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Contents

Supreme Court Giveth And The Supreme Court Taketh Away: Pre-Judgment Interest Recoverable On Um Claims But Attorneys Fees Are Not

On December 22, 2006, in a triumvirate of opinions, the Texas Supreme Court answered the questions of whether or not prejudgment interest and/or attorney fees are recoverable under uninsured/underinsured motorist coverage. In holding that uninsured/underinsured motorist coverage covers prejudgment interest that the uninsured or underinsured motorist would have owed the insured in tort liability but not attorneys' fees, the court focused on the statutory language of the Insurance Code, the Civil Practices and Remedies Code and judicial precedent.

The majority of the Supreme Court's opinion on the issues is encompassed in the *Lilithe Brainard v. Trinity Universal Insurance* Company opinion. The court noted the Insurance Code provides UIM coverage for payment to the insured of all sums that he is legally entitled to recover as damages from owners or operators of underinsured motor vehicles because of bodily injury up to the limit specified in the policy, reduced by the amount recovered or recoverable from the insurer of the underinsured motor vehicle. Further, prejudgment interest is awarded to fully compensate the injured party, not to punish the defendant. The court stated, "We have consistently viewed prejudgment interest as falling within the common law meaning of damages." The policy provided that Trinity would pay "damages" that the insured was legally entitled to recover from the negligent party. The court held that prejudgment interest the insured could have recovered from the uninsured/underinsured motorist as a result of bodily injury or property damage was covered under the policy at issue. *Brainard* at p.6. Trinity did not dispute or contend that a narrower meaning of "damages" was required by the statute. The Court distinguished the *Henson v. Southern Farm Bureau* opinion as that case dealt only with contractual prejudgment interest, not prejudgment interest as a result of tort liability.

Pre-Judgment Interest Recoverable On Um Claims But Attorneys Fees Are Not (Cont'd)

The court then set forth a calculation method for prejudgment interest which incorporated the declining principal formula. In applying the declining principal formula, the court noted that payments made by the underinsured motorist as well as PIP benefits would decrease the amount upon which prejudgment interest could be levied. The court further noted that settlement offers which remained open for acceptance, would also limit the amount of prejudgment interest which could be recovered. The court remanded the matter to the trial court to modify the judgment with regard to prejudgment interest.

With regard to the recovery of attorney's fees, the court specifically held that in the UM/UIM context, no breach of contract occurs until the carrier refused to timely pay a judgment secured against the uninsured or underinsured motorist. The court noted that under Section 38.002 of the Texas Civil Practices and Remedies Code, the insured must show that she was represented by counsel; she presented the claim to the carrier and the carrier failed to pay the just amount owned within 30 days of presentment. The court noted that the issue turned on the language in Chapter 38 that required payment for the just amount owed. "Neither requesting UIM benefits nor filing suit against the insurer triggers a contractual duty to pay. Rather, the UIM insurer is under no contractual duty to pay benefits until the insured obtains a judgment establishing the liability and underinsured status of the other motorist. Where there is not contractual duty to pay, there is no just amount owed and thus under Chapter 38 a claim for UIM benefits is not presented until the trial court signs a judgment establishing the negligence and underinsured status of the other motorist." *Brainard* at 8.

The court further noted that the insured is not required to obtain a judgment against the tortfeasor but could settle with the tortfeasor and then litigate the UIM claim coverage with its insurer. However, neither "a settlement nor an admission of liability from the tortfeasor establishes UIM coverage because a jury could find that the other motorist was not at fault or award damages that do not exceed the tortfeasor's liability insurance. *Brainard* at p.8. The court recognized "the UIM contract is unique because, according to its terms, benefits are conditioned upon the insured's legal entitlement to receive damages from a third party. Unlike many first party insurance contracts, in which the policy alone dictates coverage, UIM insurance utilizes tort law to determine coverage. Consequently, the insurer's contractual obligation to pay benefits does not arise until liability and damages are determined." *Brainard* at 8. Both Trinity and Brainard filed motions for rehearing.

