

IN THE SUPREME COURT OF TEXAS

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No. 96-0387
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ASSOCIATED INDEMNITY CORPORATION AND FIREMAN'S FUND INSURANCE
COMPANY, PETITIONERS

v.

CAT CONTRACTING, INC., GTS EQUIPMENT, INC., MICHIGAN SEWER
CONSTRUCTION CO., CONSTRUCTION EQUIPMENT CO., MARIO DIPONIO,
BENJAMIN DIPONIO, PHYLLIS DIPONIO, GUILIO CATALLO, AND ROSEMARY
CATALLO, RESPONDENTS

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ON APPLICATION FOR WRIT OF ERROR TO THE
COURT OF APPEALS FOR THE THIRTEENTH DISTRICT OF TEXAS
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Argued on October 8, 1997

JUSTICE OWEN, joined by JUSTICE HECHT, concurring and dissenting.

I join in the Court's opinion except for part III-B.

I agree with the standard for lack of good faith adopted by the Court. However, no court in the country has applied that standard to facts such as those present in this case and found bad faith. The carefully balanced articulation of "good faith" by the Court is meaningless if it is going to be misapplied, as the Court has done. I would hold that there is no evidence of improper motive or wilful ignorance of the facts.

The Court recognized that “good faith” under the parties’ indemnity agreement is not the equivalent of negligence:

“[G]ood faith” in the surety agreement before us refers to conduct which is honest in fact, free of improper motive or wilful ignorance of the facts at hand. It does not require proof of a “reasonable” investigation by the surety. Stating the proposition conversely for purposes of our evidentiary review for this particular case, “bad faith” means more than merely negligent or unreasonable conduct; it requires proof of an improper motive or wilful ignorance of the facts.

___ S.W.2d at ___. Nevertheless, the Court relies on evidence of, at most, mere negligence by Associated.

The Court relies on three pieces of evidence. First, the Court notes that Steve Mollenhauer, the Associated adjuster assigned to this claim, did not retain an independent engineering firm to investigate the cause of the leaks. However, Mollenhauer testified without dispute that, during their initial meeting, CAT’s representatives told him that *they* planned to hire an engineering firm to substantiate their claims of design error. After that meeting, Mollenhauer sent a follow-up letter to Guilio Catallo, dated September 17, 1990, stating:

Dear Mr. Catallo:

You indicated during our meeting on 9/11/90 that you intend to seek arbitration on the issues of whether the leakage problem is caused by design or workmanship problems. To substantiate your position, you were planning on retaining both an attorney experienced in construction matters and an engineering expert.

Since the deadline for the Surety’s response to the Cameron County Fresh Water Supply District is September 26, 1990, we will need a statement of your position with respect to the default by Friday, September 21, 1990 at the latest.

According to Mollenhauer's contemporaneous progress notes, Catallo called him one week later and told him that CAT was meeting with an engineering expert "possibly as early as this afternoon." However, CAT did not present any engineering report to Associated until six months later, at the parties' April 5, 1991 meeting in Houston. At that meeting, Maury Stiver, the engineer retained by CAT, presented his conclusions concerning the inadequacy of the pipeline bedding and pipe selection. It is undisputed, however, that Stiver had not visited the worksite and thus had made no physical investigation of the construction, the repair work, or the pipeline. Associated thus decided to rely on the opinion of Mollenhauer, who himself was an engineer, and Arthur Mercer, the engineer who excavated and repaired the leaks, that the leaks were caused by poor workmanship.

Under these circumstances, Mollenhauer's failure to retain an independent engineering firm cannot be evidence of dishonest motive or wilful disregard of the facts. To the contrary, it is undisputed that CAT agreed to develop this evidence, that Associated gave it an opportunity to do so, and that when CAT finally did retain an expert, Associated listened to his conclusions. Surely, Associated's decision not to accept the conclusions of an expert who had not even examined the pipeline is not evidence of dishonest motive or wilful disregard of the facts. It could be argued that Associated should have itself retained an expert to inspect the pipeline, but this is, at most, evidence of negligence. It does not approach the level of culpability required under the bad faith standard adopted by the Court.

Second, the Court notes that Mercer was a competitor of CAT, somehow suggesting that for this reason it was dishonest or improper for Associated to rely on his opinion. As noted, however, Mercer is the engineer who excavated and repaired the pipeline, and thus he was in the best position to opine as to the cause, that Mercer did have some competitive-based bias against CAT, this at most injects an element of negligence into the investigation, not dishonesty or wilful disregard of the facts. There is absolutely no evidence that Associated colluded with Mercer regarding the substance of his opinion.

Finally, the Court notes that a representative of CAT testified that during the April 5 meeting,

one of Surety's representatives stated that there was a "good case" that Owner's engineers were at fault. The Court does not explain how this isolated statement equates to evidence of bad faith. It is unclear from this testimony as to what point in the meeting Associated's representative made this statement or the context in which it was made. This testimony, standing alone, cannot constitute evidence that Associated's subsequent settlement was made with a dishonest or improper motive.

Under the Court's application of the good faith standard, any evidence that a surety did not conduct the fullest investigation possible equates to evidence of bad faith. Not only does this contradict the "dishonest in fact" test that the Court purports to adopt, it appears to be even more relaxed than the "negligence" standard that the court of appeals adopted. Moreover, this approach will wreak havoc with the tripartite suretyship relationship. The Court recognizes that the standard indemnity provisions at issue here, under which the surety is authorized to settle claims in good faith, are "critical in enabling sureties to perform efficiently." ___ S.W.2d at ___ & n.2. Under the Court's approach, however, a fact issue on good faith will exist for virtually every claim settled by sureties. This will have an obvious and profound impact on sureties' ability and willingness to settle such claims, resulting in needless litigation costs and ultimately damaging the interests of the underlying public-works projects the sureties are retained to protect.

* * *

For the foregoing reasons, I dissent from that portion of the Court's judgment affirming the take-nothing judgment against Associated on its indemnity claim. I would render judgment for Associated on its indemnity claim against CAT. I concur in that portion of the Court's judgment against CAT on its claims for affirmative relief.

Priscilla R. Owen
Justice

Opinion Delivered: February 13, 1998