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The Policyholder's Lawyer:
Remembering
Mark Kincaid
1959 – 2016

In This Issue:

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THE INSURANCE LAW SECTION OF THE STATE BAR OF TEXAS

Officers for 2016-2017

CHAIR:

L. Kimberley Steele
Sedgwick, LLP
1717 Main St., Suite 5400
Dallas, TX 75201
Ph: (469) 227-4639
Fax: (469) 227-8004
kimberly.steele@sedgwicklaw.com

CHAIR ELECT:

Meloney Perry
Perry Law P.C.
10440 North Central Expwy., Ste. 600
Dallas, TX 75231
Ph: (214) 265-6224
Fax: (214) 265-6226
mperry@mperrylaw.com

SECRETARY:

Lisa A. Songy
Tollefson Bradley Mitchell & Melendi, LLP
2811 McKinney Avenue, Suite 250
Dallas, TX 75204
Ph: (214) 665-0107
Fax: (214) 665-0199
lisas@tbmmlaw.com

TREASURER:

William J. Chriss
Gravely & Pearson, L.L.P.
606 N. Carancahua St.
Suite 1511
Corpus Christi, TX 78401
Ph: (361) 884-3330
wjchriss@gplawfirm.com

IMMEDIATE PAST-CHAIR:

J. James Cooper
Reed Smith LLP
811 Main St., Ste. 1700
Houston, TX 77002
Ph: (713) 469-3879
jcooper@reedsmith.com

TECHNOLOGY OFFICER:

Brian L. Blakeley
Blakeley Law Firm
7330 San Pedro Ave., Ste 510
San Antonio, TX 78216
Ph: (210) 826-0715
brian@blakeleylawfirm.com

PUBLICATIONS OFFICER:

Pamella A. Hopper
McGuireWoods LLP
816 Congress Avenue, Ste. 940
Austin, TX 78701
Ph: (512) 472-3067
Fax: (512) 472-3068
phopper@mcguirewoods.com

Council Members 2016-2017

(2 Yr Term Exp 2017)

Jes Alexander
IRMI
12222 Merit Drive, Suite 1600
Dallas, TX 75251-2266
Ph: (972) 687-9312
Email: jes.a@irmi.com

(2 Yr Term Exp 2017)

Jamie Rohde Carsey
Thompson, Coe, Cousins & Irons, LLP
One Riverway, Ste 1400
Houston, TX 77056
Ph: (713) 403-8209
Fax: (713) 403-8299
Email: jcarsey@thompsoncoe.com

(2 Yr Term Exp 2017)

Linda M. Dedman
Dedman Law, PLLC
Meadow Park Tower
10440 N Central Expwy., Suite 1010
Dallas, TX 75231
Ph: (214) 363-8882
Fax: (214) 363-4902
Email:
ldedman@coveragelawdallas.com

(2 Yr Term Exp 2017)

Tarron L. Gartner-Ilai
Amy Stewart PC
5307 E. Mockingbird Lane, Suite 425
Dallas, TX 75206
Ph: (214) 347-9397
Fax: (214) 975-2806
Email: tarron@amystewartlaw.com

(2 Yr Term Exp 2017)

Juan "Trey" Mendez, III
Mendez Law Firm
243 E. Elizabeth St.
Brownsville, TX 78520
Ph: (956) 541-7600
Fax: (956) 541-7612
Email: Treymendez34@yahoo.com

(2 Yr Term Exp 2017)

Hon. Gray H. Miller
Southern District of Texas
515 Rusk Avenue
Houston, TX 77002
Ph: (713) 250-5377

(2 Yr Term Exp 2017)

Douglas P. Skelley
Shidlofsky Law Firm PLLC
7200 N Mopac Expwy., Ste. 430
Austin, TX 78731
Ph: (512) 685-1400
doug@shidlofskylaw.com

(2 Yr Term Exp 2018)

Tamara D. Bruno
Pillsbury Winthrop Shaw Pittman LLP
Two Houston Center
909 Fannin St., Ste. 2000
Houston, TX 77010-1028
Ph: (713) 276-7608
Fax: (713) 276-7673
tamara.bruno@pillsburylaw.com

(2 Yr Term Exp 2018)

Robert J. Cunningham
Roach & Newton, LLP
1111 Bagby, Suite 2650
Houston, TX 77002
Ph: (713) 652-2033
Fax: (713) 652-2029
Email:
rcunningham@roachnewton.com

(2 Yr Term Exp 2018)

Rebecca S.C. DiMasi
Buchanan DiMasi Dancy & Grabouski, LLP
9600 Great Hills Trail, Ste. 300W
Austin, TX 78759
Ph: (512) 225-2800
Fax: (512) 225-2801
Email: rdimasi@bddglaw.com

(2 Yr Term Exp 2018)

Catherine L. Hanna
Hanna & Plaut, L.L.P
211 E.7th Street, Suite 600
Austin, TX 78701
Ph: (512) 472-7700
Fax: (512) 472-0205
Email: channa@hannaplaut.com

(2 Yr Term Exp 2018)

Jason C. McLaurin
Strong Pipkin Bissell & Ledyard, L.L.P.
4900 Woodway Dr., Ste. 1200
Houston, TX 77056
Ph: (713) 210-4379
Fax: (713) 651-1920
Email: jmclaurin@strongpipkin.com

(2 Yr Term Exp 2018)

Stephen A. Melendi
Tollefson Bradley Mitchell & Melendi, LLP
2811 McKinney Avenue, Suite 250
Dallas, TX 75204
Ph: (214) 665-0100
Fax: (214) 665-0199
Email: stephenm@tbmmlaw.com

(2 Yr Term Exp 2018)

Candace A. Ourso
Hall Maines Lugrin PC
2800 Post Oak Blvd., Suite 6400
Houston, TX 77056
Ph: (713) 871-9000
Fax: (713) 871-8962
Email: courso@hallmaineslugrin.com

Executive Director

Donna J. Passons
Texas Institute of CLE
P.O. Box 4646
Austin, TX 78765
Ph: (512) 451-6960
Fax: (512) 451-2911
Email: donna@clesolutions.com

Judicial Liaison

Hon. Justin "Brett" Busby
14th Court of Appeals
301 Fannin St., Ste. 245
Houston, TX 77002
Ph: (713) 274-2800

Council Advisor

Fidel Rodriguez, Jr.
Law Offices of Fidel Rodriguez, Jr.
111 Soledad St., Ste. 1300
San Antonio, TX 78205
Ph: (210) 224-1057
Fax: (210) 224-0533

Council Advisor Alternate

Michael "Carter" Crow
Norton Rose Fulbright US LLP
1301 McKinney St., Ste. 5100
Houston, TX 77010
Ph: (713) 651-5218
Fax: (713) 651-5246
carter.crow@nortonrosefulbright.com

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InsuranceLawSection.org

The Journal of Texas Insurance Law is published by the Insurance Law Section of the State Bar of Texas. The purpose of the *Journal* is to provide Section members with current legal articles and analysis regarding recent developments in all aspects of Texas insurance law, as well as convey news of Section activities and other events pertaining to this area of law.

Anyone interested in submitting a manuscript for publication should contact Pamella Hopper, Editor In Chief, at (512) 617-4504 or by email at phopper@mcguirewoods.com. Manuscripts for publication must be typed double-spaced with endnotes (PC-compatible disks are appreciated). Replies to articles published in the *Journal* are welcome.

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Mission Statement

The Insurance Law Section serves to promote the understanding and development of Texas insurance law by providing high quality educational resources to the bench, bar, and public and by promoting collegiality among those with an interest in insurance law.

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FROM THE EDITOR

By William J. Chriss
Gravely & Pearson, LLP

This issue of the *Journal* represents my last after three years as editor-in-chief. So, I am grateful to have this opportunity to thank all the people who made my tenure so rewarding, including all our associate editors and authors. Two people require particular mention.

The first, Pam Hopper, has served as assistant editor for a year now, and unbeknownst to our readers, she has been primarily responsible for editing and producing the last few issues of the *Journal*. So, the entire Insurance Law Section already knows that Pam will do a magnificent job of continuing to lead this publication when she formally replaces me next issue as editor-in-chief.

The second person, fittingly enough, is the man to whom this issue is dedicated, Mark Kincaid, whom Joe Longley aptly describes herein as "the policyholder's lawyer." In addition to Joe's article, this issue includes tributes by Phil Maxwell and Vince Morgan, as well as other articles and material cataloguing Mark's career.

Mark was instrumental in defeating attempts in the last legislative session to eviscerate consumer protections found in Article 542 of the Insurance Code (the Prompt Payment statute). He spent countless volunteer hours organizing hearing testimony and meeting with supporters and opponents of the defeated bills described in the last part of Alexandra Fernandez's article in this issue. As noted in the pages that follow, Mark's notes and papers have been accepted by the Texas Legislative Reference Library as an addition to its DTPA/Insurance Code Collection, so that all Texans can benefit from his contributions to Texas insurance legislation.

Mark also spearheaded the successful effort to promulgate pattern jury charges in insurance cases, and as further described in this issue, *Vail* was perhaps the most influential of his many victories as an appellate advocate for insureds. But as anyone who knew Mark Kincaid can well attest, it was the personal and not the professional in him that made the more lasting impression. I am reminded of Maya Angelou's maxim that "people will forget what you said; people will forget what you did; but people will never forget how you made them feel." In my own case I knew Mark for decades. We did similar legal work; we served together on the Pattern Jury Charge Committee and the Insurance Law Council; we were colleagues; but most importantly we were friends. It was a blessing that the last time I saw Mark, we were drinking with friends after a long day of insurance law continuing education, and he turned to me without warning and said, "You know man, I love you. You are really cool." Those were the last words he ever spoke to me, and here I can only repeat my response: "I love you too, brother; I love you too." We all do.

William J. Chriss
Publications Editor

William J. Chriss, of counsel to Gravely & Pearson, LLP, graduated from Harvard Law School and holds graduate degrees in History, Theology, and Political Science, including a Ph.D. in History from The University of Texas. His dissertation under H.W. Brands, Six Constitutions over Texas, was a constitutional history of the state. He has practiced insurance, trial, and appellate law for over twenty-five years and currently serves as editor-in-chief of the *Journal of Texas Insurance Law* and co-editor of the Appellate Advocate. He is a member of the American Law Institute and serves as vice-chair of the Texas Pattern Jury Charge Committee on Business, Consumer, Employment, and Insurance Law.

Comments

FROM THE CHAIR

By J. James Cooper

As my term as Chair comes to a close, I am reminded of the old saying that the absolute best position to hold in any organization is that of "Past Chair." I am particularly honored to join the distinguished group of past chairs of the Insurance Law Section of the State Bar of Texas—dedicated practitioners who have created an indelible imprint on Texas insurance law.

With the help of our talented and committed 2015–2016 Officers, Council and volunteers, I can sit back as a Past Chair knowing we knocked our year out of the ballpark. Our inaugural South Texas Insurance Law CLE event in February was a terrific success, reaching an area of the state not often targeted. Likewise, the November 2015 University of Texas Insurance Law Institute in Dallas and recent State Bar of Texas Advanced Insurance Law Seminar in San Antonio were well-attended and received rave reviews. And you won't want to miss the 21st Annual Insurance Law Institute in Houston this November 10–11, 2016—your Insurance Law Section is co-sponsoring this program with University of Texas Law-CLE. Our new Insurance Law Webinar series has resulted in three consecutive hot topic presentations by qualified and knowledgeable speakers. The committee structure is established and running smoothly. The Insurance Law Section website (www.insurancelawsection.org) has had a plethora of additional conference materials, new articles and past *Journals* added in the past year (with more still to come!) The *Journal* is churning out high-quality articles and issues on a regular basis, and our "Right Off the Press" team continues to keep up us to date with the latest cases each and every week.

Sadly, we lost a Texas legend this year—Mark Kincaid. Mark was a towering presence in Texas insurance law, and he will be sorely missed. You will read more about Mark, and his many achievements, in this issue of the Journal.

There are far too many people to thank by name in this small space, but it was my honor and privilege to serve with all of you. At the beginning of my term, I stated that my goal was to continue the tradition of leaving our next Chair with an even better Section. I can unequivocally say that we have achieved that goal. And now, Chair-Elect Kimberly Steele, I give you the same advice that President Ronald Reagan gave to his successor, President George H.W. Bush: "Don't let the turkeys get you down."

Best,

Chair, Insurance Law Section

By Joe K. Longley

THE POLICYHOLDER'S LAWYER MARK L. KINCAID 1959–2016

I first met Mark Kincaid in 1981 when he was a young law student seeking to be a law clerk at Longley & Maxwell. He got the job. This commenced a beautiful relationship that lasted 35 years until his untimely death earlier this year at age 56. It was during those 35 years that Mark became the undisputed guru, jefe, and expert on first-party insurance claims in the State of Texas. Whether Texas policyholders knew it or not—Mark Kincaid had become their lawyer!

In that 35 year period, Mark distinguished himself as a triple threat.

First, he was a trial lawyer—always going full throttle to best represent his consumer/policyholder clients—as a fair and ethical advocate on their behalf.

Next, as an appellate lawyer, he deftly wove his finely-tuned arguments in his soft-spoken style to establish insurance precedents that will guide yet unborn judges in their distillation of justice.

