

**UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF TEXAS  
HOUSTON DIVISION**

|                              |   |                        |
|------------------------------|---|------------------------|
| HOUSTON CASUALTY COMPANY,    | § |                        |
| <i>Plaintiff,</i>            | § |                        |
|                              | § |                        |
| vs.                          | § | CIVIL ACTION H-05-1804 |
|                              | § |                        |
| LEXINGTON INSURANCE COMPANY, | § |                        |
| <i>Defendant.</i>            | § |                        |

**MEMORANDUM AND RECOMMENDATION**

This is an insurance coverage dispute involving reinsurance.<sup>1</sup> Defendant Lexington Insurance Company (Lexington) has filed a motion for summary judgment (Dkt. 18), and plaintiff Houston Casualty Company (HCC) has filed a cross-motion for summary judgment (Dkt. 19). Having considered the parties submissions and all matters of record the court recommends that Lexington’s motion be denied and HCC’s motion be granted.

**BACKGROUND**

The following facts and relevant policy provisions are undisputed. This case arises out of a September 13, 1999 executive order from Governor Jeb Bush declaring a state of emergency in Florida due to Hurricane Floyd and ordering mandatory evacuations. Pursuant to that executive order, Universal Studios, a theme park in Orlando, Florida, was closed for at least one day, September 14, 1999. Hurricane Floyd changed course and did not make landfall in Florida.

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<sup>1</sup> The district court referred this case to this magistrate judge for pretrial management (Dkt. 15).

Gulfstream Insurance (Ireland) Limited (Gulfstream) issued an “all risks” policy to Seagram Company, Ltd., the owner of Universal Studios.<sup>2</sup> Universal Studios submitted a claim to Gulfstream for damages resulting from its Hurricane Floyd business interruption in the amount of \$3,354,680 and for property damage and additional expenditures in the total amount of \$771,819. Gulfstream, through its adjuster Axis Adjustment (USA) Inc., adjusted the claim to \$3,216,590 for business interruption and \$192,619 for property damage and additional expenditures. Gulfstream applied the \$250,000 policy deductible for Florida wind storm damage. Gulfstream paid the claim as adjusted.

Gulfstream retained liability for \$1,000,000 in damages under the policy. Gulfstream reinsured the remainder of its risk. Gulfstream reinsured 40% of its risk through plaintiff HCC. The HCC policy incorporates all of the policy terms, conditions, and exclusions contained in the original policy and required HCC to “follow the settlements” of the original underwriters. HCC paid Gulfstream \$786,636.00.<sup>3</sup>

HCC in turn reinsured 75% of its risk through defendant Lexington. The Lexington policy incorporates all of the policy terms, conditions, and exclusions contained in the

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<sup>2</sup> Gulfstream is a “captive” insurance company, meaning it was organized for the purpose of insuring the liabilities of its owner. HCC has presented uncontradicted evidence that Gulfstream is managed by AIG Insurance Management Services, Limited. Affidavit of Sheena Sullivan, ¶¶ 2-3, Exhibit 1 to HCC’s response and cross-motion. HCC represents, and Lexington does not dispute, that AIG Insurance Management Services, Limited is an affiliate of Lexington.

<sup>3</sup> Each of Gulfstream’s four other reinsurers also paid their allocated share.

original Gulfstream policy and required Lexington to “follow the settlements” of HCC. HCC submitted a claim to Lexington for \$589,977.00, which Lexington has not paid.

The “follow the settlements” provision contained in both the HCC and Lexington policies provides that those policies are:

Subject to all terms, clauses and conditions as original and to follow the settlements of original Underwriters in all respects within the terms of this reinsurance.<sup>4</sup>

The Gulfstream policy,<sup>5</sup> which is incorporated into the HCC and Lexington policies, contains the following relevant provisions:

**Section 5 – Perils Insured:**

This Policy insures against all risks of direct physical loss from any cause whatsoever (including general average and salvage charges on shipments covered while waterborne or airborne) except as hereinafter excluded.