Also on December 22nd, the court released its opinions in *State Farm Mutual Automobile Insurance Company v. Norris and State Farm Mutual Insurance Company v. Nickerson*. The *Nickerson* opinion only solidifies the court's ruling that attorney's fees are not recoverable in the UIM context under Texas Civil Practice and Remedies Code § 38.002. The *Norris* case addressed an additional issue with regard to the offsets in the UIM context. In *Norris,* Norris settled with the underlying carrier for $40,000 which was $10,000 less than the $50,000 policy limit. Norris argued that he would be entitled to prejudgment interest on the entire $50,000 and the Supreme Court disagreed. "UIM policies are intended to compensate injured parties 'up to the limit specified in the policy, reduced by the amount recovered or recoverable from the insurer of the underinsured motor vehicle' Texas Insurance Code Article 5.06-1(5). When Norris settled and released his claim against Johnston, he also released any interest in the difference between Johnston's policy limit and the settlement amount. The purpose of prejudgment interest is to compensate a claimant for the lost use of money due as damages during the lapse of time from the accrual of the claim and the date of the judgment. Cite omitted. Because Norris had not lost use of that $10,000, having released any entitlement to it, he can receive prejudgment interest only on the amount of the settlement ($40,000 plus the amount that exceeds Johnston's policy limit ($1,200)." *Norris* at p.2.

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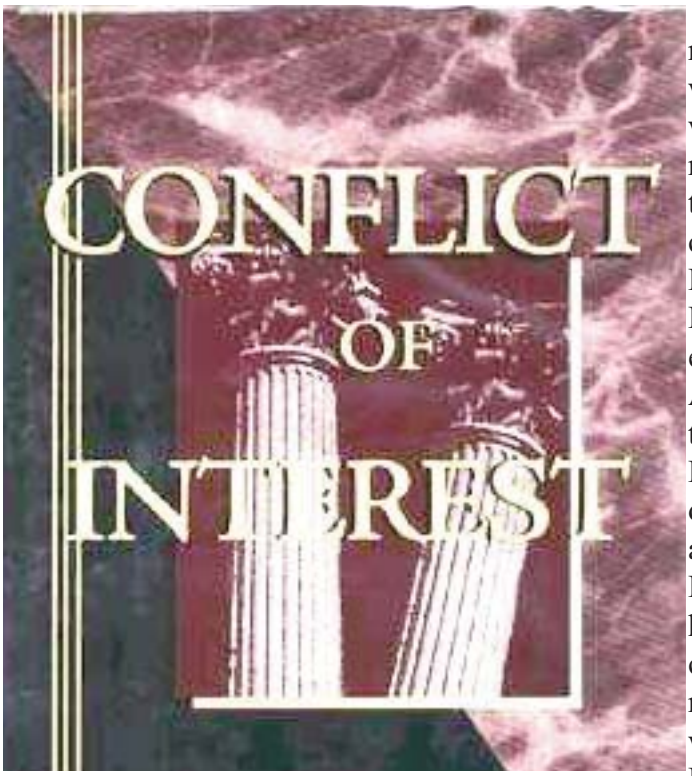
Texas Court of Appeals Adopts Standard for Disqualifying an Expert Witness' Testimony for Conflict of Interest: Formosa Plastics Corp. v. Kajima International, Inc.

Motions to disqualify experts on conflicts-of-interest grounds appear to be increasing, although it remains the rare circumstance where such motions are granted. In a case of first impression, the Corpus Christi Court of Appeals en banc affirmed the trial court's decision not to disqualify an expert witness for the plaintiff who worked at the same consulting firm as another expert witness with whom the defendant consulted (but did not ultimately use). *Formosa Plastics Corp. v. Kajima Int'l, Inc.*, ____ *S.W.3d* ____, 2006 WL 3804507 (Tex. App. – Corpus Christi Dec. 28, 2006) (en banc).



Kajima, an industrial construction company, sued Formosa for breach of contract, fraud, and quantum meruit arising out of Kajima's work on the expansion of a Formosa plant in Port Comfort, Texas. Kajima allegedly incurred $38 million in costs on a project for which it bid substantially less and was only paid $10 million by Formosa. *Formosa Plastics, 2006 WL 3804507 at *1*. Kajima blamed the cost overruns on Formosa, while Formosa contended that Kajima's cost overruns were Kajima's own fault. *Id.* at *2.

