Frank's Casing - -
Practice Implications of the Anticipated Opinions on Rehearing

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CHAPTER 2

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I. Introduction - Important Insurance Cases Pending Before the Texas Supreme Court

This paper is primarily about the Texas Appellate decision known as *Frank's Casing* (Tex. 2005). *Frank's Casing* is presently pending before the Texas Supreme Court on rehearing. Before entering into the thicket of *Frank's Casing*, it is important to note other major insurance cases which are **presently pending** before the Texas Supreme Court. The specifics of each case are beyond the scope of this paper. The mere listing of these cases demonstrates how much change may occur in the near future.

A. *Lamar Homes v. Mid-Continent* (Cause No. 05-0832, Argued February 14, 2006)

This is a landmark case involving coverage issues in the **construction defect area**. The Fifth Circuit Court certified three questions to the Texas Supreme Court, which the Supreme Court accepted:

(1) When a home buyer sues his general contractor for construction defects and alleges only damage to or loss of use of the home itself, do such allegations allege an **"accident"** or **"occurrence"** sufficient to trigger the duty to defend or indemnify under a CGL policy?

(2) When a home buyer sues his general contractor for construction defects and alleges only damage to or loss of use of the home itself, do such allegations allege **"property damage"** sufficient to trigger the duty to defend or indemnify under a CGL policy?

(3) If the answers to certified questions 1 and 2 are answered in the affirmative, does **Article 21.55** of the Texas Insurance Code apply to CGL insurer's breach of the duty to defend? *Lamar Homes, Inc. v. Mid-Continent Cas. Co.*, 428 F.3d 193 (5th Cir. 2005). Resolution of this case will likely be determinative of what is or is not covered in construction defect litigation.

B. *Fairfield Insurance Co. v. Stephens Martin Paving, L.P.* (Cause No. 04-0728, Argued November 9, 2004)

381 F.3d 435 (5th Cir. 2004). The Supreme Court accepted another certified question from the Fifth Circuit. The certified question involves **a liability insurer's duty to indemnify its insured for an award of punitive damages based on gross negligence**. The Fifth Circuit certified the following question: "Does Texas public policy prohibit a liability insurance provider from indemnifying an award for punitive damages imposed on its insured because of gross negligence?"

C. *Mid-Continent Insurance Co. v. Liberty Mutual Insurance Co.* (Cause No. 05-0261, Argued October 18, 2005)

407 F.3d 683 (5th Cir. 2005). The supreme court recently accepted this case on certification from the Fifth Circuit. The issues deal with what are the duties, if any, of a co-primary carrier to another carrier where one carrier pays more than its proportionate part of the settlement and the level of proof of that duty, if any.

D. *Unauthorized Practice of Law Commission v. American Home Assurance Co.* (Cause No. 04-0138, Argued September 28, 2005)

121 S.W.3d 831 (Tex. App.—Eastland 2004, pet. granted). The issues are whether insurance companies unlawfully practice law when they use their **attorney-employees in "captive" law firms** to defend their insureds, and whether an attorney hired by an insurance company to defend its insured has an attorney-client relationship with the insurance company itself. The Court of Appeals held that captive firms were not prohibited.

E. *GuideOne Elite Insurance Co. f/k/a Preferred Abstainers Ins. Co. v. Fielder Road Baptist Church* (Cause No. 04-0692, Argued October 20, 2005)

139 S.W.3d 384 (Tex. App.—Fort Worth 2004, pet. granted). In this case, the court of appeals held that extrinsic evidence that the insured's employee stopped working for the insured before the insured's commercial general liability insurance went into effect could not be considered under the "eight corners" rule in determining whether the insurer had a duty to defend, and that the victim's allegations were sufficient to allege a claim for damages as a result of bodily injury from sexual misconduct within the coverage of the policy's sexual misconduct provision. **The Supreme Court will have an opportunity to decide what evidence is permissible in evaluating the duty to defend.**

F. *Fiess v. State Farm Lloyds* (Cause No. 04-1104, Argued March 30, 2005)

392 F.3d 802 (5th Cir. 2004). This homeowner's coverage case is another certified question from the Fifth Circuit Court of Appeals. The case asks whether **mold which ensues from water damage is covered under the Texas HO-B policy**. The lower court also held that the "ensuing loss" clause in the mold exclusion did not create coverage for the mold losses. The Fifth Circuit surveyed Texas law and noted a split among several

Texas courts which had previously addressed the coverage issue and certified the coverage question to the Texas Supreme Court.

II. Factual and Procedural Background of Frank's Casing

A. Opinion on Original Submission: May 2005

On ***May 27, 2005***, the Texas Supreme Court reversed and remanded a Judgment from Houston Court of Appeals. The case is styled at the Supreme Court as ***Excess Underwriters at Lloyd's, London and Certain Companies Subscribing Severally but Not Jointly to Policy No. 548/TA4011FO1 v.*** **Frank's Casing Crew & Rental Tools, Inc.**, No. 02-0730. Frank's Casing is unquestionably one of the most controversial and important decisions from the Texas Supreme Court in many years. The reason is that the central holding of the "majority" - - if it remains intact on rehearing - - is a reversal of prior Texas law and practice. A copy of the 5/27/05 opinion is attached at the conclusion of this paper. The emphasis and formatting in the attached opinion is my own and not from the Court. This paper is a discussion of the case which has come to be known simply as "Frank's Casing".

B. Backdrop of *Matagorda County* (Tex. 2000)

In **December of 2000**, in *Texas Association of Counties County Government Risk Management Pool v. Matagorda County,* 52 S.W.3d 128 (Tex. 2000) ("*Matagorda County*"), **seven Justices of the Texas Supreme Court** held that an insurance carrier could not, on those facts, settle a lawsuit in response to a *Stower's* demand and thereafter seek to recover the amounts paid in settlement, even if the claims of the Plaintiff were determined **not to be covered** by the policy. The majority opinion was written by **Justice O'Neill** and held that a carrier can seek reimbursement for non-covered settlement payments ***only*** if the carrier obtains the insured's ***clear and unequivocal consent*** to the settlement ***and*** to the carrier's right to seek reimbursement. **Justice Owen** wrote a dissenting opinion in which **Justice Hecht** joined. In light of *Matagorda County*, in December of 2000 Texas law would generally not permit an insurance company to settle a lawsuit and thereafter seek reimbursement from the insured - - even if the funds were paid to settle the claims which were not covered.

C. Factual Background of *Frank's Casing*

At least a decade ago an oil platform collapsed in the Gulf of Mexico and litigation resulted. ARCO sued several parties, including Frank's Casing Crew & Rental Tools, Inc. Frank's Casing was founded in 1938 and provides oil and gas equipment rentals and sales to exploration and production customers operating in Louisiana, Mississippi, and Texas.

The excess carrier for Frank's Casing at the time of the collapse was a Lloyd's company or a Lloyd's group of carriers and are referred to by name in the opinion as **Excess Underwriters at Lloyd's, London and Certain Companies Subscribing Severally but Not Jointly to Policy Number 548/TA4011F01** ("**EU**"). EU as the excess carrier had asserted several times in one or more reservation of rights letters ("**ROR**") that there were coverage issues in the case and EU took the position that some of the Plaintiff's claims were not covered under the EU policy.

D. Settlement of the Underlying Suit

Shortly before trial in the underlying case where ARCO had sued Frank's Casing, EU attempted to settle Plaintiff's claims that EU conceded were covered under their policy, leaving unsettled Plaintiff's other claims against Frank's Casing. EU also offered as an alternative to settle the policy dispute with Frank's Casing by paying two-thirds of a global settlement with Plaintiff's. Finally, EU also offered to provide $5 million for settlement if Frank's agreed to arbitrate all coverage issues. Frank's Casing rejected all these proposals.

The in-house counsel for Frank's Casing then sought and obtained a settlement demand from the Plaintiff within the excess policy limits and forwarded the Plaintiff's aggregate $7.5 million demand to EU. EU agreed that the case should be settled for this amount and stated that they would fund the settlement up to $7.5 million, including any contribution from the primary carrier, if Frank's Casing would expressly agree that all coverage issues would be resolved at a later date. Frank's Casing refused and sent a **second letter** to EU demanding that the EU accept Plaintiff's settlement offer. The excess underwriters then advised Frank's Casing that they would pay $7.5 million, less any contribution from the primary carrier, and that EU **would** seek reimbursement from Frank's Casing for the amounts which were not covered. Frank's Casing did not respond to that letter. That same day, the underwriters contacted Plaintiff and orally accepted the settlement offer.

E. EU Files a Declaratory Judgment ("DJ") on Coverage

At the same time that EU settled Plaintiff's claims, EU informed Frank's Casing that it intended to seek

reimbursement or the $7 million it had paid. EU then filed a Declaratory Judgment seeking a declaration that there was no coverage for the claims that were settled **and** seeking reimbursement for the monies paid in settlement.

F. The Trial Court's Judgment

The trial court in the DJ initially ruled that the settlement amounts were not covered, and that EU did have a right of reimbursement for the monies paid in settlement. On December 21, 2000, the Texas Supreme Court handed down its opinion in *Matagorda County*. On February 12, 2001, the trial court reversed its ruling allowing reimbursement in light of the opinion in *Matagorda County* and concluded that EU was not entitled to reimbursement even though the claims settled were not covered by the EU policy.

G. The 14th Court of Appeals

EU appealed to the 14th Court of Appeals in Houston. In **June of 2002** the Court of Appeals, in an opinion by Justice Brister, affirmed the trial court's denial of reimbursement based on the holding of *Matagorda County*. *Excess Underwriters at Lloyd's, London and Certain Companies Subscribing Severally but Not Jointly to Policy No. 548/TA4011FO1 v. Frank's Casing Crew & Rental Tools, Inc*., 93 S.W.3d 178 (Tex. App. - - Houston [14th] June 27, 2002 **pet. granted**).

