS

Appellee Mid-Continent Casualty Company issued a commercial general liability policy listing appellants Eland Energy, Inc. and Sundown Energy, Inc. among the named insureds (primary policy). DX 32 at MC 006393, 006400. The policy period was December 31, 2004 to December 31, 2005. DX 32 at MC 006393. The policy had a $1million per occurrence limit and a $2 million general aggregate limit—the most that Mid-Continent would pay for all claims in a policy year. DX 32 at MC 006394; R 8075.

The primary policy provided that Mid-Continent "will pay those sums that the insured becomes legally obligated to pay as damages because of 'bodily injury' or 'property damage' to which this insurance applies." DX 32 at MC 006415. Mid-Continent also had "the right and duty to defend the insured against any 'suit' seeking those damages." DX 32 at MC 006415. Mid-Continent's obligation to defend ended "when we have used up the applicable limit of insurance in the payment of judgments or settlements under Coverages A or B or medical expenses under Coverage C." DX 32 at MC 006415. In other words, as long as the primary policy's limits had not been paid, the duty to defend continued. R 8207. Mid-Continent also had the right to investigate and settle claims in its discretion: "We may at our discretion, investigate any 'occurrence' and settle any claim or 'suit' that may result." DX 32 at MC 006415.

The policy also provided pollution coverage under certain circumstances. An oil and gas endorsement amended the primary policy's exclusion so that it no longer applied to a "Pollution Incident." DX 32 at MC 006507. The endorsement provided:

> "Property Damage" resulting from a "Pollution Incident" includes mandated "clean-up costs" caused by a "Pollution Incident" provided notice asserting such obligation is received by you within 180 days of the "Pollution Incident."
>
> Notice asserting such obligation must be made under statutory authority of the United States of America or by a state environmental regulatory agency.

DX 32 at MC 006507. However, the pollution coverage provided by the endorsement did not apply to cleanup costs on property Sundown leased, including its East and West Potash Facilities. R8112-13.

Mid-Continent also issued an umbrella policy that listed Eland and Sundown among the named insureds. DX 30. The umbrella policy had an aggregate limit of $5 million. R8076, DX 30 at MC 006729, 006738. It imposed no duty to defend on Mid-Continent. DX 30 at MC 006731.

Sundown provided "general liability notice of occurrence/claim" after its crude oil production facility near Port Sulphur, Louisiana was destroyed by Hurricane Katrina on August 29, 2005. PX 4. Storm surge destroyed crude oil storage tanks that were located at its East Potash and West Potash facilities on the east and west sides of the Mississippi River, respectively, resulting in the spillage

of less than 3000 barrels of crude oil. R5934. Sundown delivered the notice to Mid-Continent two weeks after the storm, on September 12, 2005. PX 4.

Chris Leopold owned property near Sundown's West Potash facility. On it were located a Dollar General Store and a boat storage shed. R6083, 6158. Both sustained severe damage. Leopold noticed that oil stained the trees on his property and what was left of the buildings. R6162-63; 8059-50. He believed that the oil came from Sundown's facility nearby. R6164.

Soon after the storm, Leopold visited a trailer in Belle Chase, Louisiana that Sundown was using as temporary offices. R6156. He identified himself and why he was there. R6157. He asked whom he needed to contact to arrange for Sundown to clean his property. R6157. The individual he was speaking with said nothing and shut the door. R6157.

Mid-Continent began its investigation of Sundown's claim, and Steve Haltom, a home office claims supervisor for Mid-Continent, acknowledged receipt of the claim in a letter to Sundown on September 16, 2005. PX 11; JX 6; R8074, 8087. Mid-Continent hired Jerry Wollaston to visit the area and survey the scope of the damage. R8091-92. After reviewing Wollaston's report, Haltom was concerned that the policies' limits would be exceeded. R8092-93.

Haltom met with Sundown's representatives at Sundown's offices in Dallas, Texas on September 21, 2005. R8094. Haltom learned that Sundown had incurred

$750,000 in costs through September 20, 2005, in complying with the Coast Guard's mandate to remove the oil. R8097. Sundown was incurring $50,000 in cleanup additional costs per day R8097. Haltom also informed Sundown that lawsuits had been filed against it. R7505.

Haltom had arranged for Steven Levine, a lawyer who specializes in environmental issues to attend the meeting. R8093, 8095. Levine told Sundown about a fund set up under the Oil Pollution Act that could reimburse Sundown for its cleanup costs. R8094-96. Also discussed at the meeting was the possible effect of Tropical Storm Rita, which was about to enter the Gulf of Mexico. R5941.

On September 23, 2005, Sundown notified Mid-Continent that it had been served in the *Blanchard* class action litigation. JX 12; R8100-01. Landowners near Sundown's facilities alleged that their property had been contaminated with Sundown's oil. JX 12 at MC 004784. Sundown was named as the sole defendant. JX 12 at MC 004784.

Also on September 23, 2005, Hurricane Rita made landfall at Beaumont, Texas. Because Katrina had destroyed Sundown's storage tanks, Rita did not cause any new oil to spill. R6008-09. Instead, it caused the dispersion of oil spilled by Katrina that had been collected by containment booms in waterways. R6008-09.

In letters dated September 28 and 29, 2005, Sundown notified Mid-Continent that it had been sued in Louisiana in the *Barasich* and *Danos* class actions. JX 14, 15. There, the plaintiffs, a group of fisherman, sought damages from a group of oil companies, including Sundown, for the spillage of oil in estuaries and waterways. JX 14 at MC 005322; JX 15 at MC 003286. Sundown and large oil companies were named as defendants. JX 14 at MC 005321-22; JX 15 at MC 003285-86.

On September 30, 2005, Mid-Continent retained Tony Clayton to represent Sundown in the litigation. R8104-05. Clayton asked Mid-Continent to hire Paul Preston, a lawyer with experience handling class actions, to assist him. R8107. Mid-Continent agreed and retained Preston to represent Sundown. R8107.

In a letter dated October 6, 2005, Sundown submitted to Mid-Continent copies of wire transfers and invoices reflecting the costs it had incurred. DX 118. Sundown submitted more than $1 million in incurred cleanup costs "for review and reimbursement." DX 118. However, Sundown did not segregate the costs incurred cleaning up its own property from those incurred for the off site cleanup required by the Coast Guard. R8114-15; PX 84. Haltom asked Wollaston to segregate the costs. PX 84.

A second meeting was arranged to discuss the defense of the lawsuits. R8122. Haltom attended the meeting on October 7, 2005, at Sundown's offices.

R8122. Clayton and Preston attended. R8122. Carl Rosenblum, who had represented Sundown in other matters, and another lawyer from Jones Walker also attended R7510.

Undercutting the class actions was discussed. R8127. Plaintiff's attorneys in the Port Sulphur area had been advertising and soliciting people to join litigation against Sundown. R6477-78; 8127. Clayton thought it imperative that Sundown be portrayed as a good corporate citizen to counter plaintiff's lawyers' radio ads seeking clients. R8127. He suggested buying advertisements showing that Sundown was a concerned citizen that would pay any claims that it owed. R8127-28. Nobody, including Rosenblum, the other Jones Walker lawyers, or Sundown voiced any opposition to Clayton's proposed plan. R8128.

Preston and Clayton also thought a visit to Sundown's facility would be tremendously beneficial. R6474. They could meet with influential citizens and demonstrate that Sundown was a good corporate citizen who was interested in the community and making an effort to resolve any legitimate claims. R6474.

Preston and Clayton also wanted to meet with Ben Slater, a landowner who had contacted Sundown after Hurricane Katrina. R6474. Slater had leased land to Sundown for its West Potash facility. R8260. They planned to undercut the *Blanchard* class action by contacting land owners who were not initially interested in joining the class and settling their claims. R6561.

Everyone agreed to coordinate legal issues through Rosenblum. R6474-75. Litigation information that was received would be sent to Jones Walker. R6475. Haltom understood the agreement pertained to the litigation and did not include Mid-Continent's investigation and settlement of claims. R8225. Haltom never agreed to limit Mid-Continent's right to investigate and settle claims. R6475.

A question was also raised regarding whether the policies' limits would be replenished by reimbursement from the OPA fund. R8222-23. Haltom initially stated that he assumed they would be replenished but then added that he did not know. R8222-23. After consulting with Mid-Continent's reinsurers, he learned that the limits would not be replenished and notified Sundown. R6495-96; JX 24 at MC 0-05263.

Several days after the meeting on October 11, 2005, Preston emailed Rosenblum stating that they had identified Sheriff Jeff Hingle, his father Irwin Hingle, who was a plaintiff in the Blanchard litigation, and Mr. Pivach as nearby property owners near Sundown's facility. JX 21. Preston stated that he and Clayton wanted to meet with Pivach, parish president Bennie Rousselle, and Ben Slater as soon as possible. JX 21. Preston noted that "Time is very much of the essence." JX 21. Rosenblum responded the next day that he would not be available for more than two weeks, until the first week of November. DX 136.

Haltom sent an October 13, 2005 email asking Rosenblum whether someone else from Jones Walker could make the trip. JX 25 at MC-005270. He stated:

> As we discussed last week, timing and an appearance at the scene is of the utmost urgency. A delay until November from an August storm for defense counsel to arrive at the site is troublesome. From the carrier's perspective, an on the scene inspection by defense counsel will clearly give a favorable impression to the local officials.

JX 25 at MC-005270. Haltom wanted Preston and Clayton to visit the area "by next week" and was "requesting Carl [Rosenblum] help to make that happen." JX 25 at MC-005270. Haltom wanted "to get lead counsel [Preston and Clayton] up to speed as quickly as possible." JX 25 at MC-005270.

On October 17, 2005, Rosenblum responded that Sundown wanted him to attend any site visit. JX 25 at MC-005269. He stated he would be in New Mexico preparing for trial until October 28 "most probably." JX 25 at MC 005269. He suggested making the visit between October 31 and November 3. JX 25 at MC-005269.

Rosenblum added that he had spoken with Slater. JX 25 at MC-005269. He stated that Slater had not filed suit and "appeared satisfied with my summary of activity and asked me to send him the most recent ES&H report. The conversation was very cordial. I did so." JX 25 at MC-005269-70.

While Slater may have been satisfied with the summary, he was not satisfied with Rosenblum. Subsequently, but on the same day, Scott Yount, a lawyer at

Preston's firm, informed Preston that he was friends with Chris Leopold. JX 25 at MC-005269. During a conversation the day before, Slater told Leopold that "he was not impressed with Rosenblum and that he did not feel anything was being done to address anyone's concerns," precisely the type of attitude that Preston, Clayton, and Mid-Continent wanted to dispel with a visit. JX 25 at MC-005269. Yount added that Leopold had offered to help them gain access to the area and show them around. JX 25 at MC-005269.

Preston then asked Haltom to authorize a visit even though Rosenblum could not attend. JX 25 at MC 005268. Haltom stated that he did not have a problem with Preston and Clayton making the trip:

> I am not concerned about some bruised ego. I agree we need to get to the site and have a plan to meet with the proper people for the proper reason. I do not think we need to go if we cannot get in front of the proper people.
>
> With that being said, I do not have a problem with you and Tony making this trip. Let's get in front of the right people and get our message out. I would like to know just what is going on, other than a daily cleaning report!

JX 25 at MC 005268. Although they discussed October 21, 24, and 25 as possible dates for the visit, Preston did not tell Haltom the day he and Clayton intended to visit. R6500.

On October 19, Rosenblum informed Haltom that he could no longer make the visit on November 2, 2005. DX 143 at SELP – 05687. On October 21

Rosenblum informed Haltom and Preston that he would be available for the visit on October 27. DX 143. Preston thought Rosenblum was intentionally trying to delay the visit. R8063. In fact, by the end of October 7, 2005 meeting, Preston was convinced that Rosenblum was trying to make a bad faith case again Mid-Continent. R8060.