But his most impressive skills took place not in the courtroom, but in the granite halls of the Texas Capitol Building. It was there that Mark Kincaid established his reputation for crafting public policy for the protection of policyholders who had little or no ability to prevent insurer abuses in the claims process.

Mark's dedication and devotion to policyholder protection was incredible. Texas had not seen anyone so laser-focused since the days of Reconstruction when determined lawmakers protected family homesteads from abuses practiced by greedy carpetbaggers and scalawags.

From 1981 until 2015, Phil Maxwell and I personally bore witness to the development of Mark's legendary talent.

Besides spending a lot of time together at the legislature, Mark and I tried twelve jury trials to verdict and were co-counsel on numerous insurance law appeals—including *Vail v. Texas Farm Bureau Mutual Insurance Company*.

Vail, it turns out, was the seminal case on the judicial application of the Texas Insurance Code's prohibition of "unfair practices in the business of insurance" to *unfair settlement practices.* Although not apparent at the time, it also began Mark's coupling of appellate advocacy with the rough and tumble "art of the possible" required for success in the legislature. Thus, 1988 was the year when Mark's artful advocacy skills took flight on behalf of an aggrieved policyholder.

Vail was decided in 1988 by a divided Texas Supreme Court. It was issued close to when "tort reform" was beginning to gain traction in the Texas Legislature—however, due to intervening political events, it was another seven years before *Vail* came to the specific attention of "tort reforming" legislators.

In 1995, when that time finally came, all of Mark's developing talents would be needed.

But first—some background.

In 1987, without using the words "tort reform," the Legislature created an Interim Joint Committee on Deceptive Trade Practices to study what legislative changes, including insurance, should be recommended to the January 1989 Legislature.

Yours truly was appointed as a "civilian" member of that Committee. In that role, I began dragging Mark along to its meetings hoping to use his superior intellect to stop any truly harmful change from being recommended to the DTPA and/or the Insurance Code, then codified as article 21.21. It became immediately apparent that Mark was a natural in applying his judicial acumen to the somewhat less polite business of lawmaking. He was, at the same time, legal expert and scholar—but also the soft-spoken common-sense friend to the Committee.

When the Committee closed its proceedings in 1988, it issued an Interim Report to the Legislature making *no recommendations* for any changes to either the DTPA or article 21.21.

Thus, with tort reform rapidly becoming legislatively "fashionable," both the DTPA and article 21.21 were spared

Joe K. Longley (www.joelongley.com) was the principal drafter of the DTPA, as well as the private remedies now found in Chapters 541 & 542 of the Insurance Code. In 2000, Texas Lawyer named him to its initial list of 100 Texas Legal Legends and, in 2003, selected him as its "Go-To-Lawyer" for Insurance Law. He has taught Insurance Law at UT Law School and, in 2011, was recipient of the Insurance Section Council's Insurance Legend award.

any major focus in the 1989 session. More importantly, Mark Kincaid was two years into his wizard internship of coupling trial and appellate advocacy with explaining, *in understandable terms*, the consequences of insurance law amendments being retailed by hundreds of insurance lobbyists. Very quickly, Mark gained the respect and trust of most, if not all, Texas lawmakers.

But 1990 brought a huge surprise putting "tort reform" temporarily on hold. Ann Richards was elected Governor.

Consequently, instead of defending policyholders' hard-won protections against weakening amendments from tort reformers in 1991, Mark got to play offense.

Mark participated in co-drafting the claims handling portions of H.B. 2—then described as "the most comprehensive insurance reform legislation in Texas history." This resulted in H.B. 2 enacting the first "prompt pay" provisions of the modern era involving "any insurer"—plus the section placing the burden of proof squarely on the insurer regarding any policy "language of exclusion."

H.B. 2 also established OPIC, the Office of Public Insurance Counsel—an office to which Mark would soon be appointed by Governor Richards in 1994.

But the tort reform "time out" did not last long.

1994 was the year Ann Richards lost to George W. Bush, bringing tort reformers back to the forefront. Emboldened with new-found power, they had the DTPA and article 21.21 targeted squarely within their crosshairs.

Thus, 1995 found Mark out of the job at OPIC and faced with the postponed 1989 legislative "showdown" over *Vail.* Legislative repeal of *Vail* loomed as a certainty—and H.B. 668 was the tort reformers' chosen vehicle.

But Mark had other plans and welcomed the challenge.

For five months in 1995, Mark and I camped out in the legislature as the enactment of H.B. 668 threatened the imminent demise of the DTPA and article 21.21. The fight was furious with emotions running high on both sides. While I lambasted the opposition daily with all the political fire I could muster, Mark kept right on plodding with his civility and unmistakable dedication to truth, right, and justice.

In April of 1995, after House sponsors came with an unacceptable committee substitute, both sides were "ordered" into private negotiations by the leadership of both the House and Senate. It was at this point that, due to an intemperate act on my part, Mark took over the entire opposition to H.B. 668. It was the best thing that happened for consumer/policyholder interests during the entire 1995 Session!

Rather than facing the legislative repeal of *Vail*, Mark single-handedly engineered its legislative codification through amending H.B. 668 to include section 4(10) to article 21.21 prohibiting certain defined "unfair settlement practices." Today, that section is found in section 541.060 of the 2005 recodification of the Code and includes the very conduct the *Vail* court declared to be an unfair settlement practice in 1988.

Mark immediately put on his legal scholar hat and went to work documenting the legislative history of H.B. 668 to establish its legislative intent.

On May 25, 1995, Mark authored a CLE article published for the State Bar's Eighth Advanced DTPA/Insurance/Consumer Law Course that reached iconic status for "legislative intent" researchers.[1]

This article became doubly important when it was cited as authority by the tort reform sponsors themselves throughout their comprehensive 1996 Texas Tech Law Review article regarding H.B. 668's legislative history.[2]

Mark's crafting of *Vail*'s legislative codification did not go unrecognized by the bill sponsors:

> ***The 74th Legislature added these new sections to assure that insureds retain protection against certain unfair settlement practices***, despite the elimination of certain claims based on violations of Insurance Commission rules. ***As one commentator has observed***, "the Legislature has clearly shown its intent that such conduct [involving unfair insurance practices exhibited by an insurer against an insured] remain subject to enforcement by a private cause of action (emphasis added). [Of course, **that *commentator*** was our very own hero**—Mark Kincaid].**[3]

Apart from engineering the codification of *Vail*, Mark was totally successful in saving the DTPA and Insurance Code private remedies from any fatal harm. Thus, 1995 established Mark Kincaid as *the* policyholder advocate to be reckoned with in future years.

This reckoning was most recently encountered in 2015.

New lawmakers came after *Vail* once again—but for a different part of its holding.

In January 2015, S.B. 1628 was introduced that would have legislatively overruled the *Vail* holding that "damage is, at a minimum, the amount of policy proceeds wrongfully withheld by Texas Farm." It provided:

> (b) For purposes of this subchapter, "actual damages" means an injury independent of the harm resulting from the insurer's denial of policy benefits. The policy benefits wrongfully withheld, as well as any attorney's fees or costs incurred to recover those policy benefits, do not constitute "actual damages" for purposes of this subchapter.

However, largely due to Mark's efforts, this latest attempt to repeal *Vail*'s damage holding was rejected on April 30, 2015 through adoption of Floor Amendment #3 by the Texas Senate. The bill itself then failed to pass and died in the House Calendars Committee during the waning days of the 2015 Session.

Thus, recovery of actual damages for unfair settlement practices, including the policy benefits themselves, was left undisturbed thanks to the advocacy of Mark Kincaid, the policyholders' lawyer.

This was the legacy of Mark Kincaid. He suffered a brain aneurysm on the afternoon of December 31, 2015, which ultimately caused his death on January 19, 2016.

1 *See* Kincaid; *Unfair Insurance Practices—The Law Under Vail, Watson & the 1995 Amendments*; State Bar of Texas 1995.

2 *See* Bivins, Montford, Hunter, Junell, Duncan and Shannon; *The 1995 Revisions to the DTPA: Altering the Landscape,* 27 Tex. Tech L. Rev. 1441 (1996).

3 See *supra*, 27 Tex. Tech L. Rev. at 1473.

By Phil Maxwell

MAKING HIS MARK ON THE LAW—MARK KINCAID AND THE TEXAS PATTERN JURY CHARGES ON INSURANCE AND CONSUMER LAW

I join in Joe Longley's tribute to Mark, as it could have been my own. Both of us tried, briefed, and argued cases with him, both of us appeared with him before the Legislature and, if we can claim just a little credit for what we are most proud of, we helped channel Mark's native ability and intelligence into what became the burning passion of his too short life—protecting the right of every Texan to truth and fair dealing. I remember as if it were yesterday a short, but very important conversation with Mark in front of the Brown Building where Joe and I practiced for many years and where Mark had worked during law school. Mark was just finishing his clerkship with Texas Supreme Court Justice Franklin Spears and was trying to decide what his next step should be. Mark knew that my first law job had been in Washington and he wanted my advice on whether he should apply with the Civil Rights Division of the Department of Justice where he thought he could "really help people who needed it." I told Mark that there were a lot of people who "really needed help right here in Texas" and that a whole bunch of them were Longley & Maxwell clients "right upstairs." I told Mark that the federal government was slow to bring enforcement actions of any kind and that, as he knew, there was nothing "slow" about Longley & Maxwell's private enforcement actions. I then told Mark what he already knew: "Joe and I want you to get upstairs and get to work the minute you leave the court." He did. And the rest of the story is writ large in the many ways that Mark gave the people of Texas "the help they really needed."

But while Joe and I shared so much of Mark's work life, I had the added privilege of serving with him on the State Bar Committee entrusted with writing pattern jury charges for insurance, DTPA and other important commercial and employment causes of action. Joe and I, along with David Bragg, had taken the first crack at DTPA and insurance jury charges in our *Texas Consumer Litigation*. Soon after it was published, the Bar created the Pattern Jury Charge Committee on Business and Consumer devoted to that project, and I was appointed to serve. When the membership of the Committee expanded, I recommended Mark be appointed, and he served with distinction for many years as its Chair and then as an active member until his death.

In order to understand the importance of Mark's work on the committee, remember how important the work of the committee is—deciding what juries will be told the law is. Of course, judges tell the jury what the law is, but only in exceptional circumstances do judges depart from "what's in the book." Converting what the appellate courts and the legislature have said into hopefully workable and understandable language is the PJC's whole reason for being. Since the law is constantly changing (I started to say "evolving" but that is not always accurate), the work of the Committee to make sense of it all never ends. And this holds especially true in insurance and consumer law, because the legislature and the courts speak often in these areas. Because Mark was a leading expert in insurance and consumer law, the Committee naturally looked to him for guidance.

But it was not just his expertise that was so important in the Committee's work. It was his manner of working with people that was the key to his success. Healthy egos and strong opinions (even on things one may not know anything about) are not in short supply whenever lawyers meet. Nor is the love of argument. While vigorous debate helps define issues and sharpen analysis, it can also be a deadly enemy of progress. Mark knew this. And so Mark rarely argued. What he did instead was listen—intently and respectfully—to those holding opposing positions. When he responded, it was with, "I know it must be me, but I'm having a little trouble trying to understand just what you're thinking. Could you help me here?" Or, "I really want to understand because if I am wrong I want to know it." These were not just tactics. Mark really *did* want to know if he was wrong,

Phil Maxwell is a former Chief of the Consumer Protection Division, Texas Attorney General's Office and was named by Texas Lawyer as one of the state's "One Hundred Legal Legends," along with former partner, Joe Longley, for their contribution to consumer law in Texas. He is co-author of Texas Consumer Litigation, along with David Bragg and Joe Longley, and has served as adjunct professor at the University of Texas School of Law, teaching insurance law and professional responsibility in the L.LM program. Phil is a past chair and current member of the State Bar's Texas Pattern Jury Charge Committee for Business, Consumer, Insurance and Employment.

but because he was generally so much better prepared, he rarely was. When Mark spoke his turn, he led with, "Here's what I have been able to figure out," and never with, "The court clearly held." Everyone was respected, listened to, and gently brought to consensus. As a result, the Committee's work got done and we all left the meetings thinking we had done it. Without Mark's help, we never would have.

Mark, you were taken from us too soon. Yet you did so much for us while you were here. In the courts, in the legislature, in teaching, in writing, and in our Committee, you left a lasting mark on the law. Thanks for your help. We really needed it.

By Roger D. Sanders with Michael W. Huddleston

REMEMBERING *VAIL* AND ONE OF ITS ARCHITECTS

Usually the story of fine legal journals unfolds with particular images or minute facts. The dark, wizened widow reached for the lawyer's hand; the police officer brushed his sandy locks back, smiling curiously.

Not here. It's been too many years to honestly relay the minute facts. But there are images, sweeping recollections of a sweaty, squeaky-voiced, bow-legged cowboy that a judge—my former partner, Ray Grisham—had sent my way. Melvin Vail was the victim, he proclaimed, of a damned insurance company's refusal to pay for his burned house. This was back in the day when all the burned, insured houses started with the company's presumption of arson. Even the ones struck by lightning.

