

*State Farm Lloyds v. Page*

No. 08-0799, June 11, 2010,  
Texas Supreme Court

Mold coverage under the  
Texas homeowner's policy:  
The Supreme Court's  
reconciliation of *Balandran*  
and *Fiess*

# *Facts*

- **The policy:** State Farm insured Page under a Texas standard homeowner's policy, form HO-B.
- **Mold damage:** Page found mold and water damage to the house and to her personal property in June 2001 caused by leaks in the sanitary sewer lines of her home.
- **Claim for coverage:** Page sought coverage for the cost of remediation for both the damage to the structure and to her personal property.

# Facts

## ■ **State Farm paid part of the claim:**

- January 2002: State Farm paid \$12,644 to cover repair and remediation of the structure, and \$13,631 to cover Page's personal property and additional living expenses.
- State Farm paid an additional \$13,042 to cover remediation of Page's attic after suit was filed.

## ■ **State Farm denied part of the claim:**

- May 2002, Page sought additional funds to repair damage to her carpet, which State Farm refused to pay,
- This resulted in a dispute and ultimately this lawsuit over the amount needed to fully remediate and repair the structure and contents.

# *Trial Court Proceedings*

- **Claims:** Breach of contract, breach of the duty of good faith and fair dealing, fraudulent misrepresentation, and DTPA and Insurance Code violations.
- **State Farm's MSJ:** (1) HO-B policy expressly excludes coverage for all mold damage; (2) No evidence that the mold damage resulted from a covered peril; (3) No evidence that Page was owed additional money; (4) Extra-contractual claims were not viable because there was no coverage under the policy.
- **Trial Court Granted MSJ:** Trial court initially denied State Farm's MSJ, but reconsidered after Supreme Court decided *Fiess v. State Farm* and then granted the MSJ based on that case.

# *On Appeal*

- **Waco Court of Appeals:** reversed, holding that *Fiess* did not apply to preclude coverage; instead the Supreme Court's 1998 decision in *Balandran v. Safeco* applied to provide coverage for the mold damage.
- **Supreme Court:** State farm argued that *Fiess* applied to preclude coverage; Page argued that *Balandran* applied to provide coverage. The Supreme Court rejected both positions.

# *The HO-B*

- **Coverage A - Dwelling (covers all risks unless excluded):**

We insure against all risks of physical loss to the property described in Section I Property Coverage, Coverage A (Dwelling) unless the loss is excluded in Section I Exclusions.

# The HO-B

## ■ Coverage B – Personal Property (covers only named perils, unless excluded):

We insure against physical loss to the property . . . caused by a peril listed below, unless the loss is excluded in Section I Exclusions.

\* \* \*

**9. Accidental Discharge, Leaking or Overflow of Water or Steam** from within a plumbing, heating or air conditioning system or household appliance.

\* \* \*

Exclusions 1.a. through 1.h. under Section I Exclusions do not apply to loss caused by this peril\*

*\* Known as the “**exclusion repeal**” provision*

# *Exclusion Applicable to Coverages A and B*

## SECTION I EXCLUSIONS

1. The following exclusions apply to loss to property described under Coverage A (Dwelling) or Coverage B (Personal Property) ...

\* \* \*

f. We do not cover loss caused by:

(2) rust, rot, **mold** or other fungi.

We do cover **ensuing loss** caused by collapse of building or any part of the building, water damage or breakage of glass which is part of the building if the loss would otherwise be covered under this policy.\*

*\*Known as the “ensuing loss” provision.*



# *Fiess v. State Farm Lloyds* 202 S.W.3d 744 (Tex. 2006)

- **Mold damage case:** some mold caused by flooding from Tropical Storm Allison, but most of mold caused by roof leaks, plumbing leaks, leaks in the HVAC system, exterior door leaks, and window leaks which had occurred before the storm.
- **Fifth Circuit's Certified Question to Supreme Court:** Does the ensuing-loss provision provide coverage for mold contamination caused by water damage that is otherwise covered under the policy?

f. We do not cover loss caused by:

(2) rust, rot, **mold** or other fungi.

We do cover **ensuing loss** caused by collapse of building or any part of the building, water damage or breakage of glass which is part of the building if the loss would otherwise be covered under this policy.

# *Fiess v. State Farm Lloyds*

## Holding

- The ensuing-loss provision reinstates coverage only as to “losses caused by an intervening cause (like water damage) that in turn follow from an exclusion listed in paragraph 1(f).”
- In other words, the water damage must be the *result*, not the cause, of the types of damage that the coverage exclusions enumerate (here, the water damage had to be the *result* of the mold, not vice versa, for the ensuing-loss provision to reinstate coverage).
- The ensuing loss must be caused by water *damage*, not merely water, else the insurance policy would become a maintenance agreement.