On October 24 Rosenblum informed Preston and Haltom that a visit was no longer necessary. JX 27. He stated that Mid-Continent's issuance of the reservation of rights letters made a visit by Preston and Clayton "unnecessary and inappropriate" because Sundown was now insisting on choosing its own counsel. JX 27. Mid-Continent had issued reservation of rights letters regarding the lack of coverage for the intentional acts alleged in the class actions litigation. R7655.

However, Preston, Clayton, and Yount were already meeting with Leopold on October 24. Haltom was unaware that they were making the visit on that date. R8242. They talked and walked around Leopold's property looking at the damage. R8045-46, 8048. Leopold was frustrated because he had been unable to talk to anyone from Sundown. R8048-50. Leopold pointed out oil on his property. R8049. They did not talk about money or engage in settlement negotiations. R8048. Preston and Clayton were there to open communication and listen. R8048, 8049, 8051. They did not visit Sundown's facility. R8047.

While they were visiting Leopold, Slater showed up unannounced and accompanied by his attorney. R8045. They visited parts of his property and inspected the damage. R8045.

In a letter dated October 24, 2005, Sundown informed Mid-Continent that the reservation of rights letters presented a conflict of interest. JX 28. It insisted on choosing its own counsel, Jones Walker. JX 28. Haltom did not agree that there was a conflict, but honored Sundown's request to choose lead counsel. JX 32. It was determined that Jones Walker became Sundown's lead defense counsel on November 15, 2005 and that Preston and Clayton would no longer represent Sundown. R6527-28, 8217; JX 37.

Preston reported that they visited land adjacent to Sundown's West Potash facility and met with Leopold and Slater. JX 30. He observed "very clear damage that most likely was caused by oil from the Sundown facility." JX 30. He recommended immediately retaining an expert to assess the damage. JX 30. Preston also assessed Leopold and Slater:

> [A]lthough Mr. Slater (who owns the land that the West Potash facility is on as well as a significant amount of surrounding land) and the Leopolds (who own a severely damaged Dollar Store and boat storage facility) remain cooperative, it would be unrealistic to expect them to remain so. If we can win them over to our side, they will be extremely effective advocates for us but could easily become just as effective as our adversaries. In particular, Chris Leopold and his wife will make sympathetic and effective witnesses and every effort should be made to, at a minimum, neutralize them. Mr. Slater appears to have a realistic view of his claims but is sophisticated and would be a

> formidable opponent. As you may recall, Mr. Slater is a practicing lawyer with the Lemle & Kelleher firm in New Orleans and when we met, he was inspecting his property with David Minvielle who is an environmental lawyer with the Lemle firm. Again, these landowners (and I believe others who may be influenced by them) currently remain cooperative and, therefore, present us with an opportunity that is unlikely to continue to exist without some good faith effort to address their claims.

JX 30. Preston did not tell Rosenblum or Sundown about the visit. R 8066.

Leopold was the type of landowner that the defense team was looking for to undercut the class action. He wanted to settle his claim without litigation. R6117; PX 222 at MC 007363-64. He was also the owner with the most land and therefore had the biggest claim. R6650. The property was located within 500 yards of Sundown's West Potash facility. R6576. Leopold knew there was oil on his property because he could see it on the trees and buildings. R6162-63; 8049-50. He also stated he could compile a list of other owners who were not part of the class action. R6117.

On November 29, 2005, Luther Holloway visited Leopold's property. R6567. Mid-Continent had hired him to obtain an estimate of the damages caused by the oil spill. R6563-64; DX 170. He took pictures and made a video of the property. R6568. The photos and video showed oil staining on the buildings and debris on Leopold's property. Haltom concluded that Leopold's property had been stained by oil spilled from Sundown's facility. R6573.

By November 8, 2005, Wollaston was finished segregating off-site cleanup costs from on-site cleanup costs. PX 84. He recommended that Mid-Continent pay Sundown $853,943.15 based on that segregation. PX 84. On November 14, 2005, Mid-Continent mailed Sundown a check for that amount. JX 35.

Sundown returned the check on December 2, 2005. JX 39; R 8117. It stated "Eland/Sundown has decided to hold its claim for clean-up expenses in abeyance at this time . . . ." JX 39; R 8117. Sundown wanted to avoid Mid-Continent's right to subrogation by seeking reimbursement from the OPA fund first, applying any reimbursement to the cleanup costs, and using policy proceeds to settle the litigation. R7488; JX 39.

Although Haltom had worked in the insurance industry for many years, he had never heard of an insured holding a claim "in abeyance." R8117-18. The policies said nothing about any right to hold a claim "in abeyance." R8118. Moreover, Sundown had already submitted invoices for cleanup costs. R8119-20.

Haltom knew from the September 21, 2005 meeting that Sundown had been incurring $50,000 per day in cleanup costs. R8120. So, in March 2006, Sundown's incurred costs were far in excess of $1 million for the off-site cleanup costs. R8120. On March 22, 2006, Mid-Continent sent Sundown a $1 million check and paid the limits under the primary policy. R8119; JX 46. Although Mid-Continent

had paid the primary policy limits it continued to pay defense costs into September 2006. R6630.

On August 18, 2006, Mid-Continent paid Sundown $5 million under the umbrella policy. R8121; JX 68. Mid-Continent paid the limits even though the total amount of cleanup costs was $5.7 million. R8121-22. Sundown had demanded that Mid-Continent pay the limits of the umbrella policy. R8121.

Dana Futrell replaced Holloway when he became incapacitated by health issues. R6577. Futrell visited Leopold on December 19, 2005 and inspected the property. R6581; JX 4. He too was convinced that oil was present. R6581-82. Leopold wanted samples to be taken and tested. R8134-35.

Futrell hired Lambert Engineers who had been recommended by Paul Muthig. R8136. Lambert took 25 soil samples from Leopold's property. JX 45. Although two of the soil samples showed petroleum contamination, the testing confirmed no detectable crude oil in the soil was on Leopold's property around the building. R8138-39; JX 47. Futrell informed Leopold that the hotspots were diesel, not crude oil. R6143. After Leopold was informed of the results, he just wanted Mid-Continent to remove the parts of the building and debris that were covered in oil. R8140.

Haltom wanted to move forward and attempt to settle the claim. R8141. He asked Futrell to obtain an estimate for treating the two hot spots and hauling off the

debris. R8141. Futrell obtained a "worst case scenario" proposal from Greco Construction. R8145-46; JX 52. Leopold had suggested that Futrell use Greco. R8143. Although Mid-Continent would not normally obtain an estimate from a contractor referred by the claimant, there were no other contractors were willing to work in the storm ravaged parish. R8143.

Greco's estimate was $98,560. JX 52. But it included "grubbing" the entire site--the removal and hauling off of the top layer of soil that would have been necessary only if the ground had been contaminated with oil. R8144-45, 8146. Because the sampling showed that ground was not contaminated, grubbing was not necessary. R8146.

Consequently, only those parts of the estimate that covered removing and hauling the contaminated debris to the hazmat landfill were relevant in determining the cleanup costs. The debris had to be hauled to a special landfill for contaminated material. R8144.

Haltom made a settlement offer to Leopold's attorney on June 2, 2006. R8155; JX 58. He explained that Greco's proposal had included grubbing that the sampling showed was not necessary. JX 59. Haltom made an offer of $54,536 based on the removal of the contaminated debris. R8156-58; JX 58, 59. The offer was based on the site inspections, the soil sampling results, and Mid-Continent's

belief that the source of the contamination was oil from Sundown's adjacent West Potash facility. R8157.

Haltom reasoned that Mid-Continent would be cutting off the head of the class action snake if it resolved Leopold's claim. R6650. Leopold was influential and owned the largest piece of property in the closest proximity to Sundown's West Potash facility. R6650. His claim would be the largest and he would receive the largest offer. R6650. If Mid-Continent settled Leopold's claim, then the value of other claims would be less because they involved less land and it was located farther away from Sundown's facility. R6650.

Lambert Engineering had included erroneous levels for reporting the concentration of the diesel in the hotpots to the Louisiana Department of Environmental Quality. R8160. Muthig had discovered the errors and traveled to the site on June 6, 2006 to discuss the findings with Lambert's representatives. R8159; DX 248. Lambert agreed that it made a mistake. R8160.

The revised soil sampling results continued to show that Sundown's oil was not in the ground on Leopold's property. R8161. But the Lambert report had also shown Sundown’s oil was not present. However, Muthig's report confirmed staining approximately 8 to 10 feet above the ground showing that oil had been floating on top of the water. R8161-62; DX 248. Leopold did not receive Muthig's report. R6142.

Haltom informed one of the Jones Walker lawyers about the offer to Leopold on July 10, 2006. DX 266. Soon thereafter Haltom received a call from Robin McGuire, Sundown's general counsel who had attended the meetings in September and October, 2005. R8163. He was almost irrational. R8163. Although the primary policy gave Mid-Continent complete discretion to investigate and settle claims, McGuire yelled at Haltom for making the offer. R8164. It was the most unprofessional business call Haltom had ever received. R8164. McGuire demanded that Haltom withdraw the offer. R8165.

Haltom then sent a letter to Leopold's attorney withdrawing the offer. R8167; JX 63. He responded that the withdrawal gave Leopold little choice but to file suit. R8167; JX 63. Haltom did not disclose that it was Sundown's idea to withdraw the offer. R8168. He learned shortly afterward that Leopold had become a member of the *Blanchard* class action. R8169.

Mid-Continent also decided it had to intervene in Sundown's OPA fund proceeding based on Sundown's misrepresentations in its application. R8171. Sundown had indicated in the application that it had not received reimbursement from its insurance carriers for the cleanup costs. R8171. The policies also gave Mid-Continent subrogation rights in relation to the $6 million in payments it had made to Sundown. R8171. Mid-Continent was concerned that it could suffer ramifications from Sundown's misrepresentations. R8171-72. It intervened to set

the record straight. R8171. Neither Sundown nor Mid-Continent was ultimately reimbursed any amounts from the OPA fund. R5970.

While Hurricane Rita's effects had been discussed at the October 7, 2005 meeting, Sundown had not filed a claim. Sundown eventually did so in a letter dated July 12, 2006, more than nine months after the storm made landfall on September 23, 2005. R8172-73; PX 152.

Mid-Continent investigated the claim, reviewing the documents from the cleanup project to determine whether a second pollution incident had occurred. R8173-74. Sundown's filing of the claim approximately nine months after the storm adversely affected Mid-Continent's ability to investigate the claim. R8177. By the time the Rita claim was filed, cleanup was complete. R8178. That made it virtually impossible to determine whether Rita had caused any damage. R8177-78. Mid-Continent was unable to determine that a covered pollution incident occurred. R8178-79. On July 19, 2007, Mid-Continent denied the Rita claims. R8178-80; JX 83.

On August 29, 2006, Mid-Continent filed suit seeking declaratory relief. R50-60. It sought a declaration that its duty to defend and indemnify terminated when it paid the $1 million check under the primary policy on March 22, 2006. R55-57. Sundown filed a counterclaim asserting claims for common law breach of the duty of good faith and fair dealing, breach of contract, and violations of the

Texas Insurance Code. R558-607. Sundown deposited the checks in the registry of the court.

Judge Fitzwater, in summary judgment proceedings, ruled that the policies gave Sundown no right to hold its Katrina claim in abeyance. R2298. He also ruled that Mid-Continent's duty to defend suits arising out of Hurricane Katrina terminated on March 22, 2006, when Mid-Continent tendered the $1 million check to Sundown. R2298.

