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Stowers Update – Effect of Coverage Defenses

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ISSUE

- IF THERE IS A COVERAGE ISSUE AND A STOWERS DEMAND IS MADE, CAN THE INSURER RELY ON THE COVERAGE ISSUE?
- IF THE INSURER IS WRONG, WHAT HAPPENS?
- TO WHAT EXTENT IS THE COVERAGE ISSUE A DEFENSE?
- IF IT IS A DEFENSE, IS IT A QUESTION OF FACT OR QUESTION OF LAW?

EARLY CASES

- Meridian Oil Production, Inc. v. Hartford Acc. and Indem. Co., No. G-91-167 (S.D. Tex., Galveston Div., Mar. 4, 1993)
  - "The Supreme Court of the State of Texas has not rendered a decision on the issue of whether Stowers is applicable in a coverage dispute situation. The issue of whether a summary judgment that insured's actions were not covered occurrences under the insurer's policies thus precluding a subsequent Stowers claim would also be one of first impression. However, the Court finds support in cases, such as State Farm Fire and Casualty Co. v. Taylor, 832 S.W.2d 645 (Tx. Ct. App.--Fort Worth 1992, writ denied Feb. 1993), that the Supreme Court of Texas, if presented with either issue would not find a viable Stowers claim."

EARLY CASES

- "The imposition of the Stowers doctrine when a coverage dispute exists or has been determined in insurer's favor would effectively eliminate the insurer's ability to contest coverage during a reservation of rights case. Under Texas law, an insurance company cannot intervene in the underlying lawsuit to contest coverage nor bring a declaratory judgment action regarding its duty to indemnify until the same lawsuit is completed. Taylor at 352. Many policies contain clauses which prohibit litigation against the insurer until the underlying litigation is completed."

EARLY

- “If a court applies Stowers in causes of action in which coverage is legitimately being contested under a reservation of rights, more insurers are apt to deny coverage outright, thus, further undermining the duty to defend and leaving policyholders with the full burden of their defense. Moreover, applying the duty to settle in this scenario would render the ‘reservation of rights’ letter useless and would force insurers into situations of unconditional acceptance.”

EARLY CASES

- "In a coverage dispute situation in which the insurer is defending under a reservation of rights, other courts have found it perfectly reasonable to allow the insured to settle with the third-party claimant if it so chooses or allow the case to go to trial. Later the insured can seek reimbursement from the insured. Of course the insurer cannot, in good faith, conduct a reservation of rights defense in a manner prejudicial to the policyholder."

OTHER JURISDICTIONS

- MOST JURISDICTIONS ADDRESSING THIS MATTER HAVE HELD THAT AN INSURER WHO REFUSES TO SETTLE BECAUSE OF A COVERAGE DEFENSE TAKES THE RISK THAT ITS CONCLUSION MAY BE INCORRECT
- Windt, Insurance Claims and Disputes, Sec. 5.5, Sixth Edition (2015)

APIE

- APIE v GARCIA, 876 S.W.2D 842 (TEX. 1994)
  - STOWERS DEMAND FOR $600K AND ISSUE WAS WHETHER THERE WERE $600K OR $200K LIMITS AVAILABLE
  - “CONVERSELY, APIE ELECTED TO BEAR THE RISK THAT ITS POINT OF VIEW MIGHT HAVE BEEN INCORRECT, WHICH COULD RESULT IN LIABILITY FOR ANY EXCESS JUDGMENT.”

