I. REGULATORY LIMITS ON CLAIMS HANDLING

A. Timing for Responses and Determinations

Texas Insurance Code § 542.051, et. seq. is the Prompt Payment of Claims Act. Section 542.055 mandates that an insurer must, not later than the fifteenth day after receipt of notice of a claim:

(1) acknowledge receipt of the claim;

(2) commence any investigation of the claim; and

(3) request from the claimant all items, statements, and forms that the insurer reasonably believes, at that time, will be required from the claimant.

With some stated exceptions, § 542.056 provides that an insurer has a duty to notify a claimant in writing of the acceptance or rejection of a claim no later than the fifteenth business day after the date the insurer receives all items, statements, and forms required by the insurer. If an insurer cannot determine whether it will accept or reject the claim, it must notify the claimant, not later than the fifteenth day after the insurer receives all relevant items and must give the reasons the insurer needs additional time. § 542.056(d). Not later than the forty-fifth day after the date an insurer notifies a claimant that it needs additional time to evaluate the claim, the insurer must reject or accept the claim. Id.

Except as otherwise provided, if an insurer delays payment of a claim following its receipt of all necessary items for a period exceeding the

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1 For eligible surplus lines insurers, the deadline is extended to not later than the 30th business day after the date an insurer receives notice of a claim.
2 “Claim” is a “first party claim,” that is, when an insured seeks recovery for the insured’s own loss as opposed to when an insured seeks coverage for injuries to a third party. Evanston Insurance Co. v. ATOFINA Petrochemicals, Inc., 256 S.W.3d 660 (Tex. 2008).
period specified in other applicable statutes or, in the absence of any other
specified period, for more than sixty days, the insurer shall pay damages and
other items as provided by § 542.060 (formerly, Section 6 of Article 21.555).
Protective Life Ins. Co. v. Russell, 119 S.W.3d 274, 286 (Tex.App.—Tyler
2003, pet. denied); see also Cox Operating, LLC v. St. Paul Surplus Lines
Ins. Co., 795 F.3d 496, 505-06 (5th Cir. 2015) (explaining that Section
542.006 mandates the insurer shall be liable to pay the beneficiary, in
addition to the amount of the claim, 18 percent per annum of the amount of
the claim as damages, together with reasonable attorney's fees). In Lamar
Homes, Inc. v. Mid-Continent Cas. Co., 242 S.W.3d 1, 16-18 (Tex. 2007),
the Texas Supreme Court held that the Prompt Payment of Claims Act applies
to an insured's claim for defense costs in a third party action. Note that
the new provision, § 542.060, describes the 18% penalty as “interest.” The
former provision did not characterize the 18% penalty as interest.

The prompt payment statute entitles physicians and providers to swift
payment of undisputed healthcare claims, yet it requires contractual privity
between the providers and health maintenance organizations (“HMOs”) in order
to be enforced. See Christus Health Gulf Coast v. Aetna, Inc., 397 S.W.3d 651
(Tex. 2013). In Christus, the plaintiffs, a group of hospitals, entered into
a contract with an intermediary of a Medicare health maintenance organization
(HMO). The court held that plaintiffs could not sue the HMO instead of the
intermediary, because there was no contract between the plaintiffs and the
HMO. There was only a contract between the plaintiffs and the HMO's
intermediary.

B. Standards for Determinations and Settlements

Claims handling standards are set forth in Chapter 541 of the Texas
Insurance Code, with Unfair Settlement Practices specifically set forth in
§ 541.060. § 541.060 makes it an unfair method of competition or an unfair
or deceptive act or practice in the business of insurance to engage in the
following unfair settlement practices with respect to a claim by an insured
or beneficiary (this list is not exhaustive):

(1) misrepresenting a material fact or policy provision
    relating to coverage at issue;

(2) failing within a reasonable time to either affirm or
deny coverage of a claim or submit a reservation of
rights to the policyholder;

(3) refusing to pay a claim without conducting a
    reasonable investigation; or

(4) failing to promptly provide to a policyholder a
    reasonable explanation of the basis in the policy, in
    relation to the fact or applicable law, for the
    insurer’s denial of a claim or offer of a compromise
    settlement of a claim.

With regard to an insurer’s conduct in paying or settling claims,
§ 541.060 (2)(A) requires an insurer to “attempt in good faith to effectuate
a prompt, fair, and equitable settlement of a claim with respect to which the
insurer’s liability has become reasonably clear.” The Texas Supreme Court
held that article 21.21 (now, Chapter 541) of the Texas Insurance Code gives
an insured a private cause of action against its liability insurer for unfair
practices in settling third-party claims. Rocor Int’l, Inc. v. Nat’l Union Fire Ins. Co., 77 S.W.3d 253 (Tex. 2002) (insurer’s unreasonable delay in settling the case caused the insured, which had self-insured retention, to incur more attorney’s fees than necessary). A third-party beneficiary or a third party with a tort claim against an insured does not have standing under Chapter 541 to sue the insurer directly. Allstate Ins. Co. v. Watson, 876 S.W.2d 145, 150 (Tex. 1994).