The jury found that Sundown did not prove its Hurricane Rita duty-to-indemnify breach-of-contract claim and its bad-faith investigation and misrepresentation claims. R3560-63. The jury also found that Sundown proved certain unfair settlement practices had been committed. R3566. But it found only that the failure to provide promptly to Sundown a reasonable explanation of the factual and legal basis in the policy for Mid-Continent's offer to Leopold was committed knowingly. R3567. The jury found that Sundown had proved its breach of the duty of good faith and fair dealing claim, which was based on alleged extreme conduct that supposedly caused injury independent of Sundown's policy claim. R3568. It found that Sundown did not prove its Hurricane Katrina duty-to-defend breach of contract claim. R3571.

The jury found that Sundown should be awarded $2 million for the increased cost of the *Blanchard* settlement. R3573. It also found additional damages of $1.75 million and $4.7 million in exemplary damages for bad faith. R3575-76.

Judge Fitzwater granted Mid-Continent's post-judgment motion for judgment as a matter of law. In a 140-page memorandum opinion and order, the court concluded that (1) Sundown did not have a claim for the breach of the duty of good faith and fair dealing in the handling of Leopold's claim; and (2) the evidence was legally insufficient to support the jury's findings that Mid-Continent had not provided a prompt, reasonable explanation for the offer to Leopold. R6928-7068.

## SUMMARY OF THE ARGUMENT

Judge Fitzwater correctly concluded that Texas law does not recognize a common-law claim for the breach of the duty of good faith and fair dealing based on the dicta in *Traver v. State Farm Mutual Automobile Insurance Co.*, 980 S.W.2d 625 (Tex. 1998, and *Republic Insurance Co. v. Stoker*, 903 S.W.2d 338, 341 (Tex. 1995). No court, including the Supreme Court of Texas, has imposed liability for common law bad faith based on the language in *Traver* and *Stoker*.

Even if there were such a claim, which there is not, the dicta applied to the handling of first party insurance claims, not the handling of third party claims like those here. Moreover, there was no evidence that Mid-Continent engaged in any

extreme conduct. It merely attempted to settle a third party claim, which the primary policy gave it a discretionary right to do. Finally, there was no evidence that the purported extreme conduct caused any injury independent and separate from the claims under the policies—another element of the language in *Stoker*.

Judge Fitzwater correctly concluded that Texas law applies. Article 21.42 mandates the application of Texas law relating to insurance to "[a]ny contract of insurance payable to any citizen or inhabitant of this State by any insurance company . . . doing business in this State . . . ." The policies here were payable to Eland and Sundown, Texas business entities that are headquartered in Dallas, Texas. Moreover, the policies were negotiated and entered into in Texas. It is undisputed that Mid-Continent is an insurance company that does business in Texas. Alternatively, application of the substantial relationship test in section 6 of the Restatement (Second) Conflicts of Laws shows that Texas law applies.

Judge Fitzwater correctly granted judgment as a matter of law on Sundown's claim under the Texas Insurance Code that Mid-Continent did not provide a reasonable explanation showing the basis in the primary policy in relation to the facts for the offer to Leopold. Haltom's July 10, 2006 letter referring to oil residue on debris on Leopold's property was sufficient to identify the primary policy's oil pollution endorsement providing coverage for a pollution incident as the basis in the policy for the offer in relation to the facts. Alternatively, Judge Fitzwater

correctly concluded that no reasonable jury could have found from the evidence that the explanation or Mid-Continent's misrepresentation of the policy was a producing cause of the $2 million in increased settlement cost of the *Blanchard* litigation.

## ARGUMENT

### I. THE DISTRICT COURT CORRECTLY RULED SUNDOWN DID NOT AS A MATTER OF LAW HAVE A BAD FAITH CLAIM BASED ON EXTREME CONDUCT.

#### A. Texas Law Does Not Recognize a Duty of Good faith For the Handling of Third-Party Claims.

An insured states a cause of action for breach of the duty of good faith and fair dealing when it alleges that there was no reasonable basis for denial of a claim or delay in payment or the insurer failed to determine whether there was any reasonable basis for the denial or delay. *Arnold v. National County Mut. Fire Ins. Co.*, 725 S.W.2d 165, 167 (Tex. 1987). The claimant "must establish (1) the absence of a reasonable basis for denying or delaying payment of the benefits of the policy *and* (2) that the carrier knew or should have known that there was not a reasonable basis for denying the claim or delaying payment of the claim." *Aranda v. Insurance Co. of N. Am.*, 748 S.W.2d 210, 213 (Tex. 1988).

> The first element of this test requires an objective determination of whether a reasonable insurer under similar circumstances would have delayed or denied the claimant's benefits. The second element balances the right of an insurer to reject an invalid claim and the duty of the carrier to investigate and pay compensable claims. This element will be met by establishing that the carrier actually knew there was no

> reasonable basis to deny the claim or delay payment, or by establishing that the carrier, based on its duty to investigate, should have known that there was no reasonable basis for denial or delay.

*Id*.

However, Judge Fitzwater recognized that under Texas law an insurer does not owe a duty of good faith and fair dealing when handling third party claims. R 6951."[A] first-party claim is stated when 'an insured seeks recovery for the insured's own loss,' whereas a third-party claim is stated when 'an insured seeks coverage for injuries to a third party.'" R6944. *Lamar Homes, Inc. v. Mid-Continent Cas. Co.*, 242 S.W.3d 1, 17 (Tex. 2007) (quoting *Universal Life Ins. Co. v. Giles*, 950 S.W.2d 48, 54 n.2 (Tex. 1997)). "'Under Texas law, an insurer owes a duty of good faith in handling its *insured's own claim* of loss.'" R6949 (quoting *Medical Care Am., Inc. v. National Union Fire Ins. Co.*, 341 F.3d 415, 425 (5th Cir. 2003) while adding emphasis and omitting citation, and citing *Vandenventer v. All Am. Life & Cas. Co.*, 101 S.W.3d 703, 722 (Tex. App.--Fort Worth 2003, no pet.)). "'An insured, however, has no claim for bad faith premised on the insurer's investigation or defense of a claim brought against it *by a third party*.'" R 6950 (quoting *Med. Care Am.* 341 F.3d at 425 and adding emphasis and omitting citations). Instead, "'[a]n insurer's common law duty in this third party context is limited to the *Stowers* duty to protect the insured by accepting a reasonable settlement offer within policy limits.'" R 6950 (quoting *Mid-Continent v. Liberty*

*Mut. Ins. Co.*, 236 S.W.3d 765, 776 (Tex. 2007)). Because Sundown's bad faith cause of action was based on Mid-Continent's handling of third-party claims, Judge Fitzwater held that "Sundown's only common law remedy in the context of a third-party claim is under *Stowers."* R 6951.

### B. Texas Courts Have Not Recognized an Exception to the Rule That an Insurer Does Not Owe Duty of Good Faith and Fair Dealing When Handling Third-Party Claims.

Sundown did not base its common law bad faith claim on the denial of or delay in payment of any claim. Instead, it argues that there are two exceptions to the rule above. First, based on two sentences from the opinion in *State Farm Mutual Automobile Insurance Co. v. Traver,* 980 S.W.2d 625 (Tex. 1998), it asserts that a claim for the breach of the duty of good faith and fair dealing exists if the insurer consciously undermined the insured's defense. Second, based on a single sentence in the opinion in *Republic Insurance Co. v. Stoker,* 903 S.W.2d 338, 341 (Tex. 1995), it asserts that a bad faith claim exists if Mid-Continent committed an extreme act that caused injury independent of the policy claim. As shown below, none of the three sentences on which Sundown relies supports the existence of a common-law bad faith claim here.

### C. The District Court Made No Ruling in Mid-Continent I Regarding the Existence of the Bad Faith Claim.

Sundown creates the false impression that Judge Fitzwater recognized an exception to the general rule in Mid-Continent I, then supposedly changed his

mind in Mid-Continent IV. Appellant's Brief at 58-59. But Judge Fitzwater never ruled that an exception existed in Mid-Continent I.

Instead, he observed that the *Stoker* court had recognized a possibility of such a claim: "*Republic Insurance Co*. also recognized that the general rule does not exclude 'the possibility that in denying the claim, the insurer may commit some act, so extreme, that would cause injury independent of the policy claim.'" R2341 (quoting *Stoker*, 903 S.W.2d at 34). He also noted that "under some circumstances the insurer can be held liable for bad faith handling of a claim even in the absence of coverage. R2341 (citing *Northwinds Abatement, Inc. v. Employers Ins. of Wausau*, 258 F.3d 345, 353 (5th Cir. 2001). But the claim there was statutory, not common law, a circumstance not present here. Judge Fitzwater did not even mention the language from the *Traver* opinion. Nowhere did Judge Fitzwater conclude that based on the language in *Stoker* or *Traver* that Sundown had a viable common-law claim for breach of the duty of good faith and fair dealing.

Sundown also claims that Judge Fitzwater's submission of the bad faith claim to the jury shows that he had concluded that a claim existed. Appellant's Brief at 58-59. However, he rebutted that contention when he addressed Mid-Continent's assertion that the questions should not have been submitted to the jury.

He submitted the common law breach of the duty of good faith and fair dealing issue in accordance with this Circuit's "preferred approach:"

> Mid-Continent maintains that the court should not have submitted this claim to the jury because Texas does not recognize this cause of action. Although the court's decision today vindicates Mid-Continent's position, the court notes that it was simply following the preferred approach. In this circuit, it is considered the better practice for a district court to "reserve ruling on the motion for [judgment as a matter of law] and let the case go to the jury." *Wiltz v. Mobil Oil Exploration & Producing N. Am., Inc.*, 938 F.2d 47, 50 (5th Cir. 1991). "The primary reason we encourage district courts to reserve judgment on motions for [judgment as a matter of law] is that if the court grants a judgment [as a matter of law], a retrial is avoided if we reverse the [judgment as a matter of law] because there is a jury verdict that can be reinstated." *Id.* (internal quotation marks and citation omitted).

R 6945. Thus, submission of the issues to the jury was not a ruling that the claim existed.

### D. The District Court Correctly Concluded No Common-Law Claim for Breach of the Duty Good Faith and Fair Dealing Has Been Recognized Based On the Language In *Traver.*

Contrary to Sundown's assertion, the *Traver* court did not "recognize[] that, unlike the mere refusal of a defense by an insurer, allegations that an insurer 'consciously undermined the insured's defense" of a third-party claim *would give rise to a claim for breach of the insured's duty of good faith and fair* dealing." Appellants' Brief at 62. A claim for the breach of the duty of good faith and fair dealing was not before the court. *Traver*, 980 S.W.2d at 626.

In *Traver*, the court of appeals held that an insurer was vicariously liable for the malpractice of the lawyers it hired to represent the insured. The Supreme Court reversed the court of appeals' holding that the insurer was vicariously liable and remanded. *Id.* at 629. The court of appeals had also held that the insured did not have a viable claim for the breach of the duty of good faith and fair dealing because it was based on the insurer's handling of a third party claim. *Id.* at 626. The insured did not apply for a writ of error on his bad faith claim, so the issue was not before the supreme court. *Id.*

The Supreme Court then rejected the insurer's contention that the scope of the court of appeals' remand was limited to claims based on the insurer's vicarious liability and that the insured had waived any claims based on the insurer's own misconduct. *Id.* at 629. It also rejected the insurer's contention that the insured's damages would be limited to the policy limits and defense costs. *Id.* The insurer based its argument on the holding in *Maryland Insurance Co. v. Head Industrial Coatings & Services, Inc.*, 938 S.W.2d 27 (Tex. 1996), which involved the insurer's erroneous refusal to defend a third-party liability claim. The court noted, "Here, the plaintiff's allegations are not that the insurer merely refused a defense, but that the insurer consciously undermined the insured's defense." *Id.* at 629. Thus, on remand, the recoverable damages did not necessarily fall within the scope of the *Head Industrial* opinion.

