NO. 07-20235

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

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**ADMINISTRATIVE SERVICES OF NORTH AMERICA, INC.,**

*Plaintiff - Appellant,*

**v.**

**THE HARTFORD FIDELITY & BONDING COMPANY and HARTFORD CASUALTY INSURANCE COMPANY**,

*Defendants - Appellees.*

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On Appeal from the United States District Court
for the Southern District of Texas

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# Brief of Appellees

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## CERTIFICATE OF INTERESTED PERSONS

*Case No. 07-20235: Administrative Serv. of N. Am. Inc. v. Hartford Cas. Ins. Co.*

The undersigned counsel of record certifies that the following listed persons and entities as described in the fourth sentence of Local 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.

**Plaintiff/Appellant:**

Administrative Services of North America, Inc.

**Counsel for Plaintiff/Appellant:**

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**Defendants/Appellees:**

The Hartford Fidelity & Bonding Company
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By:_____
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## STATEMENT REGARDING ORAL ARGUMENT

Appellant has waived oral argument. Hartford agrees that the issues in this appeal are straightforward and that the Court may resolve this case solely on the briefs without oral argument.

## STATEMENT OF ISSUES

Pursuant to Rule 28(a)(5) of the Federal Rules of Appellate Procedure, Hartford identifies the following issues that are relevant in this appeal:

1. Did the district court correctly grant summary judgment in Hartford's favor on Plaintiff's breach of contract coverage claim by determining that the default limitations period in Section 16.051 of the Texas Civil Practice & Remedies Code barred Plaintiff's coverage claim where Plaintiff failed to file the present action within four years of the contractually agreed "date of accrual" — specifically, the date on which Plaintiff admits that it discovered its alleged loss?

2. Even assuming for the sake of argument that the district court erred in granting summary judgment in Hartford's favor on limitations grounds, may this Court affirm the district court's summary judgment on the basis that the employee dishonesty policy which Plaintiff acquired from Hartford affords no coverage for Plaintiff's alleged losses from any of the following —

   a. improper bonuses that an employee paid to himself, where the policy excludes coverage for employee benefits such as bonuses?

   b. the improper diversion of funds from other shareholders for capital calls, where the policy requires that the employee have caused a loss to the insured and not to third parties?

c. the use of corporate funds to pay personal travel and entertainment expenses, where the insured has offered no evidence that the employee manifestly intended to cause the insured a loss?

3. Did the district court properly grant summary judgment in Hartford's favor on Plaintiff's DTPA and Article 21.21 claims, and may this Court affirm the district court's judgment with respect to Plaintiff's remaining extracontractual claims, on the basis that Plaintiff failed to offer any summary judgment evidence to sustain its burden of showing that it suffered any extracontractual injury independent of the contractual injuries resulting from Hartford's denial of benefits to Plaintiff?

4. Did the district court properly grant summary judgment in Hartford's favor on Plaintiff's Article 21.55 claims, and may this Court affirm the district court's judgment with respect to Plaintiff's remaining extracontractual claims, on the basis that Plaintiff has no coverage for its alleged losses under the employee dishonesty policy that Plaintiff acquired from Hartford?

5. Did the district court properly grant summary judgment in Hartford's favor on Plaintiff's common law bad faith, Article 21.21, and DTPA claims on the basis that Plaintiff failed to offer any summary judgment evidence to sustain its burden of showing that Hartford acted in bad faith by denying coverage that was not legitimately in dispute?

## STATEMENT OF FACTS

Plaintiff Administrative Services of North America, Inc. ("Plaintiff" or "ASONA"), is a company formerly in the business of providing employee benefit plan administration services for large self-funded corporations, such as Blue Bell Creameries and Academy Sports & Outdoors. (Record at 94, 593). As a third-party benefits administrator, Plaintiff was responsible for managing the employee benefit plans of its clients and, as appropriate, for distributing funds to participants in the plans. (*Id.* at 594). Consequently, Plaintiff operated trust accounts for its clients. (*Id.* at 598). Because it controlled benefit plan assets in those accounts, Plaintiff occupied a fiduciary relationship to its clients. (*Id.* at 591).

On April 25, 1997, Plaintiff hired Mark Strange as its President and Chief Executive Officer. (*Id.* at 613). Plaintiff entered into a written employment contract with Strange. (*Id.*). Under the terms of the contract, Plaintiff agreed to pay Strange a base salary of $150,000, plus incentive bonuses. (*Id.*). Moreover, the contract contemplated that Plaintiff would reimburse Strange for his reasonable entertainment and travel expenses:

> The Company shall reimburse Employee for entertainment, travel and other expenses reasonably and necessarily incurred by Employee in connection with the Company's business, subject to budgeted limitations established by the Company from time to time. Employee shall furnish to the Company such documentation with respect to any reimbursement requested by Employee hereunder as the Company shall reasonably request.

(*Id.* at 616).

Subsequently, Plaintiff purchased a Commercial Crime Policy from Defendant Hartford Casualty Insurance Company ("Hartford") to insure Plaintiff against losses resulting from "employee dishonesty." (Record at 668). The Commercial Crime Policy defined the term "employee dishonesty" as follows:

> "Employee Dishonesty" . . . means only dishonest acts committed by an "employee," whether identified or not, acting alone or in collusion with other persons, except you or a partner, *with the manifest intent* to:
>
> (1) *Cause you to sustain loss*; and also
> (2) Obtain financial benefit (other than employee benefits earned in the normal course of employment, including: salaries, commissions, fees, bonuses, promotions, awards, profit sharing or pensions[)] for:
>
> (a) The "employee;" or
> (b) Any person or organization intended by the "employee" to receive that benefit.

(*Id.*) (emphasis added). The policy became effective on November 17, 1998. (*Id.* at 662; *see also* Record Excerpts at Tab 1).

Several of the provisions of the Commercial Crime Policy imposed deadlines on Plaintiff for pursuing a claim on the policy. In particular, Paragraph 5 of the Amended Policy Provisions required that Plaintiff notify Hartford of any covered loss "as soon as possible, but not later than 60 days after discovery of [the] loss." (*Id.* at 677). Additionally, Paragraph 5 stated that Plaintiff must give Hartford "a detailed, sworn proof of loss" within 120 days after discovering the loss. (*Id.*). Paragraph 7

of the General Provisions imposed a contractual limitations period for bringing an action against Hartford under the policy:

> **Legal Action Against Us**: You may not bring any legal action against us involving loss:
>
> a. Unless you have complied with all the terms of this insurance; and
> b. Until 90 days after you have filed proof of loss with us; and
> c. Unless brought within 2 years ***from the date you discover the loss.***

(Record at 665) (emphasis added).

In early March 1999, Plaintiff discovered that its President, Mark Strange, had allegedly misappropriated funds from Plaintiff's bank and trust accounts. (Record at 569) (Affidavit of Pat Bryan: "I discovered the facts surrounding this loss beginning in March 1999."). Plaintiff reported its alleged loss to Hartford on March 19, 1999. (*Id.* at 579).[1] However, in the period following Plaintiff's notification, the nature and amount of Plaintiff's alleged loss became a moving target. As Plaintiff's counsel later confessed: "Several different amounts have been claimed as the covered loss,

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[1]Plaintiff suspended Strange from his duties on March 12, 1999, and terminated him the following week. (Record at 595). In this same time period, Plaintiff was struggling financially. On April 13, 1999, Plaintiff laid off most of its employees. (*Id.* at 94). Shortly thereafter, the Texas Department of Insurance declared Plaintiff to be insolvent and secured a temporary restraining order to freeze Plaintiff's assets. (*Id.* at 223). Likewise, the Department of Labor secured a court order appointing a receiver for Plaintiff. (*Id.* at 237, 578). Plaintiff has suggested that Strange's criminal actions caused Plaintiff's demise. (*See id.* at 578). However, an internal audit in 1999 revealed that Plaintiff's negative $3 million net worth far exceeded the largest amount of "loss" for which Plaintiff ever claimed Strange to be responsible. (*See id.* at 94 (noting that Plaintiff had only $1.1 million in assets and $4.6 million in liabilities)).

depending upon the person preparing the letter or the sworn proof of loss at any given time. Certainly, ***there is some room to argue confusion with respect to the amount of the claim***." (*Id.*) (emphasis added). For example:

- On July 2, 1999, Plaintiff, through a court-appointed receiver (*see supra* note 1), submitted its first proof of loss to Hartford in the amount of $332,700.00. The proof of loss did not identify either the dishonest employee or the alleged dishonest conduct. (Record at 579).

- On July 26, 1999, Hartford acknowledged that it had received Plaintiff's proof of loss and asked that Plaintiff submit a new proof of loss identifying the dishonest employee and the specific transactions that caused the loss. (*Id.* at 580).

- On October 8, 1999, Plaintiff submitted a supplemental proof of loss identifying Mark Strange as the dishonest employee and again specifying the amount of the loss as $332,700.00. (*Id.*).

- On October 25, 1999, Hartford asked Plaintiff to provide "copies of the documentation you are relying on to prove the claim or at least explain what it is and where it can be reviewed." (*Id.*).

- On November 1, 2000, Michael Rajt, an attorney for Plaintiff, forwarded supporting documentation to Hartford and represented that Plaintiff had now calculated its loss to be $581,872.01. (*Id.*).

- On November 14, 2000, Hartford asked Rajt to submit a revised proof of loss substantiating Plaintiff's revised calculation of its loss. (*Id.*).

- On February 9, 2001, Rajt sent additional documentation to Hartford and advised Hartford of a substantial reduction in the amount of Plaintiff's claim. (*Id.* at 581).

- On April 10, 2001, J. Patrick Bryan, the board chairman for Plaintiff, submitted another proof of loss in the amount of $390,673.60. (*Id.*).[2]

By late 2001, Plaintiff was still trying to assemble the documentation necessary to substantiate its alleged loss. (*See* Record at 581). From its various investigations, Plaintiff argued that Strange's misappropriation of funds had essentially taken three forms:

1. Strange paid himself and another employee, Jan Goehring, over $150,000 in unauthorized bonuses from the corporate payroll account. (Record at 584, 594, 607).