Formosa's original counsel, Jones Day, contacted Steven Huyghe, an expert in heavy industrial construction and president of A.W. Hutchison & Associates of California, Inc. Huyghe met with Jones Day and Formosa's in-house counsel to discuss strategy and was asked to review documents produced by both parties. *Id.* at *2. Huyghe then prepared a work plan outlining his proposed method for evaluating the case and an index of relevant documents produced by Kajima. *Id.* Huyghe also sent several letters to Jones Day, on which he copied A.W. Hutchison, who served as president of A.W. Hutchison & Associates, Inc. in Atlanta. *Id.* at *3. However, the letters received by Hutchison did not include any confidential information, but primarily consisted of budget estimates and proposals for work.

Formsa replaced Jones Day with Porter & Hedges, which chose not to retain Huyghe. Some time later, Kajima's counsel retained Hutchison and Brian Rogers, another expert in Hutchison's Atlanta office. The trial court denied Formosa's motion to disqualify Hutchison and Rogers after Huyghe testified that he had never discussed any Formosa-related information with Hutchison or Rogers, the Jones Day lawyers testified that they never spoke with Hutchison or Rogers and did not know of any confidential information disclosed to Hutchison or Rogers, and Hutchison himself testified that Huyghe had not provided him with any confidential information concerning Formosa. *Id.* at *3. At trial, Kajima received a $30 million judgment, and Formosa appealed, claiming among other things that the trial court erred in permitting Hutchison and Rogers to testify because they worked at the same firm as Huyghe.

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Formosa Plastics Corp. v. Kajima International, Inc.

The Court of Appeals held that an expert may be disqualified if the moving party can prove that (1) the moving party had an objectively reasonable basis to believe that a confidential relationship existed between that party and the expert witness, and (2) confidential or privileged information was in fact provided to the expert witness. Id. at *5 (citing Koch Refining Co. v. Jennifer L. Boudreaux MV, 85 F.3d 1178, 1181 (5th Cir. 1996). The Court explained that numerous factors could be considered in determining whether a "confidential relationship" existed between the expert and the moving party, including the number of contacts

between the expert and counsel, the existence of a confidentiality agreement, the payment of a retainer or other fee to the expert, whether work product was given to the expert, and the extent to which the expert learned of the party's litigation strategies. Id. at *6. The Court also explained that "confidential information" was largely limited to that information that was protected by the attorney-client privilege or attorney work product, such as the party's litigation strategy, the party's views of the strengths and weaknesses of each side, and the role of each expert. Id. at *7. "Confidential information" did not include technical information or information that was discoverable. Id.

Under these facts, the Court held that Formosa did not satisfy its burden of proof on its disqualification motion, because it did not show that Formosa had a confidential relationship with Hutchison or Rogers, or that Hutchison or Rogers had obtained confidential information about Formosa from Huyghe or the Jones Day lawyers. Id. at *8. The Court also held that while Huyghe would have been disqualified had Kajima hired him, it would not impute his knowledge to the other consultants and experts at his firm for purposes of disqualification. Id. "The disqualification rules applicable to attorneys, which would allow for disqualification of a firm based on imputed knowledge, should be inapplicable to expert witnesses." Id.

Although Formosa Plastics helps to clarify Texas' rules as to expert disqualification, it also emphasizes the need for counsel to confirm that the expert has run a conflicts check, to avoid defending against a motion to disqualify later in the case. It also emphasizes the need for counsel to secure a confidentiality provision within a formal retention agreement from the expert before disclosing any confidential information to that expert.

Formosa Plastics Corp. v. Kajima International, Inc.

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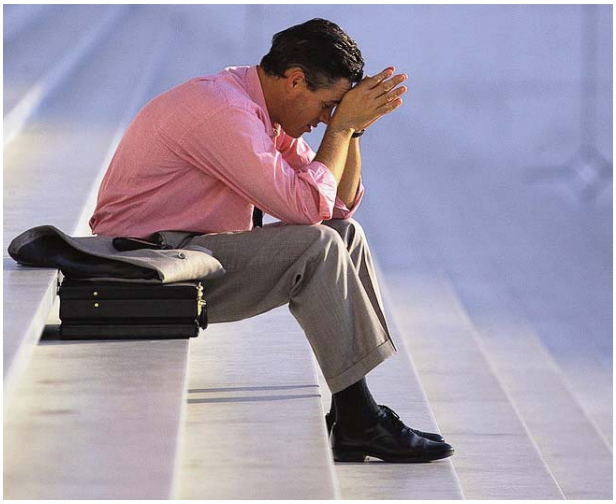
Texas Supreme Court Provides Guidance On Both Exemplary Damages And Attorneys Fees

The Texas Supreme Court has provided some long awaited guidance on the recovery of both exemplary damages as well as attorney's fees. In *Tony Gullo Motors I, LP v. Chappa*, Case No. 04-09-61 (Dec. 22, 2006), the court set forth guidelines for the recover of exemplary damages and attorneys fees in cases involving breach of contract, fraud, and violations of the DTPA.