It was early in my career, when I believed clients told all the truth. After talking to Melvin, I knew he was innocent, Texas Farm Bureau, guilty. It was simple. Except their excellent advocate, Webber Beall of Touchstone Bernays didn't see it that way, fighting me every step of the way, and then some. So, we deposed and prepared and got ready for trial. And on a hot day in 1983, we appeared before Judge R.C. Vaughn, a stately figure who looked like Texas history itself. With swept, neat white hair, he kept detailed notes in a reporter's notebook, jotting down—it seemed—every word. He rarely looked up, using his nibbed-fountain pen in a way few men did in the 1980s. The jury was friendly enough, but I was too young to really know. It was early in my career, when I believed too much and knew way too little.

Melvin was a downright picture. Squeaky voice, barrel chest, skinny legs, cowboy boots, and divorced with children *and* a sordid reputation, at least according to the credit report that inexplicably Judge Vaughn let into evidence. He publicly kicked dogs; he yelled at women, and perhaps, it was hinted, hit them; he burned his house down, even starting the fire with his ten-year-old son asleep inside. Rude, crude, and mean would be a fair assessment of the behind-the-scenes credit report the jury heard. Melvin was not moved to remorse or self-examination, at least so far as the jury could see. Of course, I can't repeat private attorney-client communications, but the report, coupled with Melvin's high-pitched voice and cocky attitude—imagine Donald Trump with little money, less hair, and no bodyguards—left me wondering how we were going to navigate the case. But, thankfully, there was the insurance company.

I had no litigation budget. Melvin was clear that he had no money to put into the case that he claimed Judge Grisham had told him wasn't to cost him a dime. And who was I to disappoint a sitting judge? So, unlike today with reams of documents and lots of experts, I managed—with my faithful paralegal, Sandi Gamblin—to put together the documents we had, along with a secret weapon. We had an expert. A real expert. He was an ex-FBI lab employee who knew arson. He went up against the insurance company's bolo-tied, turquoise-ringed expert who stopped the court reporter in front of the jury to clearly spell out his name so that the jury might properly attribute the anticipated magnificence of his courtroom performance to the right man. He was all kinds of up-to-date. He knew the rules. He knew the science. He had explanations about flash points and origins and gas chromatographs that boiled and distilled the ashes taken from four analytically significant locations around the incinerated house foundation to confirm that there was just one hot spot that he, as an expert, could opine with certainty was THE spot where Mr. Vail must have—in fact, did—pour a highly flammable accelerant out, lighting it on the way out of his house without his ten-year-old son. That's a lot of words, but it was Texas Farm Bureau's case.

It was so convincing that I wondered if we had a chance. Webber Beall was smooth as silk in defense, the expert

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Roger D. Sanders, partner in Sanders, O'Hanlon, Motley, Young & Gallardo of Sherman, Texas, has been a self-described "typical Texas country lawyer doing the Lord's work," representing individuals and small businesses for more than four decades. He has handled complex cases protecting small businesses' intellectual and tangible property against Fortune 500 companies, defending borrowers against over-reaching banks, enforcing individual's contract rights, defending citizens against government over-reach in condemnation and civil rights cases, protecting consumers from fraud and abuse, and otherwise representing the "little guy." He also taught Business Law and Organizations for several years at Austin College.

Michael W. Huddleston is an equity partner with Munsch Hardt Kopf & Harr, P.C., located in Dallas, with a state-wide practice. He is the Chair of the Insurance Recovery Practice Group at the firm. Huddleston represents commercial policyholders and assists claimants against insurance carriers in all lines of coverage. He is a Past-Chair of the Insurance Section of the State Bar of Texas. He is a Fellow in the American College of Contractual and Extra-Contractual Counsel.

flawless in experience, reputation, and logic, and my client, as the insurance company painted him, was a dog-kicking reprobate.

But we had a real expert. He had prepared me to know something no one else knew; at least not until their arson expert was on cross-examination. You see, there were four cans of ashes taken from the site. Well, actually more than that if you count the first insurance-company expert who said it wasn't arson. But the second one, this one, could find sure-fire arson in a bowl of Cheerios. He testified on direct that there were four-gallon cans that looked like paint cans, with tight lids pounded in after he had methodically taken ash samples from around the burned foundation area and then boiled each can, taking the resulting liquid from each of the four cans and burning it in the gas chromatograph to see what chemical compositions were revealed when those liquids were tested. A gas chromatograph then analyzed the liquids to show whether accelerants like kerosene or gasoline showed up chemically. The resulting graphs looked a little like a lie-detector chart: long, detailed in its markings, and providing signature findings to support the conclusions. Texas Farm Bureau's expert opined, after looking at the four charts, that they conclusively showed accelerants in one particular place, differing from linoleum or lacquers on wood flooring or drapes made of petroleum products. And he testified that process was why the sample cans contained the muddy remains of the boiling, distilling process. That's spelled gas c-h-r-o-m-a-t-o-g-r-a-p-h, as he would say it.

The expert proudly and authoritatively explained to the jury how the resulting charts were like fingerprints of the fire, with no two being alike, just like human finger prints. And when you looked at all of them, well, he just had no choice but to conclude that there was a clear pattern of accelerants present, even if his hapless insurance company predecessor arson expert couldn't find it, poor soul.

I still remember seeing him gradually grow less sure, as I asked him to humor me to open up the various cans so the jury could see better his process. Each can contained the mud left from boiling the ashes for the chemical analysis. Can 1, fine. Can 2, fine. Can 3, fine. Can 4, not so fine, for can 4 was still filled with ashes. Dry, dusty ashes filtering down though my fingers as I dipped my hand into the can. It evidently had never been boiled. But the expert, after an immodest period of sputtering, explained that while he didn't know how the mud had dried out, there were four of those gas chromatograph charts, and so surely there must have been a fifth can and somehow the other ash-mud-filled can had gotten swapped. No problem. He was still convinced that it was arson.

So I asked him to compare, in front of the jury he was impressing, the detailed "fingerprint" gas chromatograph print-outs from Can 1 and Can 4. He struggled a bit, with some quick explanations about how that might not be precise, this not being in a lab and all. So, I helped him out by holding them precisely aligned and up to the light so that the jury could see that the two charts of identical chemical fingerprints matched precisely. The jury was not amused. Webber was sputtering. The witness was sputtering. Melvin was grinning.

The last witness in the case was the Texas Farm Bureau state claims manager. He obliged by saying that, after hearing all the evidence, he'd do the same thing again, even in light of the bolo-tie, turquoise opinions of his second expert: deny the claim for arson. I thanked him, as the jury must have, for the clarity it brought to the issue. They returned a verdict for the full policy amount, $25,000 on the structure and $10,000 for contents, trebled the damages, and awarded handsome attorneys' fees of $12,640. The total judgment amounted to $140,509.84, plus interest and costs. But the jury did something else before they left the court room: they refused to shake my client's extended hand. And they refused to shake Webber's extended hand. Some came over and hugged my neck, one telling me that it was obvious I was a young lawyer and they appreciated my effort. But, one said while another nodded, "Get another suit." It seems my one navy pinstripe suit had tell-tale signs of baby spit-up over my right shoulder, which they had seen on the first day of trial, but I had not. Look, in those days an $85 Linxweiler Men's Store suit had to last.

The jury gave us damages of the sort that the DTPA and Insurance Code were intended: actual property damages set by the insurance policy, treble damages, and attorneys' fees. The appellate journey very quickly began, and it was a bumpy ride indeed.

Texas law was very much in a state of flux as *Vail* began its journey through the appellate courts. Numerous cases were working their way through the appellate courts that would eventually join with the decision in *Vail* to greatly broaden and expand the extra-contractual exposure for first-party insurance carriers.

The Dallas Court of Appeals provided the intermediate review of the *Vail* judgment. Webber deferred the handling of the appeal for the insurance company to Sid Davis, Jr., one of the best defense appellate lawyers in Dallas. Justice Keith wrote the extremely brief opinion of the court.

The Dallas court began by noting that after a barrage of special exceptions, Plaintiff was left at the time of trial with two theories:

> [1] . . . Defendant violated the TEX.BUS. and COMM.CODE, § 17.50(a)(4) by employing or using acts which violate Art. 21.21 of the Texas Insurance Code, or rules and regulations issued by the State Board of Insurance under said Art.

> 21.21, as follows: . . . (b) By engaging in practices contrary to Sec. 4 of Insurance Board Order 18663, Sec. (a), which acts were unfair or deceptive, as defined by Art. 21.21–2, Sec. 2(d) by not attempting in good faith to effectuate prompt, fair and equitable settlements of claims submitted in which liability has become reasonably clear.
>
> [2] In the alternative, Defendant violated a common law duty of good faith or conscionable conduct, in investigating, processing and denying Plaintiff's claim under the insurance policy in question.[1]

The jury answered the following "Special Issue No. 3" as to the statutory theory:

> Do you find from a preponderance of the evidence that the Defendant, after it became reasonably clear that Defendant was liable under the policy in question, if you have so found, prior to the filing of this suit, *did not attempt in good faith to effectuate prompt, fair, and equitable settlement of the claim submitted by the Plaintiffs*?
>
> *Answer:* They did not so attempt."[2]

The Dallas court noted that the fulcrum of the Vails' liability theory, section 4(a) of State Board of Insurance Regulation No. 18663, "has as its statutory base the provisions of article 21.21–2 of the Texas Insurance Code (Vernon 1981), but section 2 of this statute does not purport to create a private cause of action."[3] The court followed the Northern District ruling in *McKnight v. Ideal Mutual Insurance Co.*,[4] that "neither article 21.21–2 nor DTPA 'confers a private right' for unfair claims settlement cases."[5]

The Dallas court swiftly disposed of our arguments for a duty of good faith. The argued basis of the duty was the holding in *G.A. Stowers Furniture Co. v. American Indemnity Co.*,[6] that an insurer has "liability for fraudulent conduct, or *lack of good faith, in refusing to settle*."[7] The Dallas Court of Appeals held that *Stowers* was limited to third-party liability insurance carriers and thus the duty had no application to a first-party insurer such as Texas Farm Bureau.[8]

So, as of June 28, 1985, Vail's treble damages were taken away. He was left with recovery of only the contract benefits, interest, and the same monstrous award of $12,640 in attorneys' fees.

After the court of appeal's decision, we were joined by avowed DTPA master, Joe Longley, and his brilliant young partner, Mark Kincaid. In May of 1988, three long years later, the original recovery was restored and Texas law greatly expanded. That's the public picture. The less public picture during the interim had to do with family issues, Melvin and Maryann's divorce, sorting out client loyalty issues, Melvin being charged with molesting a child (for which the complaining witness did not show up when the criminal case was called for trial), and Melvin's death, all of which happened while the case was on appeal.

In fact, Melvin died before the filing of the application for writ of error on October 4, 1985. The writ was not granted until July 15, 1987, almost two years later. The application focused on the appropriateness of the statutory claims and the duty of good faith, particularly as expressed in *Stowers*. It was very clear that the only damages sought—and thus subject to trebling—were the lost contract benefits. The application addressed the carrier's argument that no damages were caused by the supposed improper or bad faith conduct. The carrier argued that lost contract benefits are not damages caused by bad faith conduct. The "Conclusion" to the application really says it all and more:

> In summary, Vail asks the Court to consider the remedial nature of the D.T.P.A., §17.44. and to, announce clearly the error of the Court of Appeals in declaring no private right of action for insured against an insurer which grossly contorts the claims process through its admitted bad faith. After six years—and the death of Mr. Vail—this case winds slowly up the appellate steps with Farm Bureau still clutching every nickel of Vail's premiums, and paying nothing. From this position of moral quicksand Farm Bureau claims there should be no consequence to its proven—and now conceded—connivance, deceit, and bad faith. With no more substance than a worn out fig leaf Farm Bureau defends itself alone on the nature of the product it sells: insurance policies. Somehow because the misrepresented service is part insurance policy, the insurer is to be immune. This rationale is unutterably repugnant. A crook can wear a cloak—including the suit of a Farm Bureau executive or agent who schemes to deny claims he (or his company) have earlier promised to pay. The nature of the product is no defense. If the D.T.P.A. and the Insurance Code are to have meaning, there must be some relief available to the Vails, and those like them who are intentionally wronged. In holding to the contrary the Court of Appeals erred.[9]

In 1986 and 1987, the tide began to turn on a number of issues involved in *Vail*, particularly as to the duty of good

faith. On January 28, 1987, the Texas Supreme Court held in *Arnold v. National County Mutual Fire Insurance Co*. that a duty of good faith did exist as to first-party insurers, citing *Stowers* and thus *sub silencio* rejecting the basis for the Dallas court's rejection of this theory in *Vail*.[10]

In July of 1987, the Texas Supreme Court issued its decision in *Chitsey v. National Lloyds Insurance Co*.[11] The statutory claims made in that case, like those in *Vail*, revolved around Section 16(a) of article 21.21, which declared that a cause of action for trebling actual damages may be brought by:

> Any person who has been injured by another's engaging in [1] any of the practices declared in Section 4 of this Article *or [2] in rules or regulations lawfully adopted by the Board under this Article* to be unfair methods of competition and unfair and deceptive acts or practices in the business of insurance or [3] in any practice defined by Section 17.46 of the Business & Commerce Code, as amended, as an unlawful deceptive trade practice . . . .[12]

The plaintiffs attempted to channel their claim through Board Order No. 41060, which provided in part: "Irrespective of the fact that the improper trade practice is not defined in any other section of these Rules and Regulations, no person shall engage in this State in any trade practice which is determined pursuant by law to be an unfair method of competition or an unfair or deceptive act or practice in the business of insurance."[13] The plaintiffs, however, pointed only to a jury finding as the "determination" of unfair methods of practice.[14]

The supreme court rejected this theory, noting: "A jury finding that one has engaged in prohibited conduct cannot be substituted for a declaration of what conduct is prohibited. A jury's role is to decide matters of fact and not matters of law."[15] The court suggested such an incorporation of another Board Order No. 41454 (Aug. 10, 1982) would have been appropriate, but it was not submitted or proven.[16] *Chitsey* certainly suggested the statutory path to treble damages in *Vail* might not be easy, or perhaps not even possible.

