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RATEPAYERS APPEAL OF THE DECISION BY WINDERMERE OAKS WATER SUPPLY CORPORATION TO CHANGE WATER AND SEWER RATES	§ § § § §	**BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS**

WINDERMERE OAKS WATER SUPPLY CORPORATION'S RESPONSE TO COMMISSION STAFF'S SECOND REQUEST FOR INFORMATION

Windermere Oaks Water Supply Corporation (WOWSC) files this Response to the Second Request for Information (RFI) filed by the Staff of the Public Utility Commission of Texas (Staff). The discovery request was received by WOWSC on January 19, 2021; therefore these responses are timely filed. Pursuant to 16 Tex. Admin. Code (TAC) § 22.144(c)(2)(F), these responses may be treated as if they were filed under oath.

If a responsive document exceeds 99 pages, the response will indicate that the attachment is voluminous, and pursuant to 16 TAC § 22.144(h)(2), the document will be provided electronically on the CD attached to this filing and made available for inspection at the offices of WOWSC's attorneys, Lloyd Gosselink Rochelle and Townsend, P.C., located at 816 Congress Avenue, Suite 1900, Austin, Texas 78701. Please call Hanna Campbell at 512-322-5871 during regular business hours, to make an appointment to review the documents.

Pursuant to 16 TAC § 22.144(h)(4), an index of the voluminous documents is provided, below.

VOLUMINOUS INDEX

1. Voluminous Attachments to WOWSC's Response to Staff's Second RFI

No.	Date	Title or Description	Preparer or Sponsor	Page Range	No. of Pages
2-5	February 8, 2021	Voluminous Attachment Staff 2-5—PIA Requests	Preparer: Joe Giminez Sponsor: Joe Giminez	1-113	113
2-7(i)	February 8, 2021	Voluminous Attachment Staff 2-7(i)—2017 Insurance Policy	Preparer: Joe Giminez Sponsor: Joe Giminez	114-268	155

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Respectfully submitted,

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ATTORNEYS FOR WINDERMERE OAKS WATER SUPPLY CORPORATION

CERTIFICATE OF SERVICE

I certify that, unless otherwise ordered by the presiding officer, notice of the filing of this document was provided to all parties of record via electronic mail on February 8, 2021, in accordance with the Order Suspending Rules, issued in Project No. 50664.

JAMIE L. MAULDIN

SOAH DOCKET NO. 473-20-4071.WS
PUC DOCKET NO. 50788

WOWSC'S RESPONSE TO STAFF'S SECOND RFI

Staff 2-1 Reference the $169,000 in legal expenses included in the revenue requirement used to set the rates that are the subject of this appeal. For each legal proceeding in which a portion of these legal expenses were incurred, please provide:

i. the cause number and case style;

ii. the date the suit was filed;

iii. the names of all parties to the suit;

iv. a description of the case, including a brief summary of the facts giving rise to the legal issues in the case;

v. the current procedural posture of the case;

vi. the amount of the $169,000 that was incurred in connection with the proceeding; and

vii. the amount of the $169,000 that was incurred to defend each past or current Windermere Board member who was sued individually, specifying the amount incurred by each Board member.

RESPONSE:

i. (1) *TOMA Integrity v. WOWSC,* Cause No. 47531, in the 33rd District Court, Burnet County, Texas (hereinafter, "TOMA Lawsuit");

(2) *Double F Hanger Operations, LLC, Lawrence R. Ffrench, Jr., Patricia Flunker, and Mark A. McDonald v. Friendship Homes & Hangars, LLC, and Burnet County Commissioners Court*, Cause No. 48292, in the 33rd District Court, Burnet County, Texas (hereinafter, "Double F Hanger Lawsuit").

(3) *Windermere Oaks Water Supply Corporation v. The Honorable Ken Paxton, Attorney General of Texas*, Cause No. D-1-GN-19-006219, in the 201st District Court, Travis County, Texas ("Paxton Suit").

ii. TOMA Lawsuit: March 30, 2018

Double F Hanger Lawsuit: July 9, 2018

Paxton Lawsuit: September 16, 2019

iii. TOMA Lawsuit: Plaintiff TOMA Integrity, Inc.; Defendant Windermere Oaks Water Supply Corporation.

Double F Hanger Lawsuit: Original Plaintiffs Double F Hanger Operations, LLC, Lawrence R. Ffrench, Patricia Flunker, Mark A. McDonald; Intervenor Plaintiffs Rene Ffrench, John Richard Dial, and Stuart Bruce Sorgen; Original Defendants Friendship Homes & Hangars, LLC, Burnet County commissioners Court (The Honorable James Oakley, Burnet County Judge; The Honorable Jim Luther, Jr., Commissioner Precinct One; The Honorable Russel Graeter, Commissioner Precinct Two; The Honorable Billy Wall,

Commissioner Precinct Three; The Honorable Joe Don Dockery, Commissioner Precinct Four); Added Defendants Windermere Oaks Water Supply Corporation, and its Directors William Earnest, Thomas Michael Madden, Dana Martin, Robert Mebane, Patrick Mulligan, Joe Gimenez, David Bertino, Mike Nelson, Dorothy Taylor, and Norman Morse.

Paxton Lawsuit: Plaintiff the Windermere Oaks Water Supply Corporation; Defendant the Honorable Ken Paxton, Attorney General of the State of Texas

iv. TOMA Lawsuit: TOMA Integrity Inc. (TOMA) -whose board of directors consisted of Danny Flunker, John Richard Dial, Stuart Bruce Sorgen, and Lawrence Ffrench-sued Windermere Oaks Water Supply Corporation (WOWSC) for alleged violations of the Texas Open Meeting Act involving the sale of real estate by WOWSC (First Lawsuit). The plaintiffs lost this suit and were denied review by the Texas Supreme Court.

Double F Hanger Lawsuit: A second lawsuit involving the same sale of real estate by the WOWSC was filed July 9, 2018 by Double F Hanger Operations, LLC, Lawrence Ffrench, Patricia (Patti) Flunker, and Mark McDonald (Second Lawsuit). WOWSC and each of its individual directors were added as a defendant to the Second Lawsuit on or before May 14, 2019, and John Richard Dial, Stuart Bruce Sorgen and Lawrence Ffrench (Intervenor Plaintiffs) filed an Original Petition in Intervention in the Second Lawsuit seeking similar relief regarding the same transaction from the WOWSC. Later, the original plaintiffs filed a motion to remove themselves from the suit and the Intervenor Plaintiffs have effectively taken over as the plaintiff in this proceeding. On August 24, 2020, the Intervenor Plaintiffs filed their Third Amended Original Petition. Danny Flunker, as well as Mr. Dial, Mr. Sorgen, and Mr. Ffrench are all registered Directors of TOMA, connecting them to the First Lawsuit.