Plaintiff Nury Chapa was subjected to a fraudulent bait-and-switch by Tony Gullo Motors. The evidence showed that Gullo Motors forged a number of documents and harangued Chapa when she insisted on delivery of the Toyota Highlander Limited that she



ordered rather than a base-model Highlander the defendant tendered to her. The jury awarded her almost $30,000 of actual damages (the difference in value of the two models plus mental anguish), exemplary damages of $250,000, and attorney's fees of $20,000. The Court of Appeals remitted half of the exemplary damages, reducing it to $125,000. On December 22, 2006, the Texas Supreme Court held that the exemplary damage of $125,000 on $30,000 of actual damages (a 4.33 to 1 ratio) was constitutionally excessive. *Tony Gullo Motors I, L.P. v. Chapa*, Case No. 04-0961 (Dec. 22, 2006). The court also remanded the motion to the trial court on the amount of attorney's fees recoverable, setting forth more clearly defense guidelines regarding recovery of fees when both covered and non-covered claims exist.

The Texas Supreme Court examined the guidelines established by the United States Supreme Court in *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408 (2003). The three "guideposts" set by that opinion were: (1) the nature of the defendant's conduct, (2) the ratio between exemplary and compensatory damages, and (3) the size of civil penalties in comparable cases.

The court stated that the first "guidepost," the reprehensibility of Gullo Motors conduct, in turn depended on five factors, only one of which supported an award of exemplary damages. First, Gullo Motors' actions did not cause physical, rather than economic harm. Second, they did not threaten the health or safety of others. Third, they did not involve repeated acts by the defendant, rather than an isolated incident. Fourth, although Chapa claimed she was financially vulnerable, the only harm she alleged (the lack of certain features on her SUV) did not threaten her with financial ruin. The Court did note that the final factor, that Gullo Motors' conduct was deceitful rather than accidental, pointed in Chapa's favor.

Concerning the second guidepost, the ratio between actual and exemplary damages, the Texas Supreme Court quoted the U.S. Supreme Court that "few awards exceeding a single-digit ratio . . . will satisfy due process." The Court of Appeals' remitted award exceeded four times Chapa's total compensatory award. The jury had awarded precisely three times as much for her mental anguish as were her economic damages, which ratio supported the U.S. Supreme Court's observation that emotional damages themselves often already include a punitive element. Accordingly, the Texas Supreme Court ruled that this factor showed the Court of Appeals' judgment pushed against, if not exceeded, constitutional limits.

Finally, the Texas Supreme Court considered the third guidepost, comparison of exemplary damage awards to civil penalties in comparable cases. Both potential civil penalties examined by the Texas Supreme Court were limited to $10,000 or $20,000. Although Chapa argued the possibility of criminal liability or loss of license by Gullo Motors, she presented no proof of such a sanction ever being awarded in a similar case, and the Texas Supreme Court repeated the U.S. Supreme Court's statement that, "the remote possibility of a criminal sanction does not automatically sustain a punitive damages award."

TEXAS SUPREME COURT PROVIDES GUIDANCE ON BOTH EXEMPLARY DAMAGES AND ATTORNEYS FEES (CONT'D)

Finally, the Texas Supreme Court stated pushing exemplary damages to the absolute constitutional limit in a case such as Chapa's left no room for greater punishment in cases involving death, grievous physical injury, financial ruin, or actions that endanger a large segment of the public. Therefore, although the defendant's conduct merited exemplary damages, the Court found the amount awarded was beyond constitutional limits. It remitted the case back to the Court of Appeals to find a further reduction of the exemplary damages in order to meet constitutional limits.

With regard to recovery of attorney's fees, under Texas law, plaintiff can recover her reasonable and necessary attorney's fees for successfully suing under a breach of contract or DTPA claim, but not for a fraud claim. At trial, Chapa's attorney testified about his reasonable and necessary fees, but claimed that his work on the fraud claims "could not possibly be distinguished" from that on the contract and DTPA claims. Gullo Motors objected that the fees were not recoverable because the testimony did not segregate the work between portions necessary for the claims for which fees are recoverable and those for which they are not.