The court did not equate this difference in the allegations to a bad faith claim. Nor did it identify any theory of liability that the allegations would support. In fact, Justice Gonzalez noted in his concurring and dissenting opinion that the majority remanded "without indicating what other theories of liability might be viable." *Id.* Moreover, the court made no exception for allegations of consciously undermining the defense when it declared that "the court of appeals' judgment on the *Stowers* duty, the duty of good faith and fair dealing, or any statutory claim relating to those duties the court of appeals' judgment regarding those claims is final." *Id.*

Judge Fitzwater also refused to recognize the *Traver* language as support of the existence of a common-law bad faith claim because no state or federal court had adopted the sentences as a basis for imposing liability. R6954. Sundown has failed to show otherwise.

### E. The District Court Correctly Concluded That No Common-Law Claim for Breach of the Duty Good Faith and Fair Dealing Has Been Recognized Based On the Language In *Stoker*.

Judge Fitzwater also concluded that language in the *Stoker* opinion did not establish a new kind of claim for the breach of the duty of good faith and fair dealing. Sundown asserted that the following sentence from the opinion was the Supreme Court's recognition of such a claim: "'We do not exclude, however, the possibility that in denying the claim, the insurer may commit some act, so extreme,

that would cause injury independent of the policy claim.'" *Stoker*, 903 S.W.2d at 344. Judge Fitzwater wrote a nine-page analysis correctly rejecting Sundown's contention. R6955-65.

The *Stoker* court "addressed a claim of breach of good faith and fair dealing in the context of a first-party insurance claim, not a third-party insurance claim." 6956. In other words, *Stoker* did not involve the insurer's handling of a liability claim against the insured. Instead, the insurer had denied the insured's claim under its policy for uninsured motorist benefits, a first-party claim.

Here, it is undisputed that the Leopold's claim was a third-party claim. Judge Fitzwater rejected Sundown's contention: "Sundown complains that Mid-Continent's handling of third-party claims damaged Sundown. *Stoker* says nothing regarding an insurer's duty of good faith and fair dealing in its handling of third-party claims." R 6957.

Moreover, the *Stoker* court recognized a "possibility," not a claim. In *Potomac Insurance Co. v. Woods*, 1996 WL 450687, at *6 (E.D. Tex. 1996), the court stated "[i]n dicta the [*Stoker*] court left open the theoretical possibility that in a case in which the insurer has no liability under the policy there could be a bad faith claim; however, the court made clear that only the most extreme acts could subject an insurer to bad faith liability." In *Laas v. State Farm Mutual Automobile Insurance Co.*, 2001 WL 1479228, at *4 (Tex. App.—Houston [14th Dist.] 2001,

no pet.) (not designated for publication), the court concluded "the supreme court in *Stoker*, mentioned in dicta the possibility, that in denying a claim, an insurer might commit some act, so extreme, there could be an injury independent of the policy claim." In *General Star Indemnity Co. v. Sherry Brooke Revocable Trust*, 243 F.Supp. 2d 605, 612 (W.D. Tex. 2001), the court referred to the language from *Stoker* as "a single line of dictum." In *Valley Forge Insurance Co. v. Shah*, 2009 WL 291080 at *11 n.84 (S.D. Tex. 2009), the court noted "that the *Stoker* court did not find that any extreme act had occurred in that instance and did not offer any insight into what might be considered an extreme act justifying a bad faith finding."

Even the court that issued the *Stoker* opinion did not regard it as recognizing a new type of claim for the breach of the duty of good faith and fair dealing. In *American Motorists Insurance Co. v. Fodge*, 63 S.W.3d 801, 804 (Tex. 2001), it emphasized the lack of any example of the extreme conduct. "In *Republic Insurance Co. v. Stoker*, we did not exclude the possibility that an insurer's denial of a claim it was not obliged to pay might nevertheless be in bad faith if its conduct were 'extreme' and produced damages unrelated to and independent of the policy claim. We cited no examples." (Footnote omitted.) In *Provident American Insurance Co. v. Castaneda*, 988 S.W.2d 189, 199 (Tex. 1998), the court characterized its own language in *Stoker* as "there might be liability for damage to

the insured other than policy benefits or damages flowing from the denial of the claim if the insured mishandled a claim." Judge Fitzwater concluded that the "*Stoker* language is *dicta* and expresses a mere possibility that bad faith liability could be imposed in regard to a first-party claim in specific circumstances that the Supreme Court of Texas has yet to identify." R6959.

Sundown claims "the various cases referenced by the district court show – not that Texas courts have rejected the existence of a *Stoker* "extreme act" claim – but instead that the Texas courts have consistently reaffirmed it as a possibility while not yet finding a case with facts sufficiently extreme to apply it." Appellants' Brief at 65. But despite having had more than 15 years since the *Stoker* opinion issued to transform that "possibility" into actuality, the Supreme Court of Texas, Texas courts of appeals, and federal courts have not done so. In fact, no court has even given an example of an extreme act that would cause injury independent of the policy claim that would support a common-law bad-faith claim. But even if one had, it would be relevant only to the handling of a first-party claim, not third-party claims like those here.

### F. No Texas Court Has Imposed Liability Based on the *Stoker* Language.

Confirming that the *Stoker* language is not actionable as a bad faith claim is the absence of any opinion from a Texas court using it to impose liability. Judge Fitzwater observed "[s]everal Texas courts discuss the language used in *Stoker*,

and some appear to assume that it *could* apply, but none expressly holds that *Stoker* or the *Stoker* language creates a common law claim under the facts of a particular case." R6959-60. He noted that in *Castaneda*, the supreme court concluded that even if there was a claim based on the *Stoker* language, the insured could not recover because it did not satisfy its second prong—proving injury independent of the claim. R6960 (citing *Castaneda*, 988 S.W.2d at 199). In *Deschenes v. Farmers Insurance Exchange*, 2002 WL 971911 (Tex. App.--Dallas 2002, pet. denied) (not designated for publication), the court held that evidence that the insurance agent gave the insured "inappropriate information regarding coverage" and failed to notify the insurer about a "potentially serious claim" did not raise a fact issue regarding the existence of extreme conduct. R6960 (citing *id*. at *4). Similarly, in *Gates v. State Farm County Mutual Insurance Co.*, 53 S.W.3d 826, 832 (Tex. App. – Dallas 2001, no pet.), the court concluded that if there were a bad faith claim, the insured had not raised a genuine issue of material fact that would defeat summary judgment when he presented evidence that the insurer had breached a rule 11 agreement after the claim was denied and litigation had begun. Again in *Betco Scaffolds Co. v. Houston United Casualty Insurance Co.*, 29 S.W.3d 341 (Tex. App.—Houston [14th Dist.] 2000, no pet.), the court assumed that if there were a cause of action based on the *Stoker* language the insured's allegation that the insurer had spoliated the claim file was not "'so extreme as to

cause [the insured] injury independent of its policy or bad faith claims.'" R6961 (quoting *id*. at 348). Judge Fitzwater "found no Texas state court that holds that a recovery is available under the *Stoker* language in the first-party claim context, much less in the context of handling of a third-party claim." R6962.

Judge Fitzwater also showed, that with the exception of this Court's opinion in *Northwinds Abatement, Inc. v. Employers Insurance*, 258 F.3d 345 (5th Cir. 2001), no federal court had permitted recovery under the *Stoker* language. R6963-65. In *Shah*, the court held that the extreme nature of the insured's damages did not equate to extreme action by the insurer. 2009 WL 291080 at *11. In *General Star*, the insureds argued that because the insurer waited too late to investigate and deny their claim, it engaged in extreme conduct. But the court granted summary judgment against them because they failed to provide evidence of causation or damages. 243 F.Supp.2d at 613. In *Woods*, the court noted that the *Stoker* court "hinted that the wholesale failure to investigate might be the type of act that could expose an insurer to a meritorious bad faith claim." 1996 WL 450687, at *6. However, the insureds had conceded facts that established an absolute policy defense. *Id*. at *7. The court concluded that the case did not fall within the possible exception noted in *Stoker* because "a detailed factual investigation by the insurer was not required to properly deny the claim . . . ." *Id.* Judge Fitzwater concluded: "[N]o Federal court (including *Northwinds),* as the Court will explain

below) had held that an insured can recover under the *Stoker* language for breach of the duty of good faith and fair dealing." R6965.

### G. The Court In *Northwinds* Did Not Apply the *Stoker* Language In the Context Of a Common-Law Claim For Breach Of the Duty Of Good Faith and Fair Dealing.

This Court's opinion in *Northwinds* is the only one that has recognized a recovery under the *Stoker* language. However, the claim there was not for common-law breach of the duty of good faith and fair dealing. It was statutory. The issue was whether the insured could recover based on the *Stoker* language under the DTPA or Insurance Code, when it had no viable breach of contract claim. *Northwinds,* 258 F.3d at 352.

The insured had obtained coverage through the Texas Workers' Compensation Insurance Facility. *Id*. at 348. Wausau was the primary servicing company that issued the policy. *Id*.

The insured sued Wausau for mishandling workers' compensation claims filed by the insured's employees. *Id*. It alleged that Wausau had paid the claims without a proper investigation which increased its premiums and caused it to lose business due to customer perception that the insured was a safety risk. *Id*. It alleged fraudulent and bad faith settlement practices, breach of contract, negligence, and violations of the Texas DTPA and Insurance Code. *Id*. In a previous appeal, this Court affirmed summary judgment against the insured on its

claim for breach of the duty of good faith and fair dealing. *Id*. at 349. The jury rejected the insured's breach of contract claim. *Id*.

The insured could not recover under Texas law on its remaining common-law claims for negligent claims handling and fraud on the contract because that would have violated state contort principles. To recover the defendant's conduct had to "give rise to liability independent of the fact that a contract exists between the parties . . . ." *Id*. at 352 (quoting *Southwestern Bell Tel. Co. v. Delaney*, 809 S. W. 2d 493, 494 (Tex. 1991)). The insured could not establish liability independent of the contract's existence, so its common-law claims failed. *Id*.

The insured's remaining claims were statutory. The court noted that Wausau had successfully encouraged the facility to institute baseless litigation against the insured. *Id*. at 353. The Court emphasized that there was no viable claim for the breach of the duty of good faith and fair dealing and referred to the *Stoker* language during its analysis of the insured's DTPA and insurance code claims: "Where, as here, there has been no breach of contract or violation of the duty of good faith and fair dealing, the bar for establishing extra-contractual liability is high: the insurer must 'commit some act, so extreme, that [it] would cause injury independent of the policy claim.'" *Id*. (quoting *Stoker*, 903 S.W.2d at 341). The insured sought as damages the costs it incurred defending the baseless suit. *Id*. The court held that the evidence supported the jury's finding:

> Wausau's successful efforts to persuade the Facility to sue Northwinds baselessly involved acts that a reasonable jury could find extreme, and they clearly caused Northwinds extra-contractual damages, as the company had to spend over $55,000 defending itself against the lawsuit. Examined under the deferential standard of appellate review, the evidence supports the finding of an ***extreme extra-contractual act*** sufficient to satisfy the *Stoker* standard.

*Id*. (emphasis added).