Paxton Lawsuit: On May 28, 2019, pursuant to the Public Information Act, Danny Flunker sent a Public Information Act (PIA) request to WOWSC for "copies of all legal invoices from 3/7/18 to today's date." On June 12, 2019 WOWSC filed its Original Petition for Declaratory Relief with the Attorney General of Texas (AG Lawsuit) to prevent the disclosure of the information - privileged information - that Danny Flunker sought in the PIA request. The AG agreed that WOWSC was entitled to most all of the relief sought in WOWSC's Petition for Declaratory Relief, and agreed that a majority of the time entries on the legal invoices was protected due to attorney-client and work product privilege. Danny Flunker intervened to oppose the AG's proposed settlement. There is currently a settlement agreement pending which would resolve this PIA appeal, but it has not been approved and the documents are still at issue because of Mr. Flunker's opposition.

v. TOMA Lawsuit: Final, denied review by Texas Supreme Court.

Double F Hanger Lawsuit: Action pending before trial court. Discovery is ongoing with deadlines on dispositive motions approaching but likely to be extended due to complications related to the Covid-19 pandemic.

Paxton Lawsuit: Action is currently pending before trial court. Requestor has intervened and filed a motion for discovery. WOWSC and Office of the Attorney General have agreed

to a settlement agreement. Previously, hearing was set on the motion for discovery but passed by Intervenor. Nothing else set at this time.

vi. TOMA Lawsuit: $41,654.12

Double F Hanger Lawsuit: $62,481.18

Paxton Lawsuit: $15,681.15

These amounts are estimates only. The time entries on the invoices from Enoch Kever and Lloyd Gosselink do not distinguish between different matters if the work was performed by the same person on the same day. Accordingly, it is not possible to discern specific amounts for each lawsuit and these are estimated amounts.

vii. TOMA Lawsuit: Individual board members were not named in this lawsuit.

Double F Hanger Lawsuit: These are estimates only.

Paxton Lawsuit: Individual board members were not named in this lawsuit.

Prepared by: Joe Gimenez; Mike Nelson
Sponsored by: Joe Gimenez; Mike Nelson

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PUC DOCKET NO. 50788

WOWSC'S RESPONSE TO STAFF'S SECOND RFI

Staff 2-2 For any legal proceeding listed in response to Staff 2-1 in which a final decision has been rendered, please indicate which party prevailed and explain whether the party that has not prevailed has filed an appeal of the decision.

RESPONSE:

- TOMA Lawsuit: WOWSC is the prevailing party. The Supreme Court of Texas denied TOMA's petition for review.
- Double F Hanger Lawsuit: Final decision has not been reached.
- Paxton Lawsuit: Final decision has not been reached. WOWSC voted to release the invoices at issue in the Paxton lawsuit, so this case is in the process of being withdrawn.

Prepared by: Joe Gimenez
Sponsored by: Joe Gimenez

SOAH DOCKET NO. 473-20-4071.WS
PUC DOCKET NO. 50788

WOWSC'S RESPONSE TO STAFF'S SECOND RFI

Staff 2-3 Reference the $169,000 in legal expenses included in the revenue requirement used to set the rates that are the subject of this appeal. Please identify what portion of this amount, if any, is for legal expenses incurred to respond to Public Information Act Requests.

RESPONSE:

Approximately $44,682. Lloyd Gosselink Rochelle & Townsend, P.C. did not distinguish between different matters when invoicing the WOWSC if the work was performed by the same person on the same day. While some entries were solely for work related to the PIA requests, others included work on separate matters, including assistance with member challenges to board actions on interpretations of bylaws and the articles of incorporation, a member removal petition, and compliance with Open Meetings Act law, including a new law of the 2019 Texas Legislature relating to member comments. Therefore, it is not possible to discern the exact time spent on which activity. Accordingly, this figure is an estimate as the billing practice does not allow for a specific calculation.

Prepared by: Joe Gimenez; Mike Nelson
Sponsored by: Joe Gimenez; Mike Nelson

SOAH DOCKET NO. 473-20-4071.WS
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WOWSC'S RESPONSE TO STAFF'S SECOND RFI

Staff 2-4 Please provide the total number of Public Information Act Requests Windermere responded to in 2017, 2018, 2019, and 2020.

RESPONSE:

The number of PIA Requests received by Windermere responded to for the years 2017-2020 are listed below:

- 2017: 2
- 2018: 3
- 2019: 46
- 2020: 40

Prepared by: Joe Gimenez
Sponsored by: Joe Gimenez

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PUC DOCKET NO. 50788

WOWSC'S RESPONSE TO STAFF'S SECOND RFI

Staff 2-5 For each Public Information Act Request for which legal counsel was sought, please provide a description of the request, along with a brief explanation of why Windermere sought counsel regarding its response to the request.

RESPONSE:

WOWSC has provided copies of each applicable PIA request, along with comments explaining the reason for seeking legal counsel, in ***voluminous*** Attachment Staff 2-5, being provided in electronic file-format on CD.

The WOWSC is a non-profit corporation and the Board of Directors are all volunteers. The volunteer board members are not required by law or the WOWSC's bylaws to have background and training on the Public Information Act. Prior to 2019, WOWSC had traditionally received only a few PIA requests per year (approximately 3-4) and these were just handled by various board members with some assistance from legal counsel. The WOWSC did not have a Public Information Officer at this time as it was not needed to handle the relatively small number of requests. However, in 2019, the WOWSC saw an exponential increase in PIA requests, going from an average of 3-4 per year up to a total of 46 requests in 2019. It is important to emphasize that the vast majority of these requests were from people involved in the TOMA lawsuit, described above.

Notably, on March 19, 2019, the WOWSC received its first PIA request from Rene Ffrench. Mr. French was a plaintiff in the TOMA lawsuit, which at that time was in the appeals process at Mr. Ffrench's and the other plaintiff's request. Not only was Mr. Ffrench involved in the TOMA litigation, but also he and the other requestors behind a majority of the 2019 requests were involved in a separate litigation pertaining to the same land sale under dispute in the TOMA lawsuit, which the WOWSC would ultimately be brought into in May 2019 (the Double F Hangar lawsuit). The WOWSC was therefore concerned that many of these requests were attempts to get around the formal discovery process in that case. Furthermore, the requestors had clearly demonstrated a penchant for litigation, and the WOWSC was afraid the requestors would aggressively pursue any civil and criminal penalties available if the WOWSC did not respond in the precise time and manner required by the Public Information Act. Accordingly, the WOWSC frequently sought the help of legal counsel to best ensure compliance with the requirements of each request and the hope of avoiding further lawsuits and legal penalties.