The Texas Supreme Court agreed and reversed and remanded for a new trial on the fee issue. It noted that under Texas law, attorney's fees are not recoverable unless authorized by statute or contract, and, as a result, fee claimants have always been required to segregate fees between claims for which they are recoverable and claims for which they are not. In 1991, however, it recognized an exception in *Stewart Title Guaranty Co. v. Sterling*, 822 S.W.2d 1 (Tex. 1991):

A recognized exception to this duty to segregate arises when the attorney's fees rendered are in connection with claims arising out of the same transaction and are so interrelated that their 'prosecution or defense entails proof or denial of essentially the same facts.' Therefore, when the causes of action involved in the suit are dependent upon the same set of facts or circumstances and thus are 'intertwined to the point of being inseparable,' the party suing for attorney's fees may recover the entire amount covering all claims.

(822 S.W.2d at 11-12) (internal citations omitted).

The Chapa court discussed that the various Texas courts of appeals disagreed as to what makes two claims "inextricably intertwined" as well as the unresolved question of whether possibility of segregation is a question of law, a question of fact, or a mixed question of law and fact. It noted several instances in which work that was presented by Chapa's attorney could not be reasonably related to a cause of action for which fees are recoverable as well as the inconsistent position taken by Chapa's attorney as to whether she merely had a breach of contract case or an additional fraud case.

Because of these types of problems, the court ruled that Sterling was incorrect to the extent it suggested a common set of underlying facts necessarily made all claims arising therefrom "inseparable" and all legal fees recoverable. The court agreed that many services involved in preparing a claim for which fees are recoverable must still be incurred even if there are other claims, such as standard discovery, depositions of primary actors, and voir dire. At the same time, pure tort-related claims, such as presentation of the defendant's net worth (for exemplary damages purposes), drafting of pleadings or jury charges related to fraud, and similar items are not recoverable. The court ruled that intertwined facts do not make tort-claim fees recoverable; it is only when discrete legal services advance both the recoverable and unrecoverable claims that they are so intertwined that they need not be segregated.

With respect to items that are partially applicable to both covered and non-covered claims, however, a plaintiff's attorney does not need to keep separate time records. For example, in drafting a petition containing claims for which attorney's fees are both recoverable and non-recoverable, the attorney can testify about the percentage of time that would have been necessary even if there had been no claim for which fees are not recoverable. Presumably, the same argument would hold with respect to drafting of jury charges and matters related to more specific discovery.

Texas Supreme Court Provides Guidance On Both Exemplary Damages And Attorneys Fees (Cont'd)

A defendant insurance company involved in a suit that has claims for which attorney's fees are not recoverable and claims for which they are should be prepared to use the Texas Supreme Court's clarification. If there is a large amount of work that is arguably only necessary for the claims for which fees are not recoverable, the attorney conducting a cross-examination of the plaintiff's attorney's fee expert should be prepared to note that specific work. The attorney should be prepared to challenge the attorney's fee expert on voir dire, by pre-trial motion to exclude testimony, and/or on cross-examination about items of work that were not necessary for the claims for which fees are recoverable, and, for items necessary to both types of claims, as to the relative percentages of time and effort. Attention should be paid to legal research and to matters related to dispositive motions as those types of work are particularly vulnerable to a need for segregation of time.

Finally, this opinion should be useful to insurance companies on appeals from "bad jurisdictions" in non-bodily-injury case where exemplary damage is awarded in excessive of amounts allowed under civil statutes such as the Texas Deceptive Trade Practices – Consumer Protection Act and the Texas Insurance Code, particularly where the case does not involve bodily injury. In addition to careful consideration of each of the other factors, the defendant should emphasize that pushing the constitutional limits in their particular case would leave no room for greater punishment in cases involving "death, grievous physical injury, financial ruin, or actions that endanger a large segment of the public."

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Texas Supreme Court Considers Questions of Liability Insurer's Duties to Additional Insured Who Does Not Request Defense or Coverage

In National Union Fire Insurance Co. of Pittsburgh, PA v, Beatrice Crocker, the Texas Supreme Court has been asked to address what duties, if any, are owed by a liability carrier to an insured (other than the named insured), who has been sued but has not tendered its defense or otherwise requested a defense from the insurer. This issue raises extra-contractual questions as to an insurer's duties in light of standard policy language that sets forth an insured's duties under a policy.