**Section 7 – Coverage:**

Except as hereinafter excluded, this Policy covers:

\* \* \* \*

H. **Business Interruption – Gross Earnings:** The United States, Canada and the Rest of the World, where applicable, when coverage is provided on such basis:

- (1) Loss resulting from necessary interruption of business conducted by the Insured, whether total or partial, and caused by loss, damage or destruction covered herein

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<sup>4</sup> HCC policy, Exhibit 7 to Stipulated Record (Dkt. 17); Lexington policy, Exhibit 10 to Stipulated Record (Dkt. 17).

<sup>5</sup> Gulfstream policy, Exhibit 6 to Stipulated Record (Dkt. 17).

during the term of this Policy to real and personal property as described in clause 7.A.

\* \* \* \*

M. Provisions Applicable to Business Interruption, Extra Expense, Rental Value, Leasehold Interest and Royalties Coverages

(1) Period of Recovery: The following clauses shall all be deemed the length of time for which losses may be claimed:

- a. such length of time as would be required with the exercise of due diligence and dispatch to rebuild, repair, or replace such part of the property as has been lost, destroyed or damaged, and
- b. such additional length of time to restore the Insured's business to the condition that would have existed had no loss occurred, commencing with the later of the following dates:
  - (i) the date on which the liability of the Company for the loss would otherwise terminate; or
  - (ii) the date on which repair, replacement or rebuilding of such part of the property as has been damaged is actually completed;

but in no event for more than 24 months thereafter from said later commencement date;

- c. with respect to alterations, additions, and property while in the course of construction, erection, installation, or assembly, the Period of Recovery shall be determined as provided in (a) above but such determined length of time shall be applied to the experience of the business after the business has reached its planned level of production or level of business operation;
- d. shall commence with the date of such loss or damage and shall not be limited by the date of expiration of this Policy.

\* \* \* \*

- (4) Interruption by Civil or Military Authority: This Policy is extended to cover the actual loss sustained during the period of time when, as a result of a peril insured against, access to real or personal property is impaired by order of civil or military authority.
- (5) Ingress/Egress: This Policy is extended to cover the actual loss sustained during the period of time when, as a result of a peril insured against, or as a result of extortion or bomb threat, ingress to or egress from real or personal property is thereby impaired in whole or in part.

In its motion for summary judgment, Lexington first contends that the Universal Studios claim is not covered by the policy because Universal Studios did not suffer physical damage to its property.<sup>6</sup> Second, Lexington contends that the deductible was not satisfied because business interruption damages are limited to the period the park actually was closed.<sup>7</sup>

HCC responds that Lexington's defenses are barred by the "follow the settlements" doctrine. HCC further responds that the claim is covered by the business interruption clause of the policy, including the "civil authority" and "ingress/egress" provisions, and that the amount of the claim is proper because the "period of recovery" for which the insured can recover business interruption losses extends beyond the date or dates the park was closed.

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<sup>6</sup> Lexington contends that HCC admitted this fact in communications regarding the claim. HCC presents some evidence that Universal Studios did suffer some minimal physical damage from the storm, *see* HCC's response and cross-motion, at 8, but there is no indication in the record that the business interruption was caused by any physical damage. In fact, Lexington does not take issue with HCC's payment of its share of the \$192,619.00 allocated to property damage in Universal Studios's claim. *See* Appendix to Lexington's motion. Thus, while there may be some factual dispute on this point, it is not a material dispute.

<sup>7</sup> HCC does not present evidence as to the actual number of days the park was closed. Lexington presents evidence the park was closed for 1.5 days. Universal Studios's claim includes business interruption losses for 7 days.