Prepared by: Joe Gimenez
Sponsored by: Joe Gimenez

SOAH DOCKET NO. 473-20-4071.WS
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WOWSC'S RESPONSE TO STAFF'S SECOND RFI

Staff 2-6 Please provide the total amount of legal expenses paid by Windermere in 2017, 2018, 2019, and 2020.

RESPONSE:

The total amount of legal expenses incurred by WOWSC from all law firms from 2017–2020 are included below:

- 2017: $2,247.21
- 2018: $37,981.32
- 2019: $166,583.46
- 2020: $350,503.86

Will be supplemented.

Prepared by: Joe Gimenez; Mike Nelson
Sponsored by: Joe Gimenez; Mike Nelson

SOAH DOCKET NO. 473-20-4071.WS
PUC DOCKET NO. 50788

WOWSC'S RESPONSE TO STAFF'S SECOND RFI

Staff 2-7 Where insurance claims for legal expenses were filed, please provide:

i. a copy of the insurance policy;

ii. the clause under which coverage was claimed;

iii. the amount of coverage requested;

iv. the amount of coverage provided, and

v. for each instance where a claim was not fully covered, please provide documentation explaining the reason for partial coverage or denial of coverage.

RESPONSE:

i. WOWSC has provided copies of all insurance policies in ***voluminous*** Attachment Staff 2-7(i), being provided in electronic file-format on CD.

ii. Coverage A. Insuring Agreement—Liability for Monetary Damages; Coverage B. Insuring Agreement—Defense Expenses for Injunctive Relief. Please see Attachment Staff 2-7(ii).

iii. Requesting full coverage, though there is not a specific amount yet as the claim is still being litigated.

iv. None.

v. WOWSC is currently challenging its denial of insurance coverage. Attachment Staff 2-7(ii) outlines each of the insurer's claimed exclusions, along with an explanation as to why these do not apply.

Prepared by: Joe Gimenez
Sponsored by: Joe Gimenez

shidlofsky law firm

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7200 North Mopac Expressway, Suite 430
Austin, Texas 78731
t. 512.685.1400 f. 866.232.8412

Blake H. Crawford
blake@shidlofskylaw.com

May 18, 2020

VIA E-MAIL: pflynn@networkadjusters.com
ALLIED WORLD SPECIALTY INSURANCE COMPANY
c/o Mr. Pete Flynn
General Adjuster
NETWORK ADJUSTERS, INC./APR CLAIMS
8055 Tufts Avenue, Suite 600
Denver, Colorado 80237

Re:	Named Insured:	Windermere Oaks Water Supply Corporation
	Matter:	*Rene Ffrench, et al. v. Friendship Homes & Hangars, LLC, et al.*; Cause No. 48292 in the 33rd Judicial District Court of Burnet County, Texas (the "Underlying Lawsuit")
	Insurer:	Allied World Specialty Insurance Company ("Allied World")
	Policy Number:	5105-0560-03
	Policy Period:	March 17, 2016 to March 17, 2017
	Your Claim No.:	2017001776

Dear Mr. Flynn:

This firm has been retained to represent Windermere Oaks Water Supply Corporation (the "WSC") and its current and former directors who are named as defendants in the above-referenced Underlying Lawsuit. Those current and former directors are Dana Martin, William Earnest, Thomas Michael Madden, Robert Mebane, Patrick Mulligan, Joe Gimenez, David Bertino, Mike Nelson, Dorothy Taylor, and Norman Morse (the "Director Defendants").

By letter dated December 19, 2019, Allied World denied coverage for the WSC and the Director Defendants under policy number 5105-0560-03 with respect to the Second Amended Original Complaint filed in the Underlying Lawsuit. After a review of the analysis set forth in that letter, the WSC and the Director Defendants believe that Allied World has reached an erroneous position as it relates to their defense in the Underlying Lawsuit. Please consider the following:

FACTUAL BACKGROUND

There are numerous factual allegations in the Second Amended Original Petition. These allegations give rise to potential covered liability, thereby implicating Allied World's complete duty to defend the insureds. We have highlighted herein those pertinent to the coverage provided by the Allied World policy. Please also note that WSC and the Director Defendants dispute the allegations in the pleading. Nevertheless, these allegations govern Allied World's defense

obligations. No statement herein should be deemed as an agreement with or in any way conceding any allegation made in the pleading.

The Intervenor Plaintiffs are Rene Ffrench, John Richard Dial, and Stuart Bruce Sorgen ("Intervenors"), who, according to their pleading, are members/customers and owners of the assets and revenues of the water supply and sewer service cooperative (the "Cooperative") operated through the instrumentality known as the WSC. The named defendants in the Second Amended Original Petition filed in the Underlying Lawsuit are the WSC, the Director Defendants, and Friendship Homes & Hangars, LLC ("FHH").

Intervenors assert that the individual defendants are sued in their official capacities as current or former Directors and/or Officers of the WSC, and also in their individual capacities. In the preliminary portion of the pleading, Intervenors assert that the business judgment rule does not affect their recovery,

> because (i) the acts and omissions alleged herein resulted from ultra vires acts, fraud and/or self-dealing, were grossly negligent, constituted an abdication of their responsibilities or otherwise were not within the exercise of the individual Defendants' discretion and judgment, therefore the rule is inapplicable; (ii) there is no presumption of lawfulness in connection with the individual Defendants' acts and omissions alleged herein; (iii) the acts and omissions alleged herein involve assets or property (including causes of action) that belong to the Owners, and not to some corporate entity; and (iv) the acts and omissions alleged herein were not within the honest exercise of the individual Defendants' business judgment and discretion.

In 2013, the WSC Board voted to upgrade the WSC's wastewater treatment facilities and relocate them from an approximately 10-acre tract within the Spicewood Airport community (hereinafter, the "Airport Tract"). The Directors agreed unanimously that relocating the facilities to an area east of Exeter Road would free the valuable Airport Tract for sale, which was considered the "highest and best use" of the Tract. The sale of the 10-acre Airport Tract allegedly was identified as one of the key components for funding the upgraded wastewater treatment plant improvements and other Cooperative needs.

The Board allegedly committed to the owners that the Airport Tract would be sold for the best possible price, and the proceeds would be used to defray the cost of the new facilities and for other Cooperative purposes. Intervenors assert that, following the August 2013 meeting, Directors Mulligan, Earnest, and Madden claimed to have gathered deeds and other records in preparation to engage a real estate professional to market the Airport Tract. At the Board's February 18, 2014 meeting, Mulligan allegedly was directed to obtain a survey and appraisal of the land to be sold. Intervenors assert that these Directors did none of these things.