C. Privacy Protections

Texas common law and statutory law provide for privacy protections in addition to the federal laws generally applicable to Texas residents. For example, Texas recognizes the tort of intrusion. See Valenzuala v. Aquino, 853 S.W.2d 512, 513 (Tex. 1993). This tort occurs when one intrudes on the private affairs or solitude of another, and a reasonable person would be highly offended by such an intrusion. See id. Coercive collection practices may give rise to an action for intrusion of a debtor’s privacy. See Household Credit Serv. Inc. v. Driscol, 989 S.W.2d 72, 84 (Tex.App.—El Paso 1998, pet. denied); Ledisco Fin. Serv v. Viracola, 533 S.W.2d 951, 957 (Tex. Civ. App.—Texarkana 1976, no writ). Texas also recognizes the tort of disclosure when one publicly discloses private facts, the matter publicized is not of legitimate public concern, and the publication of those facts would be highly offensive to a reasonable person of ordinary sensibilities. See Star-Telegram, Inc. v. Doe, 915 S.W.2d 471, 473-74 (Tex. 1995); Induat. Found. of the South v. Texas Indus. Accident Bd., 540 S.W.2d 668, 682-85 (Tex. 1976).

Statutory laws relating to privacy include the Interception of Communication provisions in the Texas Civil Practice and Remedies Code (TEX. CIV. PRAC. & REM. CODE ANN. § 123.001, et seq. (Vernon 1997)) and Article 18.20 of the Texas Code of Criminal Procedure (TEX. REV. CIV. STAT. ANN. art. 18.20 (Vernon Supp. 2002)) which protect against eavesdropping and wiretapping; the Texas Open Records Act (TEX. GOV’T CODE ch. 552 (Vernon 1994)); and Chapters 601 (Privacy) and 602 (Privacy of Health Information) of the Texas Insurance Code, which governs privacy in the insurance context. Under the Texas Insurance code, you must obtain authorization to disclose nonpublic personal health information. Yet, there are 31 enumerated exceptions which include underwriting, loss control, case management, investigation or reporting of actual or potential fraud, etc.

II. Principles of Contract Interpretation


The court will first look at the language of the policy because it will presume the parties intend what the words of their contract say. See Don's Bldg. Supply, 267 S.W.3d at 23. The court will then examine the entire agreement and seek to harmonize and give effect to all provisions so that

The policy's terms are given their ordinary and generally-accepted meaning unless the words were meant in a technical or different sense. Don's Bldg. Supply, 267 S.W.3d at 23; see also Sec. Mut. Cas. Co. v. Johnson, 584 S.W.2d 703, 704 (Tex. 1979). Texas courts strive to honor the parties' agreement and not remake their contract by reading additional provisions into it. See Nat'l Union Fire Ins. Co. of Pittsburg, PA v. Crocker, 246 S.W.3d 603, 606 (Tex. 2008).


III. Choice of Law

Regarding choice of law, a court in Texas must evaluate whether an insurance contract meets the requirements of Tex. Ins. Code Ann. § 21.42 and if it does, the contract is subject to Texas law. If the insurance contract does not meet the requirements of § 21.42, then a court is to apply the "most significant relationship" test of the Restatement (Second) of Conflict of Laws, § 6, to determine which state's law should control the dispute. Commer. Underwriters Ins. Co. v. Royal Surplus Lines Ins. Co., 345 F. Supp. 2d 652 (S.D. Tex. 2004).

Article 21.42 provides that Texas law applies to an insurance policy when (1) the proceeds are payable to any citizen or inhabitant of Texas, (2) the policy was issued by an insurer doing business in Texas, and (3) the policy was issued in the course of the insurer's business in Texas. TEX. INS. CODE ANN. art. 21.42 (Vernon 1981); Reddy Ice Corp., 145 S.W.3d at 341; see Hefner v. Republic Indem. Co. of Am., 773 F. Supp. 11, 13 (S.D. Tex. 1991). If article 21.42 does not mandate application of Texas law. Consequently, Texas will apply the "most significant relationship" test. See Reddy Ice Corp., 145 S.W.3d at 340.

In a class action matter the court should also consider whether laws in states in which class members reside would provide them greater relief, or whether those states have a particular interest in the claims being made. The court should pay particular attention to a state's interest in regulating the business of insurance as reflected in section 192 of the Restatement of Conflict of Laws (Second), which states: The validity of a life insurance contract issued to the insured upon his application and the rights created thereby are determined, in the absence of an effective choice of law by the insured in his application, by the local law of the state where the insured was domiciled at the time the policy was applied for, unless, with respect to the particular issue, some other state has a more significant relationship to the transaction and the parties, in which event the local law of the other state will be applied. See, Nat’l W. Life Ins. Co. v. Rowe, 164 S.W.3d 389, 391-92 (Tex. 2005) (applying and quoting § 192 of the Restatement).
IV. Duties Imposed by State Law