## ANALYSIS

### **1. Summary Judgment Standards**

This case is before the court on summary judgment. Summary judgment is appropriate if no genuine issues of material fact exist, and the moving party is entitled to judgment as a matter of law. FED. R. CIV. P. 56(c). The party moving for summary judgment has the initial burden to prove there are no genuine issues of material fact for trial. *Provident Life & Accident Ins. Co. v. Goel*, 274 F.3d 984, 991 (5th Cir. 2001). Dispute about a material fact is “genuine” if the evidence could lead a reasonable jury to find for the nonmoving party. *In re Segerstrom*, 247 F.3d 218, 223 (5th Cir. 2001). “An issue is material if its resolution could affect the outcome of the action.” *Terrebonne Parish Sch. Bd. v. Columbia Gulf Transmission Co.*, 290 F.3d 303, 310 (5th Cir. 2002).

If the movant meets this burden, “the nonmovant must go beyond the pleadings and designate specific facts showing that there is a genuine issue for trial.” *Littlefield v. Forney Indep. Sch. Dist.*, 268 F.3d 275, 282 (5th Cir. 2001) (quoting *Tubacex, Inc. v. M/V Risan*, 45 F.3d 951, 954 (5th Cir. 1995)). If the evidence presented to rebut the summary judgment is not significantly probative, summary judgment should be granted. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 249-50 (1986). In determining whether a genuine issue of material fact exists, the court views the evidence and draws inferences in the light most favorable to the nonmoving party. *Id.* at 255.

## 2. Follow the Settlements Doctrine<sup>8</sup>

There is no dispute that the reinsurance policy at issue in this case contains an explicit “follow the settlements” clause. There is also no dispute that this case involves a reinsurance contract having the same terms as the original policy.<sup>9</sup> “As its label implies, the ‘follow the settlements’ doctrine prevents facultative<sup>10</sup> reinsurers from second guessing good-faith settlements and obtaining de novo review of judgments of the reinsured’s liability to its insured.” *National Am. Ins. Co. of Cal. v. Certain Underwriters at Lloyd’s London*, 93 F.3d 529, 535 (9th Cir. 1996) (quoting *North River Ins. Co. v. Cigna Reinsurance Co.*, 52 F.3d 1194, 1199 (3d Cir. 1995)); *Houston Casualty Co. v. Certain Underwriters at Lloyd’s London*, 51 F. Supp. 2d 789, 794 n.4 (S.D. Tex. 1999).<sup>11</sup>

Pursuant to this doctrine, a reinsurer is required to indemnify its reinsured for payments that are reasonably within the terms of the original policy as long as the reinsured

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<sup>8</sup> The follow the settlements doctrine is also known as the follow the fortunes doctrine. The parties have used the terms interchangeably, and do not argue that there is any difference between the two. The policy uses the phrase “follow the settlements.”

<sup>9</sup> Some reinsurance contracts differ materially from the underlying policy and the reinsurer accepts only specific risks insured under the original policy. In such cases, a reinsured is not liable for risks beyond that which was agreed upon in the reinsurance contract. *North River*, 52 F.3d 1194, 1207 (3d Cir. 1995). This is not such a case.

<sup>10</sup> A facultative reinsurer, such as Lexington in this case, enters into a contract with its reinsured to cover a particular risk or policy. A treaty reinsurer, on the other hand, agrees to accept all its reinsured’s covered business. See *North River*, 52 F.3d at 1199.

<sup>11</sup> The parties agree that Texas law applies in this case. However, both parties have cited law from multiple other jurisdictions in support of their positions. Neither side contends that Texas law varies from that of other jurisdictions on any relevant issue.

acted in good faith. *See Christiana Gen. Ins. Corp. v. Great Am. Ins. Co.*, 979 F.2d 268, 280 (2d Cir. 1992); *Aetna Casualty & Sur. Co. v. Home Ins. Co.*, 882 F. Supp. 1328, 1346-47 (S.D.N.Y. 1995). “Good faith” in the context of the follow the settlements doctrine is not co-extensive with the duty of utmost good faith generally owed by an insurer to its insured because reinsurance involves sophisticated business entities familiar with the business of insurance who bargain at arm’s length. *North River*, 52 F.3d at 1213. Courts have not developed a uniform approach to determining the meaning of good faith in this context. The Second Circuit has held that the reinsurer must show bad faith, not mere negligence, and that the minimum standard for bad faith is gross negligence or recklessness. *Id.* at 1212-13.