According to Intervenors, the Board never listed, advertised, or marketed the Airport Tract. While some Directors have claimed that they allegedly spoke with unidentified "real estate

people," Intervenors assert that the Directors never actually marketed the Airport Tract for sale to the highest bidder. Around this same time, Martin, a local real estate agent and an owner of Windermere Airport, LLC ("Windermere Airport"), purportedly put together a proposal for the purchase by Windermere Airport of a 0.558-acre tract within the Airport Tract from the Windermere Oaks Property Owners' Association ("POA") at "fair market value."

POA members were using a 30,000 square foot portion of the Airport Tract for storage of boats and other items (the "Storage Tract"). By e-mail dated April 3, 2014, Taylor notified Mebane of the Board's vote to market the Airport Tract as a single parcel and requested that the POA items be removed from the Storage Tract. According to Intervenors, Taylor expressly acknowledged the Board's "fiduciary responsibility to our members," which prohibited the Board from taking any action that would "compromise our ability to obtain the 'best' offer from any potential buyer."

Around this same time, Martin (who was not yet on the WSC Board) became involved in the POA's efforts to acquire the Storage Tract from the WSC. In this process, Martin obtained a copy of the WSC's 2006 appraisal of a 7-acre vacant portion of the Airport Tract, including the Storage Tract. The appraisal concluded that, as of December 1, 2006, the vacant 7-acre portion was worth $350,000, or $1.15 per square foot, for light industrial development (*i.e.*, as a hangar) specifically related to the airport. In late 2014, the TCEQ approved the WSC's Closure Plan for the old wastewater treatment plant. This, according to Intervenors should have cleared the way for prompt and aggressive marketing and sale of the Airport Tract. The Directors, however, allegedly never followed through with any listing or other marketing.

Martin was elected to the WSC's Board in 2015. Shortly thereafter, she allegedly took actions associated with a portion of land known as Tract G, a Cooperative-owned hangar lot across from the Airport Tract, for $95,000, which equaled $12.75 per square foot. Intervenors allege that there is no record the Board ever voted on, or even considered, any transaction involving Tract G.

Thereafter, Martin allegedly was again involved with efforts by the POA to purchase the Storage Tract. The POA's proposed price was around $20,000 - $25,000, or in the range of $0.66 - $0.83 per square foot. The minutes of the Board's July 16, 2015 meeting reflect that the Directors (including Martin, Mebane, Earnest, Madden and Mulligan) discussed the POA's offer in executive session but took no action. Intervenors assert that the Board rejected the POA's offer.

At some point thereafter, Martin presented the other Directors with a "Purported Appraisal" of the Airport Tract. This Purported Appraisal was never considered by the Board, as it did not reflect the fair market value of the Airport Tract. Moreover, there was no indication that the Board ever professionally listed or marketed the Airport Tract, or that the Board ever fielded any offers or negotiated for sale of the Airport Tract.

In March 2016, Martin allegedly began efforts to purchase the Airport Tract. Intervenors allege that she was involved as both seller and purchaser. Martin apparently indicated that Mebane (then Board President) decided by himself that the Airport Tract should not be sold as a single parcel, as the Board had planned for years. Rather, Martin allegedly claimed that Mebane

determined that the Board should dispose of the "most valuable and desirable 3.8 acres of the Airport Tract with all of the Airport Tract's frontage along the Piper Lane taxiway to a sitting WSC Director for a fraction of its market value." Martin claimed that the March 2016 transaction was "negotiated" and that she made a "good faith" offer to purchase, which was countered by other Directors. Intervenors assert that the Board's records are devoid of any such negotiations.

According to Intervenors, the "disinterested Directors" were the same that had acknowledged a duty to market the Airport Tract as a whole to obtain the best possible offer and were aware that the Board had conveyed a comparable property for $12.75 per square foot. None of the Directors allegedly disclosed to the Owners prior to the Board's December 19, 2015 meeting that they intended to authorize the piecemeal transfer of the Airport Tract and all of the taxiway frontage for a fraction of the comparable property. The proposed transaction was never mentioned as a discussion or action item on any posted meeting agenda for any Board meeting. Instead, the Board allegedly raised the topic out of the blue at its regular meeting on December 19, 2015, and, after a 5-minute executive session, Mebane, Madden and Mulligan unanimously voted to accept an offer from Martin on behalf of FHH to carve off the frontage and separate the remainder of the Airport Tract from all taxiway access for a "net price" of $200,000, or $1.19 per square foot. Intervenors allege that there was no "appropriate resolution" to approve this sale. Moreover, the Board did not allegedly fulfill the special conditions required to approve an interested Director transaction.

Prior to closing, Martin subdivided the land she intended to purchase into two platted hangar lots. Mebane, as WSC President, signed Martin's subdivision plat on March 3, 2016. The plat was approved and recorded on March 8, 2016. The plat Martin prepared and processed, and that Mebane signed on behalf of the WSC, allegedly failed to reserve a taxiway for the remainder of the Airport Tract. Intervenors allege that there are no posted records reflecting a resolution to adopt the land transfer to Martin.

On or about March 13, 2016, Mebane and Madden allegedly executed and delivered a document purporting to be a resolution in which they "certified," as President and Secretary of the WSC, respectively, that the resolution stated therein was "an accurate reproduction of the one made" by the Board and was "legally adopted on the date of the [February 22, 2016] meeting of the Board of Directors, which was called and held in accordance with the law and the bylaws of the corporation, at which a quorum was present." The resolution described the property to be conveyed as two platted hangar lots by reference to the recorded plat, not as unplatted acreage. However, Intervenors allege that no resolution was actually adopted at the February 22, 2016 meeting or any other time. Intervenors concede in their pleading that the two deeds conveyed the platted hangar lots to FHH, not Martin individually. Thus, it is unknown whether and to what extent Martin has invested her own resources in the transaction.

Moreover, Intervenors allege that "some or all the proceeds from Martin's acquisition of the hanger lots were used to make a balloon payment on the WSC's existing debt." This was due, in part to the WSC might not being able to make its debt service obligation without the proceeds from 2016 transaction. Intervenors dispute this, but assert that "[i]f that is true, then the Director

Defendants who created that situation have far more to answer for that the 2016 fire sale. They had no authority to incur debt on behalf of the organization without adequate provision for repayment in accordance with the loan agreement." Intervenors assert that the Directors had a duty to monitor the Cooperative's financial performance and to make adjustments in the debt service plan as needed. Intervenors assert that the Directors cannot rationalize the sale of valuable Cooperative assets to mitigate the consequences of their other purported misconduct.

Intervenors continue:

> Had the WSC's fiduciaries followed through on the plan to market the Airport Tract as a whole and sell it for the highest possible price, the WSC could have retired all of its outstanding debt in March 2016 and had a tidy sum left over to pay additional facilities costs, to acquire and/or upgrade equipment required to provide the Cooperative services in compliance with applicable laws and regulations, to establish or increase the reserve fund set aside for future system upgrades and improvements and to meet any number of other Cooperative needs.