2. Strange misappropriated funds from Plaintiff's operating and trust accounts for his own personal purposes, including a down payment on a Jaguar, season tickets to the Houston Rockets and Houston Comets, and fees for a country club membership. (*Id.* at 585, 608).

3. Strange fraudulently induced other shareholders of the company to cover his share of the capital contribution that he owed Plaintiff in response to two capital calls. (*Id.* at 584, 608).

On November 28, 2001, Rajt sent a letter to Hartford adding another $76,000 to Plaintiff's calculation of the amount of its alleged loss. (*Id.* at 581, 636).

On February 8, 2002, Hartford responded to Rajt's letter and formally denied Plaintiff's claim under the Commercial Crime Policy. (*Id.* at 636). Hartford noted that, even more than two years after Plaintiff discovered its alleged loss, Plaintiff still had never supplied Hartford any documentation to establish either (a) that Strange's

[2]Plaintiff's counsel would later contend in a demand letter that the amount described in Bryan's proof of loss was "erroneous." (Record at 581).

bonuses were unauthorized or (b) that Strange's expenses were not normal business expenditures for the purpose of networking and entertaining clients. (*Id.* at 637). In addition, Hartford observed that the contractual limitations clause in the policy now barred any claim that Plaintiff might elect to pursue against Hartford:

> Notwithstanding the foregoing, the policy has specific time limitations that the insured is required to comply. In particular, under section P of the General Conditions, the insured "may not bring any legal action against us involving loss . . . unless such action is brought within 2 years from the date that you discover such loss." It is my understanding that the two-year limitation period outlined under the policy has expired and any further remedies have lapsed.

(Record at 637-38; *see also* Record Excerpts at Tab 2).

Plaintiff did not promptly do anything to preserve any rights in response to Hartford's letter. Christopher Fusselman, Plaintiff's current attorney, sent a demand letter to Hartford on May 22, 2003 — over a year after Hartford's denial of Plaintiff's claim, and over four years after Plaintiff's discovery of its alleged loss. (Record at 578). Although conceding that Plaintiff had committed errors which "led to some confusion," Fusselman argued that Hartford's coverage under the Commercial Crime Policy was "reasonably clear" with respect to Strange's bonuses, personal expenses, and diverted capital contribution. (*Id.* at 583-84). Along with the demand letter, Fusselman sent Hartford yet another proof of loss — this time increasing the amount of the alleged loss to $518,191.94. (*Id.* at 576).

Plaintiff filed the present action in state district court on August 6, 2003. (Record at 15). In its pleadings, Plaintiff asserted that Strange had misappropriated funds by:

> stealing money from ASO's payroll account for the benefit of himself and a friend; using firm money for a down payment on his personal automobile and to pay for his spouse's automobile lease expenses; purchasing at Plaintiff's expense, and using without Plaintiff's approval or authorization, season tickets to the Houston Rockets and Houston Comets basketball games and a country club membership; diverting company funds to cover his portion of capital calls among shareholders; and, a host of other unauthorized expenses for other non-approved purposes.

(Record at 16; *see also id.* at 62). Plaintiff alleged causes of action against Hartford for breach of contract, breach of the common law duty of good faith and fair dealing, violations of former Article 21.21 and Article 21.55 of the Texas Insurance Code, and violations of the Texas Deceptive Trade Practices Act. (*Id.* at 17-18, 64).[3]

After removing the case to federal court, Hartford filed three separate motions for summary judgment against Plaintiff's causes of action:

1. Hartford's Motion for Summary Judgment, April 3, 2006 ("Hartford's MSJ") — Hartford argued that Plaintiff could offer no evidence that Strange acted with the "manifest intent," as required under the policy, to cause Plaintiff to suffer loss. (Record at 365).

[3]In its original pleadings, Plaintiff sued not only Hartford, but also The Hartford Fidelity & Bonding Company ("HFBC"). However, Plaintiff dropped HFBC as a defendant in Plaintiff's First Amended Petition. (Record at 61; *see* Record at 85 ("Plaintiff's First Amended Petition eliminates all claims against HFBC and only asserts claims against Hartford Casualty.")). Therefore, while the Court's caption for the present case identifies HFBC as a defendant, Plaintiff has dismissed its claims against HFBC, and HFBC is not a party to this appeal.

2. Hartford's Limitations Motion for Summary Judgment, May 2, 2006 ("Hartford's Limitations MSJ") — Hartford argued (a) that the contractual limitations clause in the policy barred Plaintiff's contract claim against Hartford and (b) even if the contractual limitations clause were unenforceable, the default statute of limitations barred Plaintiff's contract claim because Plaintiff filed suit against Hartford more than four years after the date of accrual specified in the policy. (*Id.* at 717).

3. Hartford's Supplemental Motion for Summary Judgment, May 18, 2006 ("Hartford's Supp. MSJ") — Hartford argued that Plaintiff cannot recover on its extracontractual causes of action because (a) Plaintiff did not suffer a covered loss, (b) Plaintiff suffered no injury independent of its alleged contract damages, and (c) Plaintiff could offer no evidence that Hartford acted in bad faith. (*Id.* at 755).

Magistrate Judge Nancy Johnson recommended that the district court grant Hartford's Limitations MSJ and Hartford's Supp. MSJ. (Record at 815, 1001). The district court adopted the magistrate judge's recommendations. (*id.* at 852, 1040).

Having granted summary judgment against each of Plaintiff's causes of action, the district court entered a take nothing final judgment against Plaintiff on March 20, 2007. (*Id.* at 1041). This appeal followed.

## SUMMARY OF ARGUMENT

The district court granted summary judgment in Hartford's favor both with respect to Plaintiff's breach of contract claim and Plaintiff's extracontractual claims. This Court should affirm the district court's summary judgment.

The district court ruled that Plaintiff could not recover from Hartford on Plaintiff's contract claim because the statute of limitations barred Plaintiff's claim. The court's ruling was correct. The Commercial Crime Policy required that Plaintiff

bring its claim within two years "from the date [Plaintiff] discover[ed] the loss." Even if, as the district court found, the two year contractual limitations period was invalid, Texas law nonetheless required that Plaintiff file its coverage action within four years after the date of accrual, which the parties had contractually agreed to be the "date [Plaintiff] discover[ed] the loss." Plaintiff admits that it filed the present action more than four years after it discovered its alleged losses. And in any event, even if limitations did not bar Plaintiff's claim, the Commercial Crime Policy does not provide any coverage for Plaintiff's alleged losses.

The district court also correctly granted summary judgment in Hartford's favor on Plaintiff's extracontractual causes of action. Plaintiff asserts its extracontractual causes of action essentially as fallback measures to recover policy benefits that it otherwise may not recover under its breach of contract claim. This Plaintiff cannot do. Because Plaintiff has no coverage for its losses under the Commercial Crime Policy, it may not assert any extracontractual causes of action against Hartford. And even if Plaintiff arguably had any coverage, it has offered no summary judgment evidence to show either that Hartford acted in bad faith or that Plaintiff suffered any damages independent of its breach of contract claim. Consequently, Plaintiff has no valid extracontractual claims against Hartford.

Plaintiff may not recover either on its contract claim or on its extracontractual claims. The judgment of the district court should be affirmed.

## STANDARD OF REVIEW

The standard for reviewing an order granting summary judgment is de novo. *See In re ADM/Growmark River Sys., Inc*., 234 F.3d 881, 886 (5th Cir. 2000); *Shepherd v. Comptroller of Pub. Accounts*, 168 F.3d 871, 873 (5th Cir.1999). Likewise, the standard for reviewing an order interpreting an insurance policy is de novo. *Old Republic Ins. Co. v. Comprehensive Health Care Assocs.*, 2 F.3d 105, 107 (5th Cir. 1993). In reviewing a summary judgment, this Court is not limited to the district court's conclusions: it may affirm the district court's summary judgment on any grounds that find support in the record. *Cabrol v. Town of Youngsville*, 106 F.3d 101, 105 (5th Cir. 1997).

A summary judgment is proper where there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. FED. R. CIV. P. 56(c). If the moving party will not bear the burden of proof at trial, the moving party need only point out the absence of evidence on an essential element of the non-movant's claim. *Celotex Corp. v. Catrett*, 477 U.S. 317, 324-25 (1986). The burden then shifts to the non-movant to "go beyond its pleadings and designate, by competent summary judgment evidence, specific facts which demonstrate genuine triable issues." *Id.* The non-movant does not satisfy its summary judgment burden merely by offering conclusory statements, speculation or unsubstantiated assertions. *Douglass v. United Servs. Auto Ass'n*, 79 F.3d 1415, 1429 (5th Cir. 1996).

## ARGUMENT

Plaintiff willingly agreed to the terms of a Commercial Crime Policy which contained a contractual limitations clause stating that Plaintiff could not assert any legal action against Hartford unless it brought the action within two years "from the date you discover the loss." (Record at 665). By its own admission, Plaintiff discovered its alleged loss in March 1999. (*Id.* at 569, 771). Yet, Plaintiff did not file the present action until August 2003 — after a lengthy period in which Plaintiff, despite multiple requests from Hartford, was never able to substantiate a loss within the scope of coverage. Plaintiff not only failed to bring the present action within two years from the date that it discovered its alleged loss; it failed to bring the present action *within four years* from the date that it discovered its alleged loss.

The fact that Plaintiff has received no policy benefits for Strange's alleged misconduct is not the result of any insurance bad faith, but rather solely the result of Plaintiff's misinterpretation of the plain terms of the Commercial Crime Policy. The district court correctly granted summary judgment in Hartford's favor.