As Judge Fitzwater observed, "[t]he panel therefore mentioned the *Stoker* language in affirming the insurer's liability under the Insurance Code and the DTPA (extra-contractual remedies) in the absence of a breach of contract remedy and in light of the insured's extreme acts." R6967. The Court did not apply the language in assessing a common-law bad-faith claim: "The panel did not allow for or apply an exception to the general rule that there is no cause of action for breach of duty of good faith and fair dealing" arising from the handling of a third-party claim. R6967.

Judge Fitzwater also concluded that the *Northwinds* holding was not binding because "several Texas cases decided after *Northwinds* indicate that the *Stoker* language is not well-established Texas law." R6967. The Supreme Court did not mention *Northwinds* in two subsequent opinions. In 2005, four years after the *Northwinds* opinion but with no reference to it, the supreme court continued to characterize the *Stoker* language as a "possibility:" "We have left open the possibility that an insurer's denial of a claim it was not obliged to pay might

nevertheless be in bad faith if its conduct was extreme and produced damages unrelated to and independent of the policy claim." *Progressive Mut. Ins. Co. v. Boyd*, 177 S.W.3d 919, 922 (Tex. 2005). In *Fodge*, four months after the *Northwinds* opinion issued, the supreme court noted that a claim based on the *Stoker* language was merely a possibility: "[W]e did not exclude the possibility that an insurer's denial of a claim it was not obliged pay might nevertheless be in bad faith if its conduct were 'extreme' and produced damages unrelated to and independent of the policy claim. We cited no examples." 63 S.W.3d at 804. The court did not mention the *Northwinds* opinion.

Similarly, Judge Fitzwater noted that three subsequent opinions from Texas courts that dealt with the *Stoker* language did not mention the *Northwinds* opinion. R6968. In *Laas*, 2001 WL 1479228 at *4, *Gates*, 53 S.W.3d 831-32, and *Crocker v. American National Insurance Co.*, 211 S.W.3d at 928, 936 (Tex. App.—Dallas 2007, no pet.), the courts did not mention the *Northwinds* opinion and recognized no liability based on the *Stoker* language. Federal district court opinions also did not mention the *Northwinds* opinion. *Shah*, 2009 WL 291080, at *11 & n.84; *General Star*, 243 F.Supp.2d at 612. Judge Fitzwater correctly held:

> Based on the decisions of the Supreme Court of Texas that mentions the *Stoker* language and the decisions of Texas courts of appeals that have addressed the question, the court holds that there is no cause of action against an insurer for breach of duty of good faith and fair dealing in the context of third-party claims handling under Texas law.

R6970.

### H. In Any Event, the *Northwinds* Opinion Does Not Apply Because There the Court Dealt With Injury Independent and Separate From the Claims.

As Judge Fitzwater observed, Wausau's liability for the defense costs was independent of the claims because encouraging the facility to sue the insured did not involve Wausau's claims processing, settlement practices, or anything related to the underlying workers compensation claims. The "possibility" that the *Stoker* court recognized applied only to injury independent of the handling of the claim. But the alleged injury here was independent of the handling of the claims:

> Assuming arguendo that these are extreme acts under the *Stoker* language, *Northwinds* is distinguishable because Northwinds suffered injury that was entirely independent and separate from Wausau's handling of Northwinds' workers' compensation claims. In *Northwinds*, the servicing company (Wausau) persuaded the insurer (the facility) to baselessly sue the insured (Northwinds). Northwinds in turn sued Wausau, not only for its handling of the workers' compensation claims, but also for prompting the facility to file a lawsuit against Northwinds that caused it to suffer an injury (defense cause) that was completely unrelated to the workers' compensation claims. In contrast to *Northwinds*, Sundown does not rely on actions by Mid-Continent or injuries by Sundown that are independent of Sundown's policy claim Sundown tendered *Blanchard* to Mid-Continent and requested defense and indemnification on September 23, 2005. Sundown complains that, in handling third-party claims against Sundown, Mid-Continent acted unreasonably in its investigation and in making offers to third parties (namely, Leopold). In fact, Sundown specifically argues that Mid-Continent acted with the purpose of exhausting Sundown's *policy limits*. All of the behavior by Mid-Continent of which Sundown complains, and Sundown's alleged injuries, flow directly from Mid-Continent's handling of third-party claims pursuant to its defense and

> indemnification of Sundown under the insurance policies. And, unlike the plaintiff in *Northwinds*, Sundown does not assert that Mid-Continent encouraged the party to sue Sundown for purposes unrelated to Mid-Continent's defense and indemnification of Sundown; rather, Sundown alleges that Mid-Continent incited and encouraged third parties to sue Sundown for injuries that were the subject of the insurance policies.

R6974-75 (record citation omitted). Judge Fitzwater properly granted the motion for judgment as a matter of law because Sundown produced legally insufficient evidence that it suffered an injury independent of the handling of the claims.

Sundown claims that Mid-Continent's acts "were independent of Sundown's policy claims in that they were unrelated to the class action lawsuits or the cleanup claim which were the only claims Sundown presented to Mid-Continent and the only claims of which Sundown was aware." Appellants' Brief at 69. Sundown conveniently ignores the record and its liability theory.

The evidence established that Clayton's and Preston's visit with and Mid-Continent's offer to Leopold was related to the *Blanchard* litigation. They were designed to undercut the class action. Everyone recognized that nearby landowners were potential *Blanchard* class action members. Preston suggested a visit to show that Sundown was concerned and would pay legitimate claims. R8127-28. The visit was designed to show landowners they would not have to join the *Blanchard* litigation in order to submit their claims. R8127. Mid-Continent's offer to Leopold was also related to the *Blanchard* litigation. It was intended to keep him from

becoming a member of the *Blanchard* class action. It was designed to cut the "head off the snake" off the *Blanchard* class. R6650. Leopold was influential among nearby landowners and owned the largest piece of property in the closest proximity to Sundown's West Potash facility. R6650. His claim would be the largest and he would receive the highest offer R6650. If Mid-Continent settled Leopold's claim, then the value of other claims would be less because they involved less land and the land was located further away from Sundown's facility. R6650. Moreover, Sundown asserted that Mid-Continent was trying to manufacture claims like Leopold's so that it could exhaust the primary policy's limits and terminate its duty to defend in *Blanchard*.

The *Stoker* language does not establish a bad faith claim here for an additional reason – Mid-Continent did not deny the Katrina claim. The *Stoker* language reads: "We do not exclude, however, the possibility that ***in denying the claim***, the insurer may commit some act, so extreme, that would cause injury independent of the policy claim." The *Stoker* language recognizes no "possibility" that ***in paying*** a first-party claim, let alone a third-party claim, the insurer could commit some extreme act. Here, Mid-Continent did not deny Sundown's Katrina claim. It paid the policies' limits to Sundown. Moreover, it did not deny Leopold's claim or any other third-party's. It merely withdrew the offer to Leopold in response to Sundown's demand. No Texas court has even mentioned

the "possibility" that an insurer could commit an extreme act by paying third-party claims, let alone offering to pay them.

Sundown relies on four self-proclaimed "factors" that supposedly support the existence of a common-law bad faith claim based on the language in *Traver and Stoker*. First, it contends Mid-Continent used Preston and Clayton against Sundown to promote Mid-Continent's own interests. Appellants' Brief at 71. However, Sundown fails to point to any specific harm it sustained. Preston, Clayton, and Yount visited Leopold and Slater on October 24, 2005, to further the strategy of showing that Sundown was a good neighbor and was concerned. R8040. The trip was an opportunity to look at conditions near Sundown's facility and assess the damage. R8046. They did not discuss settlement, Sundown's liability, or cleanup costs. R8048. In short, Sundown fails to show how the visit was used against it or harmed it in any way.

Second, it contends Mid-Continent was attempting to exhaust policy limits to avoid continuing the defense of Sundown. Appellant's Brief at 72. But no reasonable trier of fact would have concluded that Mid-Continent need to "manufacture" third-party claims to exhaust primary policies' limits. At the first meeting, Sundown stated it was incurring $50,000 per day in cleanup costs. R 8097. Before Haltom made the offer to Leopold, Sundown had requested that Mid-Continent reimburse it under the primary policy for government mandated

cleanup costs. DX 118; R8112. After identifying and segregating costs attributable to the remediation of Sundown's own property, which were not covered under the primary policy. Mid-Continent paid Sundown $853,943.15, which Sundown returned. JX 35, 39; PX 84. On March 22, 2006, Mid-Continent paid the $1 million primary policy limits. R8119-20; JX 46. Haltom made the offer to Leopold on June 2, 2006. R8155; JX 58. There was no evidence that the offer to Leopold was designed to reduce or exhaust the primary policy's limits.

Sundown also says that insurers can terminate the duty to defend by settling claims for policy limits, but those settlements must be in good faith. Appellant's Brief at 72-73. It also states although the district court found that Mid-Continent tendered its primary limits on March 22, 2006, "that did not free it to waste excess limits in extravagant and excessive settlements such as it proposed to Leopold on June 2, 2006." Appellant's Brief at 73-74. But Mid-Continent never paid Leopold anything as a settlement and did not terminate its defense by exhausting the primary policy's limits through the payment of any settlement to third parties. Mid-Continent owed no duty to defend under the umbrella policy regardless of the exhaustion of its limits. DX 30 at MC-006731. It paid the umbrella policy's $5 million limits directly to Sundown, not to third parties. R8121; JX 68. Moreover, as the district court observed, the principles do not apply to the umbrella policy because Mid-Continent owed no duty to defend under it. R1398.

Third, Sundown contends that "Mid-Continent was defending Sundown under a reservation of rights at the time it committed the acts of bad faith." Appellants' Brief at 74. But Sundown ignores that before Mid-Continent had issued any reservation of rights letter, Sundown had retained independent counsel, Rosenblum and Jones Walker. Moreover, the rights reserved were not related to Leopold's claim – there was no contention or evidence that the oil on Leopold's property was the result of Sundown's intentional acts. The reservation of rights letters do not support the existence of a common law claim for the breach of the duty of good faith and fair dealing based on the *Stoker* language.

The supposed fourth factor that Sundown identifies is "the consequences of Mid-Continent's bad faith conduct were magnified because *Blanchard* was a class action." Appellants' Brief at 75. But Sundown identifies none of those purported consequences. It asserts that "Mid-Continent tried to set a high baseline for Leopold's property that they intended to apply "in seeking out and settling other claims outside the class action" and "[t]his greatly affected the ability of Sundown to resolve the class action or achieve a dismissal for nothing." Appellants' Brief at 75. Conspicuously absent is any reference to the record establishing any adverse effect Mid-Continent's purported attempt had on that ability.

Sundown also contends that Haltom's offer to Leopold was four times greater than what the *Blanchard* plaintiffs' opening settlement demand would have

yielded on a per household basis and that Sundown's exposure was increased to approximately $38 million. Appellants' Brief at 76. But the *Blanchard* plaintiffs' initial demand was $9.5 million, not $38 million. R6379, The *Blanchard* litigation settled for $2 million -- $7.5 million less than the initial demand – after Leopold joined the class and became its representative. R6393. In fact, Leopold received about half of what Mid-Continent had offered. R6395. Nor was there any evidence that the *Blanchard* class action could be dismissed with Sundown paying nothing.

## I. In Any Event, An Insurer's Attempt to Exercise Its Contractual Right to Settle a Claim Is Not an "Extreme Conduct."

Exercising a contractual right to settle claims is not extreme conduct. Sundown argues that Mid-Continent's offer was an egregious act because the Coast Guard's report purportedly showed that Sundown's oil was not spilled in the zone in which Leopold's property was located. It also faults Mid-Continent for purportedly making the offer without any conclusive evidence that the oil on the debris on Leopold's property came from Sundown's facility. But the policy did not require a third-party claim to be meritorious before Mid-Continent had the right and discretion to settle it. In short, the policy does not preclude Mid-Continent's discretion to settle doubtful, invalid, or even frivolous claims, nor does the common law.