A. Duty to Defend

1. Standard for Determining Duty to Defend

An insurer’s duty to defend is determined by the “complaint allegation rule” or the “eight corners rule,” which limits review to the four corners of the insurance policy and the four corners of the plaintiff’s petition in the underlying lawsuit. Pine Oak Builders, Inc. v. Great Am. Lloyds Ins. Co., 279 S.W.3d 650, 654 (Tex. 2009); GuideOne Elite Ins. Co. v. Fielder Road Baptist Church, 197 S.W.3d 305 (Tex. 2006); Trinity Universal Ins. Co. v. Cowan, 945 S.W.2d 819, 821 (Tex. 1997). Thus, if the facts alleged in the petition do not fall within the scope of coverage, an insurer is not legally required to defend a lawsuit against its insured. Id.; National Union Fire Ins. Co. of Pittsburg, P.A. v. Merchants Fast Motor Lines, Inc., 939 S.W.2d 139, 141 (Tex. 1997); Collier v. Allstate County Mut. Ins. Co., 64 S.W.3d 54, 59 (Tex.App.—Fort Worth 2001, no pet.) (explaining that an insurer’s “duty to defend is determined by the factual allegations of the pleadings, considered in light of the policy provisions and without reference to the truth or falsity of the allegations). In reviewing the pleadings, the court must focus on the facts alleged, not on the legal theories asserted. Merchants Fast Motor Lines, 939 S.W.2d at 141; Collier, 64 S.W.3d at 59. Further, the allegations should be considered “without reference to the truth or falsity of such allegations.” King v. Dallas Fire Ins. Co., 85 S.W.3d 185, 191 (Tex. 2002) (citing Argonaut Southwest Ins. Co. v. Maupin, 500 S.W.2d 633, 635 (Tex. 1973).

Overall, the duty to defend turns on the "factual allegations that potentially support a covered claim," while "the facts actually established in the underlying suit control the duty to indemnify."

2. Issues with Reserving Rights

An insurer's reservation of rights is the notification to the insured that the insurer will defend the insured, but that the insurer is not waiving any defenses it may have under the policy, and it protects an insurer from a subsequent attack on its coverage position on waiver or estoppel grounds. Texas Ass'n of Counties County Gov't Risk Mgmt. Pool v. Matagorda County, 52 S.W.3d 128, 133 (Tex. 2000). An insurer may undertake an insured's defense and later deny coverage by reserving its rights, so long as the insured is advised that the insurer may use a policy defense to later void its duty to defend. American Eagle Ins. Co. v. Nettleton, 932 S.W.2d 169, 174 (Tex. App.—El Paso 1996, writ denied). The insurer properly reserves its rights only when it has a good-faith belief that the complaint alleges conduct that may not be covered by the policy. Id.

A reservation of rights should be sent as soon as reasonably possible. Generally, if there is no coverage under an insurance policy as a matter of law, coverage cannot be created through theories of waiver or estoppel. In Ulico Cas. Co. v. Allied Pilots Assoc., 262 S.W.3d 773, 781 (Tex. 2008) the court held that an insurer’s policy is not expanded simply by the insurer assuming the insured’s defense without a reservation of rights letter. However, if the insurer’s actions prejudice the insured, the lack of coverage does not preclude the insured from asserting an estoppel theory to recover damages it sustains because of the insurer’s actions.
V. Extra-contractual Claims Against Insurers: Elements and Remedies

A. Bad Faith

The Texas Supreme Court first recognized the existence of the duty of good faith and fair dealing in the insurance context in Arnold v. National County Mutual Fire Insurance Co., 725 S.W.2d 165, 167 (Tex. 1987). It held that the duty arises from the special relationship that is created by the contract between the insurer and the insured. Id.; see also, Viles v. Security Nat’l Ins. Co., 788 S.W.2d 566, 567 (Tex. 1990) (recognizing that the duty arises “not from the terms of the insurance contract, but from an obligation imposed in law” as a result of the special relationship). A claim for breach of the duty of good faith and fair dealing is separate from any claim for breach of the underlying insurance contract, Viles, 788 S.W.2d at 567, and the threshold of bad faith is reached only when the breach of contract is accompanied by an independent tort. Transp. Ins. Co. v. Moriel, 879 S.W.2d 10, 17 (Tex. 1994).

Bad faith liability in the insurance context arises out of the contractual relationship between the insured and the insurer. Aranda v. Ins. Co. of N. Am., 748 S.W.2d 210, 212 (Tex. 1988). The duty of good faith and fair dealing is separate and distinct from the insurer’s settlement duties that arise under Chapter 541 of the Texas Insurance Code.

1. First Party

Those who wish to sue an insurance company for bad faith relating to the handling of a first-party claim generally have two causes of action available: (1) a common law claim for breach of the duty of good faith and fair dealing; and (2) a statutory claim for Unfair Claims Settlement Practices under Texas Insurance Code Section 541.060(a). While the common law and statutory standards of liability are generally combined, there are some differences in the type of damages that can be recovered under each and what it takes to get those damages.