In the underlying case, Crocker was allegedly injured when struck by a swinging kitchen door at the Redwood Springs Nursing Home where she was a resident. Crocker brought suit in state court against Emeritus Corporation, the owner of the nursing home, and a former nursing home employee allegedly involved in the incident, Richard Morris. Emeritus immediately tendered its defense to National Union after being served in May 2002, and National Union retained defense counsel who represented Emeritus through trial.

At Morris' deposition held just prior to trial, Morris refused to talk with Emeritus' counsel in private, although he initially conferred with Crocker's counsel. At the beginning of his deposition, Morris told both counsel that he had contacted a lawyer but had not heard back from him. Emeritus' counsel thought that Morris had an attorney and would not talk with him for that reason, but Morris had apparently called a lawyer only to find out if Crocker's allegations against him could lead to a prison term.

Morris never answered Crocker's suit, and in September 2003, Crocker moved for a default judgment against Morris. The case was called to trial in October 2003, but Morris did not enter an appearance. At the conclusion of the evidence and at Crocker's request, the case against Morris was severed into a separate lawsuit. The jury then rendered a take-nothing defense verdict against Crocker, specifically finding that Emeritus, acting through its agents, including Morris, was not negligent. The trial court subsequently granted a default judgment against Morris in the amount of $1,000,000. Morris did not contest the default judgment.

TEXAS SUPREME COURT CONSIDERS QUESTIONS (CONT'D FROM PAGE 7)

Crocker, as a judgment creditor, brought suit against National Union to collect the judgment against Morris, an additional insured under Emeritus' policy. National Union removed the suit to federal court. It was undisputed that Morris had no knowledge that he was an insured under the policy. At summary judgment, National Union argued it had no duty to defend Morris because he never tendered his defense to National Union by forwarding the suit papers and never gave any indication to National Union or Emeritus that he desired a defense. National Union also argued that Morris breached the policy's notice and cooperation conditions, and that it was prejudiced as a matter of law in that it had no authority to retain a lawyer to defend Morris without his permission. Finally, National Union argued it was not bound by the default judgment because there was not an actual trial pursuant to State Farm Fire & Casualty Co. v. Gandy, where the Texas Supreme Court had held that an insurer is not bound by an insured's agreed-to judgment where there was no actual trial. Crocker, in turn, argued that National Union was not prejudiced since it was aware that Morris had been sued and had been served with the lawsuit.

The federal district court agreed with Crocker and granted summary judgment in her favor, holding that National Union had not satisfied its burden to establish that it was prejudiced by Morris' failure to tender his defense since National Union had knowledge that Morris had been sued and served with the lawsuit prior to trial. The court also rejected National Union's argument that it was not bound by the default judgment, holding that Gandy was not applicable since the default judgment was an actual trial.

National Union appealed the district court's ruling to the Fifth Circuit Court of Appeals. In response, the Fifth Circuit addressed the history of Texas law on an insured's breach of a notice condition and turned to the Texas Supreme Court to address "unresolved" questions of Texas law. In doing so, the Fifth Circuit contrasted older Texas Supreme Court authority in an insurer's favor with more recent authority requiring an insurer to establish prejudice where there is knowledge that an insured has been sued and served with a lawsuit.

The Fifth Circuit ultimately concluded that Texas law was unsettled with respect to insureds that are ignorant of their coverage under a named insured's policy (in contrast to sophisticated additional insureds that might be charged with knowledge that they are potentially additional insureds). In particular, the court noted that the law was uncertain and presented three questions to the Texas Supreme Court at to the following: (1) what duties, if any, are owed by an insurer to defend an additional insured with whom it has no direct relationship, and who, knowing of the suit, has not expressly or impliedly requested a defense; 2) what duties, if any, does the insurer have to notify a sued additional insured (who does not know of the coverage) of its entitlement to coverage; and 3) what duties, if any, the additional insured might owe in such a situation.