### I. The District Court Correctly Granted Summary Judgment in Hartford's Favor on Plaintiff's Cause of Action for Breach of Contract

Plaintiff alleged that Hartford breached the Commercial Crime Policy by denying Plaintiff's claim for benefits under the policy. (Record at 64). Hartford filed two motions for summary judgment against Plaintiff's cause of action for breach of

contract. (*Id.* at 366, 717). The magistrate judge did not consider the merits of Hartford's MSJ, instead recommending that the district court grant Hartford's Limitations MSJ. (*Id.* at 815). The district court adopted the magistrate judge's recommendation. (*Id.* at 852). Regardless, both Hartford's MSJ and Hartford's Limitations MSJ support the district court's summary judgment in Hartford's favor on Plaintiff's breach of contract claim.

A. The Statute of Limitations Bars Plaintiff's Contract Claim Because Plaintiff Failed to Assert Its Claim Within Four Years After Discovering Its Loss

The Commercial Crime Policy required that Plaintiff file the present action within two years after discovering its loss. (Record at 665). Plaintiff has argued that the contractual limitations clause in the Commercial Crime Policy is void, citing Section 16.070(a) of the Texas Civil Practice & Remedies Code. (*See id.* at 775). Section 16.070(a) provides:

> [A] person may not enter a stipulation, contract, or agreement that purports to limit the time in which to bring suit on the stipulation, contract, or agreement to a period shorter than two years. A stipulation, contract, or agreement that establishes a limitations period that is shorter than two years is void in this state.

TEX. CIV. PRAC. & REM. CODE ANN. § 16.070(a) (Vernon 2006). The magistrate judge agreed that the contractual limitations clause was void *to the extent* that the clause effectively gave Plaintiff a period of less than two years in which to file suit on the Commercial Crime Policy. (Record at 823).

However, the limitations analysis does not end simply with the conclusion that the two year limitations period in the Commercial Crime Policy is invalid. When a contractual limitations period is invalid, a court must apply the residual limitations period in Section 16.051 of the Texas Civil Practice & Remedies Code. *United States Fidelity & Guar. Co. v. Eastern Hills Methodist Church*, 609 S.W.2d 298, 300 (Tex. App.—Fort Worth 1980, writ ref'd n.r.e.). Section 16.051 provides:

> Every action for which there is no express limitations period, except for an action for the recovery of real property, must be brought not later than four years *after the day the cause of action accrues*.

TEX. CIV. PRAC. & REM. CODE ANN. § 16.051 (Vernon 2006) (emphasis added). Section 16.051 merely identifies the residual limitations period. Nothing in Section 16.051 purports to identify the acts or events under which a claim may accrue.

In Hartford's Limitations MSJ, Hartford argued that even under the four year residual period in Section 16.051, the statute of limitations barred Plaintiff's breach of contract claim because Plaintiff did not file suit within four years after the date on which Plaintiff discovered its loss — *i.e.*, within four years of the date of accrual specified in the Commercial Crime Policy. (Record at 718).[4] The magistrate judge agreed with Hartford:

> In this instance, the insurance policy stated that any claim must be "brought within 2 years ***from the date [Plaintiff] discover[ed] the loss.***"

[4]Hartford properly alleged in its pleadings that the statute of limitations barred Plaintiff's claims. (Record at 82).

> This language is subject to only one interpretation; the parties unambiguously intended that the limitations period would begin to accrue at the time the loss was discovered. The policy established when a cause of action would accrue, and Plaintiff does not persuade the court that a void period of limitations requires that other relevant contract terms be ignored or invalidated.

(*Id.* at 825) (emphasis in original). Because Plaintiff filed suit more than four years after it discovered its alleged loss, the magistrate judge concluded, and the district court agreed, that limitations barred Plaintiff's breach of contract claim. (*Id.* at 826, 852).

Plaintiff challenges the magistrate judge's reasoning in four separate "issues" in Plaintiff's Brief of Appellant. None of Plaintiff's challenges is valid.

1. *Contrary to Plaintiff's Issue No. I, the District Court Did Not Need to Decide When a Coverage Dispute Accrues Under the Common Law*

Not surprisingly, Plaintiff agrees with the magistrate judge's conclusion that the Commercial Crime Policy did not give Plaintiff the statutorily required minimum period of two years in which to file the present action. But while agreeing with the magistrate judge's conclusion, Plaintiff "objects to the errors in the analysis and application of the law that were used to reach [this] conclusion." Plaintiff's Br. at 20. According to Plaintiff, the magistrate judge (or the district court in reviewing the magistrate judge's recommendations) should have determined that Plaintiff properly filed the present action within four years after its cause of action accrued *under the common law*. *Id.* at 21.

Plaintiff suggests that the magistrate judge ignored a line of cases which holds that "[c]auses of action under an insurance policy do not accrue until liability is denied by the insurer." *Id.* (citing, *inter alia, Murray v. San Jacinto Agency, Inc.*, 800 S.W.2d 826, 828 (Tex. 1990)). The magistrate judge did not ignore the *Murray* line of cases. On the contrary, the magistrate judge concluded that she had no need to determine the date on which a coverage claim accrues under the common law because the parties had *contractually determined* the date of accrual. (*See id.* at 825 (agreeing with Hartford that the contract language was controlling in setting "the accrual date at the time the loss was discovered" — *i.e.,* March 1999)).

The magistrate judge committed no error in her analysis. The date on which Plaintiff's claim hypothetically may have accrued under the common law is irrelevant. The parties unambiguously agreed that any coverage claim would accrue on the date that Plaintiff discovered a loss.

2. *Contrary to Plaintiff's Issue No. II, Texas Law Required Only that the District Court Invalidate the Improper Limitations Period, Not the Accrual Language in the Limitations Clause*

Plaintiff argues that the contractual limitations clause is void in its entirety under Section 16.070(a) of the Texas Civil Practice & Remedies Code. Section 16.070(a), however, does not purport to a contractual limitations clause *in its entirety*; rather, it is directed only toward the *limitations period,* which must be shorter than two years. TEX. CIV. PRAC. & REM. CODE ANN. § 16.070(a) (Vernon Supp. 2006).

Thus, the purpose of Section 16.070(a) is merely to ensure that a party has *at least two years* to assert a claim for breach of contract. *See, e.g., Stevens v. State Farm Fire & Cas. Co.*, 929 S.W.2d 665, 671 (Tex. App.—Texarkana 1996, writ denied). Nothing in Section 16.070(a) limits parties from reaching an agreement on the date of accrual for any causes of action on their contract.

If a contractual limitations *period* is void, then as the magistrate judge observed in her memorandum of law, a Texas court must look to the default limitations *period* under Section 16.051 of the CPRC. (*See* Record at 824). Section 16.051 states that a cause of action under the residual limitations period "must be brought not later than four years after the day the cause of action accrues." TEX. CIV. PRAC. & REM. CODE ANN. § 16.051 (Vernon Supp. 2006). Like Section 16.070(a), Section 16.051 addresses only the limitations *period*. Other than to say that the date of accrual is the day before limitations begins to run, Section 16.051 does not purport either to determine or to limit the date on which a party's cause of action accrues. *Id.*

The magistrate judge concluded that the limitations *period* in the Commercial Crime Policy was void because it required that Plaintiff bring its claim "***within 2 years*** from the date [Plaintiff] discover[ed] the loss." (Record at 824-25) (emphasis added). But as the magistrate judge further recognized, the fact that the limitations *period* was shorter than two years meant simply that the parties were subject to the default limitations period in Section 16.051. Neither Section 16.070(a) nor Section

16.051 addresses or affects the date on which a party's cause of action accrues. Here, the parties contractually agreed, as part of the benefit of their bargain, that any cause of action which Plaintiff might choose to file against Hartford on the policy would accrue on "the date [Plaintiff] discover[ed] the loss." (Record at 665).

Plaintiff cites *Montgomery* for the proposition that if part of a contractual limitations clause is unenforceable, then the entire clause is unenforceable. *See* Plaintiff's Br. at 23 (citing *Montgomery v. Browder*, 930 S.W.2d 772, 778 (Tex. App.—Amarillo 1996, writ denied)). *Montgomery* recognizes, however, that as long as the invalid language in a contract does not constitute the main purpose of the agreement, a court should enforce as much of the remaining language in the contract as possible to carry out the intent of the parties consistent with the law. *See Montgomery*, 930 S.W.2d at 778. "The issue is whether the parties would have entered into the agreement absent the illegal parts." *In re Kasschau*, 11 S.W.3d 305, 313 (Tex. App.—San Antonio 2004, orig. proceeding).

A court may properly reform the invalid language in a contract to carry out the intent of the parties consistent with the law. *See Butler v. Arrow Mirrow & Glass, Inc.*, 51 S.W.3d 787, 794 (Tex. App.—Houston [1st Dist.] 2001, no pet.). In *Butler,* for example, the plaintiff employer sought to enforce a covenant not to compete. The court of appeals concluded that the covenant, as worded, was an unenforceable restraint on trade because it was not reasonably limited in geographic scope.

However, the court in *Butler* affirmed the trial court's order reforming the covenant, stating that "instead of invalidating a covenant not to compete, Texas courts have usually reformed the covenant, revising the provisions to those which are reasonable under the circumstances." *Id.* *See also Martin v. Linen Sys. for Hosp., Inc.*, 671 S.W.2d 706, 709 (Tex. App.—Houston [1st Dist.] 1984, no writ).

Here, the main purpose of the contract between the parties was for Hartford to provide insurance coverage for Plaintiff. (*See* Record at 662). The limitations period in the policy was ancillary to the main purpose of the contract, and there is no reason to believe that the parties would have declined to enter into it if the period had been four years instead of two years. Only the limitations period — and not the accrual language in the policy — allegedly violated Section 16.070(a) of the CPRC. Thus, the magistrate judge properly concluded that she could enforce the accrual language in the policy in a way that would carry out the intent of the parties consistent with the law — specifically, by interpreting the contract to require that Plaintiff file any coverage lawsuit within four years from the date that it discovered its loss.