Under the common-law tort theory, an insurer fails to comply with its duty of good faith and fair dealing when, without a reasonable basis, it denies a claim or delays payment of a claim, and it knew or should have known, based on a duty to fairly investigate, that it was reasonably clear that the claim was covered by the policy. See Universe Life Ins. Co. v. Giles, 950 S.W.2d 48, 50-51 (Tex. 1997). An insurer may also violate its duty by canceling a policy without a reasonable basis. Union Bankers Ins. Co. v. Shelton, 889 S.W.2d 278, 283 (Tex. 1994). A cause of action is stated by alleging that the insurer had no reasonable basis for the cancellation of the policy and that the insurer knew or should have known of that fact. Id.

Notably, an insurer cannot be held liable for bad faith if it erroneously denies a claim, so long as there is a valid basis for denying the claim at the time of the denial. See Republic Ins. Co. v. Stoker, 903 S.W.2d 338, 340 (Tex. 1995). This does not, however, relieve an insurance carrier of its obligation to promptly investigate and process claims. See id.

2. Third Party

In Maryland Ins. Co. v. Head Indus. Coatings & Servs., 938 S.W.2d 27, 28-29 (Tex.1996)(per curiam), the Texas Supreme Court held that an insurer owes its insured no common law duty of good faith and fair dealing to...
investigate and defend claims made by a third party against the insured. In refusing to recognize a duty of good faith and fair dealing under the facts before it, the Supreme Court held that “Texas law recognizes only one tort duty in [third-party insurance cases], that being the duty stated in [G.A] Stowers Furniture Co. v. American Indemnity Co., 15 S.W.2d 544 (Tex. Comm’n App. 1929, holding approved).” Stowers imposes a duty on an insurance company to use reasonable care to avoid a judgment against its insured which is in excess of policy limits. Since the Head decision, however, the legislature has added a statutory duty. See Mid-Continent Ins. Co. v. Liberty Mut. Ins. Co., 236 S.W.2d 765, 771 (Tex. 2007) (referring to § 541.060(a)(2) of the Texas Insurance Code).

A third party can gain standing to bring an extra-contractual claim against an insurer through an assignment of rights from the policyholder. The assignment must be made after an adjudication of plaintiff’s claim against the defendant in a fully adversarial trial. State Farm Fire & Cas. Co. v. Gandy, 925 S.W.2d 696, 714 (Tex. 1996).

B. Fraud

Fraud occurs when:

1. a party makes a material misrepresentation;
2. the misrepresentation is made with knowledge of its falsity or made recklessly without any knowledge of the truth and as a positive assertion;
3. the misrepresentation is made with the intention that it should be acted on by the other party; and
4. the other party acts in reliance upon the misrepresentation and thereby suffers injury.


Fraud can also occur when:

1. a party [conceals or] fails to disclose a material fact within the knowledge of that party;
2. the party knows that the other party is ignorant of the fact and does not have an equal opportunity to discover the truth;
3. the party intends to induce the other party to take some action by [concealing or] failing to disclose the fact; and
4. the other party suffers injury as a result of acting without knowledge of the undisclosed fact.

See also New Process Steel Corp. v. Steel Corp. of Texas, 703 S.W.2d 209, 214 (Tex.App.–Houston [1st Dist.] 1985, writ ref’d n.r.e.).
C. **Intentional or Negligent Infliction of Emotional Distress (IIED or NIED)**

The elements of a claim for intentional infliction of emotional distress are:

(a) the defendant acted intentionally or recklessly;

(b) the defendant’s conduct was extreme and outrageous;

(c) the defendant’s actions proximately caused the plaintiff’s emotional distress; and

(d) the emotional distress that the plaintiff suffered was severe.

See *City of Midland v. O’Bryant*, 18 S.W.3d 209, 216-17 (Tex. 2000)(per curium); *Twyman v Twyman*, 855 S.W.2d 619, 621 (Tex. 1993)(adopting RESTATEMENT (SECOND) OF TORTS § 46 (1965)).

Texas does not impose a duty to avoid negligently inflicting emotional distress. A claimant may recover mental anguish damages only in connection with a breach of some other legal duty. *Boyles v. Kerr*, 855 S.W.2d 593, 594 (Tex. 1993).

D. **State Consumer Protection Laws, Rules and Regulations**

Significant consumer protection laws include the Texas Deceptive Trade Practices Act (Tex. Bus & Com. Code Ann. § 17.41, et seq. (Vernon 2000)); Deceptive Insurance Actions under Texas Insurance Code Chapter 541; Late Payment of Claims under Texas Insurance Code Chapter 542; and Title 28 of the Texas Administrative Code contains additional regulations that further define the foregoing statutes.

VI. **Discovery Issues in Actions against Insurers**

Generally, “a party may obtain discovery regarding any matter that is not privileged and is relevant to the subject matter of the pending action, whether it relates to the claim or defense of the party seeking discovery or the claim or defense of another party.” The Texas Rules of Civil Procedure impose two general limitations on discovery: 1) it must not be privileged; and 2) it must be relevant to the subject matter of the pending action, claim, or defense. The information sought must be reasonably calculated to lead to the discovery of admissible evidence. Tex. R. Civ. P. 192.3(a).