The Texas Supreme Court will have to decide whether it will impose a duty on liability insurers to notify insureds other than the named insured that they may be entitled to a defense. Pursuant to the standard policy language, the insured (regardless of whether the insured is the named insured, an insured, or an additional insured) owes a contractual duty to provide notice to the insurer that it has been served with a lawsuit and that it desires a defense. If the court decides to create an extra-contractual duty on insurers only with respect to insureds who do not know they are potentially entitled to coverage, it will need to decide the extent of that duty. Will a telephone call or a letter suffice? What does the communication need to say? Must the insurer reserve rights in that correspondence if there is a potential question of coverage? What if there are many potential insureds under the policy? Must the insurer ascertain whether each and every one of them is potentially entitled to a defense and then provide each of them notice? Imposing such an extra-contractual duty on insurers will potentially open a can of worms with unforeseen consequences.

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Pre-Judgment Interest Recoverable On Um Claims But Attorneys Fees Are Not (con'td from page 2)

Another note of interest is the "written notice requirement" to begin the accrual of prejudgment interest. The Supreme Court notes that prejudgment interest begins to accrue 180 days after the carrier receives written notice of the accident as opposed to the claim or alternatively on the date the lawsuit is filed, which ever is earliest. In the Norris matter, written notice of the accident was given by way of a report sent to State Farm from an attending physician. That date was approximately 49 days after the accident occurred. Thus, prejudgment interest began to accrue 180 days after the written notice of the accident from the attending physician. Further, the court noted in both Norris and Brainard that credits applied before prejudgment interest began to accrue reduced the principal. Thereafter, each credit would apply first to the accrued prejudgment interest and second to the remaining principal. However, the carrier could be liable up to the UIM policy limits for the principal plus accrued prejudgment interest remaining after the credits were applied.

These rulings by the Supreme Court virtually eliminate the risk of attorney's fees to the carrier in the UM/UIM context and may well eliminate the risk of a violation of Article 542.051 of the Texas Insurance Code. The Supreme Court has specifically recognized the unique nature of a first party claim for UM benefits. Defense counsel have long argued that since a "claim" is defined as "one that must be paid" under statutory language of 542.051 *et. seq.*, there can be no violation of the prompt payment statute until a judgment or agreement is reached regarding liability and damages in the UM context. Thus if the carrier tenders payment within five business days of the judgment, it would appear to have complied with the Insurance Code's prompt payment provisions. Logically, if the courts apply the holdings of Brainard, Norris and Nickerson to the UM cases pending before them, there should be little risk of extra-contractual exposure in the UM cases in Texas.

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AMARILLO COURT OF APPEALS IS FIRST TO APPLY BRAINARD

On February 7, 2007, the Amarillo Court of Appeals issued its opinion in *Mid Century Insurance Company of Texas v. Daniel*. In an opinion on a motion for rehearing, the court overruled the motion for rehearing but withdrew their previous opinion and judgment of November 28, 2006 and issued a new opinion. In this new opinion, the court applies the *Brainard* decision to a claim for attorneys fees and pre-judgment interest under Article 21.55, (now 542.051).

The original lawsuit involved the Daniels, the negligent third party and Mid Century as the underinsured carrier. The claims against Mid Century were severed and abated. A non jury trial on November 13, 2002, set the damages for the Daniels. After deducting the amounts paid by the liability carrier, Mid Century tendered the remaining balance of the judgment within two days. Mid Century then filed a motion for summary judgment on extra contractual claims which included Article 21.21 (now 541) and 21.55 (now 542.051 *et. seq*.). While the trial court initially granted summary judgment for the Daniels and awarded both attorneys fees and prejudgment interest under Article 21.55, the Court of Appeals reversed that judgment based on Brainard and its holding that a UM carrier's obligation to pay benefits did not arise until liability and damages were determined. Thus, Mid Century's payment within two days of judgment against a third party precluded an award of attorneys' fees under Article 21.55 §§ 4 and 6 and § 38.002 of the Texas Civil Practice and Remedies Code. The Court went further and stated that prejudgment interest was not recoverable under 21.55 because the judgment was "information necessary to secure final proof of loss" that was needed under Article 21.55.

This case is the first to apply the Brainard holding to claims under the prompt payment statute. While the opinion does not directly speak to the issue, it can be assumed that the carrier did promptly acknowledge the claim and seek information regarding the damages. However, because an agreement could not be reached with regard to both liability and damages, the court held it was appropriate to try the matter prior to requiring payment of UM benefits. Since the judgment became a required piece of information for the UM carrier, prior to its obligation to pay, and payment was then made within two days of the determination of liability and damages, the court reasoned that no violation had occurred since prior to judgment there had not been a "claim" which must be paid.