In his opinion, Justice Brister stated:

> "We recognize this case carries *Matagorda County* to a logical conclusion that is somewhat ***disquieting*** -- Frank's Casing was able to resolve the parties' coverage dispute in its own favor simply by sending a *Stowers* demand to the underwriters. Thereafter, the underwriters had to pay if ARCO's [Plaintiff's] claims were *within* the policy, but also had to pay *if they are not* within the policy because there was no right to reimbursement. But this is a matter that the Underwriters must take up with the ***superior court***." (emphasis added)

H. Supreme Court

EU followed Justice Brister's suggestion and sought relief in the Texas Supreme Court. On April 3, 2003, the Supreme Court granted EU's Petition for Review and two years later delivered its original opinion, ***Excess Underwriters at Lloyd's, London and Certain Companies Subscribing Severally but Not Jointly to Policy No. 548/TA4011FO1 v. Frank's Casing Crew & Rental Tools, Inc.***, Cause No. 02-0730, 2005 Tex. Lexis 418, 48 Tex. Sup. J. 735 (Tex. May 27, 2005). The EU policy gave Frank's Casing the right to consent to settlement.

The Court's opinion in May of 2005 resulted in an avalanche of controversy, multiple Amicus briefs, a staggering amount of blog and other professional commentary, including turmoil, anguish and delight generally in the tort litigation community. The political line-up of the players taking sides on rehearing is surprising. There are briefs by Shell Oil and Temple Inland on behalf of the **insured** - - *Frank's Casing*. Not surprisingly, they are an equal number of advocacy briefs by insurance industry representatives and non-profit trade organizations in support of EU.

The case was first argued on ***9/24/03***. In its original opinion of **May 27, 2005**, the Supreme Court remanded the case to the trial court with directions to order that Frank's Casing ***reimburse EU for the $7 million*** that EU paid to settle ARCO's claims.

Justice Brister, by this time on the Supreme Court, did not participate in the decision. After the original May 2005 opinion, Frank's Casing filed a Motion for a Rehearing on **July 20, 2005**. There were a significant number of Amicus briefs on both sides. The Supreme Court granted the Motion for Rehearing on **January 6, 2006.**

The cause was **reargued** on **February 15, 2006**. As of the date this paper is submitted, no further opinion or ruling has come down from the Court.

III. *Gandy*, *Stowers*, *Arnold*, *Giles*

There are cases which have come to be known by one name that are involved in Frank's Casing. Reference will be made in the following analysis by reference to their name only. These cases are:

Gandy and ***Griffin*** refers to S*tate Farm Fire & Cas. Co. v. Gandy*, 925 S.W.2d 696 (Tex. 1996) and *Farmers Texas County Mut. Insurance. Co. v. Griffin*, 955 S.W.2d 81, 84 (Tex. 1997). In the context of this discussion of *Frank's Casing*, these cases are important for the holding that an insurer's duty to indemnify is justiciable before the insured's liability is decided in an underlying suit when the insurer has no duty to defend and the same reasons that negate the duty to defend negate any possibility that insurer will ever have a duty to indemnify. In *Gandy*, the Supreme Court, cautioned insurers either to accept coverage or make a good-faith effort to resolve coverage before resolving the underlying claim.

Stowers refers to *G.A. Stowers Furniture Co. v. Am. Indemn. Co.*, 15 S.W.2d 544, 547 (Tex. Comm'n App. 1929, holdings approved) where the Texas

Supreme Court implied a duty imposed on an insurer to accept a settlement demand within policy limits if the claim is covered and an ordinarily prudent person would accept it. The leading recent case in the 1990's on the "*Stowers*" doctrine is *American Physicians Insurance. Exch. v. Garcia*, 876 S.W.2d 842, 849 (Tex. 1994).

Arnold refers *Arnold v. National County Mut. Fire Insurance. Co.*, 725 S.W.2d 165, 167 (Tex. 1987) where the Texas Supreme Court imposed as a matter of law a duty of good faith and fair dealing in contracts of insurance.

Giles refers to *Universe Life Insurance. Co. v. Giles*, 950 S.W.2d 48 (Tex. 1997) which is a landmark Texas Supreme Court case on what constitutes a violation of the implied duty or good faith and fair dealing in an insurance context.

IV. *Texas Association of Counties County Government Risk Management Pool v. Matagorda County* (Tex. December 21, 2000)

A. Background

Frank's Casing and the controversy created by the May 2005 opinion of the Court can only be understood in the context of the opinion of the Supreme Court in *Matagorda County*. In *Matagorda County*, the coverage was provided by the risk management pool (i.e., "**the carrier**") for *Matagorda County* ("**insured**") and excluded coverage for any claim arising out of the jail. Some jail inmates assaulted other prisoners. The assaulted prisoners brought suit against *Matagorda County*. At first **the carrier** would not even provide a defense. After negotiations, **the carrier** provided a defense subject to a ROR letter. **The carrier** also filed a declaratory judgment ("DJ") against the County and contended that the claims were not covered. The County in turn counterclaimed against the carriers in the DJ.

The prisoner Plaintiffs made an offer to settle the case within the County's policy limits. The defense lawyer (i.e., hired by the carrier) for the County advised **the carrier** that the demand was reasonable and prudent given the facts. **The carrier** asked the County to fund the settlement. The County took the position that it would not contribute to the settlement. **The carrier** then issued a second ROR reserving its rights to deny coverage and to seek reimbursement of the settlement funds from the County if the DJ established that the claims of the Plaintiffs were not covered.

The insurance policy gave **the carrier** the power to settle within its discretion. **The carrier** settled the lawsuit, amended its DJ claim, and sought reimbursement of the $300,000.00 paid in settlement. The reasonableness of the settlement was not in dispute. The DJ proceeded to trial on coverage, and the trial court, after a jury trial, rendered a DJ that the claims of the underlying Plaintiffs were not covered, and further held that **the carrier** could recover the $300,000.00 from the County. The Court of Appeals held that there was no equitable remedy to permit **the carrier** to recover the $300,000.00 settlement funds.

B. The 7-2 Majority

On December 21, 2000, the Texas Supreme Court affirmed and held that there was no right of reimbursement on these facts.

The Supreme Court divided on a **7 to 2 basis**. The majority opinion was by **Justice O'Neill**, joined by Chief Justice Phillips, and Justices Enoch, Baker, Abbott, Hankinson, and Gonzales. Justice Owen dissented and was joined by Justice Hecht.

The majority noted at the outset that whether a carrier can seek reimbursement for settlement funds paid under an ROR where there was a adjudication of noncoverage was an " . . . **issue of first impression**".

There were several facts which were "undisputed": the policy did not provide the carrier with a right of reimbursement; the County did not "expressly agree" to reimburse the carrier for the settlement. The method that the carrier utilized to assert a right of reimbursement was through an ROR.

The following issues, according to the majority, were presented:

1. Since there was no "express" consent by the County (the insured) to reimbursement, was there an "***implied consent***" or an "***implied-in-fact contract***" for reimbursement?
2. Were there sufficient circumstances in the case to warranting imposing, as a matter of law, an "equitable reimbursement obligation" under either a doctrine of "***equitable subrogation***" or ***quasi-contract theories*** of unjust enrichment or quantum meruit?

1. No Reimbursement Agreement was "Implied in Fact"

The carrier argued that since the County had been silent in response to the ROR number 2 stating the carrier would fund the settlement and then seek reimbursement, there existed an "***implied-in-fact*** contractual obligation" to provide reimbursement. The majority rejected this argument.

The majority opinion stated that an ROR can not "create rights not contained" in the policy. The policy did not provide for reimbursement. The carrier could

have inserted such provision at the time the policy issued. ROR number 2 was, the majority asserted, simply an "unilateral" effort to insert a reimbursement provision in the policy.

This "new" inserted provision, i.e. the implied provision, is binding on the insured (the County) " . . . only if the County accepted it." (emphasis added) The majority then held that the he County did not "agree" or consent "by its silence." The mere failure to object to a position letter "reserving rights" does not, standing alone, establish an "agreement" between the parties.

Likewise, while it is accurate that by allowing the carrier to defend in light of a ROR, the insured **is** agreeing "impliedly" that the carrier is not waiving these defenses merely by defending, the insured is **not** also "agreeing" - - impliedly - - to "additional obligations" not contained in the insurance contract. This distinction between an ROR which allows a defense without waiver and an ROR which purports to "create" rights not otherwise in the policy is a "critical distinction".

The majority also concluded that **there was no "meeting of the minds"**, a finding the majority deemed as an "essential element" of an "implied-in-fact contract". The Court concluded that there was no "implied-in-fact" "agreement" by the insured (County) that the carrier could fund the settlement and then seek reimbursement.

2. No Reimbursement Agreement was "Implied at Law"

The carrier also sought reimbursement under a theory of "equitable subrogation". As a general rule, a carrier paying a claim is "equitable subrogation" to any claim the insured may have against a third party responsible for the insured's injury. The majority rejected equitable subrogation on these facts seemingly on the conclusion that allowing the carrier to "unilaterally settle claims" and then step into the shoes of the Plaintiff and sue the insured "could potentially" lead to "conflict and distrust" between the carrier and its insured.

Likewise, **quasi-contractual theories** do not apply in the circumstances presented. Relying on non-Texas authorities, the majority held that reimbursement is permitted on equitable theories **only where the carrier has committed funds to settlement and where the insured had agreed for the carrier to have a right to reimbursement at a later time.** The court was unwilling to require the insured to choose between rejecting a settlement offer and accepting a financial obligation that it might not be able to pay.

C. The Main Holding

The majority opinion in *Matagorda County* then stated:

> ". . . when coverage is disputed and the insurer is presented with a reasonable settlement demand within policy limits, the insurer may fund the settlement and seek reimbursement ***only if*** it obtains the insured's clear and unequivocal consent to the settlement and the insurer's right to seek reimbursement." (emphasis added)

In a concluding Paragraph III in the majority opinion, Justice O'Neill recognized that regardless of how the issues are resolved, either the carrier or the insured " . . . will face a difficult choice when coverage is questioned."