Confirming this discretionary right is the opinion in *Wayne Duddlesten, Inc. v. Highland Insurance Co.*, 110 S.W.3d 85, 96-97 (Tex. App.—Houston [1st Dist.]

2003, pet. denied). There, the insured alleged the insurer "negligently settled and paid invalid worker's compensation claims that had been asserted against appellant." *Id*. at 97. The trial court granted summary judgment in favor of the insurer. *Id*. The court of appeals noted:

> Appellant is not alleging in this case a traditional *Stowers* claim in that appellees negligently failed to settle a claim where there was an offer of settlement within policy limits. Rather, appellant is arguing that appellees negligently settled and paid invalid worker's compensation claims that had been asserted against appellant.

*Id* . It is affirmed:

> We are not aware of any authority from the Texas Supreme Court that expressly permits plaintiffs to sue insurers, outside of the scope of *Stowers*, for the negligent handling of claims. . . . A recent Fifth Circuit decision has also noted that, with regard to third-party insurance claims, *Stowers* provides the only common law tort duty in Texas in that setting. *Ford v. Cimarron Ins. Co.*, 230 F.3d 828, 832 (5th Cir. 2000). We are unwilling to expand the scope of an insurer's duties to the insured without express language from the Texas Supreme Court authorizing us to do so.

*Id*.

In *Kreit v. St. Paul Fire & Marine Insurance Co.*, 2006 WL 322587, at *1 (S.D. Tex. 2006) (not designated for publication), a physician alleged a bad faith claim against his medical malpractice carrier for settling an invalid, "utterly frivolous" and "completely defensible" claim. The court rejected the physician's claim:

> Dr. Kreit "is not alleging in this case a traditional *Stowers* claim in that [St. Paul] failed to settle a claim where there was an offer of

> settlement within policy limits." *Duddlesten*, 110 S.W.3d at 97. Rather, it is Dr. Kreit's position that St. Paul wrongfully settled and paid an invalid medical malpractice claim against him. Such claims are not recognized under Texas law.

*Id*. at *8.

In *Methodist Hosp. v. Zurich Am. Ins. Co*., 329 S.W.3d 510, 514 (Tex. App.—Houston [14th Dist.] 2009, pet. denied), the insured asserted that a workers' compensation carrier breached the duty of good faith and fair dealing by paying claims that "were not compensable because of pre-existing conditions," "failed to dispute compensability within the deadline prescribed by the Texas Workers' Compensation Act," and "improperly approved payment of these benefits." The court held that the insurer's contractual right to settle claims included the right to settle invalid claims:

> Likewise, we reject Methodist's suggestion that the duty to defend required Zurich to dispute payment for any benefits that might not be due under workers' compensation law. This interpretation would render meaningless the provision immediately following that gave Zurich the right to settle claims. Accordingly, the duty-to-defend provision did not impose an obligation to pay only valid claims.

*Id*. at 524. While rejecting the settlement of an invalid claim as a basis for the insured's extra-contractual claims under the DTPA and Insurance Code, the court noted "the fact the insured might incur financial loss if the insurer paid an invalid claim did not persuade the court [in *Duddlesten*] to disregard the right-to-settle

provision or impose an extra-contractual duty not recognized under Texas law." The court continued:

> In fact, a Texas court has addressed, albeit in an unpublished opinion, an insured's complaint its general liability insurer improperly investigated and settled a suit for an amount that invoked the insured's high deductible, despite its disapproval. *Stevens Transport, Inc. v. Nat'l Cont'l Ins. Co*., No. 05-98-00244-CV, 2000 WL 567225 (Tex. App.—Dallas May 11, 2000, no pet.) (not designated for publication). In affirming a directed verdict for the insurer on all causes of action, including breach of contract and negligence, the court of appeals relied on the policy provision unambiguously vesting the insurer with an absolute right to settle third-party claims based on its own discretion. *Id.* at *3. The court stated, "[b]y purchasing an insurance policy that did not give [the insured] the right to reject a settlement of third party claims, [it] gave up the right to complain that the settlement caused it damages" and "*mere presence of the large deductible does not change the result*." *Id*. (emphasis added).

*Id*. at 524-25. Thus, settling an invalid claim, let alone offering to settle one, is not actionable under Texas law and is not evidence of extreme conduct even if it adversely affects the insured.

### J. Judge Fitzwater Also Concluded That No Reasonable Jury Could Have Found From The Evidence That The Offer To Leopold Caused $2 Million In Increased Costs To Settle The *Blanchard* Litigation.

Judge Fitzwater summarized Sundown's causation theory:

> In sum, and as explained more fully below, Sundown generally complains that, because of Mid-Continent's activities, Sundown was unaware of the complete circumstances surrounding the Leopold offer. Sundown maintains that, but for Mid-Continent's misconduct, Sundown would have had the opportunity to discuss the offer with Leopold and to persuade him not to join the *Blanchard* class, not to become the *Blanchard* class representative, and not to discuss his

> offer with his neighbors or other class members. Sundown suggests that, had it been given that opportunity, it would have been able to settle *Blanchard* for less than $2 million.

R6979-80. He concluded that Sundown did not support its theory with sufficient evidence:

> Sundown did not adduce any evidence, however, from which a reasonable jury could have found that, given the opportunity and the information it needed, and without any interference from Mid-Continent, Sundown would have been successful in its attempts to discuss the offer with Leopold or to persuade Leopold not to join the *Blanchard* class, not to become the class representative, or not to discuss his offer with others. In other words, although Sundown argued that it *would have tried* to accomplish these goals, it offered no evidence from which a reasonable jury could have found it more likely than not that Sundown would have succeeded. Moreover, Sundown's motivation to settle *Blanchard* was not solely based on Mid-Continent's investigation of the damage to Leopold's property and the Leopold offer. McGuire testified that one reason Sundown settled *Blanchard* was out of concern about jury sympathy for hurricane victims.

R 6980.

Similarly on appeal, Sundown does not identify any evidence in the record that supports its theory at trial. It identifies no evidence showing that it would have succeeded in persuading Leopold not to join the *Blanchard* class, not to become the class representative, and not to discuss the offer with his neighbors or class members. Nor does it show that the *Blanchard* litigation could have been resolved without Sundown paying anything. Sundown has failed to show that Judge Fitzwater's conclusion was erroneous.

## II. JUDGE FITZWATER CORRECTLY CONCLUDED THAT TEXAS LAW APPLIES.

Although it is undisputed that the significant relationship test as set out in section 6 of the Restatement (Second) Conflict of Laws applies, Sundown ignores important steps that must be followed to apply it. Instead, Sundown cherry picks portions of comments under section 6.

### A. Article 21.42 of the Texas Insurance Code Mandates The Application of Texas Law.

But section 6 does not require that the comments be consulted first or even at all. It directs a court to follow the statutory directives of the forum. §6 (1). Here, that statutory directive is article 21.42 of the Texas Insurance Code:

> Any contract of insurance payable to any citizen or inhabitant of this State by any insurance company or corporation doing business within this State shall be held to be a contract made and entered into under and by virtue of the laws of this State relating to insurance, and governed thereby, notwithstanding such policy or contract of insurance may provide that the Contract was executed and the premiums and policy) in case it becomes a demand) should be payable without this State, or at the home office of the company or corporation issuing the same.

Eland, a named insured, is a citizen of Texas because it is incorporated there, and maintains its principal place of business there. R1326. Sundown is a Texas limited partnership whose general and limited partners are citizens and residents of Texas. R1326. It is undisputed that Mid-Continent does business in the State of Texas. Both the primary and umbrella policies are payable to Eland and Sundown as the

named insureds. DX 32 at MC 6393, 6400. The contracts were made in Fort Worth, Texas. (R Supp 4 #1 291,313. Thus, Texas common law defining the duties an insurer owes to an insured is law "relating to insurance" and applies. *See* art. 21.42.

Mid-Continent raised the choice of law issue in its motion for summary judgment contending that article 21.42 governed and Texas law applied. On appeal, Sundown does not argue that article 21.42 was an erroneous basis for the granting of summary judgment and the application of Texas law.

If article 21.42 is not applicable, which it is, section 6 requires a court to determine whether the parties included an express choice of law provision in the contract. §6. If there is no express choice of law provision, a court determines whether a choice of law provision may be implied. *Scottsdale Ins. Co. v. National Emergency Serv., Inc.*, 175 S.W.3d 284, 291 (Tex. App.--Houston [1st Dist.] 2004, pet. denied); Restatement (Second) Conflict of Laws § 187 cmt. (a). Neither policy contains an express choice of law provision, but the primary policy included endorsements that show that the parties intended Texas law to apply. One endorsement is entitled "TEXAS CHANGES—DUTIES" that adds language to the "Duties Condition" section establishing the parties intended Texas law to apply.[1]

[1] The parties also included endorsement changing the policy in accordance with Wyoming law. DX 32 at MC 006447; 006462-63. However, there is no contention that Wyoming law applies here.

DX 32 at MC 006446, 006461. Other endorsements also showed that the parties intended Texas law to apply. DX 32 at MC 006450, 006446, 006464. There are no endorsements regarding Louisiana law. Thus, the second step dictated by section 6 also shows that Texas law applies. *See Sonat Expl. Co. v. Cudd Pressure Control, Inc.*, 271 S.W.3d 228, 236 (Tex. 2008) (concluding "contracts should be governed by the law the parties had in mind when the contract was made").

### B. Sundown Ignores Contacts For Applying The Principles In Section 6.

In any event, Sundown conveniently ignores the contacts listed in sections 188 and 145 of the Restatement that are "to be taken into account" when applying the principles of section 6. *See* § 188(2) and § 145 (2); *Advanced Environmental Recycling Technologies, Inc. v. American International Specialty Lines Ins. Co.*, 399 Fed. Appx. 869, 872 n.1 (5th Cir. 2010) (applying section 188); *Sonat Expl. Co. v. Cudd Pressure Control, Inc.*, 271 S.W.3d 228, 233-34 (Tex. 2008) (applying section 188); *Scottsdale Ins. Co. v. National Emergency Serv., Inc.*, 175 S.W.3d 284, 293 n.2 (Tex. App. – Houston [1st Dist.] 2004, pets denied).(although the insured elected to recover only under article 21.21 of the Insurance Code because a breach of contract claim was asserted and the tort claims related back to the contract the court evaluated the contacts under both sections 188 and 145). The reason for this is clear—the contacts heavily favor the choice of Texas law.

Section 188 of the Restatement provides:

(1) The rights and duties of the parties with respect to an issue in contract are determined by the local law of the state which, with respect to that issue, has the most significant relationship to the transaction and the parties under the principles stated in § 6.

(2) In the absence of an effective choice of law by the parties (see § 187), the contacts to be taken into account in applying the principles of § 6 to determine the law applicable to an issue include:

(a) the place of contracting,

(b) the place of negotiation of the contract,

(c) the place of performance,

(d) the location of the subject matter of the contract, and

(e) the domicil, residence, nationality, place of incorporation and place of business of the parties. These contacts are to be evaluated according to their relative importance with respect to the particular issue.

(3) If the place of negotiating the contract and the place of performance are in the same state, the local law of this state will usually be applied, except as otherwise provided in §§ 189-199 and 203."

The place of purchase and contracting was Texas. Eland, which listed its mailing address in Dallas, Texas, negotiated the purchase of the policies through an insurance agent in Fort Worth, Texas. R Supp. 4, #1 at 313. Mid-Continent's authorized representative countersigned the policies' declaration pages in Fort Worth, Texas. R Supp. 4, #1, 313. There is no evidence that Louisiana was the site of any part of the purchase or negotiation of the policies.