Instead, according to Intervenors, the Owners collectively sustained an immediate loss of $500,000 in cash when the Board sold the portion of the Airport Tract with the taxiway frontage. Moreover, the remainder of the Airport Tract "was rendered unmarketable and its value instantly diminished by $640,000" when it was separated from taxiway access.

Martin allegedly later replatted the hanger lots again to create a third hangar lot, which was conveyed to Johann and Michael Mair. The Mair property is where Martin's "Amended and Superseding Agreement" apparently proposes to locate an access easement and setback to provide a taxiway to the remainder tract.

During this same time, the WSC still allegedly has debt outstanding and incurred additional debt to pay expenses that could and should have been covered by the proceeds from the sale of the Airport Tract. The Board allegedly has struggled with strategies to restructure the debt. Intervenors assert that "the Directors do not seem to appreciate that the WSC is not permitted to have outstanding debt just because it can. The Board has postponed needed repairs and the acquisition of a generator and other equipment needed to provide the Cooperative services and to remain in compliance with applicable regulations." At the same time, the Board allegedly has raised rates, service fees, and membership fees. Moreover, the Board also allegedly has allowed the Cooperative to become financially dependent on the "extremely questionable practice of collecting standby fees from nonpatrons."

The Board's composition changed in 2018. At that time, the Board allegedly investigated the March 2016 transaction, engaging a professional forensic appraiser to analyze the financial impact of the sale. The accountant's report allegedly confirmed that the Owners sustained an immediate loss of more than $1,000,000.

Intervenors allege that the March 2016 fire sale was unauthorized, improper and unfair to the Owners and involved breaches of fiduciary duty and other misconduct by Directors. The newly constituted Board allegedly determined that its fiduciary duties required prompt efforts to recover the misappropriated property or to otherwise make the Owners whole by pursuing "all available avenues of relief." Intervenors assert that "[b]y all appearances, the Directors were doing exactly what their duties required of them. Those Directors (including Bertino, Morse and Nelson) allegedly "engaged independent qualified professionals to analyze the facts and to advise them," and upon receiving advice, the Directors prepared to move forward against Martin, FHH and others.

Intervenors assert that the Directors abruptly ceased all efforts to pursue recovery for the Owners' $1,000,000 loss and all other relief to which the Owners are entitled. According to Intervenors, they do not know why this decision was made. Nor is it known why the Directors embraced and defended the "unfaithful fiduciaries who caused the loss to begin with." There was another Director election in 2019. Earnest, who had gone off the Board, was elected to serve as a Director again. Bertino, Morse and Nelson continued on the Board. The WSC's leadership allegedly continued to use Cooperative resources to oppose efforts to restore the Owners' misappropriated property.

Intervenors allege that the Defendants engaged in various *ultra vires* acts in violation of Section 20.002(c) of the Texas Business Organizations Code. This includes the unauthorized conveyance of property; improper use of Cooperative assets; improper disbursement of Cooperative assets to benefit the Directors; and failure to recover loss. Intervenors also allege that the Directors breached their fiduciary duty to the WSC. There is also an allegation of constructive fraud against the Directors. Incorporating by reference all of the factual allegations described above, Intervenors specifically seek "actual damages from the Directors based on the alleged breach of fiduciary duties." Intervenors also seek exemplary damages and attorneys' fees, as permitted by law.

INSURANCE INFORMATION

The December 19, 2019 letter addresses only policy number 5105-0560-03, which was in effect for the policy period from March 17, 2016 to March 17, 2017. As Allied World concedes in its coverage letter, the Second Amended Original Petition includes numerous factual allegations that are asserted for the first time in that particular pleading. These claims relate back to the claims first asserted in January 2017. As Allied World appears to concede, these new claims relate back to the claims first made and timely submitted to Allied World under policy number 5105-0560-03 (effective for the policy period from March 17, 2016 to March 17, 2017) (hereinafter, the "Policy").

The Policy has the Public Officials and Management Liability Coverage Form claims-made coverage form (the "POML Coverage"), which provides coverage for Wrongful Acts, subject to a limit of $1,000,000 for each claim, and coverage for Injunctive Relief, subject to a limit of $5,000 for each action for injunctive relief. The POML Coverage is subject to a $3,000,000 aggregate

limit for all Claims, all Wrongful Acts, and Offenses, and all Actions for Injunctive Relief. The retroactive date is identified as March 17, 2000.

TEXAS DUTY TO DEFEND STANDARD

The duty to defend is a "creature of contract" arising from a liability insurer's agreement to defend its insured against claims or suits seeking potentially covered damages.[1] This defense requirement of a liability policy is "a valuable benefit granted to the insured by the policy."[2] To determine whether there is a duty-to-defend, Texas courts follow the "eight corners" rule, also known as the complaint-allegation rule.[3] Under this rule, an insurer's duty to defend is determined by the factual allegations in the pleadings, considered in light of the provisions in the policy, without regard to the truth or falsity of those allegations.[4] Thus, even if the allegations in the pleadings are groundless, false, or fraudulent, the insurer is obligated to provide the insured with a defense.[5] Importantly, Texas courts construe the allegations in the pleadings liberally in favor of coverage and resolve all doubts regarding the duty to defend in favor of the insured.[6]

"Under Texas law, it is well settled that an insurer owes a duty to defend its insured against any allegations that are covered by the policy."[7] To this extent, an insurer is obligated to provide a complete defense to its insured so long as one allegation in the complaint falls within the policy's coverage."[8] While courts cannot read facts into pleadings or imagine factual scenarios, a court must draw inferences from the factual allegations in the pleading "that may lead to a finding of coverage."[9] Put simply, the Fifth Circuit has offered insurers the following advice: "When in doubt, defend."[10]

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[1] *Loya Ins. Co. v. Avalos*, No. 18-0837, 2020 WL 2089752, at *2 (Tex. May 1, 2020); *Richards v. State Farm Lloyds*, 597 S.W.3d 492, __ (Tex. 2020).

[2] *Richards*, 597 S.W.3d at __ (quoting *Pine Oak Bldrs., Inc. v. Great Am. Lloyds Ins. Co.*, 279 S.W.3d 650, 655 (Tex. 2009)).

[3] *Zurich Am. Ins. Co. v. Nokia, Inc.*, 268 S.W.3d 487, 491 (Tex. 2008).

[4] *GuideOne Elite Ins. Co. v. Fielder Rd. Baptist Church*, 197 S.W.3d 305, 308 (Tex. 2006).