Thus, “a reinsurer is required to indemnify for payments reasonably within the terms of the original policy, even if technically not covered by it.” *National Am. Ins. Co. of Cal.*, 93 F.3d at 535. As one court explained:

This standard is purposefully low. Were the Court to conduct a de novo review of [reinsured’s] decision-making process, the foundation of the [reinsured]-reinsurer relationship would be forever damaged. The goals of maximum coverage and settlement that have been long established would give way to a proliferation of litigation. [Reinsureds] faced with de novo review of their claims determinations would ultimately litigate every coverage issue before making any attempt at settlement.

*International Surplus Lines Ins. Co. v. Certain Underwriters and Underwriting Syndicates at Lloyd’s of London*, 868 F. Supp. 917, 921 (S.D. Ohio 1994). Moreover, if a reinsurer were permitted to revisit coverage issues resolved between the insurer and its insured, the insurer would be in the position of advancing defenses to coverage against its insured that the

reinsurer would then use against it when seeking to deny coverage. *North River*, 52 F.3d at 1206.

As the court pointed out in *North River*, the follow the settlements doctrine “creates an exception to the general rule that contract interpretation is subject to de novo review.” *Id.* at 1206. The reinsurer bears the burden of proving that it is not obligated to follow the settlements of its reinsured. *See Id.* at 1207 (“‘follow the fortunes’ doctrine requires a court to find reinsurance coverage unless the reinsurer demonstrates the liability to the insured was the result of fraud and collusion or not reasonably within the scope of the original policy.”).

### **3. Application of Follow the Settlements Doctrine to Policy in This Case**

Pursuant to the “follow the settlements” clause, the court will not make a *de novo* determination as to whether or not Universal Studios’s claim is covered under the Gulfstream policy. The issues before the court are only (i) whether HCC paid the claim in good faith; and (ii) whether the claim was reasonably within the terms of the policy. *North River*, 52 F.3d at 1204 (“a court or [arbitration] panel, faced with a reinsurer’s denial of liability, would ask not whether the underlying claim was covered by the cedent’s policy, but whether there is any reasonable basis to conclude there was such coverage. Only if the ceding company pays a claim that is clearly outside the scope of its policy, would the reinsurer’s challenge be sustained” (citation omitted)).

*Independence Ins. Co. v. Republic Nat. Life Ins. Co.*, 447 S.W.2d 462 (Tex. Civ. App. 1969, *writ ref’d n.r.e.*) is one of the few cases holding that a reinsurer was not bound to pay

under a follow the settlements clause. In that case, Independence Insurance Company issued a \$100,000 policy on the life of Aubrey Graham, an employee of Twilight Acres, Inc., with Twilight as the beneficiary and the premium payer. Independence reinsured \$95,000 of its liability under the policy with Republic National Life Insurance Company.

The president of Independence, Robert Hudson, was also the owner of Twilight. Hudson's personal attorney, C.J. Humphrey, was vice-president and general counsel for Independence. At the time the policy issued, Twilight was having financial difficulties. Hudson was personally liable on some of Twilight's debt. Twilight made only two premium payments and the policy lapsed as of July 28, 1965. Graham died on August 27, 1965. Prior to Graham's death, the assets of Twilight were assigned for the benefit of creditors, with the assignee being C.J. Humphrey. Republic notified Independence both orally and in writing that the claim should not be paid. Nonetheless, Humphrey argued to the executive committee of Independence that the claim should be paid because Twilight's creditors would insist upon it. Independence paid the claim. Republic denied liability.