Like any other type of contract, an insurance policy is subject to the general rules of contract interpretation. *See Guaranty Nat'l Ins. Co. v. Azrock Indus., Inc.*, 211 F.3d 239, 243 (5th Cir. 2000); *Trinity Univ. Ins. Co. v. Cowan*, 945 S.W.2d 819, 823 (Tex. 1997). If a policy has only one reasonable meaning, "it is not ambiguous and will be enforced as written." *Comsys Info. Tech. Servs., Inc. v. Twin City Fire*

*Ins. Co.*, 130 S.W.3d 181, 183 (Tex. App.—Houston [14th Dist.] 2003, pet. denied). Plaintiff has never denied that the contractual limitations clause in its insurance policy is unambiguous and has only one reasonable meaning. The parties plainly agreed that any cause of action that Plaintiff may pursue under the policy would accrue on the date that it discovered its loss.

The magistrate judge — and the district court in adopting the magistrate judge's recommendations — correctly interpreted the Commercial Crime Policy in a way that not only was consistent with Texas law, but that also gave effect to the unambiguous intentions of the parties.

3. *Contrary to Plaintiff's Issue No. III, the District Court's Order Enforcing the Parties' Agreed Contractual Accrual Date Does Not Raise Any Legitimate Policy Concerns*

Plaintiff raises the rhetorical threat of imminent doom, suggesting that the magistrate judge's analysis could potentially require an insured "to file suit on an insurance contract before the parties had completed the presentation and assessment of the claim." Plaintiff's Br. at 25 n.5.[5] However, Plaintiff's doomsday scenario is unrealistic except in a case where the insured has itself breached the terms of the

[5]Plaintiff protests that it may be vulnerable to a "frivolous pleadings" allegation if it files a coverage action before the insurer has formally denied its claim. Plaintiff's Br. at 25 n.5. But this is not at all necessarily the case. *See, e.g., Getty Oil v. Insurance Co. of N. Am.,* 845 S.W.2d 794, 799 (Tex. 1992) (recognizing that a party may pursue an indemnity claim against an indemnitor even before the cause of action accrues for limitations purposes). At a minimum, an insured may file a declaratory judgment action requesting a declaration of policy coverage if it perceives that its insurer is moving too slowly in deciding whether to deny a claim.

policy. Here, for instance, the policy required that Plaintiff notify Hartford within 60 days after the discovery of any loss and prepare a detailed proof of loss within 120 days after discovery of the loss. (Record at 677). Plaintiff should have completed its assessment of its claim by July 1999 — within 120 days after it discovered its alleged loss in March 1999.

Under the magistrate judge's analysis, the parties could have — and should have — completed the assessment of any alleged loss *more than 3 years before limitations barred Plaintiff's breach of contract claim in March 2003.* Plaintiff's doomsday scenario arises here only because Plaintiff itself failed to comply with the requirements of the policy. Despite multiple requests from Hartford, Plaintiff repeatedly failed to submit a proper proof of loss in support of its claim for benefits. As the magistrate judge found, "[o]ver an almost three-year period, Plaintiff provided . . . proofs of loss ("POL") alleging various damage amounts." (Record at 817). Hartford could not more quickly respond to Plaintiff's claim because Plaintiff's proofs of loss were a moving target.

The magistrate judge's analysis merely holds the parties to those parts of their contractual bargain that do not violate Section 16.070(a) of the CPRC. Nothing in the magistrate judge's analysis offends public policy. Quite to the contrary, a contractual limitations clause that expresses the intent of the parties with respect to the running of limitations on a contract claim is legally valid and consistent with

general public policy. *See Vincent v. Comerica Bank*, No. H-05-2302, 2006 WL 1295494, *4 (S.D. Tex. May 10, 2006); *Canfield v. Bank One, Tex., N.A.*, 51 S.W.3d 828, 836 (Tex. App.—Texarkana 2001, pet. denied). Subject to Section 16.070, such a clause "encourages vigilance by both parties." *Canfield*, 51 S.W.3d at 836.[6]

By its terms, the Commercial Crime Policy encouraged vigilance by both parties. Plaintiff, not Hartford, is the party that failed to act vigilantly: Plaintiff filed multiple, and inconsistent, proofs of loss over a three-year period, and even after Hartford ultimately denied Plaintiff's claim in February 2002, Plaintiff delayed another eighteen months before finally filing the present action in August 2003. The parties crafted their contract precisely to avoid the type of delay that Plaintiff caused here. The magistrate judge, and the district court in adopting the magistrate judge's recommendation, correctly concluded that limitations bars Plaintiff's breach of contract claim against Hartford.

4. *Plaintiff's Issue No. IV is Illogical and Improperly Tries to Combine Two Different Elements of the District Court's Limitations Analysis*

Plaintiff asserts that the magistrate judge's analysis of Section 16.070(a) is inconsistent with her calculation of the four year limitations period. The magistrate

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[6]The very purpose of the defense of limitations is to protect parties from having to defend stale claims after memories have faded and documents have disappeared. *Computer Associates Int'l, Inc. v. Altai, Inc.*, 918 S.W.2d 453, 455 (Tex. 1994). "Society's interest in repose is to have disputes settled or barred within a reasonable time. It is based on the theory that the uncertainty and insecurity caused by unsettled claims hinder the flow of commerce." *Safeway Stores, Inc. v. Certainteed Corp.*, 710 S.W.2d 544, 545 (Tex. 1986).

judge reasoned that the contractual limitations period in the Commercial Crime Policy violated Section 16.070(a) because it effectively gave Plaintiff only one year and nine months to file suit — *i.e.,* two years minus a ninety day waiting period for Hartford to review Plaintiff's claim. (Record at 823). Plaintiff argues that, to be consistent, the magistrate judge should have equally considered the ninety day waiting period in her determination of the date on which Plaintiff's cause of action accrued:

> Hartford has admitted that ASONA's representative filed its first proof of loss on July 7, 1999. . . . If the contractual requirement of the 90 day waiting period is observed, ASONA was contractually barred from bringing a legal action against Hartford until, at the earliest, Tuesday October 5, 1999. . . . Therefore, the four year limitations period could not have run prior to Monday, October 6, 2003. ASONA filed suit on August 6, 2003. . . .

Plaintiff's Br. at 27. Plaintiff's argument makes no sense. It either miscomprehends the magistrate judge's reasoning, or it improperly merges two separate elements of the magistrate judge's analysis.

The magistrate judge cited the ninety day waiting period merely for the purpose of supporting her conclusion that the policy did not give Plaintiff at least two years in which to file its coverage action. (Record at 823). Having determined that the contractual limitations period was invalid, the magistrate judge then interpreted the policy, consistent with the default limitations period in Section 16.051 of the CPRC, to require that Plaintiff have brought its coverage claim within four years from the date Plaintiff discovered its loss. (*Id.* at 825). The magistrate judge found:

a. that Plaintiff discovered its loss in March 1999;

b. that Plaintiff filed its coverage cause of action in August 2003;

c. that limitations ran in March 2003; and

d. therefore, that Plaintiff filed its coverage cause of action more than four months after the four year limitations period expired.

(*Id.* at 826). In short, the magistrate judge reasoned that Plaintiff failed to file its lawsuit within four years (the default limitations period in Section 16.051) of the date on which Plaintiff discovered its loss (the accrual date that the parties specified in the policy). The magistrate judge had no need to consider the ninety day waiting period in applying the default limitations period under Section 16.051 of the CPRC: even with the ninety day waiting period, Plaintiff would have had over three years in which to file its lawsuit under the magistrate judge's analysis — *more than enough to satisfy the minimum two-year limitations period under Section 16.070(a) of the CPRC*.

Nor did the magistrate judge have any need to, or legitimate reason to, add the ninety day waiting period to the date on which Plaintiff's cause of action accrued. Plaintiff's argument that limitations should not have run before October 6, 2003, requires that Plaintiff rewrite the unambiguous language in the Commercial Crime Policy to require that Plaintiff have filed its lawsuit within four years "after the first date upon which Plaintiff could have filed suit following the expiration of the 90-day waiting period." That was not the parties' agreement. Instead, the parties specifically agreed that Plaintiff's cause of action would accrue as of the date when Plaintiff first

discovered its loss. Plaintiff failed to file the present action within four years after the date on which, by its own admission, it first discovered its loss.

Plaintiff improperly confuses the magistrate judge's application of Section 16.070(a) with the magistrate judge's application of the default limitations period in Section 16.051. The magistrate judge, as well as the district court, correctly found that the statute of limitations barred Plaintiff's coverage claim.

B. As a Matter of Law, the Commercial Crime Policy Affords No Coverage for Plaintiff's Alleged "Losses"

The magistrate judge recommended that the district court grant Hartford's Limitations MSJ. (Record at 815). The district court adopted the magistrate judge's recommendation and, therefore, did not consider any of the grounds for summary judgment in Hartford's MSJ. (*Id.* at 852; *see id.* at 365 (Hartford's MSJ)). The summary judgment grounds in Hartford's MSJ are equally as sound as the grounds in Hartford's Limitations MSJ. Although the district court had no reason to reach the merits of Hartford's MSJ, this Court may affirm the district court's summary judgment not only on limitations grounds, but also on the grounds in Hartford's MSJ. *See Cabrol*, 106 F.3d at 105.

Plaintiff filed at least five different proofs of loss under the Commercial Crime Policy. Although its allegations varied from one Proof of Loss to another, Plaintiff essentially sought to collect from Hartford on the basis of three alleged forms of loss: (a) that Mark Strange committed theft by stealing from Plaintiff's payroll account to

pay bonuses to himself and another employee, Jan Goehring; (b) that Strange diverted funds from other shareholders to make personal capital calls; and (c) that Strange improperly, and without authority, used corporate funds for personal expenses such as basketball tickets and a country club membership. The Commercial Crime Policy affords no coverage for any of these alleged losses.