[5] *Avalos*, 2020 WL 2089752, at *2; *Richards*, 597 S.W.3d at __; *Nokia*, 268 S.W.3d at 491.

[6] *King v. Dallas Fire Ins. Co.*, 85 S.W.3d 185, 187 (Tex. 2002); *Union Fire Ins. Co. v. Merchs. Fast Motor Lines, Inc.*, 939 S.W.2d 139, 141 (Tex. 1997); *Gore Design Completions, Ltd. v. Hartford Fire Ins. Co.*, 538 F.3d 365, 369 (5th Cir. 2008) (recognizing that the "eight corners" rule is "very favorable to insureds because doubts are resolved in the insured's favor").

[7] *Downhole Navigator, L.L.C. v Nautilus Ins. Co.*, No. 4:10–0695, 2011 WL 4889125, at *5 (S.D. Tex. May 9, 2011) (citing *Merchs. Fast Motor Lines*, 939 S.W.2d at 141), *aff'd*, 686 F.3d 325 (5th Cir. 2012).

[8] *See Canutillo Indep. Sch. Dist. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 99 F.3d 695, 701 (5th Cir. 1996); *Downhole Navigator, L.L.C.*, 2011 WL 4889125, at *5; *Am. Eagle Ins. Co. v. Nettleton*, 932 S.W.2d 169, 173 (Tex. App.—El Paso 1996, writ denied).

[9] *Gore*, 538 F.3d at 369.

[10] *Id.*

ALLIED WORLD HAS BREACHED ITS DUTY TO DEFEND

The Coverage A. Insuring Agreement of the POML Coverage states, in relevant part:

> **A. COVERAGE A. INSURING AGREEMENT – LIABILITY FOR MONETARY DAMAGES**
>
> 1. We will pay those sums that the insured becomes legally obligated to pay as "damages" arising out of a "claim" for:
>
> **a.** a "wrongful act," or
>
> * * *
>
> We will have the right and duty to defend any "claim" seeking those "damages." However, we will have no duty to defend the insured against any "claim" seeking "damages" for a "wrongful act" . . . .
>
> * * *

A. The Requirements of the Insuring Agreement are Satisfied

In the Second Amended Original Petition, Intervenors seek "damages"[11] arising out of a "claim" for a "wrongful act." In fact, the pleading contains allegations of multiple "wrongful acts." In its coverage letter, Allied World concedes this issue, expressly recognizing that the requirements to trigger the Coverage A Insuring Agreement are met. Moreover, Allied World does not contest that Director Defendants qualify as insureds. Rather, we understand that Allied World is basing its denial on what it identifies as "seven (7) enumerated exclusions that will give preclusive effect to a coverage grant." Under Texas law, Allied World has the burden to establish that an exclusion precludes coverage.[12] Allied World cannot meet this burden based on the allegations in the live pleading.

B. The "Profit, Advantage or Remuneration" Exclusion

First, Allied World relies on the "Profit, Advantage or Remuneration" Exclusion as a basis to deny coverage. That exclusion states:

> This insurance does not apply under either Coverage A or Coverage B to:
>
> * * *

[11] We note that a statute that Intervenors rely on in the pleading, TEX. BUS. ORGS CODE ANN. § 20.002 (Vernon 2019), arguably would allow for the recovery of monetary relief and compensation from directors for *ultra vires* conduct. *See* Elizabeth S. Miller & Robert A. Ragazzo, *The Ultra Vires Doctrine*, 20 TEX. PRAC., BUS. ORGS. § 27:9 (3d ed.). In any case, Intervenors specifically seek damages from the Director Defendants.

[12] *Gilbert Tex. Const., L.P. v. Underwriters at Lloyd's London*, 327 S.W.3d 118, 124 (Tex. 2010); *see* TEX. INS. CODE ANN. § 554.002 (Vernon 2019).

27. Profit, Advantage or Remuneration

> Any "damages," "defense expenses," costs or loss based upon or attributable to the insured gaining any profit, advantage or remuneration to which the insured is not legally entitled.

The term "damages" means "monetary damages." The term "defense expenses" means, in part, "reasonable and necessary fees or expenses incurred by or on behalf of the insured for . . . [l]egal fees charged by the insured's attorney."

The exclusion applies if "the insured" has gained any "profit, advantage or remuneration to which the insured is not legally entitled." Importantly, the exclusion utilizes "the insured" as opposed to "any insured" or "an insured."[13] As a result, the "Separation of Insureds" provision is implicated.[14] That provision states as follows:

8. Separation of Insureds

> Except with respect to the Limits of Insurance as described in **SECTION IV**, and any rights or duties specifically assigned to the first Named Insured, this insurance applies:
>
> **a.** As if each Named Insured were the only Named Insured; and
>
> **b.** Separately to each insured against whom "claim" is made.

As noted, Intervenors have made claims in the Second Amended Original Petition against Martin, Earnest, Madden, Mebane, Mulligan, Gimenez, Bertino, Nelson, Taylor, and Morse. Likewise, Intervenors have included as a defendant the WSC itself. With respect to Earnest, Madden, Mebane, Mulligan, Gimenez, Bertino, Nelson, Taylor, and Morse, there are no allegations in the pleading that those individuals obtained any profit, advantage or remuneration to which they were not legally entitled. Moreover, Intervenors do not make any such allegations against the WSC. In fact, the allegations appear to support the exact ***opposite*** situation. In particular, there are allegations that WSC received a significantly less amount of compensation from the sale of the Airport Tract. Thus, Allied World completely misconstrues and misapplies this exclusion as to these particular individual insureds and the WSC.

The exclusion also does not apply to Martin based on the allegations in the live pleading. In particular, Intervenors concede that the deeds reflecting the sale of the Airport Tract are in the

[13] *Ooida Risk Retention Group, Inc. v. Williams*, 579 F.3d 469, 472–73 (5th Cir. 2009) (separation of insureds provision operates to give "effect to the separate coverage promised each insured by using the term 'the insured' to refer to the particular insured seeking coverage").

[14] *See King v. Dallas Fire Ins. Co.*, 85 S.W.3d 185, 189 (Tex. 2002) (finding that when a policy contains a similar "separation of insureds" clause, the intentional conduct of one insured could not be imputed to another insured for purposes of determining an occurrence).

name of FHH, not Martin. This is confirmed by the copies of the deeds attached to the pleading. Moreover, Intervenors specifically assert that "[w]hether and to what extent Martin has ever invested her own resources in this transaction is not yet known." Thus, the allegations in the pleading do not provide sufficient basis for Allied World to rely upon this exclusion to deny coverage for Martin either, as no allegations exist that she, individually, "gain[ed] any profit, advantage or remuneration to which" she was not legally entitled.