The Texas court ruled in favor of Republic on two grounds. First, there was no valid policy in effect at the time of Graham's death. Second, Republic was not bound by the follow the fortunes doctrine because the conflicts of interest and actions of Hudson and Humphrey evidenced bad faith in paying the claim.

In *American Ins. Co. v. North American Co. for Prop. & Cas. Ins.*, 697 F.2d 79 (2d Cir. 1982), the Second Circuit found a reinsurer not liable to its reinsured for a payment that

was clearly outside the scope of its policy. In that case, an insured won a jury award against its insurer for punitive and compensatory damages. The insurer settled the claim prior to appeal. The reinsurer denied liability for the punitive damages component of the settlement. The court did not review the policy *de novo* to determine whether the policy covered the punitive damages portion of the damages award. However, the court found that the record, which contained evidence of the parties' post-policy stipulation regarding treatment of punitive damages, adequately supported the district court's ruling that the damages assessed by the jury were the type of punitive damages excluded from coverage. Under the circumstances, the court found "it would be unfair to [the reinsurer] to hold it liable for damages beyond the scope of its policy." 697 F.2d at 81.

The *Independence* and *American Ins.* cases involve exceptional circumstances. This case does not. Lexington states that HCC's claim handling was slipshod, noting that HCC originally made an advance on the claim without realizing that Gulfstream retained liability for \$1,000,000. Lexington also makes the observation that in some instances an insurer may pay a claim to preserve its business relationship with the insured, particularly where the premiums collected allow for a tidy profit after payment of the claim. However, there is no

evidence that happened in this case.<sup>12</sup> HCC's actions, even as characterized by Lexington, do not rise to the level of bad faith.

Universal Studios's claim is also reasonably within the terms of the policy. This reasonableness standard does not require the court to determine as a matter of law whether coverage actually exists under the policy. Lexington cannot second guess HCC's claims handling decision or HCC's decision to waive possible defenses. *Christiania*, 979 F.2d at 280.

HCC first argues that physical damage is not a prerequisite to recovery of business interruption losses under clause 7.H.1 of the policy. This argument is based on the distinction between the terms "loss" and "damage." HCC argues that loss is commonly understood to mean "the act of losing possession" and that "loss" must have a distinct meaning from the terms "damage" and "destruction" that follow it. Universal Studios lost possession of the park during the evacuation period. HCC further argues that clause 7.H.7 supports its position by requiring HCC to mitigate its damages by operating its business at the property if possible, *whether damaged or not*.

Standing alone, the business interruption clause of 7.H.1 limits coverage to interruptions caused by damage to real or personal property. However, the civil authority

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<sup>12</sup> The court notes that HCC is itself a reinsurer. It did not adjust the claim in the first instance, that task was undertaken by an adjuster hired by Gulfstream, Axis Adjustment (USA), Inc. Affidavit of Sheena Sullivan, ¶ 7, Exhibit 1 to HCC's response and cross-motion. Four other reinsurers also reimbursed Gulfstream for their share of the claim as adjusted by Axis. Therefore, it was reasonable for HCC to conclude it was bound to pay Gulfstream by its contractual follow the settlements agreement.

clause of 7.M.4 expressly “extends” the policy to cover actual losses “sustained during the period of time when, as a result of a peril insured against, access to real or personal property is impaired by order of civil or military authority.” And the ingress/egress clause of 7.M.5 “extends” coverage to actual losses “sustained during the period of time when, as a result of a peril insured against, or as a result of extortion or bomb threat, ingress to or egress from real or personal property is thereby impaired in whole or in part.” HCC’s interpretation of these clauses as extending coverage to instances where the insured’s property was not physically damaged, is reasonable.<sup>13</sup> As HCC argues, under Lexington’s theory the clauses would be rendered meaningless because the losses caused by physical damage would be covered under the general business interruption provision; no extension of coverage would be effected by the clauses. It is a well-established tenet of contract interpretation that a court must attempt to give effect to all contract provisions so as not to render any meaningless. *Kelley-Coppedge, Inc. v. Highlands Ins. Co.*, 980 S.W.2d 462, 464 (Tex. 1998).