1. *The Commercial Crime Policy Does Not Cover Benefits that Mark Strange or Jan Goehring Received in the Form of Bonuses*

The Commercial Crime Policy covers losses that result from "employee dishonesty." (Record at 668). Paragraph D.3.a. in the Coverage Form specifically defines "employee dishonesty" as dishonest acts that an employee commits with the manifest intent to enable the employee to obtain a financial benefit "other than employee benefits earned in the normal course of employment, including: salaries, commissions, fees, ***bonuses***, promotions, profit sharing or pensions." (*Id.*) (emphasis added). As Hartford argued in Hartford's MSJ, the plain terms of the Commercial Crime Policy exclude coverage for employee benefits earned in the normal course of employment, ***such as bonuses***. (Record at 370).

Citing the *Klyn* case from New York, Plaintiff has suggested that "[t]here is a difference between compensation voluntarily (though erroneously) paid by the employer to the employee and money embezzled from a payroll account (over which the employee had control) wherein the employee secretly pays himself unauthorized

and excessive salary, commissions and bonuses." (Record at 558-59) (citing *Klyn v. Travelers Indemnity Co.*, 273 A.D.2d 931, 709 N.Y.S.2d 780 (2000)). This Court, however, has rejected the reasoning in *Klyn*. *Performance Autoplex II Ltd. v. Mid-Continent Cas. Co.*, 322 F.3d 847, 857-58 (5th Cir. 2003). *See also Dickson v. State Farm Lloyds*, 944 S.W.2d 666, 668 (Tex. App.—Corpus Christi 1997, no writ).

The policy in *Performance Autoplex* involved exactly the same definition of "employee dishonesty" at issue in the present case. As Plaintiff does here, the plaintiff in *Performance Autoplex* argued that the policy did not exclude coverage where an employee secretly pays himself unauthorized and excessive salary or bonuses. This Court disagreed:

> Looking at the plain language of the policy, the interpretation rejecting coverage makes sense. If "in the normal course of employment" means "not obtained through employee dishonesty," the policy language excluding salaries would become mere surplusage. That is, *the language excluding salaries presumes that there are acts of employee dishonesty that result in increased employee benefits that the insured and insurer agreed to exclude from coverage.* . . . Turning to the facts of this case, our result is clear. Wall obtained unauthorized salary increases for herself and another employee while employed by Performance. This loss is not covered by the plain language of the policy, which exempts salaries from the category of employee dishonesty losses.

*Performance Autoplex*, 322 F.3d at 858 (emphasis added). *See also Dickson*, 944 S.W.2d at 668 (noting that an employee dishonesty policy excludes coverage where "an employee has dishonestly or fraudulently obtained for himself only salary or other such employee benefits").

*Performance Autoplex* is exactly on point. The term "employee dishonesty," as expressly defined in the Commercial Crime Policy, excludes coverage for any loss that Plaintiff may have incurred when Mark Strange allegedly stole money from Plaintiff's payroll account to pay bonuses to himself and to Jan Goehring.[7] Thus, the district court properly granted summary judgment in Hartford's favor to the extent that Plaintiff asserts a coverage claim for any losses allegedly arising from Strange's actions in paying improper bonuses.

2. *The Commercial Crime Policy Does Not Cover the Alleged Diversion of Funds from Other Shareholders to Pay for Personal Capital Calls*

Not only does Paragraph D.3.a. in the Coverage Form exclude coverage for improper bonus payments, but it also states that coverage under the Commercial Crime Policy extends only to employee dishonesty which causes the insured "to sustain loss." (Record at 668). Under this language, the policy affords coverage only for losses that an employee causes to the insured, not for losses that an employee may cause to a third party. As this Court has explained, employee dishonesty policies such as the Commercial Crime Policy "do not serve as liability insurance to protect employers against tortious acts committed against third-parties by their employees." *Lynch Prop., Inc. v. Potomac Ins. Co.*, 140 F.3d 622, 629 (5th Cir. 1998).

[7]Although the magistrate judge had no reason to reach the issue in the context of Plaintiff's contract claim, the magistrate judge agreed in the context of Plaintiff's extracontractual claims that bonuses are "exempted 'from the category of employee dishonesty losses' under the relevant contract provision." (Record at 1013) (citing *Performance Autoplex*, 322 F.3d at 857).

Plaintiff alleged in its pleadings that Strange diverted "company funds" to cover his share of capital calls to the shareholders. (Record at 16). But in fact, the evidence that Plaintiff tendered in response to Hartford's MSJ showed *not* that Strange diverted any funds from Plaintiff, but rather that Strange induced Plaintiff's *other shareholders* to cover Strange's share of the capital calls. Calton Boswell, a private investigator for Plaintiff, stated in an expert report:

> On at least two instances capital calls were required to be paid by the owners. Mr. Strange held a small percentage ownership in the company. When the additional capital was required Strange would notify the owners of the amount and provide false documentation about his infusion share. The other owners believed that Strange was paying his portion of the capital, however, this was not the case. He would compute the amount needed and apportion his share to the other owners and they paid his share. *In short he was stealing from the other three owners* in order to cover his fair share of the capital contribution and provided false documentation to get the funds. . . .

(Record at 608) (emphasis added).

In a case seeking to recover benefits under a policy, the insured bears the burden of offering evidence to show that its claim falls within the policy's scope of coverage. *Sentry Ins. Co. v. R.J. Weber Co.*, 2 F.3d 554, 556 (5th Cir. 1993). In Hartford's MSJ, Hartford argued:

> There is no loss to plaintiff associated with this accounting sleight of hand, even if the claim is true. Like taking money out of one's right pocket and putting it back in the left pocket; the plaintiff here ended up with the same amount of funds that it started with; thus, no financial loss was sustained by this plaintiff. While the other stockholders might be aggrieved by such an action, they are not named insureds nor parties to this lawsuit. If the policy holder suffers no loss as the result of an

> alleged employee theft, no obligation to pay arises on the part of the insurer.

(Record at 372). *Plaintiff offered no response to Hartford's argument*. (*See id.* at 552-61).

Strange's alleged misconduct in inducing other shareholders to cover his share of Plaintiff's capital calls may have been a cause of loss *to those other shareholders*. But it was not a cause of any "loss" *to Plaintiff.* Plaintiff ultimately ended up with exactly the sum of capital contributions that it had expected to receive from its shareholders, even if some of those shareholders may have proportionally contributed more of their fair share than Strange. (Record at 372). Absent any loss to Plaintiff as opposed to third parties, the district court properly granted summary judgment in Hartford's favor to the extent that Plaintiff asserts a coverage claim for any alleged "losses" arising from Strange's diversion of funds to satisfy Plaintiff's calls for personal capital contributions.

3. *The Commercial Crime Policy Does Not Cover Strange's Alleged Use of Corporate Funds to Pay Personal Expenses in the Absence of Any Evidence that Strange Manifestly Intended to Cause a Loss to Plaintiff*

Paragraph D.3.a. in the Coverage Form limits the term "employee dishonesty" to include only dishonest acts that an employee commits with the "manifest intent" to cause loss to the insured. (Record at 668). Consistent with this unambiguous language, Hartford's MSJ noted that Plaintiff must "establish more than just poor judgment on the part of an employee; it must also establish that there was a manifest

intent to cause a loss." (Record at 372-75). In particular, Hartford observed that the mere fact that Mark Strange used corporate funds for personal expenses did not establish a manifest intent to cause a loss, as corporate executives commonly use corporate credit cards and other corporate funds to pay for travel expenses and the costs of entertaining prospective clients. *Id.*

Plaintiff responded to Hartford's argument with a non sequitur, asserting that the company had not authorized Strange's expenses. (Record at 559-60). But even assuming for the sake of argument that Strange's expenses were unauthorized, Plaintiff had the burden to show that Strange both knew that these expenses were unauthorized and *manifestly intended* to cause Plaintiff to suffer a loss. Plaintiff has never offered any evidence to exclude the possibility that Strange, as Plaintiff's president and the holder of a company credit card, believed that he had the power and authority to use corporate funds for purposes such as travel expenses and entertaining prospective clients. *See Progressive Cas. Ins. Co. v. First Bank*, 828 F. Supp. 473, 475 (S.D. Tex. 1993) (granting judgment in favor of insurer where the insured bank "has not shown that the [employee] intended to cause the bank a loss").

Notably, Plaintiff failed to sustain its summary judgment burden even with respect to the authority argument that it raised in lieu of addressing the issue of manifest intent. Plaintiff argued that Strange lacked the authority to use corporate funds for personal expenses. (Record at 559-60). Yet, the affidavit of Pat Bryan that

Plaintiff offered in support of its argument at best showed only that Strange had no *express* authority. (*Id.* at 573). Plaintiff offered no summary judgment evidence to exclude the possibility that Strange had *implied* authority arising either from the nature of the business that Plaintiff entrusted to Strange or the pattern of conduct that Plaintiff allowed Strange to pursue while he was still president of the company. *Pasant v. Jackson Nat'l Life Ins. Co.,* 52 F.3d 94, 97 (5th Cir. 1995).[8]

Nor even does Plaintiff's express authority argument have any merit. Pat Bryan's affidavit asserts that "[u]nder the terms of his employment agreement, Mr. Strange was not authorized to expense his recreational activities or purchases *except for those incurred in entertaining clients and prospects*, and then *only if he properly documented* the activity or purchase he sought to expense." (Record at 573) (emphasis added). Bryan's affidavit mischaracterizes Mark Strange's employment agreement. The agreement states that Plaintiff would reimburse Strange not only for entertainment expenses, but also for "travel and other expenses reasonably and necessarily incurred by Employee in connection with the Company's business." (*Id.* at 616). Moreover, the agreement provides that Strange must furnish Plaintiff only such documentation "as the Company shall reasonably request." (*Id.*).