- THREE CASES-ALL INVOLVED STOWERS AND COVERAGE ISSUES -- THREE DIFFERENT RESULTS
  - SEGER v. YORKSHIRE INS. CO., (TEX. JUNE 2016)
  - ONEBEACON INS. CO. v. WELCH, 841 F.3D 669 (5TH CIR. NOV. 2016)
  - U.S. METALS v. LIBERTY INS. CO., 2017 WL 830398 (S.D. TEX. FEB. 2017)

SEGER

- SEGER v. YORKSHIRE INS. CO., (TEX. JUNE 2016)
  - 1992 RANDY SEGER KILLED IN DRILLING RIG ACCIDENT
  - EMPLOYED BY ECS-ECS PROVIDED SERVICES TO DIATOM DRILLING CO.
  - $500K GL POLICY
  - EXCLUDED EMPLOYEES AND LEASED-IN WORKERS/EMPLOYEES
  - SEGER WAS A "LEASED IN" EMPLOYEE
  - OCT 1998 DEMAND FOR $500,000
  - JUNE 1999 $368,190 DEMAND
  - MARCH 2001 TRIAL $250,000 DEMAND
  - TRIAL-$15M PLUS INTEREST

SEGER

- STOWERS TRIAL-JURY VERDICT OF $37,213,592.01
- APPEALED, REVERSED AND REMANDED
- OCT 2011 CASE RETRIED
- JURY FOUND SEGER NOT EMPLOYEE OR LEASED-IN WORKER
- AWARDED $71,696,547.

SEGER

- WHAT IS THE RESULT?

SEGER

- TEXAS SUPREME COURT FOUND UNDER CORRECT DEFINITION OF “LEASED-IN” WORKER THAT “RANDALL SEGER WAS A LEASED-IN WORKER AS A MATTER OF LAW.”
- THE COURT HELD THAT THE “PARENTS FAILED TO ESTABLISH COVERAGE, AN ESSENTIAL ELEMENT OF ANY STOWERS ACTION.”

SEGER

- COURT DID NOT HOLD THAT THE "EXISTENCE" OF A COVERAGE ISSUE WAS A VALID STOWERS DEFENSE
- COURT ADDRESSED UNAUTHORIZED INSURANCE ISSUES UNDER 101.201 AND 981.005
- COURT HELD EXPERT'S TESTIMONY BASED ON WRONG STANDARD WAS NO EVIDENCE

WELCH

- ONEBEACON INS. CO. v. T. WADE WELCH & ASSOC., 841 F.3D 669 (5TH CIR. NOV 2014)
  - WELCH REPRESENTED DISH NETWORK IN BOSTON CASE
  - 2005 DISCOVERY SERVED BY RMG (RUSSIAN MEDIA GROUP) ON DISH
  - NO RESPONSE FILED BY WOOTEN (WELCH)
  - MOTION TO COMPEL FILED
  - NO RESPONSE
  - FEBRUARY 2006 COURT COMPELLED RESPONSE TO ALL DISCOVERY PROPOUNDED

WELCH

- WOOTEN RESPONDED TO REQUEST FOR ADMISSIONS AND INTERROGATORIES BUT NOT VERIFIED
- NOVEMBER 20, 2006 WELCH COMPLETED APPLICATION FOR WESTPORT INSURANCE-NOT AWARE OF ANY CIRCUMSTANCES LIKELY TO LEAD TO A CLAIM
- DECEMBER 20, 2006 WELCH SAID STATEMENTS MADE TO WESTPORT WOULD BE TRUE AS TO ONEBEACON

WELCH

- ONEBEACON POLICY ISSUED 12/20/06-07 WITH RETRO DATE OF JANUARY 4, 1995
- ONEBEACON HAD EXCLUSION FOR CIRCUMSTANCES INSURED REASONABLY BELIEVED PRIOR TO INCEPTION OF POLICY WOULD RESULT IN A CLAIM
- FEB 2007 RMG FILED MOTION FOR SANCTIONS FOR FAILURE TO COMPLY WITH FEBRUARY 2006 ORDER COMPELLING DISCOVERY
- JULY 12, 2007 DEATH PENALTY SANCTIONS ENTERED
- WOOTEN DID NOT TELL DISH OR THE FIRM