The district court in *Fountain Powerboat Indus., Inc. v. Reliance Ins. Co.*, 119 F. Supp. 2d 552 (E.D.N.C. 2000), was faced with determining whether recovery under an

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<sup>13</sup> Lexington cites *Roundabout Theatre Co. v. Continental Cas. Co.*, 751 N.Y.S.2d 4 (N.Y. App. [1st Dept.] 2002), as support for the proposition that a business interruption clause limits recovery to instances of physical loss. While that case involves a similar business interruption clause and similar definition of the “perils insured against,” it does not involve extended coverage under a civil authority or ingress/egress provision. In fact, the court distinguished the policy in *Roundabout Theatre Co.* from a policy containing a civil authorities extension. *Id.* at 9. The court also recognized that Roundabout’s position regarding coverage was exactly opposite to the position it had taken in a prior lawsuit against its agent for failing to obtain business interruption coverage for off-site property damage. *Id.* at 9-10.

ingress/egress provision similar (but not identical) to that present in this case required property damage.<sup>14</sup> The plaintiff conceded that business interruption coverage generally requires that the interruption be caused by damage to covered property, but relied upon the ingress/egress clause of its policy to extend such coverage. *Id.* at 556. The court held that property damage was not necessary to plaintiff’s recovery. The court further held that the “civil authority” provision<sup>15</sup> in the policy similarly did not require physical loss, but covered any loss sustained due to lack of access to the property. *Id.* at 557. In so holding, the court noted that “[a] ‘loss’ is not predicated on physical damage but is one category of recovery along with damage and destruction as indicated by the use of the alternative coordinating conjunction ‘or’.” *Id.* Moreover, the *Fountain Powerboat* court determined that the plaintiff could recover not only for the period of time that ingress/egress was actually blocked, but for “the length of time to restore Fountain’s business to the condition that would have existed

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<sup>14</sup> The policy at issue in *Fountain Powerboat* provided:

This policy covers loss sustained during the period of time when, as a direct result of a peril not excluded, ingress to or egress from real and personal property not excluded hereunder, in thereby prevented.

119 F. Supp. 2d at 556.

<sup>15</sup> That provision provided:

This policy is extended to cover the loss sustained during the period of time when, as a direct result of a peril not excluded, access to real or personal property is prohibited by order of civil or military authority.

*Id.* at 557.

had no loss of ingress/egress occurred.” *Id.* at 558. The *Fountain Powerboat* case, while not controlling, supports the conclusion that HCC’s position is reasonable.

In supplemental briefing, Lexington argues that the cases *United Air Lines, Inc. v. Insurance Co. of the State of Penn.*, 439 F.3d 128 (2d Cir. 2006), and *By Development, Inc. v. United Fire & Cas. Co.*, No. Civ. 04-5116, 2006 WL 694991 (D.S.D. March 14, 2006), reinforce its position.<sup>16</sup> In *United Air Lines*, the Second Circuit held that United, whose facilities at Ronald Reagan Washington National Airport (“Airport”) suffered no significant physical damage as a result of the September 11 attack on the Pentagon, could not recover for its lost earnings caused by the disruption of flight service and the government’s temporary shutdown of the airport. *Id.* at 129. At issue was a Property Terrorism & Sabotage Insurance Policy providing coverage for “loss resulting directly from the necessary interruption of business caused by damage to or destruction of [United] Insured Locations [which include United facilities at both the World Trade Center and the Airport] resulting from Terrorism.” *Id.* (changes in original). The above quoted policy section also contained a “Civil Authority Clause” which stated: “[t]his section is specifically extended to cover a situation when access to the Insured Locations is prohibited by order of civil authority as a direct result of damage to adjacent premises.” *Id.* The court found it unnecessary to determine whether the Pentagon was an “adjacent premises.” *Id.* at 134. The court denied coverage on the ground that United’s business interruption at the Airport was caused by the threat of additional