Vail was argued in November of 1987. Mark Kincaid opened and Joe Longley closed. The carrier was again represented by Sid Davis of the Touchstone firm. Finally, in May of 1988, the Texas Supreme Court reached a decision.

The supreme court in *Vail* held that there was in fact a right to recover under the DTPA and the Insurance Code for unfair claims settlement practices. The court noted a number of steps necessary to get to that conclusion in *Vail*. First, section 17.50(a)(4) of the DTPA makes actionable the "use or employment by any person of an act or practice in violation of Art. 21.21, Texas Insurance Code, as amended, or rules and regulations issued by the State Board of Insurance under Art. 21.21, Texas Insurance Code, as amended."[17] Second, the DTPA thus incorporates section 16 of 21.21 of the Insurance Code, which permits recovery as well for:

> [1]any of the practices declared to be unfair or deceptive by Section 4 of article 21.21;
>
> [2]conduct defined in rules or regulations lawfully adopted by the Board under article 21.21 as unfair methods of competition and unfair or deceptive acts or practices in the business of insurance; or
>
> [3]any practice defined by Section 17.46 of the Business & Commerce Code, as amended, as an unlawful deceptive trade practice. Tex. Ins. Code Ann. art. 21.21, § 16(a) (Vernon Supp.1988).[18]

This is essentially the first step. The second comes through the incorporation of "regulations." As the court noted, the Vails argued that State Board of Insurance, Board Order 18663[19] itself had a section 4 permitting further incorporation of any practice (a) defined by the Insurance Code or regulations or rules to be unfair, and (b) any practice "determined pursuant to law" to be unfair.[20]

The court found that article 21.21-2, section 2(d) (defining as an unfair practice failing to attempt to settle when liability is reasonably clear) was in fact incorporated through 4(a) the Board Order despite the fact that that provision had been found to have not been intended to provide a private right of action.[21] The court recognized that in fact the Vails were not attempting to recover under 21.21-2. The source of the right of recovery came from section 17.50(a)(4) of the DTPA and article 21.21, § 16 of the Insurance Code.[22]

Distinguishing *Chitsey*, the supreme court stated that "[w]hile a jury finding does not constitute 'a determination of law,' this court is empowered to determine whether conduct constitutes an unfair or deceptive act."[23] Such a determination, the court held, could be incorporated through section 4(b) of Board Order 18663. Thus, the court held that its adoption of the duty of good faith in *Arnold* and *Aranda v. Insurance Co. of North America*[24] amounted to such a determination.[25] Alternatively, the court found that treble damages were also recoverable because section 16 of 21.21 itself incorporates the "laundry list" of prohibited conduct in the DTPA under section 17.46, along with "unlisted" deceptive acts noted in that provision. The jury finding that the carrier "failed to exercise good faith in the investigation, processing, and denial of the claim" supported this recovery as well.[26]

Importantly, the Texas Supreme Court directly addressed whether the loss of contract benefits could ever be a form of

actual damages recoverable for either statutory or common-law bad-faith claims practices. The court framed the argument as follows: "Texas Farm contends that the Vails cannot recover on the basis of Texas Farm's conduct after the home was destroyed by fire because the Vails only claimed damages recoverable under the insurance contract."[27] The court concluded:

> We hold that an insurer's unfair refusal to pay the insured's claim causes damages as a matter of law in at least the amount of the policy benefits wrongfully withheld. *Aetna Casualty & Surety Co. v. Marshall*, 724 S.W.2d 770, 771–72 (Tex. 1987); *Royal Ins. Globe Co. v. Bar Consultants, Inc.*, 577 S.W.2d 688, 694 (Tex.1979); *Allstate Ins. Co. v. Kelly*, 680 S.W.2d 595, 605 (Tex. App.—Tyler 1984, writ ref'd n.r.e.). The Vails suffered a loss at the time of the fire for which they were entitled to make a claim under the insurance policy. It was not until Texas Farm wrongfully denied the claim that the Vails' loss was transformed into a legal *damage*. That damage is, at minimum, the amount of policy proceeds wrongfully withheld by Texas Farm.[28]

Vail is still good law. The federal courts are simply effectively ignoring it.

The court emphasized that the fact that the denial spawned a breach-of-contract action along with extra-contractual claims did not preclude recovery of the policy benefits in an extra-contractual suit. The court reasoned:

> It would be incongruous to bar an insured—who has paid premiums and is entitled to protection under the policy—from recovering damages when the insurer wrongfully refuses to pay a valid claim. Such a result would be in contravention of the remedial purposes of the DTPA and the Insurance Code. Tex. Bus. & Comm. Code Ann. § 17.44 (Vernon 1987); Tex. Ins. Code Ann. art. 21.21, § 16 (Vernon Supp.1988). . . .
>
> The Vails offered evidence that Texas Farm had wrongfully denied the claim, resulting in a failure to pay $35,000 when due. The Vails thus sustained $35,000 as *actual damages* as a result of Texas Farm's unfair claims settlement practices.[29]

Justice Raul Gonzales, joined by Justice Culver, dissented. Justice Gonzales emphasized that the opinion created a private right of action when the legislature had intended the opposite result. The dissent argued that "the majority has had to resort to a tortured reading of the DTPA, the Insurance Code, and Vail's pleadings, and has ignored our recent opinion in *Chitsey v. National Lloyds Ins. Co*."[30]

The insurance industry and the defense bar were not happy with the decision in *Vail.* Many commentators echoed the dissent, noting several "suspect" logical leaps were necessary to cobble together the causes of action alleged.[31] One thing is relatively certain: the Texas Supreme Court clearly wanted to make a definitive statement approving these causes of action. Having approved the duty of good faith in *Arnold*, the Vails could have recovered under that theory. The key to *Vail*, however, was the path it recognized to treble damages.

Much of the statutory and regulatory framework relied upon in *Vail* is now gone. What is left is a continuing fight over whether the loss of contract benefits can serve as actual damages sufficient to allow trebling. *Vail* again came to the forefront with the certification in *In re Deepwater Horizon*.[32] The court in its certification decision observed:

> [W]e find it prudent to obtain clarity from Texas itself. The parties' arguments regarding whether Vail remains good law "illuminate the magnitude and wide ramifications . . . for insurance law" that this issue presents. *In re Deepwater Horizon*, 728 F.3d 491, 500 (5th Cir.2013), *certified question answered*, 470 S.W.3d 452 (Tex. 2015), *reh'g withdrawn* (May 29, 2015). We thus conclude that certification is appropriate here.[33]

Vail is still good law. The federal courts are simply effectively ignoring it.[34] The suggestion that it has been overruled *sub silencio* is unreasonable and simply wrong. Fortunately or unfortunately, *Deepwater* settled and the Texas Supreme Court's position on *Vail* remained an unresolved matter, at least in the Fifth Circuit and some federal courts.

Not surprisingly, Mark Kincaid, discussing the *IBEX* decision, beautifully articulated the source of the confusion over modern readings of *Vail* and the decision of the Texas Supreme Court in *Provident American Insurance Co. v. Castañeda*[35]:

> It is hard to follow the AFS/IBX court's reasoning that the attorney's fees damages were not recoverable yet could be the separate injury. What is more troubling, and clearly incorrect, is the court's conclusion that a separate injury is required for an insured to recover for unfair insurance practices. The court correctly quoted its prior holding in *Parkans*, but misapplied

it. A number of cases have stated that there must be a separate injury for an insured to recover for unfair claims handling. This statement can be true when the insurer *does not* owe the claim.

. . .

The statement that an independent injury is required is correct in that context, where the insurer *does not* owe the claim. The policy benefits cannot be damages, because the policy benefits are not owed. Thus, if there is no independent injury then there is no basis for extracontractual liability.

The Fifth Circuit's decision in *Parkans* was another example of this principle properly applied. In *Parkans*, the court first found there was no coverage for the claim and then found there could be no extracontractual recovery for bad faith, because there were no injuries independent of the contract damages. Of course, since those contract damages were not recoverable, they could not serve as damages for the unfair insurance practices.

The *Parkans* court relied on the Texas Supreme Court's decision in *Provident American Insurance Co. v. Casteneda*, 980 S.W.2d 189, 198–99 (Tex. 1998). In *Provident*, the supreme court did state that there was no evidence of an independent injury, but it did so after concluding that the insurer was not liable for unfair settlement practices. In *Provident*, the insureds did not sue for breach of contract, so the court was not considering whether they could or could not recover contract damages. What the court did consider was that the insurer had a reasonable basis to deny the claim, even if it is was wrong. Obviously, a reasonable denial of the claim could not cause any damages. The court found no evidence to support the claim for loss of credit reputation, and then concluded that there was no other independent injury. This statement regarding an independent injury made some sense in *Provident*. The policy benefits could not be damages for an unfair claim denial, when the court found there was no unfair claim denial. In other words, the insurer was not liable because it had not committed a violation—according to the court—not because the benefits wouldn't be damages if the insurer had committed a violation.[36]

Mark further explained:

> The Texas Supreme Court expressly addressed this issue in the leading case of *Vail v. Texas Farm Bureau Mutual Ins. Co.*, 754 S.W.2d 129, 136 (Tex. 1988), rejecting the insurer's argument that damages for an unfair settlement practice had to be something more than the amount due under the policy. The supreme court held that damages for a wrongful refusal to pay are at least equal to the policy benefits, as a matter of law . . . It would be exceedingly odd for the legislature to create a cause of action that says recovery of "actual damages" is allowed for failing to settle once liability is reasonably clear, but to hold that the most common damages—policy benefits—were not recoverable and the insured had to establish some other bizarre "independent injury." The legislature could have done that, but the language it chose certainly does not disclose that it did. The supreme court's analysis and holding in *Vail* do not allow such a conclusion.[37]

And so, one of the appellate wizards responsible for *Vail* has provided a great defense to its continued viability. We are all thankful he put his thoughts down in words before departing this old world much too soon. Ironically, his opposing counsel, Sid Davis, passed away a few years earlier, also much too soon. I suspect that they are now enjoying a long celestial discussion of *Vail* and other issues.

Strangely, as commentators speculated that the Texas Supreme Court was looking for a case to reverse *Vail*, my associate, Ron Huff, and I tried a case against Germania Insurance that gained a *Vail*-like recovery.[38] Whose case would be better to reverse *Vail*, than mine, a few years later? In sum, we survived the court of appeals, but the supreme court granted writ. I told my clients we were doomed. Yet, Ron and I showed up to argue to the court. I don't recall all who were there, but I do remember Justice Raul Gonzales, a *Vail* dissenter, was joined by Justice Cornyn, Justice Oscar Mauzy, and the others. It was clear from the questions that it was a bad day at consumer's Black Rock. My associate nobly argued our position, but I had the sense that if we didn't score four touchdowns in five minutes, it was over. So, when I rose to conclude, I essentially told them that I understood they had their sights set on reversing *Vail*, and certainly that was their prerogative, but in fairness to them, they needed to find a case with better facts. I referenced trial court exhibits the clerk had given me permission to fish out of the supreme court files, and showed the court the argument that had won at trial: the Germania adjuster was essentially deaf, but denied the claim over the phone. He hadn't heard a word of the claim, but denied it anyway.

Apparently that was enough for the court. The next day they dismissed the appeal as being improvidently granted. And *Vail* lived for another day.

1 *Texas Farm Bureau Mut. Ins. Co. v. Vail*, 695 S.W.2d 692, 694 (Tex. App.—Dallas 1985), *rev'd in part*, 754 S.W.2d 129 (Tex. 1988) (quoting appellant's brief).

2 *Id.* n.4 (emphasis added).

3 *Id.*

4 *McKnight v. Ideal Mut. Ins. Co.*, 534 F. Supp. 362 (N.D. Tex. 1982).

5 *Vail*, 695 S.W.2d at 694–95.

6 *G.A. Stowers Furniture Co. v. Am. Indem. Co.*, 15 S.W.2d 544, 547 (Tex. Comm'n App. 1929, holding approved) (emphasis added).

7 *Vail*, 695 S.W.2d at 694 (quoting *Stowers*, 15 S.W.2d at 547).

8 *Id.* at 694.

9 Application at 23.

10 *Arnold v. Nat'l County Mut. Fire Ins. Co.*, 725 S.W.2d 165 (Tex. 1987).

11 *Chitsey v. Nat'l Lloyds Ins. Co.*, 738 S.W.2d 641 (Tex. 1987).

12 *Id.* at 642 (quoting Tex. Ins. Code Ann. art. 21.21, § 16(a) (Vernon 1981) (repealed)).

13 *Id.* at 643–44.

14 *Id.* at 644.

15 *Id.* at 643.

16 *Id.*

17 *Vail*, 754 S.W.2d at 131–32.