One remedy for a **carrier** who can not obtain the consent of the insured is to seek a "prompt resolution of the coverage dispute" in a DJ action, a remedy which was encouraged in *Gandy* and *Griffin*.

If adopted, the resolution proposed by the carrier - - to allow reimbursement - - would " . . . undermine *Gandy*" by reducing the carrier's incentive to seek early revolution of the coverage disputes. In this case there was a two year delay from the time that the DJ was filed and the date the case was settled.

The **carrier**, the Court concluded, was in the business of risk allocation and was " . . . **in the best position to assess the viability of its coverage dispute**." If a policy provision is vague, then the fault lies with the drafter of the policy. The insurance company is in a better position to "handle this risk" by including the payment of non-covered claims through underwriting or putting reimbursement provisions in the policy.

D. Dissent - Owen and Hecht

Justice Owen framed her dissent in terms of unjust enrichment by the insured. *Matagorda County* received settlement funds to which it was not entitled. Therefore, the County should bear its own liabilities.

When a carrier reserves its right to contest coverage, and the carrier settles a case based on a demand which the insured deems reasonable, then - - based on a "obligation" ***implied in law*** - - the carrier can seek reimbursement even though there was no **real** "agreement" either express or implied. To Justice Owen, the reasoning of *Buss v. Superior Court*, 939 P.2d 766 (Cal. 1997) was persuasive in holding that there was a "right of reimbursement" " . . . implied at law based on principles of restitution."

1. Right of Reimbursement Was Implied at Law

Implying this obligation "as a matter of law" was

not unprecedented according to Justice Owen. The *Stowers's* obligation itself is a "duty" which was imposed by the Court in 1929 "as a matter of law". There is no "principled basis", Justice Owen argued, for the carrier to pay the costs of settling the underlying litigation when the claims have been adjudicated as not within the coverage the *Matagorda County* had purchased. The County got a benefit for which it did not bargain and has been unjustly enriched.

It is true, Owen noted, that an insured who has no coverage for certain claims may be "vulnerable". This vulnerability is not something that the carrier has done, but, apparently, a "choice" " . . . not to obtain full coverage". Owen asserted that the Court's statement was also "irrational". Regardless of the size of the claim, the " . . . financial obligation to pay that claim remains with the insured. An insured's lack of financial resources does not change that fact."

2. On Different Facts, Reimbursement Might Be Implied in Fact

Owen agreed that there was no ***"implied-in-fact"*** *agreement* between the County and the carrier in this case - - that is, based on common law contract principles. But the Court, Owen asserted, went overboard in closing the door on future "**implied-in-fact"** agreements with regard to reimbursement. The issue should, for Owen, be decided on a case by case basis. Implied-in-fact agreements are contracts.

Owen sited non-Texas cases for the proposition that silence in this context can create an implied agreement. Owen took the position that **had the County "demanded" that the carrier settle the litigation**, then Owen would find an "implied-in-fact" agreement, despite a contention by the County that there was no obligation to reimbursement. Owen would also find an implied contract if the carrier proposed to settle unless otherwise instructed by the insured and the insured did not object to settlement.

V. New Faces on the Supreme Court

It is in this context of *Matagorda County* that *Frank's Casing* came ***originally*** before the Texas Supreme Court. Between the time of *Matagorda County* in December of 2000 and the *Frank's Casing* opinion in May of 2005, the Supreme Court underwent a wholesale turnover of the Justices.

1. ***Six*** (Phillips, Enoch, Baker, Abbott, Hankinson, Gonzales) of the Justices in the seven judge majority in *Matagorda County* were no longer on the Court in May of 2005.
2. Justice O'Neill, who wrote the majority opinion in *Matagorda County*, remains on the court and wrote a concurring opinion in *Frank's Casing*.
3. Justice Owen, who wrote the dissenting opinion in *Matagorda County* and who also wrote the 5/2005 Plurality Opinion in *Frank's Casing* is no longer on the Court and had moved to the Fifth Circuit within a month after the opinion *Frank's Casing* was delivered.
4. Justice Willett was appointed to the Court in August 2005.
5. Justice Hecht who joined Justice Owen's dissent in *Matagorda County* remains on the Court and joined the plurality opinion in *Frank's Casing* in part and concurred in part.
6. Justice Brister was the author of the Court of Appeals opinion and has not participated in any aspect of *Frank's Casing*.
7. Justice Johnson was appointed to the Court on March 15, 2005 and did not participate in the argument on original submission of *Frank's Casing*. Justice Johnson did not participate in the May 27, 2005 opinion. Justice Johnson did sit at the February 2006 argument on rehearing and will participate on all further votes on the disposition of the appeal.
8. Out of the nine justices who were on the Court and who voted on *Matagorda County*, ***only two are still on the court***: Justice O'Neill (majority in *Matagorda County*) and Justice Hecht (dissenting in *Matagorda County*).
9. There will be six Justices who will now vote on the disposition of Frank's Casing who were not on the Court at the time of the *Matagorda County* decision. They are Justices:
    1. Wainwright (Elected with a term commencing on 1/1/03);
    2. Green (elected and took office on 1/1/05);
    3. Chief Justice Jefferson;
    4. Medina (appointed in 2004 at the time that Justice Jefferson became Chief Justice);
    5. Justice Johnson (appointed on March 15, 2005);
    6. Justice Willett (appointed in August of 2005).
10. There will be two Justices who will now vote on the disposition who were not participating in the opinion on original submission: Justice Johnson and Justice Willett.

VI. Breakdown of the May 2005 Opinion

A. Controversy

The opinion of *Frank's Casing* created a firestorm in Texas. Not only were there a passionate surge of Amicus briefs, there has been an outpouring of "comment". There have been several law review articles. Use of the phrase "**Frank's Casing**" in quotes in an "Advanced Search" in Yahoo or Google or Gigablast leads to literally hundreds of comments or blogs or articles.

Some of this must be called lobbying. Most consciously as special interest pleading, on February 6, 2006, some nine days before oral argument and after losing on original submission, Frank's Casing filed of record with the Supreme Court a copy of a "Roundtable Discussion" which was a special section printed in the January 30, 2006 *Texas Lawyer*. Counsel stated that the discussion " . . . provides practical perspectives on the impact of the Court's decision on business and insurance issues".

B. Majority Opinion: Justice Owen

Justice Owen wrote the opinion for a five Justice majority. Her opinion has three major Parts (I, II, & III) and has four subparts under Part II - - A, B, C, & D. Hecht, O'Neill, and Wainwright concurred. Part I is an Introduction and does not cite any cases other than *Matagorda County*. The general holdings of the majority are noted, but not discussed in any detail.

1. Part II - A - BROAD RULE (No Analysis)

Part II - A of Owen's opinion is the most far-reaching part of the action of the Supreme Court. Parts II - A and II - B set a completely new direction in Texas law. If Parts II - A and II - B remain intact with the new members of the Court, considerable areas of tort litigation in Texas will never be the same.

The members of the Court who now remain in who joined in Part II - A are: Jefferson; Hecht; Medina; Green. Unless Willett or Johnson join these four, there will not be a majority of the Supreme Court to embrace these broader holdings.

a. The "Brister" Factor

To make matters more uncertain and complex, it seems probable (though not a certainty by any means) that if, as, and when the same issues presented in this appeal are raised in another case, that Justice Brister would most likely join in Part II - A. Thus, even if Justice Willett and Johnson do not join Part II - A, it seems reasonable to believe that, barring some dramatic change of position by either Jefferson, Hecht, Green, or Medina, Part II - A will become Texas law - - either in this case or some later case as long as the present configuration of the Justices of the Supreme Court remains the same. Part II - A, then, represents the views as of May of 2005 of Jefferson; Hecht; Medina; and Green. Justices Willett's and Johnson's views are unknown. Justices Wainwright and O'Neill did not join in Part II - A.

b. Characterization of *Matagorda County*

II - A described *Matagorda County* as a situation where the carrier had an unilateral right to settle without the consent of the insured. The concern of the Court in *Matagorda County*, II - A was that a carrier could accept a claim out of the insured's "financial reach" and that the insured would be required to reimburse the carrier. The insured would have to choose between rejecting Plaintiff's claim within policy limits or accepting a "possible obligation" that would be beyond its means. II - A then stated the "concern" of the Court in *Matagorda County* is "ameliorated" in "at least" two situations.

c. The Major Holding

In these two situations "at least", the carrier has a "right to be reimbursed if it has timely asserted its reservation of rights, notified the insured it intends to seek reimbursement, and paid to settle claims that were not covered:"

> **When the insured demands that the carrier accept a settlement offer that it within policy limits; or,**
>
> **When the insured expressly agrees that the settlement offer should be accepted.**

Part II - A is interesting in that there is not a single case or other authority cited or mentioned. Part II - A merely announces the holding of these Justices (only five at the time which included Justice Owen) that the law of reimbursement in Texas would be changed dramatically. There is no reference to any other cases or discussion. The holding is simply announced. Therefore, the "us" of the Court whose "concerns" are "ameliorated" are those five Justices who joined in II - A.