WELCH

- DECEMBER 2007 WELCH COMPLETED RENEWAL APPLICATION FOR ONEBEACON
- ANSWERED “NO” AS TO WHETHER ANY LAWYER HAD BEEN SANCTIONED OR KNOWLEDGE OF CIRCUMSTANCES THAT MIGHT LEAD TO A CLAIM

WELCH

- FEBRUARY 2008 DISTRICT COURT AFFIRMED SANCTIONS
- WELCH AND DISH LEARNED OF SANCTIONS
- APRIL 2008 WELCH NOTIFIES ONEBEACON
- JUNE 4, 2008 WELCH TELLS ONEBEACON THAT RMG WANTS $105,800,000 TO SETTLE
- DECEMBER 2010 DISH ASKS ONEBEACON TO MAKE ITS POLICY LIMITS AVAILABLE
- ROR SENT BY ONEBEACON

WELCH

- JUNE 14, 2011 DISH OFFERS TO SETTLE AND RELEASE WELCH FIRM FOR POLICY LIMITS BUT NOT RELEASE WOOTEN
- JUNE 27, 2011 WELCH ASKS ONEBEACON TO PAY LIMITS
- AUGUST 5, 2011 ONEBEACON DECLINES OFFER
- AUGUST 22, 2011 ONEBEACON RESCINDS POLICY AND FILES DJ ACTION
- MARCH 2013 IN ARBITRATION PROCEEDING ARBITRATOR AWARDS DISH $12.5M AGAINST WELCH WHICH WAS CONFIRMED BY STATE COURT JUDGE IN JUNE 2013

WELCH

- WHAT IS THE RESULT?
- HOW WOULD YOU HAVE ANSWERED THE APPLICATION: “HAVE YOU OR ANY MEMBER OF YOUR FIRM EVER BEEN DISBARRED, REFUSED ADMISSION TO PRACTICE LAW, SUSPENDED, REPRIMANDED, **SANCTIONED**, FINED, PLACED ON PROBATIION, HELD IN CONTEMPT . . .”
- DID THE JULY 12, 2007 DEATH PENALTY SANCTIONS ORDER FORM A “REASONABLE BASIS TO BELIEVE THAT YOU HAD COMMITTED A WRONGFUL ACT, VIOLATED A DISCIPLINARY RULE, OR ENGAGED IN PROFESSIONAL MISCONDUCT”?

WELCH

- JURY VERDICT OF $12.5M ACTUAL DAMAGES FROM JUDGMENT, $8M LOST PROFITS, $5M PUNTIVE DAMAGES AND $7.5 ADDITIONAL DAMAGES UNDER INSURANCE CODE

WELCH

- AT TRIAL JURY FOUND THAT ONEBEACON DID NOT PROVE ITS CLAIM FOR RESCISSION AND DID NOT PROVE THE PRIOR KNOWLEDGE EXCLUSION. COURT OF APPEALS FOUND SUFFICIENT EVIDENCE TO SUPPORT THE FINDING OF THE JURY THAT WELCH DID NOT MAKE A MISREPRESENTATION IN APPLICATION

WELCH

- COURT DID NOT HOLD THAT THE EXISTENCE OF THE COVERAGE DEFENSE (APPLICATION AND PRIOR-KNOWLEDGE EXCLUSION) WAS A DEFENSE TO STOWERS NOR WAS IT RAISED BY ONEBEACON
- COURT ALSO RULED THAT A STOWERS DEMAND TO LESS THAN ALL OF THE INSUREDS IS A VALID STOWERS DEMAND CONTRARY TO PATTERSON v. HOME STATE (2014)

US METALS

- U.S. METALS v. LIBERTY INSURANCE CO., 2017 WL 830398 (S.D. TEX. 2017)
  - 9/1/09-9/1/10 LIBERTY POLICY PERIOD
  - JUNE 2010 EXXON DISCOVERED LEAKS IN FLANGES
  - U.S. METALS SOLD 350 FLANGES FOR REFINERIES IN BATON ROUGE AND BAYTOWN.
  - JUNE 10, 2011 SUIT FILED FOR $6,345,824 REPAIR COSTS AND $16,656,000 LOSS OF USE