C. Violation of Law and Criminal Acts Exclusions

Allied World has also raised the "Violation of Law" exclusion. That exclusion states:

> This insurance does not apply under either Coverage A or Coverage B to:
>
> * * *
>
> **19. Violation of Law**
>
> "Damages," "defense expenses," costs, or loss arising from an insured's willful violation of any federal, state, or local law, rule, or regulation.

Allied World focuses its discussion of this exclusion on the assertions of violations of the Texas Open Meetings Act (the "TOMA"):

> In this matter, there were violations of the [TOMA] as there was no public notice given to WOWSC members of the upcoming meeting nor items listed on the agenda. Given the allegations, Allied World further reserves its rights to limit coverage to the extent the insured willfully violated any federal, state, or local law, rule or regulation.

The pleading, however, is not based exclusively on purported violations of the TOMA. In fact, there are allegations of "wrongful acts" that have nothing to do with any type of violation of the TOMA or other violation of a federal, state, or local law.

The term "wrongful act" is defined broadly as "any actual or alleged error, act, omission, neglect, misfeasance, nonfeasance, or breach of duty . . . by any insured in the discharge of their duties for the Named Insured, individually or collectively, that results directly but unexpectedly and unintentionally in 'damages' to others." Intervenors assert numerous "wrongful acts" throughout the pleading.

As an example, Intervenors allege that Mulligan, Earnest, and Madden failed to "gather deeds and other records in preparation to engage a real estate professional to market the Airport Tract." Intervenors also assert that Mebane, as Board President, improperly decided on his own that the Airport Tract should not be sold as a single parcel. The WSC allegedly failed to reserve a taxiway for the remainder of the Airport Tract. Intervenors allege that there are no posted records

reflecting a resolution to adopt the land transfer to Martin. Moreover, there are allegations that Mebane, Martin, Madden, Mulligan and Earnest did not adopt the appropriate resolution for sale of the Airport Tract at the Board's February 22, 2016 meeting. There are also claims that Earnest, Gimenez, Nelson, Bertino, Taylor, and Morse improperly chose to seek a mediated resolution of the dispute with Martin and FHH, which was to the detriment of the WSC. Additionally, Intervenors assert that all members of the Board, and thus the WSC itself, improperly incurred debt, which has led to delays in upgrading equipment and caused rates to be raised for the members of the Cooperative.

None of those alleged "wrongful acts" that are within the Second Amended Original Petition constitute a violation of TOMA. Nor do Intervenors even make an allegation that these "wrongful acts" constitute a violation of TOMA. Thus, the live pleading contains multiple allegations against the WSC and the individual Director Defendants of "claims"[15] for "wrongful acts" that do not relate, in any form or fashion to a "willful violation of a federal, state, or local law, rule, or regulation." As a result, this exclusion does not provide a basis for Allied World to deny coverage.

Even with respect to any claims for purported violations of the TOMA, no allegation exists that any of the alleged violations were *willful*. The term "willful" is not defined in the Policy. That term is generally understood to mean a "[v]oluntary and intentional" act that "involves conscious wrong or evil purpose on the part of the actor." The term willful is stronger than voluntary or intentional; it is traditionally the equivalent of malicious or evil. For those claims that involve the TOMA, because there are no such allegations in the pleading that rise to this level, the exclusion is simply not applicable.

Moreover, it is questionable whether this exclusion is even implicated by the allegations involving the TOMA. In particular, the "Criminal Acts" exclusion states:

> "Damages," "defense expenses," costs or loss arising out of or contributed to by any fraudulent, dishonest, criminal or malicious act of the insured (except

[15] In the Policy, the term "Claim" means:

- **a.** written notice, from any party, that it is their intention to hold the insured responsible for "damages" arising out of a "wrongful act" or offense by the insured;
- **b.** a civil proceeding in which "damages" arising out of an offense or "wrongful act" to which this insurance applies are alleged;
- **c.** an arbitration proceeding in which "damages" arising out of an offense or "wrongful act" to which this insurance applies are claimed and to which the insured must submit or does submit with our consent;
- **d.** any other civil alternative dispute resolution proceeding in which "damages" arising out of an offense or "wrongful act" to which this insurance applies are claimed and to which the insured submits with our consent; or
- **e.** a formal proceeding or investigation with the Equal Employment Opportunity Commission, or with an equivalent state or local agency.

A "claim" does not mean any ethical conduct review or enforcement action, or disciplinary review, or enforcement action.

> for "sexual abuse" which is excluded in the Sexual Abuse exclusion below), ***or the willful violation of any statute, ordinance or regulation committed by or with the knowledge of the insured***. However, we will defend the insured for covered civil action subject to the other terms of this Coverage Form until either a judgment or final adjudication establishes such an act, or the insured confirms such act.

The TOMA—and basis for Allied World's position that the Violation of Laws exclusion is triggered—is a statute appearing at Section 551.001 *et seq.* of the Texas Government Code. The "Criminal Acts" exclusion does not bar defense coverage, as it requires "either a judgment or final adjudication"[16] that an act involved a *willful* violation of statute. At the very least, the language of these exclusions creates an ambiguity as to the scope of their application because, while they both purport to bar coverage for the same or similar conduct, one of them entitles the insured to a defense until it is established that an excluded violation occurs while the other does not. Needless to say, however, neither exclusion provides a basis for Allied World to escape its duty to defend.

D. Attorney's Fees and Court Costs Exclusion

Allied World further relies on exclusion 5. to deny coverage. That exclusion precludes coverage for "[a]ny award of court costs or attorney's fees which arises out of an action for 'injunctive relief'." First, there has been no "award of court costs or attorney's fees" in this matter. Thus, the exclusion does not apply on its face. Second, even if there was an award of attorney's fees and court costs to Intervenors, this exclusion would not apply to any "damages" or "defense expenses" as those terms are defined in the Policy.[17] As a result, this exclusion does not serve as a basis to deny the duty to defend and will not apply to negate the duty to indemnify in its entirety either in the event a judgment is entered against the insureds.

E. Claims Against Other Insured / ERISA, COBRA and WARN Act Liability Exclusions

Allied World next cites to exclusion 8. (Claims Against Other Insured) as precluding coverage and recommends that this matter be submitted to a D&O carrier, and then suggests that the ERISA Exclusion (exclusion 15.) may "apply as to fiduciary duties."