2. Part II - B - BROAD RULE PLUS ANALYSIS

Part II - B represented the same five Justices as Part II - A. Part II - B appears to be the rationale of the five Justices for the broad holding in II - A even though II - B does not explicitly or expressly mention Part II - A.

a. Estoppel - *Stowers* Demand

The first premise of II-B is that, under *Stowers*, an insurance company does not have a duty to accept any offer within policy limits unless, quoting *Stowers*, "an ordinarily prudent person, in the exercise of ordinary care, as viewed from the standpoint of the assured, would have." II - B stated that once the insured (i.e. Frank's Casing) *"Stowerized"* the excess underwriters - - presumably meaning that the insured demanded that the carrier settle the case, that the insured can not " . . . thereafter take the inconsistent position that the settlement offer was reasonable if the insurer bore the cost of settling but unreasonable if the insured ultimately bore the cost."

b. Reasonableness of Settlement

II - B seems to mean that if a settlement is deemed "reasonable" for the carrier to pay, then the insured can not complain that it is not reasonable for the insured to pay if the insured "ultimately bore the cost". Therefore, if "an insured" triggers a " . . . *Stowers* duty" and settlement takes place at that level or lower, then the insured can not claim - - i.e. is estopped from asserting - - that the settlement is too "financially burdensome" for the insured if it turns out the claims against the insured are not covered.

c. What *Stowers* Means

The *Stowers* duty is the due diligence of a prudent person in the management of her own business or was such that a prudent carrier would accept it. The determination of whether a settlement is "reasonable" is an "objective standard" of an assessment of the exposure of the insured. Whether the insured has no assets or substantial assets is not a factor in any judgment on the" reasonableness of a settlement offer". Citing *Garcia*, II - B recited the three requirements for a *Stowers* demand: within the "scope of coverage"; within policy limits: terms are such that a prudent carrier would accept considering the exposure.

d. Implication of "Demand" by the Insured

Therefore, where the insured demands that the carrier accept the settlement offer, the insured is "deemed" to view the settlement as reasonable. It follows, therefore, according to II-B, that the offer is one that a "reasonable insured should accept if there is no coverage".

The insured "knows" that if the case is not settled, there is a risk that a judgment "larger then the settlement offer" will be entered. It follows, according to II-B, that

> ". . . Requiring an insured to reimburse its insurer for settlement payments if it is later determined there was no coverage **does not prejudice the insured**." (emphasis added)

This is true because the insured's substantial exposure to a judgment against it greater than the settlement amount has been eliminated at its insistence and for an amount which it agrees was reasonable.

e. Insured's Financial Ability is Beside the Point

Coverage should not be created just because the insured can not afford to pay a judgment. "The insurer should be entitled to settle with the injured party for an amount the insured has agreed is reasonable and to seek recoupment from the insured if the claims against it were not covered."

> This outcome - - according to II - B is " . . precisely the same position it would have been in absent any insurance policy, except that the insurer is now the insured's creditor rather than the injured third party."

f. Reimbursement Encourages Settlement

Reimbursement, II-B argues, encourages settlement " . . . even when coverage is in doubt." Here II-B cites without discussion *Blue Ridge Ins. Co. v. Jacobsen*, 22 P.3d 313, 321 (Cal. 2001). Third parties benefit from these settlements since the "risk" of no coverage is now shifted from the "injured Plaintiff". Now, it seems, the coverage dispute between an insured and its insurer can be resolved after the injured plaintiff is compensated. The risk to the "injured plaintiff" is "lessened."

g. Coverage is King

Whether the carrier or the insured bears the cost of a "reasonable settlement" should depend on whether there "is coverage". Denial of a right of reimbursement "tilts the playing field".

h. Hobson's Choice if No Right of Reimbursement

Without reimbursement, the carrier can: (a) refuse to settle and "face a bad faith claim"; (b) settle and have right of recourse even if it is determined that there is no coverage. If it is determined, as here, that there was no coverage in the first place, if reimbursement is denied, then the outcome is the creation of coverage "where there was none."

Here II - B notes the comments of "concern" of Justice Brister at the Court of Appeals level. Relying

again on *Blue Ridge*, II - B concluded this section by noting that reimbursement is necessary since the carrier " . . . had not bargained to bear these costs and the insured had not paid the insurer premiums for the risk."

3. Part II - C - Reimbursement Agreement "Implied in Fact"

Part II - C represented the views of a total of seven Justices - - the same five of II - A and II - B plus Justice O'Neill and Justice Wainwright. II - C represents the view of six Justices who are still on the Court.

a. "Express Agreement"

Part II - C is one paragraph. II - C states that Part C is a "second situation" in which reimbursement will be permitted where a coverage dispute exists. This "second situation" is described in II - C as where the insured (a) has "***expressly agreed***" that the offer should be accepted, (b) **and** the carrier has notified the insured that it "intends to seek reimbursement".

In II - C, *Matagorda County* is distinguished as a case in which the risk pool could not settle without the "consent" of the County. Here, II - C notes, EU could not settle without the consent of Frank's Casing.

b. The Insured Consented

Frank's Casing made an "informed decision" to "consent" to settle the litigation, " . . . knowing" that EU "intended to pursue coverage issues and to seek reimbursement . . . ". As the insured, Frank's Casing had "control" over whether to settle. An insured who "agrees to the settlement" and benefits from having claims released can not complain of reimbursement if the claims are not covered.

c. No Case Law Discussion

II - C does not cite to or discuss a single case or authority other than *Matagorda County*. Part II - C does not attempt to "explain" or "clarify" or "modify" of overrule *Matagorda County*.

4. Part II - D - Reimbursement Agreement Implied at Law

Part II - D represented the views of a total of six Justices - - the same five of Justice Owen's opinion plus Justice O'Neill. II - D represents the view of five Justices who are still on the Court. Part II - D does not represent the views of Justice Wainwright.

a. Reimbursement is Implied at Law

II - D begins by the assertion that, in fact, an "agreement to reimbursement"by *Frank's Casing* is "implied in law" in the facts of this case. It is recognized that *Matagorda County* held that was no "quasi-contract" on the facts of that case.

II - D goes to great lengths to show why the opinion of Justice O'Neill in *Matagorda County* was not quite right or was in possible need of "clarification" including a detailed discussion of each authority cited by Justice O'Neill in *Matagorda County*.

b. *Matagorda* "Clarified"

Bottom line: "to the extent" that *Matagorda County* indicated that the "only" time that reimbursement could exist was where there was an "express agreement" to seek reimbursement, " . . . we **clarify** that there are additional circumstances that will give rise to a right of reimbursement. Those include the circumstances in the case presently before us." (emphasis added)

5. Part III - Louisiana Law (Conflicts Analysis)

Part III of Justice Owen's opinion deals with choice of law issues relating to the law of Louisiana. Part III represented the view of five Justices only. Justices O'Neill and Wainwright did not join in Part III.

Without any discussion of why Louisiana law was relevant in any event, Part III begins by noting that there is no Louisiana case law at all on whether a carrier is entitled to reimbursement on these facts.

Part III then divines Louisiana law to be that there would be such a right of reimbursement "in this case". There is noted a 1974 Louisiana Supreme Court opinion which preceded a Louisiana statutory provision which was something akin to statutory unjust enrichment. Based on this single case and the Louisiana unjust enrichment statute, Justice Owen stated in a seemingly tentative holding that **"it appears"** Louisiana would permit EU to obtain reimbursement from Frank's Casing. Thus, Part III concluded, since Texas and Louisiana law are the same, there is no need to determine which law applies.

C. Concurring Opinions

1. Hecht

Justice Hecht is intent on making several points. Most prominently, Hecht wants *Matagorda County* to be overruled. Hecht dissented in *Matagorda County* and states here that *Matagorda County* was **"wrongly**

decided".

a. Overrule *Matagorda*

Whatever "distinctions" exist between *Matagorda County* and *Frank's Casing* are "immaterial". Hecht notes that here the insured had a right to consent to settlement and that Frank's Casing"demanded" that EU settle the case. These circumstances were not present in *Matagorda County*, but, according to Justice Hecht, ". . . neither distinction matters to the decision in this case."

b. Consent is Not Essential

The case for Hecht is not about forcing a settlement on the insured. In both *Matagorda County* and *Frank's Casing*, the insured "wanted" the case to settle. The insureds in both cases wanted to "have their cake and eat it too." **Consent to settlement is not an essential condition or reimbursement. Similarly, it does not matter that the insured made a "demand".** The *Stowers* duty, Hecht notes, comes from a "demand" for a reasonable offer, and it is not necessary for a Stower's duty for the insured to join in the demand.

Justice Hecht believes that the ruling in this case "effectively overrules" *Matagorda County*, " . . . as it should". Hecht then repeats basically the same argument that he used in his dissent in *Matagorda County*. Hecht notes that *Matagorda County* was "especially egregious" since the loss fell "on the public" - - the taxpayers of the "risk pool's other members". Hecht also takes pains to rebut a number of assertions made by Justice O'Neill in her concurring opinion.

c. Protections Exist - Is Carrier's Act Unreasonable?

Hecht concludes by saying that "perhaps it is necessary to stress, again" that "no one" suggests that a carrier can *"unilaterally"* settle for a "unreasonable amount" or "in circumstances that actually (rather than hypothetically) prejudice the insured, and then force reimbursement from the insured. Neither *Matagorda County* or *Frank's Casing*, according to Hecht, "involved such a situation, and the Court has never been ". . . cited to a case involving such a situation."

If such a case exists, Hecht concluded, "statutory prohibitions against unfair practices" by insurance companies such as Articled 21.21 and Article 21.55 **"offer full relief"**.

An insured, Hecht ended, ". . . should not be allowed to unreasonably withhold consent to settlement" to force the insurers to pay a claim and abandon coverage issues at the risk of incurring "statutory liabilities".

d. What Hecht Wants

The right to reimbursement depends on two things: (a) reasonableness of settlement; (b) coverage. That, according to Justice Hecht, " . . . is the essence of today's decision."