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[8]Even if an employee lacks express authority to do something, an employer may grant implied authority by allowing the employee to believe, through words or a course of conduct, that he has the power to do something. *See Pasant,* 52 F.3d at 97. Here, Plaintiff undoubtedly received the regular statements reflecting the charges on its company credit card. Absent any evidence to suggest that Plaintiff complained about the charges to Strange, the evidence shows only that Plaintiff apparently raised the issue for the first time *after* Strange left the company.

Plaintiff has never offered any summary judgment evidence showing (a) that Strange's alleged personal expenses were not actually valid entertainment, travel or other expenses which Strange necessarily incurred in connection with his business as Plaintiff's president, (b) that Plaintiff ever reasonably requested that Strange provide documentation to support Strange's claims for reimbursement, and (c) above all, that Strange manifestly intended to cause Plaintiff to suffer a loss. Thus, the district court properly granted summary judgment in Hartford's favor to the extent that Plaintiff asserts a coverage claim for any losses arising from Strange's use of corporate funds for alleged personal expenses.

## II. The District Court Correctly Granted Summary Judgment in Hartford's Favor on Plaintiff's Extracontractual Causes of Action

In addition to Plaintiff's breach of contract claim, Plaintiff also alleged several extracontractual causes of action against Hartford — specifically, claims for breach of the common law duty of good faith and fair dealing, violations of former Article 21.21 and Article 21.55 of the Texas Insurance Code, and violations of the Texas Deceptive Trade Practices Act. (Record at 17-18, 64). Hartford filed a motion for summary judgment arguing that Plaintiff could not recover on its extracontractual claims because (a) Plaintiff suffered no independent injuries, (b) Plaintiff had no coverage for its alleged losses, and (c) Plaintiff could offer no evidence that Hartford acted in bad faith. (Record at 856) (Hartford's Supplemental MSJ). The magistrate

judge recommended that the district court grant Hartford's motion. (Record at 1001). The district court adopted the magistrate judge's recommendation. (*Id.* at 1040).

The district court correctly ruled that Plaintiff may not recover on any of its extracontractual claims. Accordingly, this Court should affirm the district court's summary judgment in Hartford's favor on Plaintiff's extracontractual claims.

A. As a Matter of Law, Plaintiff Cannot Recover on Its Extracontractual Claims Because Plaintiff Has Failed to Show that It Suffered Any Injuries Independent of Its Claim for Breach of Contract

In Hartford's Supplemental MSJ, Hartford asked the district court to grant summary judgment against each of Plaintiff's extracontractual claims because Plaintiff could not show that it had suffered any injuries independent of its cause of action for breach of contract. (Record at 764). The magistrate judge, and the district court in adopting the magistrate judge's recommendation, agreed that the independent injury rule barred Plaintiff from recovering on its DTPA and Article 21.21 claims. "The court finds that Plaintiff has not alleged any damages that can substantiate an extra-contractual claim under the Texas Insurance Code or DTPA. For this reason, too, its causes of action premised under Article 21.21 and the DTPA cannot stand." (Record at 1019-20).

Although the magistrate judge applied the independent injury rule only against Plaintiff's DTPA and Article 21.21 claims, the rule applies equally to bar *each* of Plaintiff's extracontractual claims. "An insured is not entitled to recover extra-

contractual damages unless the complained of actions or omissions cause injury independent of the injury resulting from a wrongful denial of policy benefits." *United Serv. Automobile Ass'n v. Gordon*, 103 S.W.3d 436, 442 (Tex. App.—San Antonio 2002, no pet.). *See Parkans Int'l LLC v. Zurich Ins. Co.*, 299 F.3d 514, 519 (5th Cir. 2002); *see also Walker v. Federal Kemper Life Assurance Co.*, 828 S.W.2d 442, 454 (Tex. App.—San Antonio 1992, writ denied) (holding that an insured must prove an extracontractual injury beyond "the injury that would always occur when an insured is not promptly paid its demand").

Significantly, Plaintiff does not attack the district court's summary judgment in Hartford's favor on the independent injury rule. *See* Plaintiff's Br. at 15 & 29 n.6 (noting that Plaintiff appeals only the "first and third" grounds for summary judgment in the magistrate judge's memorandum on Hartford's Supplemental MSJ). Having failed to challenge one of the grounds on which the district court granted summary judgment, Plaintiff has, at a minimum, waived any argument that the district court improperly rendered judgment in Hartford's favor on Plaintiff's DTPA and Article 21.21 claims — the two claims for which the magistrate judge found the independent injury rule to be dispositive. *See, e.g., Brinkmann v. Dallas County Deputy Sheriff Abner*, 813 F.2d 744, 748 (5th Cir. 1987).

This Court may apply the independent injury rule to affirm the district court's summary judgment on each of Plaintiff's extracontractual causes of action. Plaintiff

suggests that the rule only bars it from seeking exemplary damages, not from pursuing "policy proceeds under a bad faith cause of action." Plaintiff's Br. at 15. *See also id.* at 35-36 (citing *Twin City Fire Ins. Co. v. Davis*, 904 S.W.2d 663 (Tex. 1995)). By definition, however, policy proceeds are not an *extracontractual* form of damages; rather, they are exactly the type of contract damages which, under Texas law, an insured may recover only under a breach of contract cause of action. *See Parkans Int'l LLC*, 299 F.3d at 519; *Gordon*, 103 S.W.3d at 442.

The decision in *Twin City* is not to the contrary. *Twin City* was a workers' compensation case in which the carrier refused to pay for the cost of a hot tub as therapy for a back injury. *Twin City Fire Ins. Co.*, 904 S.W.2d at 664-65. The trial court awarded the plaintiff $3500 in actual damages for the cost of the hot tub, as well as $100,000 in exemplary damages. *Id.* at 665. On appeal, the carrier argued that the exemplary damages award was improper because the trial court had awarded only a contract measure of actual damages, not tort damages. The Texas Supreme Court agreed with the carrier:

> A breach of contract alone will not support punitive damages; the existence of an independent tort must be established. . . . The mere availability of a tort-based theory of recovery is not sufficient; actual damages sustained from a tort must be proven before punitive damages are available.

*Id.* at 665. The supreme court did *not* hold, as Plaintiff contends in the present case, that "damages for policy benefits *are* available under a bad faith claim." Plaintiff's

Br. at 35 (emphasis in original). Instead, the court in *Twin City* held only that *exemplary damages* are *not* available under a contract claim — *i.e.,* that an insured must suffer tort damages, above and beyond unpaid policy benefits, to recover an award of exemplary damages. *Twin City Fire Ins. Co*., 904 S.W.2d at 665-66.

In workers' compensation cases involving facts similar to those in *Twin City*, Texas courts have not interpreted *Twin City* to permit an insured to recover damages for policy benefits under a bad faith claim. *See, e.g, Hulshouser v. Texas Workers' Compensation Ins. Fund*, 139 S.W.3d 789, 792 (Tex. App.—Dallas 2004, pet. denied) (applying the independent injury rule to bar bad faith claims where a compensation claimant only asserted damages for the denial of benefits and not any independent injuries). Indeed, the court in *Twin City* itself recognized that the independent injury rule bars a compensation claimant from pursuing an extracontractual cause of action unless the claimant can establish an injury independent of his compensation claim. *Twin City Fire Ins. Co.,* 904 S.W.2d at 667 (citing *Aranda v. National County Mut. Fire Ins. Co.*, 725 S.W.2d 165, 167 (Tex. 1987)).[9]

Here, Plaintiff has neither alleged nor offered any evidence to show that it suffered any injury independent of its breach of contract cause of action for unpaid

[9]Subsequent to *Twin City*, the Texas Supreme Court reversed a judgment awarding damages in a bad faith action where the jury did not award damages for any injury independent of policy benefits. *Provident Am. Ins. Co. v. Castañeda*, 988 S.W.2d 189, 199 (Tex. 1998).

policy benefits.[10] Although the magistrate judge cited the independent injury rule as a basis for rejecting Plaintiff's DTPA and Article 21.21 claims, this Court may properly rely on the independent injury rule to affirm the district court's summary judgment with respect to each of Plaintiff's extracontractual causes of action.

B. As a Matter of Law, Plaintiff Cannot Recover on Its Extracontractual Claims Because Plaintiff Has Failed to Show that It Has Any Coverage Under the Commercial Crime Policy for Its Alleged Losses

Plaintiff's extracontractual causes of action arise not simply from an allegation that Hartford improperly denied Plaintiff's claim for coverage under the Commercial Crime Policy, but rather from an allegation that Hartford denied Plaintiff's claim *in bad faith*. However, if the policy afforded no coverage, then as a matter of law, Hartford could not have acted in bad faith in denying Plaintiff's claim. *See Republic Ins. Co. v. Stoker*, 903 S.W.2d 338, 340 (Tex. 1995). And if Hartford did not act in bad faith, then Hartford cannot be liable on *any* of Plaintiff's extracontractual causes

[10]Because Plaintiff does not challenge the magistrate judge's analysis of the independent injury rule, Plaintiff has made no effort in its brief on appeal to show that it suffered any injury independent of its breach of contract claim. In the district court, Plaintiff suggested that it had suffered economic damages in the form of "additional storage costs for all of the documents that Defendant has insisted Plaintiff continue to store while Defendant continues to deny the claim." (Record at 864). However, Plaintiff had a contractual obligation to store all of the documents that Hartford needed to review in evaluating Plaintiff's claim. (*Id.* at 666) (Commercial Crime Policy at Crime General Provisions ¶ 16 ("You must keep records of all Covered Property so we can verify the amount of any loss.")). Moreover, Hartford was not responsible for Plaintiff's alleged storage costs: the state district court presiding over Mark Strange's criminal prosecution ordered Plaintiff to preserve all documents relating to Strange's employment with the company. (*Id.* at 688). Thus, as the magistrate judge observed, Plaintiff's alleged storage costs were not an independent tort injury, but rather stemmed "either from a criminal case wholly unrelated to Defendant's denial of coverage or from the usual costs associated with maintaining a lawsuit contesting an allegedly wrongful denial of policy benefits." (*Id.* at 1019).

of action. *See Higginbotham v. State Farm Mut. Auto Ins. Co.*, 103 F.3d 456, 460 (5th Cir. 1997); *Emmert v. Progressive County Mut. Ins. Co.*, 882 S.W.2d 32, 36 (Tex. App.—Tyler 1994, writ denied).