18 *Id.* at 132–33 (quoting Tex. Ins. Code Ann. art. 21.21, § 16(a) (Vernon Supp. 1988)).

19 State Bd. of Insurance, Board Order 18663 § 4 (now 28 Tex. Admin. Code § 21.3) (Hart 1986).

20 *Vail*, 754 S.W.2d at 133.

21 *Id.* at 133–34.

22 *Id.* at 134.

23 *Id.* at 135.

24 *Aranda v. Ins. Co. of N. Am.*, 748 S.W.2d 210, 213 (Tex. 1988).

25 *Vail*, 754 S.W.2d at 135.

26 *Id.*

27 *Vail v. Texas Farm Bureau Mut. Ins. Co.*, 754 S.W.2d 129, 136 (Tex. 1988).

28 *Id.* at 136.

29 *Id.* at 136–37 (emphasis added).

30 *Id.* at 137–38.

31 *See, e.g.*, R. Brent Cooper & Michael W. Huddleston, *"Annual Survey of Texas Law—Insurance Law,"* 43 Sw. L.J. 343, 355–56 (1989).

32 *In re Deepwater Horizon*, 807 F.3d 689 (5th Cir. 2015).

33 *Id.* at 693.

34 *See, e.g.*, *Great Am. Ins. Co. v. AFS/IBEX Fin. Servs., Inc.*, 612 F.3d 800, 808 & n.1 (5th Cir.2010); *Parkans Int'l, L.L.C. v. Zurich Ins. Co.*, 299 F.3d 514, 519 (5th Cir. 2002).

35 *Provident Am. Ins. Co. v. Castañeda*, 988 S.W.2d 189, 198–99 (Tex. 1998)

36 Mark L. Kincaid et al., *Annual Survey of Texas Insurance Law 2010*, J. of Consumer & Com. L., 59, 62–64 (2010).

37 *Id.* at 64.

38 *Germania Ins. Co. v. Dicken*, No. 05-90-00325-CV (Tex. App.—Dallas filed Mar. 19, 1990); No. D-1119 (Tex. filed June 6, 1991).

By Vincent E. Morgan

MARK KINCAID TRIBUTE — NOTES FROM A FORMER STUDENT

I first met Mark Kincaid when he was my professor for a course on Texas Insurance Litigation at The University of Texas School of Law. At the time, he wasn't a whole lot older than the rest of the class but he'd already achieved professional accomplishments befitting a career's worth of work. Although he started that semester as my teacher, by the end of it he was one of my mentors. Over the years we became colleagues, and ultimately, friends. Each of these roles are worthy of tribute, but I want to focus most on his work as a teacher and how it helped make his students better lawyers.

I remember him explaining complicated concepts in ways that were easy to understand— something great trial lawyers can do. He also knew that sometimes humor was as good an aid as any in helping keep an afternoon class on insurance law interesting even to those who didn't love it. He explained why he fought for policyholders. Those who had a different leaning at least came away with a healthy respect for his side of the docket. The universe of insurance cases wasn't as large then as it is now, so Mark covered the old and the new but none of it ever seemed like it was old to him. He taught ethics too, and made sure we knew that they were as important to being a lawyer as knowing the facts of your case or what a statute said.

At the end of the semester, he took the whole class out to Scholtz Garten. Maybe he did this because he needed it before grading our papers, or maybe he thought we needed it after his exam, but mostly I think he did it to reinforce the point that we were becoming part of a community.

There was no suitable textbook at the time so Mark hand-picked key cases, statutes and regulations for our materials, and then sprinkled practical tips on lawyering in between. Many years later, one of those tips came in handy in my own practice and I called Mark the next day to thank him for it. He was gracious as always and acted like it was no big deal, but I hope it gave him some idea of how much his students valued the things he taught us.

Years later, I served as head of the Nominating Committee for the Insurance Law Section. We looked for candidates with different backgrounds such as policyholder vs. carrier, geographic location, big firm vs. small firm, etc. In the middle of that process, something made me think of Mark. Our committee could not think of any lawyer besides Mark who had made more of an impact on Texas insurance law but never served on the Council. Although there are often many more qualified individuals than there are open slots on the Council, nominating him was an easy choice. I don't know if Mark found it worth his time, but I do know that the Council and the Section were better off with him there and we are worse off now that he is not.

We can't avoid missing him, but we can make sure we don't forget Mark proved that being a good lawyer and a good person are not incompatible, and that was the most valuable lesson he taught his students.

Vince Morgan is a litigation partner in the Houston office of Pillsbury Winthrop Shaw Pittman LLP. He represents clients in a wide variety of industries on all aspects of insurance and risk management issues but has a particular emphasis on helping clients deal with claims involving man-made and natural catastrophes. Over his career, he has helped clients recover billions of dollars in negotiations, litigation and arbitration. Mr. Morgan is a past Chair of the Insurance Law Section of the State Bar of Texas and has been selected by his peers for more than a decade in rankings such as Texas Super Lawyers, Best Lawyers in America and EuroMoney's Insurance and Reinsurance Expert Guide. He has been named "Insurance Lawyer of the Year" by US News & World Report and has had a top ranking for several years in Chambers USA's "Band 1" for Insurance in Texas.

P.O. Box 12667
Capitol Station
Austin, Texas 78711-2667

joe@joelongley.com

LAW OFFICES
OF
JOE K. LONGLEY
1609 Shoal Creek Boulevard
Suite 100
Austin, Texas 78701-1022

512/477-4444
800/792-4444
512/477-4470 FAX

www.joelongley.com

April 8, 2016

Ms. Mary Camp
Director
Texas Legislative Reference Library
1100 Congress Ave.
Austin, TX 78701

RE: Donation of the "Mark L. Kincaid Papers" to the Joe K. Longley – Philip K. Maxwell DTPA/Insurance Collection – [Longley & Maxwell Collection].

Dear Ms. Camp:

It is my pleasure to enclose the "Mark L. Kincaid Papers" on the thumb drive being tendered to you with this letter.

This donation has been made possible through the generosity of the late Mr. Kincaid's widow, Joan E. Kincaid – and fills in the significant gaps in the legislative archive materials contained in the Longley & Maxwell Collection (1973-2001).

Included are documents relating to the passage of House Bill 668 in the 74th Legislative Session (1995) – and the extensive materials relating to the failure of SB 1628 to pass the 84th Legislative Session in 2015. Both of these events have significantly affected the protection of consumer and policyholder rights of Texas citizens.

Mark Lyndon Kincaid was recognized by Texas lawmakers as the leading authority on unfair insurance practices – particularly in matters relating to first-party coverages for homeowners and automobile insurance.

It is with great pleasure that I tender these papers to the Texas Legislative Reference Library for its archives and collection in memory of Mark L. Kincaid.

With kindest personal regards,

Sincerely,

Joe K. Longley

Joe K. Longley

JKL/mep

ANNOUNCING THE MARK L. KINCAID LEGISLATIVE PAPERS

The Texas Legislative Reference Library has recently received a collection of documents from the late Austin attorney Mark L. Kincaid. Mr. Kincaid was known as "The Policyholder's Lawyer." He had established a reputation for crafting public policy for the protection of insurance policy holders who had little or no ability to prevent abuses in the claims process. Kincaid's papers enhance the Joe K. Longley-Philip K. Maxwell Deceptive Trade Practices Act Legislative Archive housed at the library.

Spanning two decades, from 1995 through 2015, the collection showcases Kincaid's efforts to curb tort reform, to document the 74th Legislature's intent behind H.B. 668, and to monitor and influence changes to the Deceptive Trade Practices Act. The collection includes legislation, analyses on a variety of bills, testimony transcripts, PowerPoint presentations, and correspondence with many interested parties.

Mark L. Kincaid passed away on January 19, 2016, but he leaves a legacy of research and experience that will benefit the legislative and legal communities for years to come. The collection is not yet entirely processed by the Library, but we couldn't wait to give you a preview.

TEXAS LAW

We are writing to you—former students, colleagues, and friends of Mark Kincaid— to ask you to help fund a scholarship in his memory. Mark was a remarkable trial lawyer, an exceptional adjunct professor, and a true leader in his practice area. We remember him even more (and suspect many of you do as well) for his kind heart, fantastic story-telling, and passion for music--not to mention his goal to cook the perfect pot of chili and rack of ribs.

After Mark's passing, the Law School received several contributions in memory of Mark, and we decided the best way to honor him was to create a scholarship on his behalf. Mark loved the Law School – first as a law student and later as an adjunct professor. We believe the best way to remember Mark is to create a legacy for him at the school he loved by endowing this scholarship. We are hopeful that many of you are willing to help establish a legacy at the Law School for Mark by making a contribution to the Mark L. Kincaid Endowment for Excellence Scholarship in Law.

To endow Mark's scholarship, we need to raise a minimum of $50,000. We also want to exceed the minimum to ensure that the scholarship will provide the most substantial benefit possible for students and serve as a fitting tribute to Mark and his legacy as a teacher, mentor, and friend to so many of us.

All pledges and contributions, in any amount, will make a difference. As indicated on the attached card, pledges may be paid over up to five years. Thank you for helping us support Texas Law students and honor our friend and colleague, Mark Kincaid. We hope to hear from you soon.

Sincerely,

B. Russell Horton, '86

Joe K. Longley, '69

Phillip K. Maxwell, '69

Thomas M. Melsheimer, '86

Vincent E. Morgan, '00

By Alexandra Fernandez

EMERGING ISSUES IN THE CALCULATION OF INTEREST UNDER THE TEXAS PROMPT PAYMENT OF CLAIMS ACT

I. Introduction

The Texas Prompt Payment of Claims Act[1] ("TPPCA") provides a series of deadlines to which insurance companies must adhere during the claims-handling process. Its express purpose is "to promote the prompt payment of insurance claims" and states:

> If an insurer that is liable for a claim under an insurance policy is not in compliance with this subchapter [Subchapter B of Chapter 542], the insurer is liable to pay the holder of the policy[,] in addition to the amount of the claim, interest on the amount of the claim at the rate of 18% a year as damages.[2]

The deadlines imposed by the TPPCA are presented chronologically in terms of the claims-handling process.

- First, §542.055 states the insurer shall acknowledge receipt of the claim, request information the insurer believes it requires, and begin investigation of the claim, within 15 days [or 30 days, for surplus lines insurers] of receiving notice of the claim;

- Next, §542.056 states not later than the 15th business day after the date the insurer receives all items required by the insurer to secure final proof of loss, the insurer notifies the insured of (1) acceptance, (2) rejection, or (3) the need for additional time to decide (not more than 45 days);

- §542.057 states that *if* the insurer notified the insured of acceptance of the claim under §542.056, the insurer must pay the claim within 5 business days;

- Finally, §542.058 states that if an insurer does not pay a (covered) claim 60 days after receiving all items reasonably requested and required under §542.055, the insurer shall pay damages and other items as provided in §542.060.[3]

The Texas Supreme Court rarely opines on TPPCA issues. Federal courts interpreting the TPPCA have recently issued some important opinions that are bound to play a key role in future TPPCA disputes.

II. Recent Developments in TPPCA Interest Penalty Jurisprudence

A. What Violations of the TPPCA Trigger the 18% Penalty?

Historically, one area of contention in TPPCA disputes has been the calculation of the penalty when an insurer violates an early claims-handling deadline and later denies a covered claim. Insurers have pointed out that §542.058 is the *only* subsection that references the enforcement provision (§542.060), and thus argue that *only* a violation of §542.058 triggers the penalty. The Fifth Circuit recently rejected this argument and ruled *any* violation of §§542.055-542.058 triggers the penalty, while the Texas Supreme Court has not addressed the issue.[4]

Because courts have previously calculated the penalty interest when only a violation of §542.058 is pleaded and proved, there has been a dearth of guidance regarding when the penalty begins to accrue when an insurer violates §§542.055 or 542.056.

B. When Does the 18% Penalty Begin to Accrue?

Courts interpreting the TPPCA have been split regarding the precise date to begin calculation of the 18% penalty for early claims-handling deadline violations.

Some courts held that the day after the earliest deadline violation is the date the penalty interest should start to accrue. For example, in *Primrose Operating*, the jury found that the insurer violated §§542.055(a) and 542.056.[5] The federal district court held that the penalty began to accrue on the very first date of violation, i.e., the day after the deadline in §542.055(a): date of notice of claim + 15 days + 1 day.[6]

Other courts have interpreted the TPPCA to mean the penalty can only be enforced through a violation of

Alexandra Fernandez is a Senior Associate at Zelle LLP in Dallas. Alexandra's practice focuses on litigating large, complex insurance coverage disputes involving property insurance policies, as well as commercial and professional liability insurance disputes, and subrogation matters.

§542.058, and thus used §542.058's 60-day period in determining the date the penalty begins to accrue even when an earlier TPPCA violation occurred. For example, where insurers violated §542.055(a), some courts calculated the accrual of the penalty as follows: date of notice of claim + 60 days + 1 day.[7] Other courts have calculated accrual as: date of notice of claim + 15 days + 60 days + 1 day.[8]

However, the Fifth Circuit has recently issued two opinions that adopt the methodology in *Primrose Operating*, *supra*, and do not tack on a 60-day period when an earlier TPPCA deadline is missed.