Discovery does have limitations imposed by the rules. The court may limit discovery if it determines that the discovery requests are: (a) unreasonably cumulative or duplicative, or obtainable from some other source that is more convenient, less burdensome, or less expensive; or (b) the burden or expense of the proposed discovery outweighs its likely benefit, taking into account the needs of the case. Tex. R. Civ. P. 192.4 (a), (b). The rules also protect from unlimited discovery so-called “work product,” which is defined as: “core work product,” i.e., the work product of an attorney or his or her representative, containing the attorney’s or representative’s “mental impressions, opinions, conclusions, or legal theories,” which are not discoverable; and “other work product,” discoverable only on a showing of substantial need and undue hardship on the part of the party seeking discovery. Tex. R. Civ. P. 192.5(b)(1), (2).
A. Discoverability of Claims Files

1. Claims file in same suit.

Non-privileged portions of the claim file of a party’s insurance company (when the insurance company is not a party) is generally discoverable in the same suit. See e.g., In re Ford Motor Co., 988 S.W.2d 714, 719 (Tex. 1998). However, if the insurance carrier is a party or in a first party claim, if the claim file is exempt from discovery under one cause of action, the party cannot get it for another cause in the same suit. Maryland Am. Gen. Ins. Co. v. Blackmon, 639 S.W.2d 455, 457-58 (Tex. 1982). An insurer is entitled to assert privilege to protect its claim file so long as its liability under the policy remains undetermined.

2. Claims file in separate suit.

The claim file of an insurance company is sometimes discoverable in another suit. See, e.g., Turbodyne Corp. v. Heard, 720 S.W.2d 802, 804 (Tex. 1986); Eddington v. Touchy, 793 S.W.2d 335, 337 (Tex.App.-Houston [1st Dist.] 1990, orig. proceeding); but see Humphreys v. Caldwell, 888 S.W.2d 469, 471 (Tex. 1994)(after first suit, Defendant in that suit sued Plaintiff’s carrier; claim file in first suit was not discoverable).

B. Discoverability of Reserves

When a party seeks information beyond the insurance agreement’s contents – such as the amount of reserve set for a particular claim - courts will rely on the general discovery standard to determine if the information requested must be produced. In re Dana Corp., 138 S.W.3d 298, 304 (Tex. 2004); see also Simon v. G.D. Searle & Co., 816 F.2d 397, 404 (8th Cir. 1987) (allowing discovery of corporate risk management documents, because they related to notice issues relevant to the products liability claim); Wegner v. Cliff Vliesman, Inc., 153 F.R.D. 154, 161 (N.D. Iowa 1994) (denying discovery request for information about remaining insurance coverage available, because plaintiff already received copies of applicable insurance policies as the procedural rules required and additional information was not relevant to underlying suit); Indep. Petrochem. Corp. v. Aetna Cas. & Sur. Co., 117 F.R.D. 283, 288 (D.D.C. 1986) (denying discovery of information about insurance reserves and reinsurance, because routine estimates used to calculate this information were not based on thorough factual and legal consideration for each insured, and therefore, the information was not relevant to the underlying coverage dispute). Texas has not definitively decided whether information about reserves is discoverable. But one Texas court has noted that “the question of whether reserves information is relevant in coverage or bad faith cases may be ... a complex issue.” In re Gen. Agents Ins. Co. of Am., Inc., 224 S.W.3d 806, 822 n.16 (Tex. Civ. App. - Houston [14th Dist.] 2007).

C. Discoverability of Existence of Reinsurance and Communications with Reinsurers

Texas has also not addressed the issue of whether information about reinsurance is discoverable, but, as noted above when a party seeks information beyond the insurance agreement’s contents courts will rely on the general discovery standard to determine if the information requested must
be produced. As to the existence of reinsurance the same rule applies, i.e. 1) it must not be privileged; and 2) it must be relevant to the subject matter of the pending action, claim, or defenses. As to communications the same rational as noted in section D below would apply.

D. Attorney-Client Communications

The attorney-client privilege is codified in Texas Rule of Evidence 503. The attorney-client privilege protects confidential communications between a lawyer and a client or their respective representatives made to facilitate the rendition of professional legal services to the client. The privilege may be invoked if the information or documents were prepared after a lawsuit had been filed or if there was good cause to believe that a lawsuit was likely.

An adjuster’s handwritten notes can qualify as privileged. See In Re Certain Underwriters at Lloyd's, 294 S.W.3d 891 (Tex.App.—Beaumont 2009, no pet.). In that case, the insurer hired an adjusting company to assist with the investigation. Id. at 895. The adjusting company’s employee made handwritten notes of conversations that he had with the underwriters’ representatives or attorneys. Id. In response to a subpoena, the company produced its file, which contained these handwritten notes. Id. The underwriters then sought the return of the notes, arguing that they were privileged. Id. at 896. The trial court denied the motion, and a mandamus petition followed. Id. In conditionally granting relief, the appellate court determined that the documents were privileged. Id. at 900. The court held that the underwriters had a reasonable basis for the belief that there was a substantial chance of litigation during the time period covered by the notes. Id. Next, the court held that the substantial need and undue hardship exceptions did not allow the policyholders to retain the notes. Id. at 901.