The Texas Supreme Court recently discussed this issue in *Progressive County Mutual Insurance Co. v. Boyd*, 177 S.W.3d 919 (Tex. 2005). The trial court in *Boyd* ruled that the plaintiff could not recover for breach of an uninsured motorist policy because the jury found that the plaintiff had not been involved in an accident with an uninsured motorist. The supreme court concluded that the jury's verdict barred the plaintiff from recovering on any extracontractual causes of action:

- With respect to the plaintiff's Article 21.55 cause of action, the court noted: "There can be no liability under article 21.55 if the insurance claim *is not covered* by the policy." *Id.* at 922 (emphasis added).

- With respect to the plaintiff's common law bad faith cause of action, the court noted: "Boyd's common-law bad-faith claims are also negated by the determination in the breach of contract claim that *there was no coverage*." *Id.* (emphasis added).[11]

- With respect to the plaintiff's Article 21.21 and DTPA causes of action, the court noted: "Because the common-law bad-faith standard is the same as the statutory standard, Boyd's claim for treble damages predicated on bad faith pursuant to article 21.21 of the Insurance Code and section 17.46 of the DTPA must likewise fail. . . . The determination that Boyd's article 21.21 claim is not valid disposes of Boyd's claim

[11]The court in *Boyd* acknowledged that it had "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." *Boyd*, 177 S.W.3d at 922. The summary judgment evidence here, however, shows neither that Hartford committed any extreme misconduct nor that Plaintiff suffered any valid measure of damages independent of its breach of contract claim. *See supra* pages 33-37.

> under 17.50 of the DTPA, which is also predicated on a violation of article 21.21 of the Insurance Code." *Id.*

*See also State Farm Life Ins. Co. v. Martinez,* 216 S.W.3d 799, 806-07 (Tex. 2007); *Fire Ins. Exch. v. Sullivan*, 192 S.W.3d 99, 107-08 (Tex. App.—Houston [14th Dist.] 2006, pet. denied).

Here, the magistrate judge concluded that Plaintiff had no valid claim under Article 21.55 because Plaintiff lacked coverage for its alleged losses under the Commercial Crime Policy. (Record at 1020) ("Hartford cannot be 'ultimately found liable' for coverage under the insurance policy."). The same reasoning, however, applies not solely to Plaintiff's Article 21.55 claim, but equally to each of Plaintiff's extracontractual causes of action. *Boyd* and analogous cases confirm that an insurer does not act in "bad faith" by denying a claim that the insurer has a valid right to deny. As this Court has explained, "an insurer will not be faced with a tort suit for challenging a claim of coverage if there was any reasonable basis for denial of that coverage." *Higginbotham*, 103 F.3d at 460.

Hartford had a reasonable basis for denying Plaintiff's coverage claim. First, as the magistrate judge recognized, "Plaintiff is barred by limitations from litigating its breach of contract claim." (Record at 1020). When the limitations period expired, Plaintiff's remedies for any alleged breach of contract lapsed. *See supra* at 11-24. Because Hartford is not liable to Plaintiff for breach of contract, Hartford likewise cannot be liable to Plaintiff on any extracontractual causes of action. *See Boyd,* 177

S.W.3d at 922; *cf. Hewlett-Packard Co. v. Benchmark Electronics, Inc.*, 142 S.W.3d 554, 565 (Tex. App.—Houston [14th Dist.] 2004, pet. denied) (holding that where limitations barred a breach of contract claim, it also barred an extracontractual claim arising out of the same contract).

Second, even assuming for the sake of argument that limitations does not bar Plaintiff's coverage claim, Plaintiff's alleged losses do not fall within the scope of coverage under the Commercial Crime Policy:

a. *Improper Bonuses*. The term "employee dishonesty," as defined in the Commercial Crime Policy, excludes coverage for any losses that Plaintiff may have incurred when Mark Strange allegedly stole money from Plaintiff to pay bonuses to himself and Jan Goehring. *See Performance Autoplex*, 322 F.3d at 858; *see also supra* at 24-27.

b. *Diversion of Funds from Other Shareholders for Capital Calls*. The Commercial Crime Policy extends coverage only for employee dishonesty that causes a loss to the insured, as opposed to a third party. Strange's alleged misconduct in inducing other shareholders to cover his share of Plaintiff's capital calls was not a cause of any "loss" to Plaintiff. *See Lynch Prop., Inc.*, 140 F.3d at 629; *see also supra* at 27-29.

c. *Personal Expenses.* The Commercial Crime Policy furnishes coverage only for dishonest acts that an employee commits with the "manifest intent" to cause

loss to the insured. Plaintiff has never offered any evidence, either to Hartford in support of its proofs of loss or to the district court in response to Hartford's MSJ, showing that Strange manifestly intended to cause Plaintiff a loss by using corporate funds to pay personal travel and entertainment expenses. *See supra* at 29-32.

Absent any coverage under the Commercial Crime Policy, Plaintiff has no valid extracontractual causes of action against Hartford. Although the magistrate judge found the absence of coverage dispositive only as to Plaintiff's Article 21.55 claim, this Court may and should affirm the district court's summary judgment in Hartford's favor with respect to each of Plaintiff's extracontractual causes of action.

C. In the Absence of Any Summary Judgment Evidence that Hartford Acted in Bad Faith, Plaintiff Cannot Recover on Its Common Law Bad Faith, Article 21.21 and DTPA Causes of Action

Plaintiff's causes of action for common law bad faith and for violations of Article 21.21 and the DTPA each require evidence that Hartford acted in *bad faith*. *Boyd,* 177 S.W.3d at 922. "[E]vidence showing only a bona fide coverage dispute does not, standing alone, demonstrate bad faith." *State Farm Lloyds v. Nicolau*, 951 S.W.2d 444, 448 (Tex. 1997). *See Transportation Ins. Co. v. Moriel*, 879 S.W.2d 10, 17 (Tex. 1994). "Nor is bad faith established if the evidence shows the insurer was merely incorrect about the factual basis for its denial of the claim, or about the proper construction of the policy." *Travelers Personal Sec. Ins. Co. v. McClelland*, 189 S.W.3d 846, 854 (Tex. App.—Houston [1st Dist.] 2006, no pet.).

Bad faith focuses not on whether the insurer correctly denied the insured's claim, but rather on the insurer's conduct in rejecting the claim. *Lyons v. Millers Cas. Ins. Co.*, 866 S.W.2d 597, 601 (Tex. 1993). An insurer that has a "reasonable basis for denying a claim, even if the [fact] finder eventually determines that basis to be erroneous, enjoys immunity from statutory bad faith under the Texas Insurance Code and the Texas Deceptive Trade Practices Act." *MacIntire v. Armed Forces Benefit Ass'n*, 27 S.W.3d 85, 519 (Tex. App.—San Antonio 2000, no pet.). *See also Parkans Int'l LLC*, 299 F.3d at 519 (holding that where the insurer had a reasonable basis for denying coverage, the law shields the insurer from extracontractual liability "whether the tort claims are common-law or statutory").

Here, the magistrate judge concluded, and the district court agreed, that the parties at most had only a bona fide coverage dispute, which was insufficient as a matter of law to demonstrate the type of bad faith necessary to support an Article 21.21, DTPA or common law bad faith claim. (Record at 1010) (citing *United States Fire Ins. Co. v. Williams*, 955 S.W.2d 267, 268 (Tex. 1997)). The magistrate judge's conclusion was correct. Plaintiff advances an assortment of arguments in an effort to suggest that the evidence at least raises "reasonable inferences" that Hartford acted in bad faith. Plaintiff's Br. at 33. None of Plaintiff's arguments survives even minimal scrutiny — either under the evidence or under the law.

1. *Hartford Did Not Make Any Actionable Misrepresentation to Plaintiff in Hartford's Letter Denying Plaintiff's Coverage Claim*

Plaintiff argues that Hartford misrepresented both the law and the terms of the Commercial Crime Policy by asserting in its denial letter that limitations barred Plaintiff's coverage claim. *See* Plaintiff's Br. at 33-34. Hartford stated in its denial letter "that the two-year limitation period outlined under the policy has expired and any further remedies have lapsed." (Record at 637-38). The magistrate judge concluded that this statement was not an actionable misrepresentation:

> Although Defendant's understanding was later found to be void under Texas law, its agent was relying on an express contractual term assumed to be valid at the time the denial letter was sent. *There is no evidence that this assertion was known by the agent to be false when it was made*.

(Record at 1015). The magistrate judge's conclusion was correct. Hartford did not make any actionable misrepresentation to Plaintiff.

Plaintiff protests that the magistrate judge did not "point to any evidence that Hartford's agent *actually did* assume the provision *to be* valid when he made the misrepresentation." Plaintiff's Br. at 33 (emphasis in original). However, Plaintiff has confused the burden of proof. To defeat summary judgment, Plaintiff had the burden to produce some evidence showing that Hartford's agent knew that the contractual limitations clause was void. *See Celotex Corp.*, 477 U.S. at 322 (noting that the party opposing summary judgment must offer evidence establishing the challenged elements of its cause of action). The magistrate judge found that Plaintiff

offered no such evidence. (Record at 1015). In the absence of any such evidence, any inference of "bad faith" would have been unreasonable.

