

Fifth Circuit Addresses Contractual Liability Exclusion

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In its recent decision in *Colony Nat'l Ins. Co. v. Manitex, L.L.C.*, 2012 U.S. App. LEXIS 3311 (5th Cir. Feb. 20, 2012), the United States Court of Appeals for the Fifth Circuit, applying Texas law, considered what constituted an “insured contract” for the purpose of a contractual liability exclusion in a general liability policy.

Manitex involved two asset purchase agreements effecting a transfer of the assets and certain liabilities of an initial product manufacturer. JLG manufactured and sold a line of boom truck cranes. Powerscreen purchased JLG's assets and liabilities, including JLG's liabilities associated with the cranes. Powerscreen, in turn, was sold to Manitex, which assumed Powerscreen's liabilities associated with the cranes. Manitex was insured under a general liability policy issued by Colony. During the Colony policy period, an individual was injured while using of the JLG manufactured cranes. That individual later filed suit against JLG, and Manitex provided JLG with a defense in the suit. Colony sought a judicial declaration that it did not have an obligation under its policy to indemnify Manitex for its own indemnity obligations vis-à-vis JLG. The United States District Court for the Western District of Texas ruled on motion for summary judgment that Colony at least had a duty to reimburse Manitex for costs incurred in defending JLG. On interlocutory appeal, however, the Fifth Circuit reversed the lower court.

The exclusion at issue in *Manitex* was a contractual liability exclusion barring coverage for “bodily injury” or “property damage” for which Manitex became obligated to pay “by the reason of the assumption of liability in a contract or agreement.” The exclusion contained a typical exception for liability “assumed in an ‘insured contract,’” but only if the “bodily injury” or “property damage” occurred subsequent to the execution of the contract or agreement. “Insured contract,” in turn, was defined as:

- f. That part of any other contract or agreement pertaining to your business (including indemnification of a municipality in connection with work performed for a municipality) under which you assume the tort liability of another party to pay for "bodily injury" or "property damage" to a third person or organization. Tort liability means a liability that would be imposed by law in the absence of any contract or agreement.

At issue for the court was whether Manitex's purchase agreement constituted an “insured contract,” and more specifically, whether Manitex assumed JLG's tort liability pursuant to the agreement it entered into with Powerscreen.

Colony argued that the “insured contract” exception did not apply because the purchase agreements did not effect a transfer of JLG’s tort liabilities to Manitex. The court summarized Colony’s argument as follows:

[Colony] contends that JLG is the only entity that has any “tort liability” as the policy defines that term because only JLG’s liability would be imposed by law in the absence of any contract or agreement. Manitex’s liability, argues Colony, can only be imposed by operation of the Powerscreen–Manitex Purchase Agreement. Therefore, that liability is not “tort liability,” but contractual liability, and as a result, the Powerscreen–Manitex Purchase Agreement is not an insured contract, and Manitex’s liability falls within the contractual liability exclusion and outside of coverage by the policy.

The lower court rejected this very argument, concluding among other things, that Manitex assumed JLG’s tort liabilities, and that “[a]n insurance policy that specifically covered contractually-assumed tort liability, yet removed from coverage any agreement involving more than a single contractual link, seems unlikely to have been intended by the parties.”

The Fifth Circuit, however, took a much more narrow view of the “insured contract” exception, concluding that Manitex did not contractually assume JLG’s tort liabilities, but instead assumed only the liabilities of Powerscreen. The court found a significant distinction to be critical:

Powerscreen’s liability arose strictly from a contract, namely, its purchase agreement with JLG. If that contract did not exist, then Powerscreen would have had no liability related to the [underlying] claims. Powerscreen’s liability, therefore, was not one that “would be imposed by law in the absence of any contract or agreement.” Therefore, it was not “tort liability.”

Thus, the court concluded, because the Manitex agreement with Powerscreen did not effect a transfer of Powerscreen’s tort liabilities, it did not constitute an “insured contract,” and the contractually liability exclusion, therefore, barred coverage for Manitex’s costs in defending JLG.