# *Fiess v. State Farm Lloyds*

## Limitations to Holding

- Did not address personal property coverage under paragraph 9 (accidental discharge, leakage or overflow of water) because this issue not appealed. See note 3.
- Did not address mold caused by air-conditioning and plumbing leaks, because claim was not preserved. See note 26.
- Only addressed mold caused from roof and window leaks.
- So . . . *Fiess* did not “unequivocally vitiate coverage for all mold damage no matter the cause” (This was State Farm’s position in *Page*.)

# *Balandran v. Safeco*

## 972 S.W.2d 738 (Tex. 1998)

- **Foundation damage case:** Damage to dwelling caused by foundation movement resulting from an underground plumbing leak.
  - Note that plumbing leak is a covered Section B peril, but this case does not involve property damage.
- **Relevant exclusion in policy:** Exclusion 1.h “We do not cover loss under Coverage A (Dwelling) caused by settling, cracking, bulging, shrinkage, or expansion of foundations . . . .”
- **Issue:** Does exclusion repeal provision apply only to Coverage B, or to both Coverage A and B? In other words, is the foundation movement exclusion repealed as to Section A dwelling coverage because the movement was caused by a plumbing leak?

# The HO-B

## ■ Coverage A - Dwelling (covers all risks unless excluded):

We insure against all risks of physical loss to the property described in Section I Property Coverage, Coverage A (Dwelling) unless the loss is excluded in Section I Exclusions.

## ■ Coverage B – Personal Property (covers only named perils, unless excluded):

We insure against physical loss to the property . . . caused by a peril listed below, unless the loss is excluded in Section I Exclusions.

\* \* \*

**9. Accidental Discharge, Leaking or Overflow of Water or Steam** from within a plumbing, heating or air conditioning system or household appliance.

\* \* \*

Exclusions 1.a. through 1.h. under Section I Exclusions do not apply to loss caused by this peril\*

*\*Known as the “**exclusion repeal**” provision*

# *Balandran v. Safeco*

## *Exclusion Repeal Provision*

- **Safeco's position** – location, location, location. The exclusion repeal provision is located in Coverage B section of the HO-B policy and thus only applies to Coverage B (personal property)
- **Balandran's position** – on its face, the exclusion repeal provision applies to *any* loss, not just personal property loss.

## *Balandran v. Safeco*

### **Holding: Exclusion repeal applied to *both* Coverage A and B**

- **Ambiguity:** Court considered both parties' interpretation of the applicability of the exclusion repeal provision to determine if there was ambiguity.
- **Insurer's interpretation** that exclusion repeal provision must be construed by considering its context within the policy was reasonable. *Sharp v. State Farm Fire & Cas. Co.*, 115 F.3d 1258 (5<sup>th</sup> Cir. 1997) supported this position.

# *Balandran v. Safeco*

## **Holding: Exclusion repeal applied to *both* Coverage A and B**

- **Policyholder's interpretation** was also reasonable for several reasons:

1. **“Loss” v. “Personal Property Loss”**: The exclusion repeal provision expressly applied to “loss” caused by a plumbing leak, and was not by its terms limited to “personal property loss.” The fact that the exclusion repeal provision was placed in Coverage B did not necessarily limit its application to Coverage B – it could have been placed there because that is the only place in the policy that the “accidental discharge” risk is described.
2. **Render part of policy meaningless**: Safeco's interpretation of the policy would render part of the policy meaningless, because personal property is not ever likely to be damaged by foundation movement (under Coverage B), while damage to the dwelling is always likely to occur (Coverage A).



# *Balandran v. Safeco*

## **Holding: Exclusion repeal applied to *both* Coverage A and B**

- **Policyholder's interpretation** was also reasonable for several reasons:
  3. **History of form:** Court also noted that the policyholder's interpretation was even more reasonable based on the history of the current HO-B form. The exclusion repeal provision was moved to the Coverage B section in the current form, but the changes were meant to simplify the policy and not to change coverage.
  
- **Rule of *Contra Proferentem*:** Because both Insurer's and policyholder's interpretations were reasonable, there was ambiguity. Under rule of *Contra Proferentem*, Court adopted the construction urged by policyholder.

# The Guiding Principles of Contract Interpretation

Guiding Principle #1: When analyzing an insurance contract, we are guided by the well-established principles of contract construction.

Guiding Principle #2: The primary goal is to determine the contracting parties' intent through the policy's written language.

Guiding Principle #3: The Court must read all parts of the contract together, giving effect to each word, clause, and sentence, and avoid making any provision within the policy inoperative.

Guiding Principle #4: The Court's analysis is confined to the four corners of the policy, and extrinsic evidence may not be considered to determine whether an ambiguity exists.