The place of performance was Texas and Oklahoma. Eland's notice of claim was prepared by its insurance agent in Fort Worth, Texas. R Supp. 4, #1 341-42. Written correspondence regarding the claims passed between Eland's office in Dallas, Texas and Mid-Continent's home office in Tulsa, Oklahoma. R Supp. 4, #1 344-45, 350, 359-60, 362. Mid-Continent tendered payment under both policies to Eland in Dallas, Texas. R Supp. 4, #1 at 359-60, 365-67, 374-76. Sundown provided notices of suits from its office in Dallas, Texas to Mid-Continent in Tulsa, Oklahoma. R Supp. 4, #1 at 378, 379, 380. Correspondence regarding Sundown's claim for cleanup costs associated with Hurricane Rita was sent from its office in Dallas, Texas to Mid-Continent in Tulsa, Oklahoma. R Supp. 4, #1 at 392-94. Mid-Continent investigated Leopold's claim in Louisiana and conveyed a settlement offer to his attorney in Louisiana from Oklahoma. At least three meetings between Sundown and Mid-Continent were held in Eland's and Sundown's offices in Dallas, Texas regarding the claims. R8094, 8122, 6330-31.

The location of the subject matter of the contract is anywhere Sundown and Eland were potentially liable and covered occurrences under the terms of the policies. Sundown can incur liability anywhere Eland or Sundown has facilities or conducts operations. They are both headquartered in Texas. Sundown owned the oil production facility in Louisiana and property in Texas, Oklahoma, Kansas, and

New Mexico, which could have given rise to the insureds' liability. DX 32 at MC006399.

Eland and Sundown are Texas business entities. Eland is incorporated in Texas and maintains its principal place of business there. R Supp. 4, #1 at 419. Sundown is a "Texas domestic limited partnership", whose general and limited partners are citizens and residents of Texas. para. 2, third amended counterclaim. R Supp. 4, #1 at 419. Its principal place of business is Dallas, Texas. R Supp. 4, #1 at 419. Mid-Continent is incorporated in Oklahoma, has its principal place of business there, and does business in Texas. R Supp. 4, #1 at 420. None of the parties are incorporated in, reside in, or have their principal place of business in Louisiana.

When an insurance policy covers risks located in many states, the location of the underlying suits and of the specific insured risk that is the subject of those suits are not determinative. *Pennzoil-Quaker State Co. v. American International Specialty Lines Ins. Co.*, 653 F.Supp.2d 690, 703 (S.D. Tex. 2009). Instead, the places of contracting and negotiation, and the parties' domicile, residence, nationality, place of incorporation, and place of business are the primary factors to consider. *Id.* Here, those factors show that Texas law applies.

The contacts under section 145 also establish that Texas has the overriding interest and its law applies. Section 145 provides:

(1) The rights and liabilities of the parties with respect to an issue in tort are determined by the local law of the state which, with respect to that issue, has the most significant relationship to the occurrence and the parties under the principles stated in § 6.

(2) Contacts to be taken into account in applying the principles of § 6 to determine the law applicable to an issue include:

(a) the place where the injury occurred,

(b) the place where the conduct causing the injury occurred,

(c) the domicile, residence, nationality, place of incorporation and place of business of the parties, and

(d) the place where the relationship, if any, between the parties is centered.

These contacts are to be evaluated according to their relative importance with respect to the particular issue.

The relationship between Mid-Continent, Eland, and Sundown is centered in Texas. The relationship was created by insurance policies entered into in Texas. Mid-Continent owed a duty of good faith and fair dealing based on those policies. The agent who negotiated the policy on Eland's and Sundown's behalf is located in Texas. Meetings regarding the handling of claims were conducted in Dallas. The litigation coordination agreement that Sundown claims Mid-Continent did not follow was made at one of those meetings. Mid-Continent made payments under the policies to Sundown in Texas.

The alleged conduct that caused the alleged injury occurred in Oklahoma and Louisiana. The plan to visit Leopold's property was proposed in Texas and

approved in Oklahoma. The visit occurred in Louisiana. The decision to convey an offer to Leopold was made in Oklahoma and conveyed from Oklahoma to Leopold's attorney in Louisiana. The alleged injury occurred in Louisiana– the purported increase in the cost to settle the Blanchard litigation. Texas law has the most significant relationship and it applies. *See Scottsdale Ins. Co.*, 271 S.W.3d at 295 (concluding that Texas law applied because the place where the relationship was centered leaned strongly toward the application of Texas law, although Texas was not the location of the injuries or the conduct causing the injuries).

### C. Sundown Fails To Establish Any Conflict Between Louisiana And Texas Law That Must Be Resolved Through A Choice Of Law Analysis.

Before reaching the choice of law analysis, there must first be a conflict between Texas and Louisiana law. *Sonat Expl. Co. v. Cudd Pressure Control, Inc.*, 271 S.W.3d, 228, 231 (Tex. 2008) Sundown has not shown that Louisiana recognizes a claim for breach of the duty good faith and fair dealing based on extreme conduct in the denial of third-party claim that results in injury independent of the claim. Instead, it relies on Louisiana authorities that deal with the termination of the duty to defend through the payment of settlements to third parties that exhaust policy limits.

*Stanley v. Trinchard*, 500 F.3d 411, 429 (5th Cir. 2007), involved an allegation that the insurer breached its duty of good faith and fair dealing by

settling a liability claim against the insured for policy limits without negotiating a full release. But Sundown did not base its claim for the breach of the duty of good faith and fair dealing on Mid-Continent's settlement of a third-party claim for the primary policy's limits without obtaining a full release for Sundown. Sundown could not prove such an allegation because there was no evidence that Mid-Continent settled with any third party. Instead, both the primary and umbrella policies' limits were exhausted when Mid-Continent made payments to Sundown, reimbursing it for mandated cleanup costs. The *Stanley* opinion did not refer to "extreme" conduct, address a bad faith claim, or conclude that the making of a settlement offer to a third-party breach the duty of good faith and fair dealing.

Sundown also relies on *Pareti v. Sentry Indemnity Co.*, 536 So.2d 417 (La. 1988), in an attempt to establish a conflict. But the insured there did not allege a breach of the duty of good faith and fair dealing. Sundown relies on the following dicta:

> [A]ny payment of the policy limits which does not release the insured from a pending claim (e.g., unilateral tender of policy limits to the court, the claimant or the insured), even if sufficient to terminate the duty to defend under the wording of the policy involved, raises serious questions as to whether the insurer has discharged its policy obligations in good faith.

*Id* at 424.

Sundown's claim for breach of the duty of good faith and fair dealing was not based on any failure by Mid-Continent to obtain a release on Sundown's

behalf. It was based on Preston's and Clayton's visit to Leopold's property, Mid-Continent's subsequent settlement offer to Leopold, and the purported effect it had on the *Blanchard* settlement.

Nor did Mid-Continent unilaterally tender policy limits. It paid them in response to Sundown's request, supported by invoices, seeking reimbursement of incurred cleanup costs. Thus, the claim asserted in *Pareti* was not asserted here and cannot form the basis of any conflict between Texas and Louisiana law.

In *Roberie v. Southern Farm Bureau Casualty Ins. Co.*, 194 So.2d 713 (La. 1967), a *Stowers* situation was presented. The insured sued the insurer to recover the amount of the judgment in the underlying litigation that exceeded policy limits. *Id*. at 714. The court held that the insurer's rejection of settlement offers was not in bad faith. *Id.*at 716. However, not advising the insured of settlement offers received from the plaintiffs and of his potential liability was bad faith:

> However, the insured, Roberie, was kept in the dark; he was never apprised of the offers of compromise nor warned of his potential liability; he was ignored. He needed information and advice on the point of his potential liability, which he was not given by his representative, his insurer. A conflict of interest arose between the insurer and the insured. The insurer failed to discharge its duty towards its insured, thereby precluding any decisive action on his part. We find that the actions of Southern Farm Bureau Casualty Insurance Company towards Roberie were more than negligent; they were in bad faith and in utter disregard of Roberie's natural desire to protect himself from financial loss.

*Id*.

Here, there is no assertion that Sundown was kept in the dark regarding any settlement offers that Mid-Continent *received* from third-parties. At all times, Sundown had independent counsel to give it information and advise it regarding its potential liability and navigate any conflict of interest. The insured in *Roberie* did not. Nor did the *Roberie* court recognize a bad faith claim based on a settlement offer an insurer made to a third-party. The holding in *Roberie* does not establish a a conflict between Texas and Louisiana law.

## III. JUDGE FITZWATER CORRECTLY GRANTED JUDGMENT AS A MATTER OF LAW ON THE JURY'S FINDING THAT MID-CONTINENT DID NOT PROVIDE PROMPTLY TO SUNDOWN A REASONABLE EXPLANATION OF THE BASIS IN THE POLICY FOR THE OFFER TO LEOPOLD.

A motion for judgment as a matter of law challenges the legal sufficiency of the evidence to support the verdict. *Brennan's Inc. v. Dickie Brennan & Co.*, 376 F.3d 356, 362 (5th Cir. 2004).

> Judgment as a matter of law is appropriate with respect to an issue if "there is no legally sufficient evidentiary basis for a reasonable jury to find for [a] party on that issue. FED.R.CIV.P. 50. This occurs when the facts and inferences point so strongly and overwhelmingly in the movant's favor that reasonable jurors could not reach a contrary verdict. In considering a Rule 50 motion, the court must review all of the evidence in the record, drawing all reasonable inferences in favor of the nonmoving party; the court may not make credibility determinations or weigh the evidence, as "those are jury functions. In reviewing the record as a whole, the court must disregard all evidence favorable to the moving party that the jury is not required to believe. That is, the court should give credence to the evidence favoring the nonmovant as well as that evidence supporting the moving party that

> is uncontradicted and unimpeached, at least to the extent that that evidence comes from disinterested witnesses."

*Id*. (citation omitted),

Section 541.060 (a) (3) of the Texas Insurance Code requires an insurer "to promptly provide a policyholder a reasonable explanation of the basis in the policy, in relation to the facts or applicable law for the insurer's . . . offer of a compromise settlement of a claim." The jury found that Mid-Continent failed to provide such an explanation for the Leopold offer. R3565-66. Judge Fitzwater noted that the standard was "whether a reasonable jury could have found from the evidence that a reasonable insurer would not in these circumstances have provided a similar explanation to Sundown." R7014. He concluded a reasonable jury could not have so found from the evidence.

Judge Fitzwater relied on Haltom's July 10, 2006 letter which stated: "In addition, based on the findings of no contamination to the property of Mr. Leopold other than some oil residue on some of the debris, we have extended an offer of $54,536.00 to Mr. Leopold. We have not had a response." R2015. Sundown now claims that the language was not a reasonable explanation. As Judge Fitzwater pointed out, "Sundown does not directly address Mid-Continent's averment that the July 10, 2006 letter to Sundown was a reasonable explanation of the basis in the policy, in relation to the facts or applicable law, for the Leopold offer." R7015. Nor does it now.

Instead, Sundown questions the district court's statement that the estimate that Futrell obtained was attached to Haltom's July 10, 2006 letter. Appellant's Brief at 94-95. But the estimate was not necessary to show the ***basis in the policy*** for the offer. The letter's reference to oil residue on the debris shows that the pollution endorsement providing coverage for a pollution incident was the basis in the policy for the offer in relation to the facts.

In any event, Sundown also received the estimate on which the offer was based on July 10, 2006 at the latest. Haltom sent the estimate via email to one of Sundown's lawyers. JX 58; DX 298 (Sundown's lawyer's e-mail to Haltom referring to "the undated/unsigned letter from Futrell Adjusting to you (what was the date of that letter?), attached to your letter to me of July 10th . . . .") The estimate contains costs for removing oil-covered debris and grubbing. DX 289. The $54,536 offer included only amounts necessary to remove the debris that contained oil. JX 58.