As to the Tripartite Relationship between the Insurer, Insured and Insurance Defense Counsel, the liability policy may grant the insurer the right to take “complete and exclusive control” of the insured’s defense. G.A. Stowers Furniture Co. v. American Indemnity Co., 15 S.W.2d 544, 547 (Tex. Comm’n App. 1929, holding approved). When defending unconditionally, the insurer has complete control of the defense. This control of the insured’s defense includes authority to accept or reject settlement offers and, where no conflict of interest exists, to make other decisions that would normally be vested in the client (the insured).

A defense attorney, as an independent contractor, has discretion regarding the day-to-day details of conducting the defense, and is not subject to the client’s control regarding those details. The attorney may not act contrary to the client’s wishes, but the attorney is in complete charge of the minutiae of court proceedings and can properly withdraw from the case, subject to the control of the court, if he is not permitted to act as he thinks best. Moreover, because the lawyer owes unqualified loyalty to the insured, see Employers Cas. Co. v. Tilley, 496 S.W.2d 552, 558 (Tex. 1973), the lawyer must at all times protect the interests of the insured even if those interests would be compromised by the insurer’s instructions. Under these circumstances, the insurer cannot be vicariously responsible for the lawyer’s conduct. See Ingersoll-Rand Equip. Corp. v. Transportation Ins. Co., 963 F. Supp. 452, 454-55 (M.D. Pa. 1997).

Finally, reliance upon the advice of counsel may be considered in mitigation of damages, but it does not constitute a defense.
VII. Defenses in Actions Against Insurers

A. Misrepresentations/Omissions: During Underwriting or During Claim

An insurer may avoid liability under a policy if it issued the policy in reliance on a false representation that was material to the risk. It is a question of fact whether a misrepresentation made in the application for the policy or if the policy itself was material to the risk or contributed to the contingency or event on which the policy became due and payable. Tex. Ins. Code Ann. § 705.004 (Vernon 2009); see also Odom v. Insurance Co. of Pennsylvania, 455 S.W.2d 195, 198 (Tex. 1970) (affirming cancelation of automobile liability policy based on material false statements in the policy application).

B. Failure to Comply with Conditions

In order to enforce a condition precedent to coverage, an insurer must prove that it was prejudiced by the insured’s failure to comply with the relevant condition. See Hernandez v. Gulf Group Lloyds, 875 S.W.2d 691, 692-94 (Tex. 1994); Hanson Prod. Co. v. Americas Ins. Co., 108 F.3d 627 (5th Cir. 1997). By demanding that an insurer prove prejudice, Texas law requires that only a material breach of a contract excuses performance. See Hernandez, 875 S.W.2d at 693. This prejudice requirement clearly applies to occurrence-based policies. See PAJ, Inc. v. The Hanover Ins. Co., 243 S.W.3d 630 (Tex. 2008) (holding that an insured’s failure to timely notify its insurer of a copyright infringement claim or suit does not defeat coverage under the advertising injury coverage of an occurrence-based CGL policy if the insurer was not prejudiced by the delay). The prejudice requirement also applies to claims-made policies as long as notice is given within the policy period or other specified reporting period. See Prodigy Communications Corp. v. Agricultural Excess & Surplus Insurance Co., 288 S.W.3d 374, 382 (Tex. 2009); and Financial Industries Corp. v. XL Specialty Insurance Co., 285 S.W.3d 877, 879 (Tex. 2009).
The assistance and cooperation of the insured is normally a condition precedent of almost every insurance policy and a requirement of the insured for defense and indemnity. But even if there is no evidence that the condition precedent of cooperation was satisfied, an insurer will not escape liability unless it was prejudiced by the lack of cooperation. See Harwell v. State Farm Mut. Auto. Ins., Co., 896 S.W.2d 170, 173-74 (Tex. 1995).

In PAJ, Inc. v. The Hanover Insurance Co., 243 S.W.3d 630, 636-37 (Tex. 2008), the court held that "an insured's failure to timely notify its insurer of a claim or suit does not defeat coverage if the insurer was not prejudiced by the delay." PAJ involved an occurrence-based commercial general liability ("CGL") policy with a prompt-notice provision that required the insured to notify the insurer of "an occurrence or an offense that may result in a claim 'as soon as practicable.'" Id. at 631-32. PAJ's untimely notice did not defeat coverage in the absence of prejudice to the insurer. Id. at 636-37. In a claims-made policy, when an insured gives notice of a claim within the policy period or other specified reporting period, the insurer must show that the insured's noncompliance with the policy's "as soon as practicable" notice provision prejudiced the insurer before it may deny coverage. See Prodigy Commc'n's Corp. v. Agric. Excess & Surplus Ins. Co., 288 S.W.3d 374, 382 (Tex. 2009).