First, in *Cox Operating*, where the jury found the *surplus lines insurer* violated both §§ 542.055(a) and 542.056(a), the Fifth Circuit concluded that the penalty should begin to accrue 30 days after the date the insurer *received notice of the claim* (i.e. the penalty was based on the violation of §542.055(a) - the earliest violation).[9]

Second, in *Weiser-Brown*, where the insurer violated §542.056(a) (for failing to notify the insured of acceptance or rejection of the claim within 15 days of receiving information necessary to secure proof of loss), but did not violate §542.055, the Fifth Circuit affirmed that the penalty began to run 15 days after the insurer received the information necessary to secure proof of loss.[10]

C. How Do The TPPCA Penalties Apply in Appraisal Cases?

The appraisal process is now commonly used to resolve disputed insurance claims. When the insurer fully and timely pays any additional amounts found to be payable on the claim pursuant to an appraisal award, for over a decade courts have uniformly held that the insurer is insulated from TPPCA penalties.[11] This is logical considering compliance with appraisal typically means there has not been a breach of contract, and because paying an appraisal award is not an admission that the claim was covered by the policy.[12]

However, Judge Boyle of the Northern District of Texas recently issued an opinion in *Graber v. State Farm*[13] that does not conform to precedent. The insurer complied with the early claims-handling deadlines, paid the policyholder per the adjuster's estimate, did not deny coverage, did not breach the contract, and paid the full appraisal award a few days after the appraisal was complete. In spite of this, the court refused to grant the insurer's motion for summary judgment on the TPPCA claim.[14]

Without guidance from the Texas Supreme Court, *Graber* appears to be an anomaly, especially considering the fact that, since *Graber* was decided, other courts have issued opinions in line with the prior precedent.[15]

III. Issues on the Horizon

A. The 18% Penalty May Stop Accruing Long Before Judgment is Rendered

It is well known that an insurer can shorten the time period during which the penalty accrues by filing an interpleader,[16] and reduce the amount of the penalty by tendering an unconditional partial payment to the insured,[17] but these remedies tend to apply where only a §542.058 violation (a delay in payment) is at play. A footnote in the recent *Cox Operating* opinion contains an apparent avenue insurers can take to reduce the penalty when an earlier claims-handling deadline is at the center of the controversy.

The Fifth Circuit stated the penalty accrues until the earlier of (1) "the date judgment is rendered in favor of the insured," or (2) "the date the insurer takes the action it failed to take earlier, triggering the penalty."[18] The court went on to state that since the insurer did not raise an argument as to when the interest stopped accruing, "we have no occasion to address whether [insurer] 'cured' its deadline violation so as to stop the accrual of interest sometime before the date of the judgment."[19]

The insurer in *Cox Operating* failed to timely request documents or commence investigation under §542.055(a). Thus, in context, the Fifth Circuit seems to imply that the insurer may have been able to cut the accrual period short by sufficiently demonstrating that it requested documents and/or commenced an investigation before the date of the judgment.

D. Calculating Penalty Interest on Claims With No Finite Value at Time of Denial

The amount of an insured's claim (and/or the amount for which an insurer is liable) is often based on third-party invoices that the insured has not incurred, in amounts the insured cannot necessarily predict, at the time the insured submits its notice of claim to the insurer. Consider duty to defend or environmental clean-up coverage, where the amount of the claim can increase every month.

Naturally, there are questions regarding when the 18% penalty begins to accrue on such claims. The TPPCA language does not provide specific guidance on these calculations, but courts in the Fifth Circuit have recently indicated the methodology is based on the date of the TPPCA violation and not necessarily the date the cost was incurred.

The insured in *Cox Operating* had liability coverage for legally required pollution clean-up and incurred covered pollution clean-up costs in differing amounts per month over a two-year period. The insurer violated §542.055(a) early in that two-year period, before many of the pollution clean-up costs were incurred. The insurer argued it was

unjust for the 18% penalty to be based on the ultimate claim amount, and urged the court to follow *Lamar Homes, Inc. v. Mid-Continent Cas. Co.*, 242 S.W.3d 1 (Tex. 2007) and hold that accrual should not begin until after the insured incurred the cost.

The Fifth Circuit rejected the argument for several reasons. The insurer in *Lamar Homes* wrongfully denied its duty to defend, which constituted a §542.058 violation, and there was no indication the insurer violated §§ 542.055 or 542.056 prior to denying coverage. The Fifth Circuit also distinguished *Lamar Homes* by indicating that, because it was a duty to defend case, the claim had "no finite value" at the time the insurer denied the claim. Thus the penalty could not be calculated until the cost was actually incurred.

This "finite value" reasoning was also used in a federal district court case, *Devonshire Real Estate v. American Ins. Co.*, involving property damage where the court rejected the insurer's argument that the 18% penalty could not accrue on additional damage amounts until the supplemental documentation was submitted to the insurer. The court distinguished *Lamar Homes* by stating, in *Lamar*, "the insured . . . suffered an actual loss that is quantified after the insured retains counsel and begins receiving statements for legal services" but the insured in *Devonshire* "suffered an actual loss when its property was damaged by a wind and hail storm." [20]

Absent legislation or guidance from the Texas Supreme Court, it appears in some cases that the penalty can accrue on costs the insured has not incurred or paid.

Nevertheless, a concrete methodology for calculating the penalty interest on claim amounts that increase over time cannot be gleaned from these cases. For obvious reasons, §§ 542.055 or 542.056 violations are uncommon in duty to defend cases, but if there were such a violation, it is not clear whether or not these courts would wait for the insured to incur a defense cost before the penalty on that cost could accrue. Further, it is unclear how these courts would have calculated the penalty in *Cox Operating* had there *only* been a §542.058 violation in the middle of the two-year pollution clean-up process.

Absent legislation or guidance from the Texas Supreme Court, it appears in some cases that the penalty can accrue on costs the insured has not incurred or paid. The insurers in *Cox Operating* and *Devonshire* focused their arguments on *Lamar Homes*, which the courts could distinguish. The issue has yet to be fleshed out, and parties on both sides of the issue in future disputes will no doubt formulate new arguments for the courts to consider.

E. Proposed Legislation Would Have Significant Impact on TPPCA Application

Companion bills SB 1628 and HB 3787 were proposed in the 2015 Texas legislative session and would have changed the application of the TPPCA in at least three major areas, discussed below. This legislation passed the Texas Senate, was voted on favorably by the House Insurance Committee, but died in the House Calendar Committee without ever being put up for a full vote before the House. It is anticipated that similar legislation will be put forth for the upcoming 2017 session.

Bona Fide Disputes. There can be no common law bad faith when there exists a "bona fide dispute" as to the claim.[21] This standard has also been applied to statutory claims under Chapter 541.[22] However, such a dispute is not presently a basis to avoid the 18% penalty under Chapter 542.[23] The penalties are essentially a strict liability standard.

The proposed legislation would have changed the current language in §542.060 making an insurer who "is not in compliance" with Chapter 542 liable for the 18% penalty, to limiting the penalty to insurers who "*knowingly fail* to act in compliance" with Chapter 542. A proposed amendment to §542.060(a-1) explicitly stated there would be no penalty for a claim to which there is a bona fide dispute as to the insurer's liability.

Notice Requirement. A proposed amendment to §542.0595 would have made actions under §542.060 subject to the same prior notice of action requirements of §541.154. If an insured brought suit without providing the required 60-day notice, the §542.060 action would be subject to abatement or dismissal to the same extent provided by §541.155.

Appraisal. Under proposed amendment §542.0601, an insurer would not be liable under §542.060 if the appraisal process was invoked by the insured (before or after the commencement of litigation), or by the insurer (before or 60 days after the commencement of litigation), and the process resulted in a valid, signed award paid by the insurer not later than the 15th day the insurer received the award. This amendment would have clarified the application of the holding in *Breshears v. State Farm Lloyds*, as opposed to *Graber v. State Farm*, discussed *supra*.

There is also increasing recognition and concern about the fact that the 18% penalty—a percentage written into the

legislation at a time when mortgage and other interest rates were at or near an 18% level—is outdated and excessively punitive in the unprecedented low-interest rate environment that has existed over the past several years.

IV. Conclusion

Over the last few years, federal courts interpreting the TPPCA have made several *Erie* guesses attempting to clarify the proper scope of penalty interest under the TPPCA. As interpreted by these courts, insurers that fail to follow the claim-handling deadlines for covered claims will be exposed to the statutory penalty on the entire amount of the covered claim beginning on the earliest date the insurer violated the TPPCA. In some cases, the penalty will begin to accrue on costs before the insured even incurs them. While insurers can cut the penalty period short by subsequently complying with the statute, the impact of these federal decisions will be felt until Texas state courts and/or the Texas legislature provide different guidance and interpretations.

1 *See* Tex. Ins. Code §§542.051–542.061 (comprising Subchapter B of Chapter 542 of the Texas Insurance Code ["TIC"]), formerly codified under Article 21.55 of the TIC. No substantive changes were made when the TPPCA was re-codified.

2 §§542.054 and 542.060.

3 Certain deadlines in the TPPCA are extended 15 days when the insurer is a surplus lines insurer and/or in the event the Texas Insurance Commissioner declares a weather-related catastrophe. §§542.055, 542.057, 542.059.

4 *Cox Operating, LLC v. St. Paul Surplus Lines Ins. Co.*, 795 F.3d 496, 508 (5th Cir. 2015). The Fifth Circuit declined to certify St. Paul's questions, and made an Erie guess in determining questions regarding the accrual date of the penalty.

5 *Primrose Operating Co. v. Nat'l Am. Ins. Co.*, No. 5:02-CV-101-C, 2003 U.S. Dist. LEXIS 12447, at *1–4 (N.D. Tex. July 15, 2003); *see also Texas Farmers Insurance Company v. Cameron*, 24 S.W.3d 386, 398-99 (Tex. App.—Dallas, 2000, pet. denied) (pointing out accrual date could have been earlier based on a §542.056 violation as opposed to the later §542.058 violation).

6 The insurer specifically raised a complaint about this calculation in its appeal to the Fifth Circuit. The court apparently accepted the methodology when it affirmed the trial court's rulings on all issues except pre-judgment interest. *Primrose Operating Co. v. Nat'l Am. Ins. Co.*, 382 F.3d 546, 551, 556 (5th Cir. 2004).

7 *See Philadelphia Indem. Ins. Co. v. CRES Management, LLC*, No. 4:09-01032, 201 U.S. Dist. LEXIS 29386, at *13–14 (S.D. Tex. March 22, 2011); *GuideOne Lloyds Ins. Co. v. First Baptist Church of Bedford*, 268 S.W.3d 822, 834 (Tex. App.—Forth Worth 2008, no pet.). Technically, these two cases used 75 days instead of 60 days because the 15-day extension for weather-related catastrophes under §542.059 applied.

8 *Great Am. Ins. Co. v. AFS/IBEX Fin. Servs, Inc.*, No. 3:07-CV-924-O, 2009 U.S. Dist. LEXIS 131107, at *4–5 (N.D. Tex. Feb. 13, 2009), *aff'd*, 612 F.3d 800 (5th Cir. 2010) (the insurer "either (1) had all of the items, statements, and forms it believed would be required from [the insured], or (2) failed to request such items as required" by §542.055(a), and, pursuant to §542.058(a), the insurer was required to pay the claim within 60 days after the 15-day deadline "at the latest.").

9 *See Cox Operating*, 795 F.3d at 508–509 (finding the district court's calculation of the accrual as date of notice + 60 days + 1 day was erroneous but pointing out that since the insured did not cross-appeal to seek the earlier accrual date the district court's ruling was affirmed).

10 *Weiser-Brown Operating Co. v. St. Paul Surplus Lines Ins. Co.*, 801 F.3d 512, 517 (5th Cir. 2015) (the insurer received sufficient information to secure a final proof of loss on November 6, and the penalty began to accrue on November 21). Note, neither party apparently pointed out that §542.056(a) states the deadline is the "15th business day" not just "the 15th day."

11 *E.g.*, *Blum's Furniture Co. v. Certain Underwriters at Lloyds London*, 459 F. App'x 366, (5th Cir. 2012); *Barry v. Allstate Tex. Lloyds*, No. 4:14-CV-870, (S.D. Tex. March 31, 2015); *Breshears v. State Farm Lloyds*, 155 S.W.3d 340, 344 (Tex. App.—Corpus Christi 2004, pet. denied).

12 *See Amine v. Liberty Lloyds of Tex. Ins. Co.*, No. 01-06-00396-CV, 2007 Tex. App. LEXIS 6280, 2007 WL 2264477, at *4–5 (Tex. App.—Houston [1st Dist.] Aug. 9, 2007, no pet.).

13 *Graber*, No. 3:13-cv-2671-B, 2015 U.S. Dist. LEXIS 77361 (N.D. Tex. June 15, 2015).

14 The court appeared to base its holding on a "gotcha"—interpreting language in a letter written by the insurer as an acknowledgement that the appraisal award was for *covered* damages. *Id.* at 26.

15 *E.g.*, *Diszdar v. State Farm Lloyds*, No. 7:14-cv-402 (S.D. Tex. Feb. 4, 2016); *Burks v. Metro. Lloyds Ins. Co. of Texas*, No. H-14-591, (S.D. Tex. July 8, 2015); *Bernstein v. Safeco Ins. Co. of Illinois*, No. 05-13-01533-CV, 2015 WL 3958282 (Tex. App.—Dallas, June 30, 2015, no pet.).