US METALS

- LIBERTY **DENIED COVERAGE** AND US METALS SUED IN FEDERAL COURT
- NOVEMBER 22, 2011 US METALS SETTLES FOR $2.2M
- JULY 2, 2013 TRIAL COURT GRANTS SUMMARY JUDGMENT TO LIBERTY
- CASE APPEALED TO 5TH CIRCUIT AND CERTIFIED TO TEXAS SUPREME COURT

US METALS

- TEXAS SUPREME COURT HELD THE COST OF REPLACING THE FLANGES WAS COVERED

- LIBERTY POLICY HAD LIMITS OF $1M
- SETTLEMENT $2.2M
- WERE COVERED DAMAGES ABOVE LIMITS-$6.3M

US METALS

- SUMMARY JUDGMENT GRANTED BY DISTRICT COURT ON STOWERS-
- “HOWEVER, PLAINTIFF HAS NOT MADE A SHOWING CREATING A GENUINE ISSUE OF MATERIAL FACT THAT DEFENDANT DID NOT HAVE A REASONABLE BASIS FOR DENYING THE CLAIM.”

US METALS

- NO INDICATION IF DEMAND TO SETTLE FOR POLICY LIMITS
- COURT DID NOT ADDRESS NEED FOR STOWERS DEMAND
- COURT DID NOT ADDRESS THE FACT THAT COVERED DAMAGES EXCEEDED POLICY LIMITS

ISSUE

- IS COVERAGE A DEFENSE TO A STOWERS ACTION AND IF SO, HOW DOES IT WORK?

COVERAGE ISSUES

- APIE v GARCIA
  - "THE STOWERS DUTY IS NOT ACTIVATED BY A SETTLEMENT DEMAND UNLESS THREE PREREQUISITES ARE MET: (1) THE CLAIM AGAINST THE INSURED IS WITHIN THE SCOPE OF COVERAGE, (2) THE DEMAND IS WITHIN THE POLICY LIMITS, AND (3) THE TERMS OF THE DEMAND ARE SUCH THAT AN ORDINARILY PRUDENT INSURER WOULD ACCEPT IT, CONSIDERING THE LIKELIHOOD AND DEGREE OF THE INSURED'S POTENTIAL EXPOSURE TO AN EXCESS JUDGMENT."

COVERAGE ISSUES

(1) THE CLAIM AGAINST THE INSURED IS WITHIN THE SCOPE OF COVERAGE-

SEGER v. YORKSHIRE INS. CO.

WHEN MUST COVERAGE EXIST? AT THE TIME OF THE STOWERS DEMAND OR AT THE TIME OF THE JUDGMENT?

COVERAGE ISSUES

- (2) THE DEMAND IS WITHIN THE POLICY LIMITS

  ONLY LOOK AT COVERED DAMAGES-ST PAUL FIRE & MARINE INS. CO. v. CONVALESCENT SERVICES, INC.

COVERAGE ISSUES

- (3) THE TERMS OF THE DEMAND ARE SUCH THAT AN ORDINARILY PRUDENT INSURER WOULD ACCEPT IT

  US METALS -- QUESTION OF LAW -- TRIAL COURT HAD EARLIER SAID THERE WAS NO COVERAGE. HOW COULD YOU SAY THERE WAS NO REASONABLE BASIS EVEN THOUGH LATER PROVEN TO BE WRONG?

COVERAGE ISSUES

- WELCH-FACT QUESTION-JURY WAS ABLE TO DETERMINE WHETHER IT WAS REASONABLE FOR ONEBEACON TO RELY ON THE PRIOR KNOWLEDGE EXCLUSION
- QUESTION OF FACT COVERAGE ISSUE -- UP TO THE JURY
- QUESTION OF LAW COVERAGE ISSUE -- MAY BE A MATTER OF LAW