C. Challenging Stipulated Judgments: Consent and/or No-Action Clauses

The leading case in this area is State Farm Fire & Casualty Co. v. Gandy, 925 S.W.2d 696 (Tex. 1996). The court held that the amount of any agreed judgment between a plaintiff and an insured, rendered without a "fully adversarial" trial, would neither bind the carrier nor be admissible as evidence of the amount of the insured’s damages. But see Evanston v. Atofina, supra, (liability insurer that wrongfully denies coverage is precluded from challenging reasonableness of settlement paid by its insured). Additionally, the Gandy court held that a pre-judgment assignment of an insured’s rights against its liability carrier is invalid, at least where the carrier has tendered a defense and made a good-faith attempt (e.g., filing of a declaratory judgment action) to determine coverage.

D. Statutes of Limitations

The statute of limitations for an action for breach of good faith and fair dealing is two (2) years from the date the cause of action accrued. Tex. Civ. Prac. & Rem. Code § 16.003(a); Murray v. San Jacinto Agency, Inc., 800 S.W.2d 826, 827 (Tex. 1990). Generally, the limitations period accrues when the insurer denies coverage. Id.

The statute of limitations for contract actions is four years. Tex. Civ. Prac. & Rem. Code § 16.004. Homeowner’s policies, however, commonly provide that suit must be brought against the insurer within two years and one day after the cause of action accrues. See also Tex. Civ. Prac. & Rem. Code § 16.070 (stating that contracts which establish a limitations period that is shorter than two years is void in Texas).


VIII. Trigger and Allocation Issues for Long-Tail Claims
A. Trigger of Coverage

Texas follows the "actual injury" or "injury-in-fact" approach, that the insurer must defend any claim of physical property damage that occurred during the policy term. The court declined to recognize a manifestation rule or exposure rule for the property damage claims alleged under this policy. It was recognized that pinpointing the moment of injury retrospectively is sometimes difficult, but would not exalt ease of proof or administrative convenience over faithfulness to the policy language. Further, looking to the date of actual injury, besides being consistent with the policy terms, is also consistent with scholarly authority. Those principles include construing the policy according to general rules of contract construction to ascertain the parties' intent. Don's Bldg. Supply, Inc. v. OneBeacon Ins. Co., 267 S.W.3d 20, 23 (Tex. 2008); Cox Operating, LLC v. St. Paul Surplus Lines Ins. Co., 795 F.3d 496, 505-06 (5th Cir. 2015).

The relevant inquiry is when the injury happens and when damage comes to pass, not when damage comes to light. Vines-Herrin Custom Homes, L.L.C v Great American Lloyd Ins. Co., 357 S.W.3d 166 (Tex. Civ. App.--Dallas 2011, no pet.)

As to bodily injury claims, they present a more complex problem in that Texas has not specifically adopted any trigger theory. The best authority is from the Fifth Circuits’ Erie guess as to what Texas would choose as the event that triggers the insurer's duty to defend in an asbestos lawsuit. In Guar. Nat'l Ins. Co. v. Azrock Indus. Inc., 211 F.3d 239, 243-47 (5th Cir. 2000), the Fifth Circuit decided, for the purposes of determining an insurer's duty to defend its insured in claims alleging personal injury from continuous exposure to asbestos products a court need only examine the face of the underlying plaintiff’s complaint. To trigger a duty to defend, the pleading must allege (1) exposure to a asbestos-containing products during the policy period and (2) that such exposure caused bodily injury -- even if the particular asbestos-related disease was not diagnosed until sometime after the policy expired.

B. Allocation among Insurers

Texas courts have not provided much in the way of guidance on how insurers were to allocate cost amongst themselves regarding cost of defense or indemnity. Where multiple insurers have a duty to provide a complete defense, neither must pay all of the defense costs because they share the duty until one has either exhausted its policy limits or is declared impaired. See Utica Nat'l Ins. Co. v. Tex. Prop. & Cas. Ins. Guar. Assoc., 110 S.W.3d 450, 458 (Tex. App.-Austin 2001), rev'd on other grounds, Utica Nat'l Ins. Co. v. Am. Indem. Co., 141 S.W.3d 198, 47 Tex. Sup. Ct. J. 845 (Tex. 2004).

Allocating indemnity payments among multiple carriers requires a different calculation and will look to the trigger question of when the bodily injury or property damage occurs. If a single occurrence triggers more than one policy, covering different policy periods, then different limits may have applied at different times. In such a case, the insured's indemnity limit should be whatever limit applied at the single point in time during the coverage periods of the triggered policies when the insured's limit was highest. The insured is generally in the best position to identify the policy or policies that would maximize coverage. Once the applicable limit is identified, all insurers whose policies are triggered must allocate
funding of the indemnity limit among themselves according to their subrogation rights.