16 *E.g.*, *State Farm Life Ins. Co. v. Martinez*, 216 S.W.3d 799, 806-807 (Tex. 2007) (interpleader of policy proceeds halted the accrual of penalty interest after insurer violated §542.058(a)).

17 *E.g.*, *Republic Underwriters Ins. Co. v. Mex-Tex, Inc.*, 150 S.W.3d 423, 427 (Tex. 2004).

18 *Cox Operating*, 795 F.3d at 506 (footnote 2).

19 *Id.*

20 *Devonshire Real Estate & Asset Mgmt., LP v. Am. Ins. Co.*, No. 3:12-cv-2199-B, 2014 U.S. Dist. LEXIS 135939, at *70–71 (N.D. Tex. Sept. 26, 2014).

21 *Higginbotham v. State Farm Mut. Auto. Ins. Co.*. 103 F.3d 456, 459 (5th Cir. 1997).

22 *Id.* at 460 (Chapter 541 was previously codified as Article 21.21 of the Texas Insurance Code).

23 *E.g.*, *Id.* at 461; *Wellisch v. United Servs. Auto Assn.*, 75 S.W.3d 53, 58 (Tex. App.—San Antonio, 2003, pet. denied).

By Rachelle H. Glazer and David S. White

RECENT FIFTH CIRCUIT AND TEXAS SUPREME COURT INSURANCE DECISIONS

TEXAS SUPREME COURT

Property Is Not Harmed by the Mere Installation of Defective Products.

U.S. Metals, Inc. v. Liberty Mutual Group, Inc., No. 14-0753, 2015 WL 7792557 (Tex. Dec. 4, 2015)

In this case, the Supreme Court of Texas answered several questions certified from the Fifth Circuit, chiefly whether a policy covering "physical injury" covers damage due to the mere installation of a defective part or parts. Also at issue was the breadth of an exclusion for "impaired property."

This case arose out of a dispute over flanges.[1] U.S. Metals, Inc. sold ExxonMobil a few hundred flanges for use in building sulfur-removing diesel units at refineries in Texas and Louisiana.[2] The contract provided for "industry standard" flanges.

Unfortunately, some of the flanges leaked. Upon investigation ExxonMobil determined that the flanges were not up to industry standard, requiring replacement of the flanges to avoid the possibility of fires or explosions.[3] ExxonMobil then sued U.S. Metals for the cost of replacement and the harm to their business, resulting in a settlement for $2.2 million. U.S. Metals sought coverage from its commercial general liability insurer, Liberty Mutual Group.[4]

Liberty Mutual denied coverage, first because Liberty Mutual denied that installation of the flanges had caused "physical injury" (the triggering condition for liability under the policy), and second on the basis of two exclusions in the insurance policy: one excluding coverage for "'property damage' to 'your product,'" and the other excluding "'[p]roperty damage' to 'impaired property' or property that has not been physically injured, arising out of ... [a] defect, deficiency, inadequacy or dangerous condition in 'your product'."[5] Liberty Mutual argued that this latter exclusion meant that if the harm to ExxonMobil could have been cured simply by replacing U.S. Metal's flanges, then U.S. Metals would not be covered for the cost of that replacement.

The Fifth Circuit had found that the Texas Supreme Court had not weighed in on whether the important terms "physical injury" (governing whether the policy applied) and "replacement" (governing whether the exclusions applied) were ambiguous.[6] The Fifth Circuit therefore certified that question to the Texas Supreme Court, and further asked the Texas high court to apply the terms if the court did not find them ambiguous.[7]

The Texas Supreme Court summarized the relevant legal questions:

> First: did the mere installation of the faulty flanges physically injure the diesel units when the only harm at that point was the risk of leaks? Or put more generally: is property physically injured simply by the incorporation of a faulty component with no tangible manifestation of injury? And second: is property restored to use by replacing a faulty component when the property must be altered, damaged, and repaired in the process?[8]

Reasoning by analogy to earlier faulty workmanship cases, the Texas Supreme Court answered the first question in the negative.[9] Texas courts have long held that while in some instances particularly bad work could result in actual damage, in general faulty workmanship was not itself property damage. Moreover, the court noted that under Texas law, a cause of action for damages resulting from a defective product arises *when the damage occurs*, not when

Rachelle ("Shelley") H. Glazer is a Partner at Thompson & Knight LLP in Dallas and focuses her practice on business and contract disputes, including complex insurance contract disputes. She has extensive experience in coverage analysis, business interruption claims, bad-faith litigation, and agent misrepresentation claims. She has previously chaired the Torts and Insurance Practice Section of the Dallas Bar Association and been named one of The Best Lawyers in America® in Insurance Law for 2012–2015 and a Texas Super Lawyer® in Insurance Coverage for 2012–2015. She can be reached at Rachelle.Glazer@tklaw.com.

David S. White is Counsel at Thompson & Knight LLP in Dallas and focuses his practice on insurance coverage law and commercial litigation. His expertise includes general coverage, directors and officers, and bad-faith litigation, and he counsels clients on strategies to strengthen risk management programs through insurance and contractual indemnification arrangements. He has been named one of The Best Lawyers in America® in Insurance Law for 2012–2015. He can be reached at David.White@tklaw.com.

the defect is discovered.[10] However, the court explained that the units *were* physically injured in the process of removing and replacing the flanges, so the court still had to consider whether the damage caused in the replacement process was excluded.[11]

That question was more complicated, because the replacement caused more than one type of damage. First, there were the general costs of removing and replacing the flanges, including the costs of shutting down operation of the diesel units.[12] Second, the replacement process damaged welds, gaskets, insulation, and coating around the flanges, none of which were a part of the flanges themselves.[13] Here the court split the baby: replacing the flanges was clearly excluded—the flanges were, after all, U.S. Metal's product—but the other repairs (to restore the gaskets, insulation, etc.) were not excluded.[14]

That the Texas high court has joined the majority of states in rejecting mere incorporation of a defective component as property damage should come as no surprise.[15] Of greater interest for policyholders is the court's willingness to restore coverage from the grip of the "your-products" and "impaired-property" exclusions by considering the paint, welds, nuts, and bolts sticking to the excluded product as covered property not within the scope of the exclusions. This may salvage at least a duty to defend in some otherwise hopeless cases.

FIFTH CIRCUIT

"Other Insurance" Provision Doesn't Require Exhaustion of Legal Remedies Against an Intransigent Indemnitor Before the Insurer is Obligated to Pay.

In re Deepwater Horizon, 807 F.3d 689 (5th Cir. 2015), *certified question accepted* (Dec. 4, 2015).

The *Deepwater Horizon* litigation remains a fertile source of new and interesting questions of insurance law, as the Fifth Circuit continues to find. In the latest installment of this large, complex litigation, the Fifth Circuit decided two insurance questions and certified a third to the Texas Supreme Court, marking the second time during this litigation that the Fifth Circuit has requested the Texas high court's opinion.[16]

The first question the court considered was the scope of an "other insurance" provision. The insurance contract at issue contained a provision declaring that coverage was excess to any "other insurance" that "applies."[17] The policy defined "other insurance" broadly enough to encompass indemnity agreements with third parties as well as other kinds of insurance arrangements.[18] Cameron International Corporation (the named insured) and Liberty Insurance Underwriters (the insurer) disagreed about the effect of this provision.

The dispute arose when Transocean, Cameron's third-party indemnitor, refused Cameron's indemnity request.[19] Cameron sued Transocean but also demanded coverage from Liberty under the terms of the policy.[20] Liberty claimed that coverage under the policy had not yet been triggered because Transocean might still be required to pay, and coverage under the policy would be in excess to whatever Transocean might still pay because of the "other insurance" provision.[21]

Cameron responded that the policy defined the coverage as excess to any other insurance that "applies" and argued that the use of the present tense implied that what mattered was what "other insurance" *actually and presently* applied at the time of the claim.[22] The Fifth Circuit agreed based on the plain language of the policy.[23] The court also noted, as the district court had, that if Liberty's interpretation was correct, Cameron would have been better off if it had insurance but *no* indemnity agreement, since in that case at least one of the two parties who had agreed to cover Cameron would have had to pay immediately.[24]

Second, when Cameron eventually settled with Transocean on terms providing that Transocean was not required to indemnify Cameron, Liberty argued that this interfered with its subrogation rights, and still refused to pay.[25]

Strike two for Liberty. The Fifth Circuit determined that Liberty's refusal to pay had been a breach of contract.[26] Moreover, not only had Liberty constructively denied a legitimate claim, but also it had violated the prompt pay provisions of the contract.[27] This breach, the court determined, resulted in Liberty waiving its rights to subrogation.[28]

Finally, the Fifth Circuit considered whether Cameron had alleged a sufficient injury to state a separate claim against Liberty under the Texas Insurance Code. The Code allows an insured to file a suit seeking "actual damages" from an insurance company for various wrongful acts.[29] The only damages Cameron alleged in its claim against Liberty were its attorney fees and the policy benefit.[30] The fact that Cameron had not asked for any other damages set up a conflict between a recent Fifth Circuit decision (holding that Texas law required an injury *in addition to* failure to pay),[31] and long-standing (but now doubtful) Texas Supreme Court precedent.[32] The Fifth Circuit certified this important question of significant state interest to the Texas Supreme Court, rather than try to resolve it on its own.[33]

This decision could have broader ramifications than the bare facts would suggest. While this case involved a potential deadbeat indemnitor, the court's reasoning could conceivably lead to the same result in a case in which a primary insurer denies coverage, leaving the excess insurer on the hook. This case suggests that for an excess insurer facing such a situation, the safest thing to do would be to provide coverage so that it does not accidentally waive its

subrogation rights. Then, when the insured prevails against the primary insurer, the excess insurer can seek to be made whole.

This could be the last time the *Deepwater Horizon* case figures prominently in one of these updates, but I wouldn't bet the house on it.

Insurers Cannot Avoid Statutory Prompt-Pay Liability by Pointing to Missing Information That Did Not Affect the Coverage Decision.

Weiser-Brown Operating Co. v. St. Paul Surplus Lines Insurance Co., 801 F.3d 512 (5th Cir. 2015).

In this case, the Fifth Circuit had to interpret the Texas Prompt Pay Act. The most important question before the court was whether the insured's failure to submit certain information to the insurer meant that the fifteen-day limit for the insurer to accept or reject the claim had never begun, where the insurer had made its coverage decision without regard to the missing information.

Weiser-Brown Operating Co., an Arkansas-based oil company, had a "control-of-well" insurance policy with St. Paul Surplus Lines Insurance Co.[34] The policy provided for reimbursement of costs to regain control of wells that had gone out of control because of an unintended surge of oil, gas, water, or other fluid.[35] In August 2008, Weiser-Brown lost control of a well.[36] Weiser-Brown filed a claim in March 2009, and St. Paul's adjuster requested information.[37] Weiser-Brown sent St. Paul some, but not all, of the information it requested, and in June 2009 the adjuster requested additional documents, which Weiser-Brown supplied.[38]

After a few months of discussion, the adjuster concluded in September 2009 the well was never out of control. Weiser-Brown sent more information, but in February 2010 the adjuster reaffirmed its position and asked for a response. After a few more communications, Weiser-Brown challenged the adjuster's neutrality and filed suit against St. Paul for breach of contract and bad faith.[39]

At trial, the jury found that St. Paul had breached its contract with Weiser-Brown.[40] As part of that claim, Weiser-Brown had argued that it was entitled to 18% interest on damages under the Texas Prompt Pay Act.[41] The parties had agreed to reserve that issue for the court in the event the jury came back for Weiser-Brown.[42] The district court found for Weiser-Brown, holding that St. Paul had violated the Prompt Pay Act.[43] St. Paul timely appealed.[44]

The Texas Prompt Pay Act provides, in relevant part:

> (a) Except as provided by Subsection (b) or (d), an insurer shall notify a claimant in writing of the acceptance or rejection of a claim not later than the 15th business day after the date the insurer receives all items, statements, and forms required by the insurer to secure final proof of loss.
>
> . . .
>
> (d) If the insurer is unable to accept or reject the claim within the period specified by Subsection (a) or (b), the insurer, within that same period, shall notify the claimant of the reasons that the insurer needs additional time. The insurer shall accept or reject the claim not later than the 45th day after the date the insurer notifies a claimant under this subsection.[45]

On appeal St. Paul argued that because neither it nor its adjuster had ever received three specific pieces of information, it had never received "all items, statements, and forms required by the insurer to secure final proof of loss."[46] St. Paul contended that the fifteen-day period had therefore never begun, and it therefore had not violated the Prompt Pay Act.[47]

Specifically, St. Paul indicated that although it had received invoices showing well-control costs, Weiser-Brown had never submitted evidence it had actually paid the invoices.[48] Second, St. Paul said that Weiser-Brown had never submitted proof of its insurable interest, which after some back and forth turned out to mean proof that none of the interest holders in the well had opted out of coverage.[49] Third, St. Paul claimed that it had never received the engineering data underlying Weiser-Brown's claim, specifically "mud reports" and "check sheets."[50]

The court was not persuaded. In a footnote, the court indicated that the second piece of missing information was not even missing—St. Paul's adjuster had acknowledged its receipt of written confirmation that no interest holders had opted out of coverage.[51] With respect to the other pieces of information, the court found first that St. Paul and its adjuster had not requested it in their later communications with Weiser-Brown.[52] More importantly, however, the court found that the information clearly was not necessary to St. Paul's coverage determination, because the adjuster had made the decision without it.[53] The court summarized its holding pithily: "[t]he insurer cannot avoid liability under [the Prompt Pay Act] by pointing after-the-fact to missing information, the absence of which did not affect the insurer's decision."[54] The court therefore affirmed the district court's award of 18% interest on damages pursuant to the Prompt Pay Act.[55]

This case sounds a cautionary note for insurers. The Prompt Pay Act cannot be avoided merely because an insured fails to completely respond to every request for documents. Insurers should ask for all of the information they need to make a

decision, each and every time they communicate with the insured, especially if communications regarding the claim continue over a long period. If an insurer still can't make a decision, it must communicate this to the insured and ask for additional time, or agree to pay part of the claim but not the rest until additional information is provided, as the statute allows.[56]

Exclusive Dealing Arrangements with Insurance Brokers Are "Business of Insurance" Under McCarran-Ferguson Act, and Immune from Sherman Act Attacks.