Even assuming for the sake of argument that Hartford's agent knew that the contractual limitations clause was void, Hartford's statements as to the effect of the clause were not a producing cause of any damages to Plaintiff. *See MacIntire*, 27 S.W.3d at 92 (noting that representations cannot form the basis for extracontractual liability unless they are a producing cause of damages). Although Hartford's letter cited the two year limitations period in the Commercial Crime Policy, Hartford's conclusion ultimately was that Plaintiff's remedies had "lapsed." (Record at 638). The magistrate judge, as well as the district court, correctly determined that Plaintiff's remedies have, in fact, lapsed under the applicable default statute of limitations. *See supra* at 11-24. Therefore, Hartford's conclusion, even if not its reasoning, was accurate and no producing cause of any damages to Plaintiff.

Moreover, Hartford's denial letter contained only one paragraph discussing the limitations issue. The bar of limitations was not the sole factor that Hartford cited in support of its decision to deny Plaintiff's coverage claim. Indeed, the vast majority of Hartford's letter described at length the *factual* grounds for Hartford's decision to deny Plaintiff's claim. (Record at 636-38). Hartford's denial letter cited reasonable factual grounds for its decision to deny Plaintiff's claim, and Plaintiff can claim no injury in Hartford's representations about the effect of the two year contractual

limitations clause when Hartford otherwise properly denied Plaintiff's claim. Accordingly, the district court correctly granted summary judgment in Hartford's favor on Plaintiff's extracontractual causes of action.

2. *Plaintiff is Incorrect in Arguing that Hartford's Liability under the Commercial Crime Policy Ever Became "Reasonably Clear"*

Plaintiff argues that "Hartford's denial of the claim was unreasonable because there is evidence that coverage for at least . . . part of the claim [was] reasonably clear." Plaintiff's Br. at 30. However, Plaintiff has made no attempt to identify or discuss the "evidence" that, in its view, establishes that the factual grounds in Hartford's denial letter were unreasonable. Nor did it make any such attempt in the district court: in its response to Hartford's Supplemental MSJ, Plaintiff merely quoted the allegations in its live pleadings and asserted, without proof, that Hartford's liability was reasonably clear. *See* Record at 863-68; *cf. Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 256-57 (1986) (noting that pleadings and raw allegations do not satisfy the requirement for summary judgment proof).

As Hartford observed in its letter denying Plaintiff's claim, Plaintiff has never demonstrated that Hartford had any liability to Plaintiff under the Commercial Crime Policy. With respect to Plaintiff's claim for losses from unauthorized bonuses, Hartford had a reasonable basis for relying on case law such as *Performance Autoplex* to conclude that the plain language of the policy excluded coverage for unauthorized bonuses. *See Performance Autoplex*, 322 F.3d at 858. At best, Plaintiff can respond

only that there might be some New York case law contrary to *Performance Autoplex*. (*See* Record at 862). But even then, the New York case law would mean only that the policy was ambiguous; and as a matter of law, an insurer does not act in bad faith by denying coverage on the basis of a favorable interpretation of ambiguous policy language. *See Parkans Int'l LLC*, 299 F.3d at 519.

With respect to Plaintiff's claim for losses from personal expenses, Hartford had a reasonable basis for concluding that the expenses were valid employment perks that Plaintiff extended to Strange to assist him in his role as a corporate executive. In fact, as the magistrate court recognized, Plaintiff itself has acknowledged that some of Strange's entertainment expenses may very well have been proper "subject to the documentation requirements contained under the express terms of his employment agreement." (Record at 1014; *see also* Record at 908). In its denial letter, Hartford invited Plaintiff to provide documentation supporting its contention that Strange's personal expenses were unauthorized and provided no benefit to the company. (Record at 637). Plaintiff did not do so.

At a minimum, the summary judgment evidence here shows only that the parties had a bona fide coverage dispute — and certainly *not* that Hartford's liability to Plaintiff under the Commercial Crime Policy ever became "reasonably clear." *See Provident Am. Ins. Co. v. Castañeda*, 988 S.W.2d 189, 194 (Tex. 1998) (holding, as a matter of law, that an insurer is not subject to extracontractual claims where the

evidence as to its liability under the insurance policy is at best conflicting). Accordingly, the district court correctly granted summary judgment in Hartford's favor on Plaintiff's extracontractual causes of action.[12]

3. *Hartford Has No Liability to Plaintiff for Any Alleged Delay in Its Investigation of Plaintiff's Coverage Claim*

Plaintiff argues that even if Hartford's liability were not reasonably clear at the time of Hartford's letter denying coverage, "Hartford still had statutory and common law obligations of its own *to attempt to clarify coverage*." Plaintiff's Br. at 30 (emphasis added). Citing the Texas Supreme Court opinion in *Vasquez*, Plaintiff suggests that Hartford did not conduct a reasonable investigation of Plaintiff's claim. *Id.* (citing *Minnesota Life Ins. Co. v. Vasquez*, 192 S.W.3d 774, 780 (Tex. 2006)). Plaintiff misconstrues *Vasquez*. Contrary to Plaintiff's argument, *Vasquez* does not stand for the proposition that when an insurer denies a claim, the insurer has a further obligation to reconsider and redetermine coverage after its denial. *Vasquez*, 192 S.W.3d at 780. *Vasquez* holds simply that when coverage is still an open question, "an insurer cannot sit on its hands . . . to keep things that way." *Id.*

By the time that Hartford denied Plaintiff's claim, coverage was no longer an open question: Hartford had correctly determined that the Commercial Crime Policy

[12]Plaintiff never showed any reasonable inference that Hartford's liability *ever* became reasonably clear. But as the magistrate court noted, Plaintiff also never showed that Hartford's liability was reasonably clear *prior to* Hartford's February 2002 letter denying Plaintiff's coverage claim. (Record at 1010).

did not cover Plaintiff's alleged losses. (Record at 636-38). If Hartford owed no liability under the policy, then the reasonableness of Hartford's investigation could not be a source of injury to Plaintiff. Plaintiff has offered no evidence that it suffered any injury independent of its breach of contract claim — much less any injury resulting from the reasonableness of Hartford's investigation independently of the denial of Plaintiff's coverage claim. Absent any such evidence, Plaintiff may not recover for any alleged delay or other impropriety in Hartford's investigation of Plaintiff's claim. *See id.* at 780; *Castañeda*, 988 S.W.2d at 198.

Moreover, Plaintiff has offered no evidence to raise even an inference that Hartford failed to conduct a reasonable investigation. Plaintiff cites a document that "appears to be a summary of claim notes." Plaintiff's Br. at 31 (citing Record at 982-92).[13] However, to support a extracontractual cause of action based on an improper delay, the evidence must show "(1) the absence of a reasonable basis for denying or delaying payment of the benefits of the policy and (2) the insurer knew or should have known there was not a reasonable basis for denying the claim or delaying payment of the claim." *Estrada v. State Farm Mut. Auto. Ins. Co.*, 897 F. Supp. 321, 323 (W.D. Tex. 1995). The "claim notes" show no such thing.

[13]Plaintiff's reliance on these notes is based on the fallacious assumption that the absence of entries on the notes means that something which should have happened did not happen. This, in itself, is not a reasonable inference. Plaintiff offers no evidence that the notes are a comprehensive record of all of Hartford's actions in investigating Plaintiff's claim.

First, the "claim notes" reflect on their face that Hartford had a reasonable basis for delaying its investigation of Plaintiff's claim: *Plaintiff's counsel asked Hartford to delay its investigation.* The notes contain an entry on December 7, 2000, stating: "Rec. call from Michael Rajt regarding loss. He advised me that the documentation and substance of loss was going to change and that I should put my review on hold until the accountant completes his review. He said to wait until I received further documentation before I start my analysis." (Record at 982). Not only do the notes provide no evidence that any inactivity was due to bad faith, but as the magistrate judge found, the notes in fact support the opposite conclusion that *Plaintiff itself wanted delay*. (Record at 1013).

Second, the "claim notes" reveal that Hartford also had a reasonable basis for delaying its investigation of Plaintiff's claim on the basis that Plaintiff's claim was a moving target. Plaintiff's counsel acknowledged that "[s]everal different amounts have been claimed as the covered loss depending upon the person preparing the letter or the sworn proof of loss at any given time." (Record at 579). In fact, Plaintiff's counsel further admitted that "[c]ertainly, there is some room to argue confusion with respect to the amount of the claim." (*Id.*). Plaintiff can cite no case or legal principle to support the notion that Hartford acted in "bad faith" by indulging Plaintiff's desire to submit a series of modified and inconsistent claims over a period of two-and-a-half years.

Plaintiff complains that the magistrate judge, in reviewing the "claim notes," improperly determined "the most reasonable inference to be drawn" from the notes. Plaintiff's Br. at 32 (citing *Honore v. Douglas*, 833 F.2d 565, 567 (5th Cir. 1987). It is true that where "the evidence before the court, viewed as a whole, *could lead to different factual findings and conclusions*," the district court cannot pick the "most" reasonable inference. *Honore*, 833 F.2d at 567 (emphasis added). This, however, is not such a case. For there to be more than one reasonable inference, Plaintiff's inference from the evidence would have to be reasonable. *Southway Theatres, inc. v. Georgia Theatre Co.*, 672 F.2d 485, 493 (5th Cir. 1982) (noting that a non-movant is only entitled to the benefit of reasonable inferences, not unreasonable ones).

Plaintiff's proposed inferences from the claim notes are not reasonable. The summary judgment evidence, even when interpreted in the light most favorable to Plaintiff, shows that Hartford's delay, if any, in investigating Plaintiff's coverage claim was both reasonable and no source of injury to Plaintiff. Accordingly, the district court correctly granted summary judgment in Hartford's favor on Plaintiff's bad faith, DTPA, Article 21.21, and Article 21.55 causes of action.

## CONCLUSION AND PRAYER

The district court correctly adopted the magistrate judge's recommendations and granted summary judgment in Hartford's favor. Hartford respectfully requests that this Court affirm the district court's judgment.

Respectfully submitted,

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## CERTIFICATE OF SERVICE

I hereby certify that a true and correct printed and electronic copy of this Brief of Appellees has been served on the following counsel of record for Appellant Administrative Services of North America, Inc., on this 19th day of June, 2007:

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Dated: _____