2. O'Neill

O'Neill joined in Parts II-C & II-D. O'Neill thought that the remainder of the Owen opinion was "**unduly broad and based at least in part upon faulty assumptions**." O'Neill agrees that where the policy gives the right of consent to the insured, reimbursement is reasonable.

a. The Owen Opinion is Narrow

O'Neill states that she does not "read" the Court's opinion (the opinion of Justice Owen) that reimbursement will exist merely by the insured's "agreement" with the carrier's decision to settle - - where there is no "consent to settle" or no allowing the insured to "assume" his own defense. In a standard homeowner or auto policy, O'Neill concludes that a carrier cannot "unilaterally impose" reimbursement where none exists in the policy.

b. The Majority is Wrong on *Stowers*

Despite her "reading" of the opinion, O'Neill stays the "Court' "ventures beyond." O'Neill argues that even though the insured "demand" settlement from the carrier, it does not follow that the settlement is "reasonable" from the point of view of the insured. *Stowers*, according to Justice O'Neill, was designed for the insurance company. ***Stowers* presumes coverage and " . . has no application in determining an insurer's reimbursement right when coverage is disputed, citing *Garcia*.**

c. The Insured's Ability to Pay is Relevant

The insured's ability to pay is relevant for O'Neill. O'Neill dissents from any holding that would allow reimbursement merely by the insured asking the carrier to accept a settlement demand within the policy limits.

d. O'Neill Disagrees With Wainwright

In addition to her disagreements with the opinion of the "Court" (the Owen opinion), Justice O'Neill goes to great lengths to distinguish her views from Justice Wainwright in his concurrence. O'Neill does not agree

that there was any "implied consent" to reimbursement in this case. Frank's Casing no more waived its position on reimbursement than a carrier waives its coverage positions when it issues an ROR. Finally, Justice O'Neill faults Justice Wainwright for his comments on *Matagorda County's* deviation from "common-law contract principles".

e. Consent = Quasi-Contract

The bottom line for Justice O'Neill is that on the facts of this case, Frank's Casing had an "***implied-in-law" reimbursement obligation*** because it consented to the settlement and the carrier could not have settled without that consent. Justice O'Neill does not mention Justice Hecht, but she concludes that the recognition in Part II C & D of an "implied reimbursement right" is "entirely consistent" with *Matagorda County*.

3. Wainwright

The concurring opinion of Justice Wainwright is quite interesting. Wainwright begins his lengthy concurring opinion by stating that "before today", as a general rule contract and quasi-contract principles could not be considered in a determination whether there was a right or reimbursement on these facts.

a. Wants Rule Based on Common Law Contract Principles

This "rule" was established by *Matagorda County*. *Matagorda County*, according to Justice Wainwright, erected an "uncommon standard" for contract formation. *Matagorda County* "precluded" "normal" application of common law principles. Justice Wainwright concluded that "normal" common law principles were adequate to assess whether Frank's Casing has "agreed", and Wainwright would agree only to apply those principles.

b. What the Majority Does is "Policy"

He joined only in III - C of the opinion. The remainder of Owen's opinion according to Wainwright is "not inconsistent with precedent", but "based on equitable and policy considerations" and concludes that the parties are "bound by a contract implied by law".

c. Insurance is Still a Contract

Justice Wainwright still believes that, despite the regulations of insurance and court made changes such as *Arnold*, insurance is "fundamentally" still based on the "agreement of the parties." Here both Frank's Casing and EU know that the policy did not address reimbursement. Thus, for Justice Wainwright, " . . . the following decision trees grew."

Justice Wainwright then concludes that there was, in fact, a literal "contract" or "agreement" by Frank's Casing to permit reimbursement since Frank's Casing did not reject the offer of EU or did not make a counteroffer.

d. Silence Created a "Contract"

By inaction or silence, therefore, a "contract" was formed by which Frank's Casing"agreed" that EU would settle and then the issue of coverage would be litigated. Wainwright reaches this conclusion from the fact that the carrier stated that its offer to fund was contingent on a right of reimbursement. **Wainwright would not allow reimbursement unless there was a "legally enforceable agreement" at the time of settlement to permit reimbursement.**

e. "Equities" Are Not Enough for Reimbursement

The mere "equities" of the parties, according to Wainwright, do not support allowing a right of reimbursement. For an insured to merely acknowledge the reasonableness of the settlement does not support allowing the carrier to seek reimbursement. The threat by EU to sue Frank's Casing does not change the insurance contract - - which has no right of reimbursement. **But Frank's Casing did "bind itself" by acquiescing in the settlement.**

For Wainwright, the parties "sink or swim" based on the "agreements they enter", unless the facts are such that they effect a change of the agreement under contract law or involve fraud, extortion or some other basis for "altering a contract". The "factors" that the Court cites are not "central" to a reimbursement analysis.

f. *Stowers* Does Not Alter the Insurance Policy

Justice Wainwright then makes the following comment which deserves to be quoted in full:

> **"I disagree with the Court's reasoning that the weight and potential severity of a *Stowers* or bad faith insurance verdict can serve as a basis to alter the agreement of the parties.** Insurance is a consensual arrangement not subject to change by the threat of a lawsuit. If *Stowers* or bad faith actions are skewing litigation and parties' legitimate incentives, **then *Stowers* actions may need to be addressed by the appropriate branch rather than allow threat of such actions to serve as a basis for reimbursement.**" (emphasis

added)

g. Reimbursement Should be Allowed Only if a "Real" Contract Exists

Wainwright concludes that where the policy does not provide for reimbursement, then there is no such right unless the carrier can show that the contract was "altered" by the conduct of the parties including "***implied-in-fact contracts***" and "quasi-contracts" where the carrier gives notice of its intent to seek reimbursement in a "timely" ROR letter or makes reimbursement a "condition" of a subsequent agreement.

h. This Case is a "Tangled Mound of Considerations"

The current case, for Justice Wainwright, "involves a set of tangled yet important interests and policy considerations". Slight variations can lead to varying results in similar cases. Adjudication of each case based on the "equities of the parties" will lead to case by case "adjudication". After a review of factors, " . . . then the courts' balancing will begin."

Instead, Wainwright believes that the "contractual relationship" should govern. Wainwright concludes by stating: "This case raises a tangled mound of considerations."

VII. Implications

A. Can an Insured Now Avoid Reimbursement?

Justice Hecht is clearly correct when he states that a *Stowers* duty does not arise from or depend upon a "demand" from the insured. A great Texas tradition of piling on has developed over the years. Plaintiff makes a demand. Not only is the Plaintiff "demanding" settlement. The insured has often found it necessary to jump in the fray and makes its own "Demand" that the carrier settle the case.

This is what Frank's Casing did in this case. But, as Justice Hecht makes clear, it is the demand from the Plaintiff that triggers the *Stower's* duty, not any demand from the insured. See Footnote 4 in Justice Hecht's concurring opinion.

Therefore, in those cases where Plaintiff makes a demand to the carrier within policy limits which is, on the surface, reasonable, what should the insured do?

1. Understand Coverage

First, the insured must be crystal clear what the "coverage issues" are. The insured's defense counsel and perhaps personal counsel should have long since been aware of exactly where all the coverage bones were buried. This is a huge change in and of itself in Texas law.

2. Do Not "Demand" Settlement

It has been suggested that a prudent insured would respond to a Plaintiff's demand as follows:

> "Dear Carrier: Here is a demand from the Plaintiff. We leave it to you to protect our interests. We want you to pay everything you are contractually obligated to pay. Please do not pay any more."

3. What Triggers Reimbursement?

Under the logic of Justice Hecht, the duty of the carrier under *Stowers* and *Garcia* is identical - - the insured does not have to say anything. Would pure and non-committal silence by the insured constitute an "express agreement" for Justice Hecht to trigger reimbursement? It would seem that this conduct would trigger reimbursement for Hecht, but not for O'Neill or Wainwright and possibly not for the other four majority Justices. This issue - what really triggers a right of reimbursement - will be decisive on rehearing.

B. General Practice Rule in the Future

Unless the holdings in *Frank's Casing* are drastically changed on rehearing, **as a general rule defense counsel and personal counsel should never "demand" that the carrier settle the case or write the carrier and state that the settlement is "reasonable" unless and until all coverage issue are resolved or where there has been some kind of agreement with the carrier on coverage.** There is just too much risk that the carrier would jump on the settlement and then turn on the insured and seek reimbursement.

Even if the insured is judgment-proof, the fact and reality of the expense of defending another lawsuit just after this one has settled is a fate which the insured will most likely do just about anything to avoid.

C. Implications for Mediation

Frank's Casing will be huge in terms of its impact at mediation. Mediators are going to have to fully understand the nuances of *Frank's Casing*. There are several instances in Central Texas where all of the defense counsel and all of the carrier's have expressly agreed to mediation solely on the condition that all *Frank's Casing* rights to reimbursement are waived by all carriers in writing in advance of the mediation. This type of agreement reflects how profoundly *Frank's*

Casing changes Texas law. Reimbursement was never in the back of any defense lawyer's or personal lawyer's mind until the opinion of *Frank's Casing*.

D. Pressure on the Insured

The balance of power has been - by Frank's Casing - tilted from a bias against the carrier, to a bias against the insured. While this may be overstated to some extent, clearly the insured who is solvent and who can respond truly to a large settlement and have the means to spend and lose at the trial of a coverage dispute - - that insured is under the gun in light of *Frank's Casing* in those types of cases where coverage issues are prominent - - such areas being, without limitation, construction defect litigation, employment litigation, and homeowner's litigation (i.e. quasi-intentional torts).

Given a (1) solvent insured and (2) major coverage issues, the leverage which an aggressive carrier now has under *Frank's Casing* against its own insured is significantly greater than before May of 2005. A solvent insured in a case where coverage issues are important **must** get ready for all "*Frank's Casing*" issues.

E. Coverage Issues Are No Longer on the Back Burner

For decades, "coverage issues" got buried in settlement. This is, in essence, what the Supreme Court is putting an end to in this case. Any lawyer who has any significant tort experience in Texas over a 20 year period knows this fact to be accurate. Carriers paid, and payment by settlement ended "coverage disputes" 99% of the time. No one gave any consideration to "reimbursement". Also, it has been repeated countless times by "defense counsel" hired by carriers to represent the insured - - "I cannot worry about coverage issues". That is no longer true in light of *Frank's Casing*. Both counsel for Plaintiff and counsel for Defendant and personal counsel for the insured must understand "coverage" from the very beginning. The reason is that the insured can not wait until the last minute to be in a position to decide what to do.