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<sup>16</sup> *United Air Lines* and *By Development* involved disputes between an insured and its insurer; no reinsurance was at issue in either case.

terrorist attacks, not by damage at the Pentagon. *Id.* at 134-35. The court’s decision was not dependent in any way on whether or not United’s facilities actually suffered physical damage. *Id.* at 133 n.3. The fact-based determinations by the court in *United Air Lines* are of little or no value in deciding this case.

In *By Development*, the district court was required to interpret *de novo* the meaning of an insurance policy provision providing coverage for losses caused by an “action of civil authority that prohibits access” to the plaintiff’s property. *Id.* at \*4. Under the policy at issue, coverage for losses due to lack of access was not triggered until access had been prevented for 72 hours. *Id.* at 5. The evacuation and road closure order that prohibited access to plaintiff’s property was in effect for 54 hours. *Id.* The plaintiff argued that it was nonetheless entitled to recover under the policy because it continued to suffer substantial business losses even after the specific evacuation order that caused it to close was lifted. *Id.* at 1. The court held that the plain language of the policy provided coverage only for the period during which access was actually prohibited by the civil authority. *Id.* at 6. *Lexington* cites this case as support for its position that Universal Studios’s claim was overstated because it included losses for a business recovery period beyond the day the park was actually closed due to the evacuation order. But *By Development* does not involve interpretation of a “period of recovery” provision such as clause 7.M.1 in the policy in this case, and cannot be read as holding that in all instances damages under a business interruption provision are limited to the period a business is actually closed. *Cf. Lexington*

*Ins. Co. v. Island Recreational Dev. Corp.*, 706 S.W.2d 754, 756 (Tex. App.–Beaumont 1986, writ ref’d n.r.e.) (trial court’s finding that terms of policy allowed for period of rebuilding business was “certainly not inconsistent with a business interruption endorsement.”). The fact and policy-specific rulings in *By Development* do not mandate a conclusion that Universal Studios’s claim was clearly beyond the scope of the policy so as to overcome the effect of the policy’s follow the settlements provision.

### CONCLUSION

Lexington has not shown that HCC paid Gulfstream’s claim in bad faith or that the underlying claim was not reasonably within the terms of the Gulfstream policy. Thus, Lexington is bound by the follow the settlements doctrine to pay HCC’s claim. The court recommends that Lexington’s motion for summary judgment (Dkt. 18) be denied, and HCC’s cross-motion for summary judgment (Dkt. 19) be granted.<sup>17</sup>

HCC has also asserted a claim under Texas Insurance Code Article 21.55 for wrongful denial of coverage. That claim remains pending.

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<sup>17</sup> Lexington also has objected to the Affidavit of Sheena Sullivan, Exhibit 1 to HCC’s response and cross-motion, as conclusory, containing legal conclusions, and hearsay. Lexington does not point out what statements in the affidavit are objectionable or why. Sullivan was the underwriting manager for AIG Insurance Management Services, Limited, which managed the insurance operations of Gulfstream. Her affidavit addresses claims handling issues about which she states she has personal knowledge. Lexington’s objection is overruled. The court notes that Lexington has contradicted none of the assertions in Sullivan’s Affidavit other than the assertion that Universal Studios suffered property damage. The court did not rely on that fact in reaching its decision. *See infra* n.3.

The parties have ten days from service of this Memorandum and Recommendation to file written objections. Failure to file timely objections will preclude appellate review of factual findings or Lexington's objection is overruled. legal conclusions, except for plain error.

*See* FED. R. CIV. P. 72.

Signed at Houston, Texas on June 15, 2006.

  
Stephen Wm Smith  
United States Magistrate Judge