Sanger Insurance Agency v. HUB International, Ltd., 802 F.3d 732 (5th Cir. 2015).

The *Sanger* case deals with the intersection of antitrust law and insurance law, and the bounds of the McCarran-Ferguson Act. The Fifth Circuit held that exclusive dealing arrangements between insurance brokers and insurers can neither be attacked under federal antitrust laws, nor challenged as unfair trade practices under the Texas Insurance Code.

The plaintiff Sanger Insurance Agency claimed that its business development plans were thwarted by a competing insurance program of another insurance broker, HUB International, Ltd.[57] Specifically, Sanger wanted to improve its position in the market for veterinary professional liability insurance, which it claimed was 90% dominated by the HUB program.[58] Sanger sued HUB under sections 1 and 2 of the Sherman Act, sections 15.05(a)-(c) of the Texas Free Enterprise and Antitrust Act, and for unfair trade practices under the Texas Insurance Code.

The district court granted summary judgment in favor of HUB on all claims, holding that broker exclusive-dealing arrangements fell within the "business of insurance" regulated by the states (in this case, Texas) under the McCarran-Ferguson Act, and did not fall under the exception for "boycott, coercion, or intimidation," and therefore could not be challenged under the Sherman Act.[59] On the state antitrust claims, the district court concluded that Sanger did not meet the prerequisite of being "prepared to enter the market."[60] Finally, the district court found that the alleged trade practices represented neither tortious interference nor a boycott under the Texas Insurance Code, and so were not unfair trade practices under Texas state law.[61]

The Fifth Circuit partly agreed with this assessment with respect to the federal antitrust laws. First, the Fifth Circuit found that Sanger could show federal antitrust standing.[62] Where a plaintiff is not currently in business in the market in which antitrust violations are alleged, the plaintiff must show (1) an intent to enter the market, and (2) preparedness to enter it.[63] Based on Sanger's evidence of foreclosed business opportunities, the court found that Sanger met both prongs of this test.[64]

Having found standing, the court nevertheless found that the alleged exclusive-dealing arrangements, because they fell within the definition of "business of insurance" under the McCarran-Ferguson Act and did not fall within a relevant exception, were regulated under state law.[65] The court began by enunciating the Supreme Court's famous three criteria test for determining whether certain business practices fall within the business of insurance:

> first, whether the practice has the effect of transferring or spreading a policyholder's risk; second, whether the practice is an integral part of the policy relationship between the insurer and the insured; and third, whether the practice is limited to entities within the insurance industry.[66]

The court explained that even atypical broker-insurer relationships usually fall within the first criterion, and in this case HUB's role was necessarily to "funnel a broad risk pool to particular insurers."[67] Moreover, the court found that because the arrangement affected how and from whom insureds bought insurance, the second criteria was met as well, and the third criteria was not in dispute.[68]

At this point, Sanger's last stab at federal antitrust claims was the McCarran-Ferguson Act's exemption for conduct that amounted to "boycott, coercion, or intimidation." The court found, however, that this exception did not apply where the alleged "boycott" was by only a single broker, even where that broker coordinated with various insurers, provided the insurers did not directly coordinate with each other.[69]

The court's remaining holdings were largely governed by its disposition of the federal antitrust issues. The court's holding on the federal "boycott, coercion, or intimidation" exception, for instance, determined its finding on the state law unfair trade practices claim, because the provision of Texas law under which Sanger alleged its trade practices claim closely tracked the language of the federal law.[70] The court was therefore bound to affirm summary judgment on that claim.[71] On the other hand, the court's determination that Sanger had standing under federal antitrust laws meant it also had standing under state antitrust laws, which revived a potential state antitrust claim as well as a tortious interference claim; the court refused to affirm the district court's summary judgments on those claims and remanded.[72]

Like all cases interpreting the scope of "business of insurance," this case is likely to be frequently cited in the future even though it arguably does not break new ground in confirming the general proposition that broker-insurer relationships fall within the "business of insurance" for the purposes of McCarran-Ferguson. *Sanger* does, however, suggest an avenue for insurers and brokers to avoid antitrust liability, while still excluding potential market entrants.

The court's decision that brokers and insurers may enter into exclusive-dealing arrangements so long as individual insurers do not coordinate with one another directly suggests a mechanism for avoiding the application of the "boycott, coercion, or intimidation" exception. Insurers and brokers should be careful, however, since *Sanger* does not rule out the possibility of state antitrust enforcement.

Injury from Toxic Installation Falls Within Pollution Exclusion Because Injuries Suffered Resulted from Vapors, Not Mere Physical Contact.

Evanston Insurance Co. v. Lapolla Industries, Inc., No. 15-20213, 2015 WL 9460301 (5th Cir. Dec. 23, 2015).

Lapolla Industries, Inc. manufactures polyurethane insulation.[73] Evanston Industries, Inc. was their Commercial General Liability (CGL) insurer.[74] A contractor installed Lapolla insulation in a house being renovated; the owners, who did not reside in the rooms in which the insulation was installed, reported respiratory distress and were forced to move out.[75] Ultimately, the owners sued the contractors and Lapolla.[76] Evanston filed suit for a declaratory judgment that it was not required to provide defense costs under the pollution exclusions in its CGL policies with Lapolla.[77]

The district court, after a thorough analysis, came to the conclusion that the exclusion applied, and Lapolla was not entitled to coverage for its defense costs.[78] Ultimately, the question came down to how the injuries were caused—whether by direct physical contact with the insulation, or by vapors released or discharged in the installation process.[79] The policy defined "pollution" thusly:

> "Bodily Injury" or "property damage" which would not have occurred in whole or part but for the actual, alleged or threatened *discharge, dispersal, seepage, migration, release or escape of pollutants at any time. . .* . Pollutants mean any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals, electromagnetic fields and waste. Waste includes materials to be recycled, reconditioned or reclaimed.[80]

Applying the eight-corners rule, the district court found, and the Fifth Circuit agreed, that the homeowners' pled injuries caused by "odors" and "vapors."[81] The court therefore inferred that the injuries were caused by a discharge, dispersal, or release under the policy, and were thus subject to the exclusion.[82]

On appeal, Lapolla argued that the Fifth Circuit should apply an exception to the eight-corners rule and look at extrinsic evidence in the form of deposition testimony that some plaintiffs had physically touched the insulation.[83] The court considered the argument but noted that under the appropriate precedent, the exception to the eight-corners rule applied only where it was "initially impossible" to determine coverage based on the pleadings themselves.[84] The Fifth Circuit found that the underlying plaintiff's complaint clearly alleged excluded injuries, and the extrinsic evidence suggesting an alternative theory of causation did not retroactively render impossible a determination of coverage based only on the complaint and the policy.[85] The Fifth Circuit affirmed the district court on all grounds, holding that Lapolla was not entitled to defense costs.[86]

This case changes little, but it does clarify the scope of the exception to the eight-corners doctrine. Neither insurers nor policyholders should expect to be able to establish sufficient ambiguity to show that it is "initially impossible" to determine coverage under the policy and the complaint by offering extrinsic evidence inconsistent with a theory of causation that is plain on the face of the complaint.

1 *U.S. Metals, Inc. v. Liberty Mut. Group, Inc.*, No. 14-0753, 2015 WL 7792557, at *1 (Tex. Dec. 4, 2015).

2 *Id.*

3 *Id.*

4 *Id.*

5 *Id.* The policy further defined "impaired property" (for which coverage is excluded) to include any property that could be restored to use by the "replacement" or repair of "your product."

6 *U.S. Metals, Inc. v. Liberty Mut. Group, Inc.*, 589 Fed. Appx. 659, 663 (5th Cir. 2014), *certified question accepted* (Sept. 26, 2014), *certified question answered sub nom.*, *U.S. Metals, Inc. v. Liberty Mut. Group, Inc.*, No. 14-0753, 2015 WL 7792557 (Tex. Dec. 4, 2015).

7 *Id.*

8 *U.S. Metals*, 2015 WL 7792557, at *3

9 *Id.* at *6

10 *Id.*

11 *Id.*

12 *Id.* at *2.

13 *Id.*

14 *Id.* at *6–7.

15 Indeed, arguably more surprising is the insured's reliance in this matter on Judge Posner's *Erie* misstep in *Eljer Mfg., Inc. v. Liberty Mut. Ins. Co.*, 972 F.2d 805 (7th Cir. 1992), which the Illinois Supreme Court rejected in *Travelers Ins. Co. v. Eljer Mfg., Inc.*, 757 N.E.2d 481 (Ill. 2001).

16 The first instance was *In re Deepwater Horizon*, 728 F.3d 491, 500 (5th Cir. 2013), in which the Fifth Circuit asked the Texas Supreme Court whether the interaction of indemnity and additional-insured language in a drilling contract and the text of the applicable umbrella policy created coverage where the umbrella policy, read alone, would not. The Texas Supreme Court

answered that question in *In re Deepwater Horizon*, 470 S.W.3d 452 (Tex. 2015).

17 *In re Deepwater Horizon*, 807 F.3d 689, 693 (5th Cir. 2015), *certified question accepted* (Dec. 4, 2015).

18 *Id.*

19 *Id.* at 692.

20 *Id.*

21 *Id.* at 693.

22 *Id.* at 694.

23 *Id.* at 694–95

24 *Id.* at 695.

25 *Id.* at 696.

26 *Id.*

27 *Id.* at 696–97.

28 *Id.* at 697.

29 *Id.*

30 *Id.*

31 *See generally Great Am. Ins. Co. v. AFS/IBEX Fin. Servs., Inc.*, 612 F.3d 800 (5th Cir. 2010).

32 *See generally Vail v. Texas Farm Bureau Mut. Ins. Co.*, 754 S.W.2d 129, 136 (Tex. 1988) (holding that for the purposes of enhanced damages under the Texas Deceptive Trade Practices Act an "insurer's unfair refusal to pay the insured's claim causes damages as a matter of law in at least the amount of the policy benefits wrongfully withheld.").

33 *Deepwater Horizon*, 807 F.3d at 698–99.

34 *Weiser-Brown Operating Co. v. St. Paul Surplus Lines Ins. Co.*, 801 F.3d 512, 515 (5th Cir. 2015).

35 *Id.*

36 *Id.* at 515–16.

37 *Id.* at 516.

38 *Id.*

39 *Id.*

40 *Id.* at 517.

41 *Id.* at 516–17.

42 *Id.* at 517.

43 *Id.*

44 *Id.*

45 Tex. Ins. Code Ann. § 542.0.56 (West 2015)

46 *Weiser-Brown*, 801 F.3d at 519.

47 *Id.*

48 *Id.* at 523

49 *Id.*

50 *Id.* at 523–24.

51 *Id.* at 523 n.9.

52 *Id.* at 524.

53 *Id.*

54 *Id.*

55 *Id.* at 517, 530.

56 *Id.* at 524.

57 *Sanger Ins. Agency v. HUB Intern., Ltd.*, 802 F.3d 732, 734 (5th Cir. 2015)

58 *Id.*

59 *Id.*

60 *Id.*

61 *Id.*

62 *Id.* at 741.

63 *Id.* at 738.

64 *Id.* at 738–41.

65 *Id.* at 747.

66 *Id.* at 742.

67 *Id.* at 744.

68 *Id.* at 745. The court did not deeply analyze the question of whether Texas or any other states in which HUB operated regulated insurance, because the court found Sanger's arguments on this point to be incomplete and unpersuasive. *Id.* at 745–46.

69 *Id.* at 746–47.

70 *Id.* at 749.

71 *Id.*

72 *Id.* at 748–49.

73 *Evanston Ins. Co. v. Lapolla Indus., Inc.*, No. 15-20213, 2015 WL 9460301, at *1 (5th Cir. Dec. 23, 2015).

74 *Id.*

75 *Id.*

76 *Id.*

77 *Id.* at *2.

78 *Id.* at *5.

79 *Id.* at *2.

80 *Id.* (emphasis added).

81 *Id.* at *3.

82 *Id.*

83 *Id.* at *4.

84 *Id.*

85 *Id.*

86 *Id.* at *5.

STATE BAR OF TEXAS
Insurance Law Section
P.O. Box 12487, Capitol Station
Austin, Texas 78711-2487

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