Frank's Casing will alter significantly the dynamics of last-minute settlement demands. The risks of last-minute settlement are no longer on the carrier alone. In those areas where coverage issues are prominent - - construction, employment, intentional tort and negligence claims, the huge elephant of reimbursement will be looming. Alert counsel on all sides will now have to take Request for Disclosure requests for "the policy" or "all policies" very seriously. For those who have not done "defense work", it will come as a shock how difficult it often is to "get the policy". It is now going to be an even more important task to get the policy and to get the policy "right". Every Plaintiff should ask for and obtain all reservation of Rights letters, through discovery. This should be discoverable and produced. Production should not be delayed. There should also be an agreed supplementation to the Plaintiff on any supplemental reservation of rights.

F. "Factors" to Consider After *Frank's Casing*

The following is a list of "factors" that have been given great importance in light of *Frank's Casing*.

1. Close Attention must be paid to all reservation of rights letters.
2. Did the carrier reserve a right to seek reimbursement in the ROR? This may or may not be determinative, pending the final opinion in *Frank's Casing*.
3. A must: obtain exact copies of the policies. Not an approximation. The insured must pay close attention to this. Defense counsel hired by the carrier can no longer shift that risk to the carrier. This "policy" may have significant reimbursement implications.
4. All counsel are going to be paying a lot more attention to the "coverage issues."
5. Is the insured solvent? This will have a significant impact on the *Frank's Casing* issues. If the insured is solvent, then there must be a higher level of scrutiny on all coverage issues in light of the potential right of reimbursement.
6. In settlement demands, Plaintiffs must consider *Frank's Casing*. In the future, Plaintiff may well tailor the settlement demand to craft the demand only on certain issues for "payment", but with the release of all claims. This "rationalization" of the demand may have an outcome on evaluation and reasonableness for *Stower's* and/or bad faith purposes.
7. The insured, defense counsel, and personal counsel must use extreme care in commenting on settlement demands. No knee-jerk letters to the carrier.
8. *Frank's Casing* issues must be explored and understood prior to the agreement to mediate and certainly at any mediation. Unless care is used, there could be an inadvertent *Frank's Casing* "***trigger***" of reimbursement by "demands" made at mediation. Query: Would the mediation privilege bar these conversations? Answer: Probably not.
9. In any mediation Rule 11 agreements, consider directly addressing *Frank's Casing* and

reimbursement issues to eliminate reimbursement per a signed mediation "Rule 11" Agreement. At mediation, get all carriers to sign off on *Frank's Casing* waivers and raise the issue before settlement.

10. Care must be used in settlement documents and settlement documentation. Should reimbursement be addressed? If so, how? Should the carriers formally sign the settlement papers waiving reimbursement?
11. Carriers should be highly sensitive to last minute demands and use *Frank's Casing* issues to offset this pressure. *Frank's Casing* equalizes the power considerations in last minute demands.
12. *Frank's Casing* does not address defense costs. How will this be handled in the future? This is an aspect of reimbursement that is not faced or discussed in any of the *Frank's Casing* opinions. This "defense costs" issue is discussed in some depth in the Briefs and specifically in the Amicus briefs.
13. There is the additional issue of "***allocation***." This is the issue of whether or not a carrier could state that the case was settled for $100,000 and thereafter seek reimbursement for $30,000 on the grounds that out of the $100,000, $30,000 was allocated to "non-covered claims." This allocating issue is not addressed in the *Frank's Casing* opinions.
14. In light of these "allocation" and "defense costs" issues, any agreement on *Frank's Casing* issues should be confirmed in writing, and **if** all *Frank's Casing's* reimbursement rights are waived by the carriers, a writing should rule out and dispose of any allocation for non-covered claims, any claim for reimbursement on defense costs, **and** any claim for reimbursement on indemnity.
15. As to carriers, significant carrier attention must be given now to reservation of rights letters. In the first place, a right of reimbursement should be reserved specifically and prominently displayed in the reservation of rights letter. Further, the carrier should avoid prophylactic reservation of rights provisions with a consideration of whether or not these will trigger an independent right to counsel under *Davalos*. See discussion of the *Davalos* opinion below.
16. For the insured, on receipt of a draconian reservation of rights letter, the insured should consult personal counsel to consider whether, under *Davalos*, there is an independent right to counsel. Negotiations with the carriers may then proceed so that the carrier waives the right of reimbursement while the insured waives the right of independent counsel. It is my belief that this will likely be the "typical" mode of negotiations early in the suit between the carriers and insureds in light of *Frank's Casing*. This is one potential aspect of how the insured can regain some leverage *vis a vis* the carrier.
17. Another key consideration is the "***reasonableness***" of the settlement. Defense counsel and personal counsel should use care on commenting on the reasonableness of a settlement demand or a settlement posture. While the counsel for EU stated in oral argument that there was no change of the ethical obligations of the defense lawyer in light of the holding in Frank's Casing, many other commentators and counsel in the Amicus briefs have taken a different position and have concluded that *Frank's Casing* will necessarily mean significant new ***ethical considerations*** and dilemmas for the defense lawyer.

G. Ethical Issues for Defense Counsel: *Frank's Casing* and *Davalos*

Nearly every commentator or observer who has read *Frank's Casing* has noted that the defense lawyer hired by the same carrier who may be later seeking reimbursement is going to face numerous and repetitive ethical quandaries. The leading case that is relevant to these ethical issues is *Davalos v. Northen County Mutual*, 140 S.W. 3d 685 (Tex. 2004). It has been suggested that a reservation of right to seek reimbursement is an irreconcilable conflict under *Davalos* for which the insured is entitled to separate and independent counsel. Justice Hecht's concurrence can be read to support the need for independent counsel since Hecht "highlights" the potential significant conflict between the carrier and the insured. Carriers frequently attempt to "reserve their rights" on provisions which almost certainly never would be applied. Under *Davalos* and in light of *Frank's Casing*, "prophylactic" reservations may tip the scales over to a requirement for independent counsel under Davalos.

H. Malpractice Implications

Where coverage issues are important, the reality now is that the insured will be under pressure of exposure more than ever before in Texas. This "pressure" will almost certainty be shifted to some extent downstream - - first to the defense lawyer hired by the

carrier in the form of ***legal malpractice***, and then to the E&O carrier for the agent. Where there is "no coverage", frequently one finds the claim that "the agent made me do it" or the agent certainly was responsible for the lack of coverages. It is highly likely that both of these causes of action will become far more frequent than in the past.

VIII. Conclusion

Justice Wainwright states that Frank's Casing presents a "**tangled mound of considerations"**. That is an understatement. For any fair minded neutral who read all of the briefs which were submitted to the Court, one comes away with great sympathy for the Court.

It would be difficult to overstate the degree of hand wringing, the unending parading of horribles, and the prediction of the fall of civilization if the Court does not change its position in this case. What is unspoken is that this case is a result which any experienced tort counsel in Texas has seen - - the last minute "demand" with a super short fuse. All or nothing. Accept this demand or a calamity will occur to you.

Most of us have seen competent counsel and qualified insurance professionals surrender in fright rather than face the outcome of a trial and have a Monday morning quarterback criticize them if they guess wrong under *Stowers*. The Supreme Court was tired of it. It seems unfortunate that the Court was not furnished with more creative solutions. The outcome is still in doubt until the Court rules again and the new Justices express their views and/or votes on the issues.

Appendix A
Full Text of the Opinions

Excess Underwriters v. Frank's Casing

#02-0730 / / 2005 *Lexis* 418
48 *Texas Supreme Court Journal* 735.
Argued 9/24/03
First Opinion Delivered 5/27/05
Rehearing Granted 1/6/06;
Reargued 2/15/06.

Introductory Paragraph: **Owen** + Jefferson, Hecht, Medina & Green (5)

Part I Opening: **Owen** + Jefferson, Hecht, Medina & Green + **O'Neill** (6)

Part II-**A**: **Owen** + Jefferson, Hecht, Medina & Green (5)

Part II-**B**: **Owen** + Jefferson, Hecht, Medina & Green (5)

Part II-**C**: **Owen** + Jefferson, Hecht, Medina & Green + **O'Neill & Wainwright**(7)

Part II-**D**: **Owen** + Jefferson, Hecht, Medina & Green + **O'Neill**(6)

Part III: Louisiana Law: **Owen** + Jefferson, Hecht, Medina & Green (5)

Concurring Opinion: Justice **Hecht**

Concurring Opinion: Justice **O'Neill**

Concurring Opinion: Justice **Wainwright**

Emphasis in Bold and Highlighting Was Added

Opinion Delivered

May 27, 2005
Opinion: By Justice Owen
Joined by: Jefferson, Hecht, Medina and Green

The issue in this case is whether excess insurance carriers that disputed coverage but that settled third-party claims against their insured are entitled to recoup the settlement payments from their insured when it was subsequently determined that the claims against the insured were not covered. There was no express agreement allowing reimbursement. The trial court granted summary judgment for the insured, holding there was no right to reimbursement, and the court of appeals affirmed [1]. Both courts concluded that this Court's decision in *Texas Association of Counties*

[1] 93 S.W.3d 178, 179.

County Government Risk Management Pool v. Matagorda County [2] was controlling. **Because the facts at issue in that case differ from those before us today, and because we are persuaded that a right of recoupment can arise even absent an insured's express agreement to reimburse settlement payments made by an insurer if there is no coverage,** *Matagorda County* **does not foreclose reimbursement in this case**. We accordingly reverse the court of appeals' judgment and remand this case to the trial court to enter judgment in the excess underwriters' favor.