# The Guiding Principles of Contract Interpretation

Guiding Principle #5: Whether a particular provision or the interaction among multiple provisions creates an ambiguity is a question of law.

Guiding Principle #6: Only if the policy is subject to two or more reasonable interpretations may it be considered ambiguous.

Guiding Principle #7: Only if the policy is ambiguous does the rule of *contra proferentem* apply.

# *State Farm v. Page*

## Waco Court of Appeals Holding

- The court of appeals, broadly applied *Balandran*, holding that the *entire exclusion repeal provision is ambiguous*.
- On appeal to the Supreme Court, Page argued that the decision by the Court of Appeals was proper because the *Balandran* opinion analysis was based upon the repeal provision's reference to "loss" rather than "personal property loss," and on the drafters' intent that there be no substantive change in coverage under the redrafted policy.

# *State Farm v. Page*

## Supreme Court's Holding

- Calling the 10<sup>th</sup> District's decision "sweeping," the Supreme Court held its holding in *Balandran* was confined to the foundation damage exclusion contained in 1.h.
- In the context of the facts in this case and the exclusion involved, there was no ambiguity in the policy created where the exclusion repeal provision applied only to the section in which it was located (Coverage B). Therefore, the exclusion repeal provision only applied to Coverage B.

# *State Farm v. Page*

## Bases for Holding

1. **Drafting history doesn't count:** As stated by the Court in *Fleiss*, an ambiguity may not be created by extrinsic evidence concerning the prior HO-B policy. Therefore, any comments made by the Court in *Balandran* regarding the drafting history of the HO-B policy could not create an ambiguity in the policy. In any event, there was nothing to indicate that the prior version of the policy unambiguously covered mold damage resulting from plumbing leaks as it did for foundation damage.

# *State Farm v. Page*

## Bases for Holding

2. **“Loss” v. “Personal Property Loss” is not enough:** The fact that the exclusion repeal provision refers to “loss” caused by a plumbing leak and is not by its terms limited to “personal property loss” cannot “in isolation, bear the weight of rendering the entire repeal provision ambiguous.”
3. **Must read policy as a whole:** The exclusion repeal must be examined in light of the facts of the case, the particular policy exclusion in issue, by reading all parts of the policy together and “giving meaning to every sentence, clause, and word to avoid rendering any portion inoperative.”

# *State Farm v. Page*

## Bases for Holding

### 4. Part of policy is not rendered meaningless:

- This case is different than *Balandran* involving losses excluded under exclusion 1(h) – foundation damage. The exclusion repeal provision was ambiguous *with respect to the foundation damage exclusion* because the losses excluded – i.e., foundation damage – by their very nature apply only to *dwelling* coverage. If the exclusion repeal provision only applied to personal property coverage, it would render a provision meaningless.
- The opposite is true with respect to the mold exclusion. Applying the exclusion repeal to *both* Coverages A and B in the context of mold damage caused by water intrusion would render the entire mold exclusion “nugatory.” (In other words, mold damage is always caused by water.)



# *State Farm v. Page* Bases for Holding

## 4. Part of policy is not rendered meaningless:

- Limiting the exclusion repeal provision to Coverage B *where it appears in the policy* does not render the provision wholly inoperative as it did in *Balandran* – there can be mold damage to both a dwelling and to personal property.

# Court's Opinion Consistent with 5<sup>th</sup> Circuit's Erie Guess

The Court expressly held that its decision was consistent with the Fifth Circuit's holding in *Carrizales v. State Farm Lloyds*, 518 F.3d at 348.

There, Court held that the exclusion repeal did not apply to mold contamination in the Carrizales's garage that was caused by plumbing leaks.

Making an *Erie*-guess about how the Supreme Court would decide the question, the Fifth Circuit concluded that the interaction between the mold exclusion provision and the exclusion repeal provision under Coverage B did not create an ambiguity.

Although the repeal provision is located in the section of the policy that deals with plumbing leaks, the Court held: "it does not follow that every exclusion is repealed with respect to plumbing leaks." Looking at each policy provision and determining its effect in light of the repeal provision: "we cannot envision the role the mold exclusion would play if Coverage A (implicitly) as well as Coverage B (explicitly) covered mold damage resulting from plumbing leaks."

# State Farm Lloyds v. Page

## Lessons Learned

- Follows all recent Supreme Court cases with emphasis on using rules of construction to interpret the policy language as written.
- Have to look at the facts of each case in the context of the applicable exclusion separately.
- *Contra Proferentem* won't apply unless the court finds two competing *reasonable* interpretations of the policy.
- Here, rule that an interpretation should not render any part of policy meaningless seems to be the most important to the Court.

# THE END

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