If other courts of appeals follow Amarillo in its application of the Brainard holding, it may become increasingly difficult for insureds to recover any statutory penalties under Article 542.051 in the uninsured/underinsured motorist context.

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Subrogation's Made Whole Doctrine: Not A Tool For Extracting A Double Recovery

Insureds are increasingly attempting to use the made whole doctrine to block insurers' subrogation rights, thereby increasing their total recovery. The United States District Court for the Northern District, Judge Sam Lindsay presiding, however, recently issued an opinion rejecting such use of the made whole doctrine. See *Veazey v. Allstate Texas Lloyds*, 2007 WL 29239 (N.D. Tex. Jan. 3, 2007).

In Texas, an "[a]n insurer is not entitled to subrogation if the insured's loss is in excess of the amount recovered from the insurer and the third party causing the loss." *Ortiz v. Great Southern Fire and Cas. Ins. Co.*, 597 S.W.2d 342, 343 (Tex. 1980)(citations omitted). This principle, referred to as the made whole doctrine, stands for the proposition that "when either the insurer or the insured must to some extent go unpaid, the loss should be borne by the insurer for that is a risk the insured has paid it to assume." Id. at 344. Even with respect to an insurer's contractual right to subrogation, some courts have held that such reimbursement rights are still subject to the equitable principles of the made whole doctrine. *Fortis Benefits v. Cantu*, 170 S.W.3d 755, 758 (Tex. App.—Waco 2005, pet. granted August 25, 2006).

In Veazey a suspected defect in the insureds' automobile caused it to catch fire, destroying the vehicle and the insured's house. Following the fire, the insureds' homeowners' insurer paid policy limits to the insureds for the damages to the house, their personal property and for living expenses. The insureds, however, claimed damages in an amount almost eight times greater than their policy limits and filed a lawsuit against the manufacturer of the automobile. Having paid policy limits to the insureds, the insurer then intervened in the lawsuit asserting its subrogation rights against the manufacturer. The insurer ultimately settled its subrogation claim against the manufacturer before trial. Thereafter, the insureds also settled their claim against the manufacturer prior to trial.

The insureds then filed a declaratory judgment action against their insurer seeking a declaration that the insurer had no right, as the insureds' subrogee, to enter a settlement agreement with the third-party tortfeasor before the insureds could recover for all of their alleged losses resulting from the fire. The insureds contended that because they had not been made whole through their settlement with the tortfeasor, their insurer was not entitled to subrogation and should be required to turn over the money it received from the tortfeasor in its own settlement as a subrogee. The insurer moved for summary judgment arguing that the made whole doctrine did not apply and that it was not obligated to turn over its settlement proceeds to the insureds.

In granting the insurer's summary judgment, the court holds that under the specific facts of the case, the made whole doctrine is not applicable, and the insureds were attempting to misuse it. While the court acknowledges the Ortiz opinion, Judge Lindsay notes that there is no authority supporting the position that until the insureds recover 100% of their claimed damages, the insurer has no right to recover its vested subrogation interest directly from the third-party tortfeasor. Rather, the court finds that an insurer may be entitled to subrogation, even though the insured has not been "made whole."

The court clarified that recovery in tort for uninsured losses belongs exclusively to the injured plaintiff, and that an insurer is only entitled to subrogation for tort payments for insured losses for which the plaintiff has already been compensated. The court also notes that, unlike other injured plaintiffs who rely on the made-whole doctrine as a shield from their insurers' reimbursement claims for non-insured damages, the insureds in Veazey were improperly attempting to use the doctrine as a sword to extract a double recovery for payments covering insured losses. In essence, the court concludes that the insureds could not make up for their inadequate policy limits by extracting additional payments from their insurer's subrogation recovery.

The Veazey opinion appears to be the first opinion in Texas expressly recognizing that the made whole doctrine does not block an insurer's right to subrogation recovery for covered losses which it paid to the insured. It should be noted, however, that the Texas Supreme Court has granted review and recently heard oral argument in *Fortis Benefits v. Cantu*, 170 S.W.3d 75 (Tex.App.-Waco 2005, pet. granted), a case where the Waco Court of Appeals rejected an insurer's attempt to enforce its subrogation rights on a claim where an automobile accident victim's health insurer sought reimbursement following the insured's settlement of his tort claims. Accordingly, it is expected that in the near future, the Texas Supreme Court will further clarify the extent of the made whole doctrine in Texas.

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