Part I

Opinion: By Justice Owen
Joined by: Jefferson, Hecht, Medina and Green
Plus Justice O'Neill

Frank's Casing Crew & Rental Tools, Inc. fabricated a drilling platform at its facility in Louisiana for ARCO/Vastar. The platform was installed in the Gulf of Mexico and collapsed several months later. ARCO sued Frank's Casing, among others.

Frank's Casing had a primary liability policy with limits of $1 million, and Frank's Casing had obtained excess coverage of up to $10 million from Certain Companies Subscribing Severally But Not Jointly To Policy No. 548/TA4011F01 and Excess Underwriters at Lloyd's, London (whom we will call the excess underwriters). The excess underwriters issued reservation of rights letters in which they asserted that certain of ARCO's claims against Frank's Casing were not covered.

The primary carrier retained defense counsel for Frank's Casing. ARCO made a pre-trial settlement offer of $9.9 million, which Frank's Casing rejected. Two weeks before trial, the excess underwriters contacted ARCO directly, without Frank's Casing's knowledge, and attempted to settle only the claims the underwriters were willing to concede were covered. No agreement was reached. ARCO subsequently offered to settle all claims against all defendants for $8.8 million, which would have required Frank's Casing to contribute about $7.55 million. The excess underwriters proposed to Frank's Casing that the underwriters pay two-thirds of that amount, that Frank's Casing pay one-third, and that all coverage issues would be waived by the underwriters. In the alternative, the underwriters proposed that they pay $5 million and that all coverage issues be resolved in arbitration. Frank's Casing did not accept either proposal.

As trial approached, the excess underwriters retained counsel to associate with Frank's Casing and its primary carrier in the defense of ARCO's claims, as the underwriters were entitled to do under the excess liability policy [3]. ARCO's suit against Frank's Casing proceeded to trial, and it readily became apparent that Frank's Casing was the target defendant. By the close of the second day of trial, Frank's Casing's in-house counsel had contacted ARCO and requested that it make a settlement demand within the excess policy's limits, suggesting $7 million. ARCO promptly responded with a demand of $7.5 million, which Frank's Casing communicated to the excess underwriters accompanied by a demand that the underwriters accept this offer, thus "Stowerizing" the excess underwriters [4]. The underwriters agreed that the case should be settled for this amount and stated that they would fund the settlement up to $7.5 million, less any contribution from the primary carrier, if Frank's Casing would expressly agree that all coverage issues would be resolved at a later date. Frank's Casing refused and sent a second letter demanding that the underwriters accept ARCO's settlement

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[2] 52 S.W.3d 128, 44 Tex. Sup. Ct. J. 215 (Tex. 2000).

[3] The policy provides: The Underwriters shall not be called upon to assume charge of the settlement or defense of any claim made or suit brought or proceeding instituted against the Assured but Underwriters shall have the right and shall be given the opportunity to associate with the Assured or the Assured's underlying insurers or both in the defense and control of any claim, suit or proceeding relative to an occurrence where the claim or suit involves, or appears reasonably likely to involve Underwriters, in which event the Assured and Underwriters shall co-operate in all things in the defense of such claim, suit or proceeding. [*6]

[4] See *G.A. Stowers Furniture Co. v. Am. Indemn. Co.*, 15 S.W.2d 544, 547 (Tex. Comm'n App. 1929, holdings approved).

offer. The excess underwriters then advised Frank's Casing that they would pay $7.5 million, less any contribution from the primary carrier, and seek reimbursement from Frank's Casing. That same day, the underwriters contacted ARCO and orally accepted the settlement offer. The primary carrier simultaneously tendered its remaining policy limits, approximately $500,000, to settle the lawsuit.

The excess insurance policy required Frank's Casing's approval of any settlement,[5] and it gave that approval. A written settlement agreement among ARCO, Frank's Casing and the excess underwriters preserved "any claims that exist presently" between Frank's Casing and the underwriters. Prior to that agreement's execution, the excess underwriters had filed this suit against Frank's Casing for reimbursement, and Frank's Casing had answered.

In the coverage litigation, the excess underwriters and Frank's Casing filed cross motions for summary judgment. Among the issues presented to the trial court was whether Texas or Louisiana law governed, and the trial court applied Texas law. The trial court initially dismissed Frank's Casing's counterclaims and granted three separate motions for partial summary judgment for the excess underwriters, finding that none of ARCO's claims against Frank's Casing were covered, requiring Frank's Casing to reimburse the excess underwriters, and awarding the underwriters $7,013,612.00. Shortly thereafter, however, this Court issued *Texas Association of Counties County Government Risk Management Pool v. Matagorda County* [6]. The trial court then directed Frank's Casing to file a motion for new trial only on the issue of reimbursement, and Frank's Casing complied. After further briefing and another hearing, the trial court withdrew its order granting partial summary judgment on the reimbursement issue and signed a take-nothing judgment against the excess underwriters.

The court of appeals affirmed, although it noted: "We recognize this case carries *Matagorda County* to a logical conclusion that is somewhat disquieting - Frank's was able to resolve the parties' coverage dispute in its own favor simply by sending a *Stowers* demand to the Underwriters. . . . But this is a matter that the Underwriters must take up with the superior court."[7] The excess underwriters petitioned this Court for review, and we granted that petition.

We conclude that the law of both Texas and Louisiana entitle an insurer to reimbursement under the facts of this case. Accordingly, we do not decide which state's law governs. We first consider Texas law.

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[5] The policy provided: "The Assured shall make a definite claim for any loss for which the Underwriters may be liable under this policy within twelve (12) months . . . after the Assured's liability shall have been fixed and rendered certain either by final judgment against the Assured after actual trial or by written agreement of the Assured, the claimant, and Underwriters."

[6] 52 S.W.3d 128, 44 Tex. Sup. Ct. J. 215 (Tex. 2000).

[7] 93 S.W.3d at 180.

Part II

Opinion: By Justice Owen
Joined by: Jefferson, Hecht, Medina and Green

In *Matagorda County*, the County was sued after inmates armed with razor blades physically and sexually assaulted other inmates in the County's jail [8]. The County's policy with the Texas Association of Counties' risk pool specifically excluded any claim arising out of the operation of the jail [9]. The risk pool nevertheless agreed to defend the inmates' suit against the County with a reservation of rights and concurrently sought a declaratory judgment that the inmates' claims were not covered [10]. Before the declaratory judgment action was resolved, the inmate plaintiffs offered to settle their suit against the County for $300,000, which was within policy limits [11]. The County advised the risk pool that this was a reasonable settlement offer, [12] but did not ask the risk pool to accept the offer and refused to fund the settlement itself, insisting that there was coverage [13]. The risk pool then sent the County a letter, reasserting its position that there was no coverage, but advising the County that the risk pool would fund the settlement and then seek reimbursement from the County in the declaratory judgment action [14]. The County did not respond, and the risk pool settled the inmates' claims [15]. The County subsequently stipulated in the declaratory judgment action that the settlement amount was reasonable [16]. This Court held that an implied-in-fact agreement that the risk pool could seek reimbursement could not be found from the County's silence in response to the risk pool's letter stating it would seek reimbursement after it funded the settlement [17]. The Court also concluded that the doctrine of equitable subrogation did not apply [18]. Finally, the Court concluded that the quasi-contractual theories of quantum meruit and unjust enrichment should not be applied [19]. In resolving these issues, the Court's opinion said that the risk pool was not entitled to reimbursement unless the insured "consented to the settlement and the insurer's right to seek reimbursement. [20]

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[8] 52 S.W.3d at 129.

[9] Id.

[10] Id.

[11] Id.

[12] Id. at 129.

[13] Id. at 130.

[14] Id.

[15] Id.

[16] Id.

[17] Id. at 131-33.

[18] Id. at 134.

[19] Id.

[20] Id. At 135.

Part II - A

Opinion: By Justice Owen
Joined by: Jefferson, Hecht, Medina and Green

In *Matagorda County*, the insurer had the unilateral right to settle claims against the insured without the insured's consent [21]. One of the chief concerns expressed by the Court in *Matagorda County* was that when an insurer has the unilateral right to settle, an insurer could accept a settlement that the insured considered out of the insured's financial reach, and the insured could be required to reimburse the insurer for that amount [22]. "The insured is forced to choose between rejecting a settlement within policy limits or accepting a possible financial obligation to pay an amount that may be beyond its means, at a time when the insured is most vulnerable." [23] **The facts of the case before us today lead us to conclude that this concern is ameliorated if not eliminated in at least two circumstances:**

1) when an insured has demanded that its insurer accept a settlement offer that is within policy limits, or

2) when an insured expressly agrees that the settlement offer should be accepted.

In these situations, the insurer has a right to be reimbursed if it has timely asserted its reservation of rights, notified the insured it intends to seek reimbursement, and paid to settle claims that were not covered.

Part II - B

Opinion: By Justice Owen
Joined by: Jefferson, Hecht, Medina and Green

The insured in this case, Frank's Casing, specifically demanded that the excess underwriters accept and fund ARCO's settlement offer. Even when a claim is covered, an insurer has no duty to accept a settlement offer within policy limits unless "an ordinarily prudent person, in the exercise of ordinary care, as viewed from the standpoint of the assured, would have." [24] When Frank's Casing "Stowerized" the excess underwriters, it could not thereafter take the inconsistent position that the settlement offer was reasonable if the insurer bore the cost of settling but unreasonable if the insured ultimately bore the cost. Once an insured asserts that a settlement offer has triggered a *Stowers* duty, and the insurer then accepts that settlement offer or a lower one, the insured is estopped from asserting that the settlement is too financially burdensome for the insured to bear if it turns out the claims against the insured are not covered.

We have said that the duty imposed by *Stowers* is to "exercise 'that degree of care and diligence which an ordinarily prudent person would exercise in the management of his own business.'" [25] We have also said that the *Stowers* duty is viewed from the perspective of an insurer: "the terms of the demand are such that an ordinarily prudent insurer would accept it." [26] Both statements are correct. Whether a settlement offer within policy limits is a reasonable one is

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[21] Id. at 130. [*12]

[22] Id. at 135.