Addressing the "Claims Against Other Insured" exclusion first, the express language of that exclusion limits its applicability to "claims" brought "By a Named Insured." The only Named Insured on the Policy is "Windermere Oaks Water Supply Corporation." As that entity is not identified as an Intervenor in the Second Amended Original Petition and is not otherwise making

[16] Under Texas law, the "final adjudication" phrase means that the exclusion applies only if there is a finding of a *willful* violation of statute through final judgement or settlement in the underlying matter, not in a parallel coverage action or parallel lawsuit. *See e.g.*, *Pendergest-Holt v. Certain Underwriters at Lloyd's of London*, 600 F.3d 562, 573 (5th Cir. 2010) (citing *Westport Ins. Corp. v. Hanft & Knight, P C.*, 523 F. Supp. 2d 444, 454–55 (M.D. Pa. 2007); *Virginia Mason Med. Ctr. v. Executive Risk Indem. Inc.*, No. C07-0636MJP, 2007 WL 3473683 at *5 (W.D. Wash. Nov. 14, 2007)).

[17] *See BancorpSouth, Inc. v. Fed. Ins. Co.*, 873 F.3d 582, 588 (7th Cir. 2017).

claims against another insured or Named Insured in the Second Amended Original Petition, the exclusion is inapplicable. Moreover, the "ERISA, COBRA and WARN Act Liability" exclusion is not implicated at all. According to the U.S. Department of Labor website,

> ERISA protects the interests of employee benefit plan participants and their beneficiaries. It requires plan sponsors to provide plan information to participants. It establishes standards of conduct for plan managers and other fiduciaries. It establishes enforcement provisions to ensure that plan funds are protected and that qualifying participants receive their benefits, even if a company goes bankrupt.[18]

As this matter does not involve any such claims, that exclusion is wholly inapplicable.

F. Contractual Liability Exclusion

While not specifically discussed, Allied World apparently also relies on the Contractual Liability Exclusion to deny coverage. That exclusion bars coverage for "damages," "defense expenses," costs or loss based upon, attributed to, arising out of, in consequence of, or in any way related to any contract or agreement to which the insured is a party or a third-party beneficiary, including, but not limited to, any representations made in anticipation of a contract or any interference with the performance of a contract. The Second Amended Original Petition includes allegations of "wrongful acts" that have no connection to any purported contract, including allegations that the Board and the WSC improperly incurred debt, that certain members of the Board failed to properly market and advertise the Airport Tract, and that members of the Board improperly voted to seek resolution of the dispute with Martin and FHH. As such, this exclusion does not provide a basis for Allied World to deny defense coverage.

G. Exemplary Damages and Requirement of "Loss"

Allied World also states as follows:

> In the complaint, the plaintiffs have made a claim for punitive damages. Allied World denies any obligation to provide payment for punitive damages, or any other damages, that do not meet the definition of "loss" or "losses" as defined above and by the policy. You should, therefore, take whatever actions you deem appropriate to protect your interests, including notifying any prior carriers that may provide coverage for this loss.

Intervenors *do* seek exemplary damages in the Second Amended Original Complaint. As Allied World concedes, however, Intervenors also seek monetary "damages." Importantly, though, there is no definition of "loss" or "losses" within the POML Coverage of the Policy. As such, there is no basis to disclaim coverage for any potential award of exemplary damages, which will be nothing

[18] Fact Sheet: What is ERISA, U.S. Department of Labor, https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/fact-sheets/what-is-erisa (last visited May 15, 2020).

more than a "monetary" damages award covered by the Policy. Likewise, there is no blanket prohibition on the insurability of exemplary damages under Texas law.[19]

ALLIED WORLD HAS BREACHED ITS OBLIGATION TO PAY "DEFENSE EXPENSES" FOR INJUNCTIVE RELIEF UNDER COVERAGE B

Allied World has also improperly denied coverage under Coverage B. That insuring agreement states:

> **C. COVERAGE B. INSURING AGREEMENT - DEFENSE EXPENSES FOR INJUNCTIVE RELIEF**
>
> 1. We will pay those reasonable sums the insured incurs as "defense expenses" to defend against an action for "injunctive relief" because of a "wrongful act," . . . to which this insurance applies.

The term "injunctive relief" means equitable relief sought through a demand for the issuance of a permanent, preliminary or temporary injunction, restraining order, or similar prohibitive writ against an insured, or order for specific performance by an insured. In the Second Amended Original Petition, Intervenors seek to enjoin certain actions taken by the Board. Contrary to Allied World's position, these allegations specifically implicate the Coverage B Insuring Agreement.

The only reason for denial provided by Allied World as to this particular coverage is that "the Petition seeks 'damages', defined to mean monetary damages, arising out of a 'claim' for a 'wrongful act'." While we agree that Intervenors seek "damages" arising out of a "claim" for a "wrongful act," Allied World apparently ignores the fact that Intervenors also seek certain forms of equitable relief (*i.e.*, "injunctive relief") in this pleading. Thus, Allied World owes this particular coverage under the Policy.

CONCLUSION

In sum, Allied World has breached its duty to defend the WSC and the Director Defendants under Coverage A of the POML Coverage of the Policy because no exclusions eliminate the defense obligation. Allied World also has wrongfully denied coverage to the WSC and the Director Defendants under Coverage B of the POML Coverage of the Policy. Accordingly, the WSC and the Director Defendants respectfully request that Allied World reconsider its position and immediately agree to provide a complete defense to the WSC and the Director Defendants, as required under Texas law. Additionally, they are entitled to reimbursement of their "defense

[19] *See, e.g., Fairfield Ins. Co. v. Stephens Martin Paving, LP*, 246 S.W.3d 653, 670 (Tex. 2008) (declining to make a broad proclamation of public policy as to the insurability of exemplary damages).

expenses" they have incurred.[20] Finally, Allied World is also liable for statutory penalties based on its improper denial of coverage.[21]

We look forward to Allied World's prompt response.

Best regards,

Blake H. Crawford

[20] *See Lafarge Corp. v. Hartford Cas. Ins. Co.*, 61 F.3d 389, 397 (5th Cir. 1995) (explaining that Hartford was obligated to pay that portion of attorneys' fees incurred from the time after the pleading that implicated the duty to defend was tendered).

[21] Texas law imposes obligations on an insurer under the Texas Prompt Payment Act to promptly acknowledge, investigate, and adjust first-party insurance claims. *See* TEX. INS. CODE § 542.051 *et seq.* The Supreme Court of Texas has explicitly held that an insured's right to a defense benefit is a "first-party claim" within the meaning of the Prompt Payment Act. *Lamar Homes, Inc. v. Mid-Continent Cas. Co.*, 242 S.W.3d 1, 20 (Tex. 2006). The statute states that an insurer, who is "liable for a claim under an insurance policy" and who does not promptly respond to, or pay, the claim as the statute requires, is liable to the policy holder or beneficiary not only for the amount of the claim, but also for "interest on the amount of the claim at the rate of eighteen percent a year as damages, together with reasonable attorney's fees." TEX. INS. CODE § 542.060(a).

CD ATTACHED

TO VIEW PLEASE CONTACT

CENTRAL RECORDS

512-936-7180