Sundown claims that the district court was incorrect when it stated: '"By email, Haltom explained to Chernekoff that the Futrell estimate was based on a proposal of Greco Construction and Haltom sent the Greco Construction proposal to Sundown on July 26, 2006.'" Appellant's Brief at 95 (citing R7008, 7015-16). Sundown contends that a "Contractor's Invoice" from Greco in the amount of $98,560 was attached, but is not an estimate. Appellants' Brief at 95. It claims that

work had already been performed and completed for the agreed amount of $98,560. Appellants' Brief at 95. But the document does not show that the work had already been performed, nor does Sundown refer to any evidence supporting that. In fact, the evidence shows that the document was the Greco Construction proposal that Futrell obtained.

The document does not show that it was paid or called for payment. The blanks at the bottom that would be filled out if the services had been rendered but not paid for are blank. DX 289. Nor is the document marked "paid." DX 289. In fact, it states "Price good for 30 days," which indicates a proposal yet to be accepted. DX 289.

Futrell, the adjuster who obtained the proposal from Greco, confirmed that the Contractor's Invoice" was the proposal from Greco. He testified the proposal was from Greco and was dated May 2, 2006, the same date as the purported invoice. R6221. He stated it was in the total amount of $98,560, the same amount as the "invoice." R6221. In fact, he read line by line through the estimate which corresponded almost exactly with the "invoice:"

"That's Mr. Greco's proposal, correct?

A. Correct.

Q. And it's dated May 2nd?

A. Yes.

> Q. But what is the total amount of the proposal?
>
> A. $98,560.
>
> Q. And can you tell us what the different elements were that were to be included in that amount?
>
> A. The disconnect of the power lines from rear building, $800. Pressure wash, which included the front building and slab, rear building, slab only, $6,000. The grubbing, $20,200. Entire site. Bring in fill and grade to original grade. Remove two hot spots by slab of rear building. Demo, $12,000, rear building only. The debris removal of 59,560, which includes the grubbed material, debris from storm, demo-ed building, total cost $98,560.

R6221. The purported "invoice" was Greco proposal. DX 289.

Sundown also claims it was error for the Judge Fitzwater to rely on the Muthig report that showed oil staining eight to 10 feet above the ground. Appellants' Brief at 96. But he did not rely on the report to show that Haltom's letter provided a reasonable explanation for the basis in the policy for the offer. He referred to the Muthig report when he rejected Sundown's contention that Mid-Continent was required to produce everything related to Sundown's claim:

> [A]nd although Sundown argues that Mid-Continent should have provided the Muthig report in response to Chernekoff's request for all documents related to the Leopold offer, the statute does not require that the insurer provide everything the insured's requests. The statute only obligates the insurer to provide a reasonable explanation for the basis in the policy, in the relation to the applicable facts or law, for the offer. Moreover, even if Haltom was not forthcoming regarding the documents within his possession, that does not make Mid-Continent's July 10, 2006 explanation unreasonable. Haltom's later conduct would not of itself have enabled a reasonable jury to find that Mid-Continent's prior explanation of the offer was unreasonable.

> The jury could only reasonably have found from the evidence that Sundown was upset because an *offer of settlement was made*, not that Mid-Continent failed to provide a prompt explanation of the factual or legal basis in the policy for the offer.

R7016.

Sundown also attempts to transform section 541.060(a)(3)'s requirement of a reasonable-explanation requirement to a reasonable settlement offer requirement. Sundown contends that the ***offer*** to Leopold was unreasonable because the soil sampling turned up only diesel oil, debris resulting from the storm surge would have had to have been cleaned up regardless of the oil residue, and Haltom was purportedly not responding to a legitimate claim when he made the offer. Appellants' Brief at 99. However, section 541.060(a)(3) does not require the insurer to provide an explanation showing that the offer was reasonable. As Judge Fitzwater observed, "If Sundown proved anything at trial, it established that a reasonable insurer *would not have made the offer*, but this is a different question from the one the jury answered, and it is not pertinent to the claim under consideration." R7016.

Sundown contends that the explanation was not prompt. Judge Fitzwater noted that Sundown did not raise that contention:

> "Sundown does not appear to argue that the explanation given for the Leopold offer was not prompt. Mid-Continent made the offer to Leopold's attorney on June 6, 2006, and Mid-Continent sent on July 10, 2006 the letter that it contends was a reasonable explanation of the offer. Because Sundown has not argued that Mid-Continent did not

> promptly provide an explanation for the Leopold offer, and because the explanation followed the offer by a little more than one month, the court will assume *arguendo* that the explanation was prompt."

R7014 at n.31. Thus, promptness was not a contested issue in the district court.

In any event, Judge Fitzwater had ruled before trial during the summary judgment proceeding that Sundown failed to address evidence that would have permitted a reasonable jury to conclude that if Sundown had been notified of the offer within 10 days of the date it was made, it could have persuaded Leopold not to join the *Blanchard* litigation, and kept its costs from increasing. He concluded that "A reasonable jury could only find that Sundown was injured by making of the settlement offer itself, coupled with Mid-Continent's failure to inform Leopold that Sundown's spills may not have impacted his property." R 1017. Thus, there was no evidence that any lack of promptness in providing the explanation for the offer caused any increased costs of the *Blanchard* settlement.

Sundown notes that Judge Fitzwater's alternative ruling that the evidence was legally insufficient to support the jury's finding that Mid-Continent's purported failure to give a prompt, reasonable explanation for the offer to Leopold and its purported misrepresentation of the policy were producing causes of $2 million in increased costs of the *Blanchard* settlement. Appellant's Brief at 104. Sundown based its damages theory on the fact that it did not pay anything in the *Barasich* and *Danos* lawsuits*:* "[B]oth McGuire and Allen testified that the actions

of Mid-Continent grossly inflated the expectations of the *Blanchard* plaintiffs and were the reason they were unable to get the case dismissed without payment (as in *Barasich* and *Danos*) and had to settle for $2 million, plus an agreement to remediate any Sundown oil found on the class members' property—the best they could do under the circumstances." The results in *Danos* and *Barasich* are not evidence from which a jury could reasonably conclude that Sundown could have resolved the *Blanchard* litigation without payment.

Sundown conveniently ignores that it was a co-defendant in the *Barasich* and *Danos* lawsuits with titanic oil companies who were accused of polluting fishing waters with millions of gallons of oil. In *Barasich*, the plaintiffs alleged four defendants spilled 5,900,440 gallons of oil collectively. JX 14 at p. Mid-Continent-005323. Sundown was alleged to have spilled a mere 13,000 gallons. JX 14 at p. Mid-Continent-005323. Oil industry titans Shell Pipeline Co., Chevron Corporation, and Bass Enterprises were alleged to have spilled 1,063,400, 1,044,000, and 3,780,000 gallons respectively. JX 14 at p. Mid-Continent-005323. Similarly, in *Danos*, Sundown was named as a co-defendant with titanic oil companies who allegedly spilled 6,334,440 gallons of oil collectively. The plaintiffs alleged Sundown spilled 13,000 gallons of oil. They alleged that Bass Enterprises, Shell Oil Co., and Chevron Corporation spilled 4,241,000, 1,051,000, and 991,000 gallons respectively. JX 15 at pp. MC-003288-89.

The *Blanchard* litigation was fundamentally different. Sundown was the *only* defendant and the claimants were *only* landowners within close proximity to Sundown's facilities and its oil spill. JX 12. Sundown was the only defendant that the *Blanchard* plaintiffs alleged caused the spill that polluted their property. There were no allegations that Sundown was a member of a group of oil companies that polluted the plaintiffs' land. And it was undisputed that Sundown's oil had spilled.

Judge Fitzwater noted that the evidence did not permit the jury to find that the explanation for the offer caused the $2 million in increased cost to resolve the *Blanchard* litigation:

> Sundown did not introduce evidence that would have enabled a reasonable jury to find that, had Mid-Continent provided every report, detail, and fact known to it and relevant to the Leopold offer, Sundown would not have incurred the increased costs of the *Blanchard* settlement. A reasonable jury could have only found from the evidence that the Leopold *offer* or the *withdrawal* of the Leopold offer – which arguably was necessary only because the offer was made in the first place – was a producing cause of the increased costs of the *Blanchard* settlement. In fact, the explanation of the offer occurred after the offer was made, in accordance with the Primary Policy. Mid-Continent was therefore permitted under the Primary Policy to wait 10 days after making an offer to inform Sundown that it had done so. This confirms the court's holding that, at most, a reasonably jury could have found *the making of an offer* was a producing cause of the increased costs of the *Blanchard* settlement. Judge Fitzwater added that even if Leopold had not joined the class "the trial evidence would not have enabled a reasonable jury to find that, without Leopold as class representative or class member, *Blanchard* would have settled for less than $2 million."

R7019. Nor did Sundown produce evidence that the plaintiffs in either suit dismissed the litigation without receiving any kind of settlement from Sundown's' co-defendants.

## CONCLUSION

Mid-Continent respectfully requests the Court to affirm the judgment.

Respectfully submitted,

MARTIN, DISIERE, JEFFERSON & WISDOM, L.L.P.

By: */s/ Bruce E. Ramage*
Bruce E. Ramage
Texas Bar No. 16492500
*ramage@mdjwlaw.com*
Levon G. Hovnatanian
Texas Bar No. 10059825
*hovnatanian@mdjwlaw.com*
808 Travis, 20th Floor
Houston, Texas 77002
(713) 632-1700 – Telephone
(713) 222-0101 – Facsimile

ATTORNEYS FOR APPELLEE,
MID-CONTINENT CASUALTY COMPANY

## CERTIFICATE OF SERVICE

This is to certify that a true and correct copy of the above and foregoing motion has been forwarded to all of the individuals listed below by the method indicated on this, the 2nd day of May, 2012:

Carl D. Rosenblum
*crosenblum@joneswalker.com*
Madeleine Fischer
*mfischer@joneswalker.com*
Alida C. Hainkel
*ahainkel@joneswalker.com*
JONES, WALKER, WAECHTER, POITEVENT,
CARRÈRE & DENÈGRE, L.L.P.
201 St. Charles Avenue, 51st Floor
New Orleans, Louisiana 70170-5100
*(via the court's Electronic Filing System and facsimile no. (504) 589-8208)*

*(Attorneys for Defendants-Appellants Eland Energy, Inc. and Sundown Energy LP)*

*/s/ Bruce E. Ramage*
Bruce E. Ramage

## CERTIFICATE OF COMPLIANCE WITH RULE 32(A)

1. This brief complies with the type-volume limitation of FED. R. APP. P. 32(a)(7)(B) because:

☑ this brief contains **16,794** words, excluding the parts of the brief exempted by FED. R. APP. P. 32(a)(7)(B) (iii), *or*

☐ this brief uses a monospaced typeface and contains [*state the number of*] lines of text, excluding the parts of the brief exempted by FED. R. APP. P. 32(a)(7)(B)(iii).

2. This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and type style requirements of Fed. R. App. P. 32(a)(6) because:

☑ this brief has been prepared in a proportionally spaced typeface using **MS Word 2010** word processing program in 14 font size, Times New Roman, *or*

☐ this brief has been prepared in a monospaced typeface using [*state name and version of word processing program*] with [*state number of characters per inch and name of type style*].

*/s/ Bruce E. Ramage*
(Signature of filing party)

Attorney for: MID-CONTINENT CASUALTY COMPANY

Dated: May 2, 2012