A commentator has noted that the court in Garcia did not address or adopt a specific allocation approach, nor did it express when such allocation among carrier should take place, but at least provided a framework under Texas law for the proposition that any one insurer should not be burdened with an undue or unfair share of the indemnity obligation. When allocating defense cost and indemnity payments among multiple policy periods and insurers, equity is the theme that unites the holdings rendered by various Texas courts. “The Mathematics of Insurance Coverage” Alex Shilliday, Journal of Texas Insurance Law, Volume 12 Number 1, Summer 2012.

IX. Contribution Actions

Under Texas law contribution is a method for determining how much each defendant who is liable for the plaintiff’s damages must pay the other liable defendants. If one defendant pays more than its share of the plaintiff’s damages, that defendant has a right to be reimbursed by another liable defendant for the overpayment. This right to reimbursement is called a right of contribution. Tex. Civ. Prac. & Rem. Code § 33.015.

The Texas Supreme Court has held that any "direct claim for contribution between co-insurers disappears when the insurance policies contain 'other insurance' or 'pro rata' clauses." Mid-Continent Insurance Co. v. Liberty Mutual Insurance Co., 236 S.W.3d 765 (Tex. 2007). Additionally, the Supreme Court held that because the right of subrogation is based on a situation where the insurer "stands in the shoes" of its insured, if the insured is fully indemnified it will have no right to pass to the insurer for the insurer to enforce. Since Mid-Continent, it appears that federal and state courts are split with regard to the proper scope of Mid-Continent as applied to contribution and subrogation claims by co-insurers.

In 2010, the Fifth Circuit noted that "Mid-Continent left open the separate question of whether a co-insurer that pays more than its share of defense costs may recover such costs from a co-insurer who violates its duty to defend a common insured. Trinity Universal Ins. Co. v. Emp'rs Mut. Cas. Co., 592 F.3d 687, 694 (5th Cir. 2010). This decision was subsequently criticized by the Third Court of Appeals in Austin which held that the question of whether a co-insurer may recover when it pays more than its proportionate share of defense costs, finding instead that the contribution claim for defense costs was barred as a matter of law. See Truck Ins. Exch. V. Mid-Continent Cas. Co., 320 S.W.3d 613, 622-23 (Tex. App. -- Austin 2010).

Finally, a recent decision by the 14th Court of Appeals in Houston re-examined Mid-Continent as it applied to contractual subrogation and held that Mid-Continent does not prohibit a co-insurer from bringing a subrogation claim against another co-insurer where the insured was not fully indemnified and the "other insurance" clauses were mutually repugnant and did not limit the co-insurer's indemnity obligations. U.S. Fid. & Guar. Co. v. Coastal Ref. & Mktd., Inc., 369 S.W.3d 559 (Tex. App. -- Houston [14th Dist.] 2012, no pet.).
Duty to Settle

The duty of an insurer to accept reasonable settlement demands is known as the Stowers duty. The Stowers duty is the only common law tort duty that an insurer owes its insured when handling a third-party claim. The elements of a cause of action against an insurer for breaching its Stowers duty are the following:

1. The insured had an insurance policy with the insurer;
2. A third party offered to settle its claim against the insured within policy limits;
3. The insurer owed a duty to accept reasonable settlement offers within policy limits;
4. The insurer breached its duty by not accepting the settlement offer; and
5. The breach proximately caused injury to the insured.


In Rocor, the Texas Supreme Court recognized that there exists statutory liability from an insurer to its insured for failing to settle a third-party claim, at least where the insurer’s unreasonable delay in settling the case caused the insured (with a self-insured retention) to incur more attorney’s fees than necessary. Rocor Int’l v. National Un. Fire Ins. Co., 77 S.W.3d 253 (Tex. 2002). To establish liability for the insurer's failure to reasonably attempt settlement of a claim against the insured under either Texas Insurance Code or Stowers, the insured must show that:

1. the policy covers the claim;
2. the insured's liability is reasonably clear;
3. the claimant has made a proper settlement demand within policy limits, and;
4. the demand's terms are such that an ordinarily prudent insurer would accept it.

Id.

If a coverage dispute exists, and you are an insured, be careful what you wish for. In Texas, an insurer that settles a claim against its insured when coverage is disputed may seek reimbursement from the insured should it later be determined that no coverage exists. The insurer may seek reimbursement if the insurer “obtains the insured’s clear and unequivocal consent to the settlement and the insurer’s right to seek reimbursement.” Excess Underwriters at Lloyd’s v. Frank’s Casing Crew & Rental Tool, Inc., 246 S.W.3d 42 (Tex. 2008); Tex. Ass’n of Counties County Gov’t Risk Mgmt. Pool v. Matagorda County, 52 S.W.3d 128, 135 (Tex. 2000). The end result of the long-awaited Frank’s Casing opinion is that unless an insurance
policyholder's contract provides the insurer with the right to reimbursement of settlement proceeds following a coverage dispute, then the insurer cannot unilaterally create such a right. For such a right to exist the insurer must "obtain the insured's clear and unequivocal consent to the settlement and the insurer's right to seek reimbursement." See Tex. Ass'n of Counties County Gov't Risk Mgmt. Pool v. Matagorda County, 52 S.W.3d 128, 135 (Tex. 2000).