[23] Id.

[24] *G.A. Stowers Furniture Co. v. Am. Indemn. Co.*, 15 S.W.2d 544, 547 (Tex. Comm'n App. 1929, holdings approved).

[25] *Am. Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842, 848, 37 Tex. Sup. Ct. J. 561 (Tex. 1994) (quoting *Stowers*, 15 S.W.2d at 547).

[26] Id. at 849 ("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)

determined by an objective standard based on an assessment of the likelihood that the insured will be found liable and the range of potential damages for which the insured may be held liable, including "the likelihood and degree of the insured's potential exposure to an excess judgment." [27] The reasonableness of a settlement offer is not judged by whether the insured has no assets or substantial assets, or whether the limits of insurance coverage greatly exceed the potential damages for which the insured may be liable. It is an objective assessment of the insured's potential liability.

When there is a coverage dispute and an insured demands that its insurer accept a settlement offer within policy limits, the insured is deemed to have viewed the settlement offer as a reasonable one. If the offer is one that a reasonable insurer should accept, it is one that a reasonable insured should accept if there is no coverage. The insured knows that if the case is not settled, a judgment may be rendered against it for which there is no insurance coverage. Typically, a party considers a settlement reasonable when there is a substantial risk that if the case proceeds to trial, a judgment larger than the settlement offer will be entered against it. Requiring an insured to reimburse its insurer for settlement payments if it is later determined there was no coverage does not prejudice the insured. The insured's substantial exposure to a judgment against it greater than the settlement amount has been eliminated, at its insistence, and by its own admission the settlement amount was reasonable. The insured is in the same, or at least no worse, position than it would have been in if there had been no policy. Insurance coverage should not be created where none exists merely because an insured could not afford to pay a judgment if the case were tried or to fund a settlement demand from an injured third party. The insurer should be entitled to settle with the injured party for an amount the insured has agreed is reasonable and to seek recoupment from the insured if the claims against it were not covered. From the insured's point of view, it is in precisely the same position it would have been in absent any insurance policy, except that the insurer is now the insured's creditor rather than the injured third party.

Reimbursement rights encourage insurers to settle cases even when coverage is in doubt [28]. This inures to the benefit of injured third parties. When an insurer settles a claim for which coverage is in doubt, the risk that the insured lacks the resources to fund a settlement is shifted to the insurer and is lifted from the injured plaintiff who sued the insured [29]. The coverage dispute between an insured and its insurer can be resolved after the injured plaintiff is compensated. Thus, an injured plaintiff's risk that the defendant has no coverage and may be financially unable to fully compensate the plaintiff is lessened.

Whether the insurer or the insured ultimately bears the cost of a reasonable settlement with a third party should depend on whether there is coverage. As pointed out by the California Supreme Court and our own court of appeals in the present case, denying a right of reimbursement once an insured has demanded that an insurer accept a reasonable settlement offer from an injured third party can significantly tilt the playing field [30]. The insurer would have only two options. It could refuse to settle and face a bad faith claim if it is later determined there was coverage. Or it could settle the third-party claim with no right of recourse against the insured if it is determined there was no coverage, which effectively creates coverage where there was none [31]. As the California Supreme Court concluded, "Reimbursement

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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.").

[27] Id.

[28] See *Blue Ridge Ins. Co. v. Jacobsen*, 25 Cal. 4th 489, 106 Cal. Rptr. 2d 535, 22 P.3d 313, 321 (Cal. 2001).

[29] Id.

[30] See id. (observing that the insured's objection to a reservation of rights "would create coverage contrary to the parties' agreement in the insurance policy and violate basic notions of fairness"); Excess Underwriters, 93 S.W.3d at 180 (observing that denying reimbursement was "somewhat disquieting - Frank's was able to resolve the parties' coverage dispute in its own favor simply by sending a *Stowers* demand to the Underwriters").

[31] *Blue Ridge*, 22 P.3d at 321; Excess Underwriters, 93 S.W.3d at 180. [*18]

should be available because the insurer had not bargained to bear these costs and the insured had not paid the insurer premiums for the risk." [32]

Part II - C

Opinion: By Justice Owen
Joined by: Jefferson, Hecht, Medina and Green
Plus Justice O'Neill and Justice Wainwright

A second situation in which reimbursement will be permitted is when there is a coverage dispute, the insured has **expressly agreed** the third party's settlement offer should be accepted, and the insurer has notified the insured that it intends to seek reimbursement. In *Matagorda County*, the County agreed that the settlement amount was reasonable [33]. But the risk pool had the right to, and did, settle without the County's consent [34]. Here, the underwriters could not settle without Frank's Casing's consent. Frank's Casing had the option of continuing the litigation. Frank's Casing made an informed decision between continuing to defend ARCO's suit and consenting to settle that litigation, knowing that the excess underwriters intended to pursue coverage issues and to seek reimbursement of the amount paid in settlement. The insured had control over whether to settle for the sum offered by ARCO or continue the litigation. An insured who agrees to the settlement and benefits by having claims against it extinguished cannot complain that it must reimburse its insurer if the claims against the insured were not covered by its policy.

Part II- D

Opinion: By Justice Owen
Joined by: Jefferson, Hecht, Medina and Green
Plus Justice O'Neill & not Justice Wainwright

In cases such as the one presently before us, an agreement to reimburse **an insurer is implied in law** [35]. It is quasi-contractual [36]. In *Matagorda County*, this Court held that a quasi-contract did not arise under the facts of that case [37]. In explaining why, the Court cited three cases and a law review article for the proposition that "the few courts that have considered the settlement-reimbursement question have generally opted to recognize a reimbursement right only if the insured has authorized the settlement and agreed to reimburse the insurer should the insurer prevail on its coverage defense." [38] The three cases cited were *Medical Malpractice Joint Underwriting Association of Massachusetts v.*

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[32] *Blue Ridge*, 22 P.3d at 320 (citing Buss v. Superior Court, 16 Cal. 4th 35, 65 Cal. Rptr. 2d 366, 939 P.2d 766, 776 (Cal. 1997)).

[33] *Tex. Ass'n of Counties County Gov't Risk Mgmt. Pool v. Matagorda County*, 52 S.W.3d 128, 130, 44 Tex. Sup. Ct. J. 215 (Tex. 2000).

[34] Id.

[35] *Blue Ridge*, 22 P.3d at 320 ("'The insurer therefore has a right of reimbursement that is implied in law as quasi-contractual, whether or not it has one that is implied in fact in the policy as contractual.'" (quoting Buss, 939 P.2d at 776)).

[36] Id.

[37] 52 S.W.3d at 134.

[38] Id.

Goldberg, [39] *Mt. Airy Insurance Co. v. Doe Law Firm*, [40] and *Val's Painting & Drywall, Inc. v. Allstate Insurance Co* [41]. However, only one of those decisions, *Mt. Airy*, held that reimbursement is limited to the circumstance in which there was an express agreement that the insurer would be entitled to reimbursement if there was no coverage [42]. *Val's Painting* held that even absent an express or implied-in-fact agreement, an insurer may obtain reimbursement if "it has secured specific authority to make that settlement or has notified the insured of a reasonable offer by the claimant and given the insured an opportunity to assume the defense." [43] Goldberg, extensively relied on in *Matagorda County,* [44] expressly agreed with Val's Painting that reimbursement is required when the insured had been given the opportunity to assume its own defense after notification of a reasonable settlement offer [45]. Goldberg held "an insurer [who] defends under a reservation of rights to later disclaim coverage . . . may later seek reimbursement for an amount paid to settle the underlying tort action" if the "insurer [has] notified the insured of a reasonable settlement offer and given the insured an opportunity to accept the offer or assume its own defense." [46] Similarly, the law review article cited in *Matagorda County* concluded that "most courts to consider this question have held that the insurer can obtain reimbursement of settlement funds if the insured has authorized the settlement and agreed to reimburse the insurer in the event the insurer prevails on the coverage issue, or if the insurer has notified the insured of a reasonable offer and given the insured the opportunity to assume the defense." [47] After citing these three cases and the law review article, *Matagorda County* said,

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[39] 425 Mass. 46, 680 N.E.2d 1121 (Mass. 1997). [*22]

[40] 668 So. 2d 534 (Ala. 1995).

[41] 53 Cal. App. 3d 576, 126 Cal. Rptr. 267 (Cal. Ct. App. 1975).

[42] 668 So. 2d at 538.

[43] 126 Cal. Rptr. at 274.

[44] *Tex. Ass'n of Counties County Gov't Risk Mgmt. Pool v. Matagorda County*, 52 S.W.3d 128, 133, 134-35, 44 Tex. Sup. Ct. J. 215 (Tex. 2000).

[45] *Med. Malpractice Joint Underwriting Ass'n of Mass. v. Goldberg*, 425 Mass. 46, 680 N.E.2d 1121, 1129 n.30 (Mass. 1997) ("We recognize that Val's Painting is the holding from another jurisdiction. We nevertheless find its reasoning sound.").

[46] Id. at 1129.

[47] Jerry, The Insurer's Right to Reimbursement of Defense Costs, 42 ARIZ. L. REV. 13, 70 n.220 (2000) (emphasis added). This footnote said in its entirety: “A similar question can be asked of the indemnity obligation: Is it possible, in circumstances where the defense is being provided under reservation to contest coverage, for the insurer to settle the underlying litigation and reserve a right to obtain reimbursement of the settlement amounts in the event it is determined that the plaintiff's claim(s) against the insured are outside the coverage? In this situation, like the reimbursement of defense costs situation, the insurer performs an obligation-indemnity-while reserving a right to claim that the indemnity duty was not owed on account of lack of coverage and to retrieve the funds that were advanced to resolve the underlying claim. Most courts to consider this question have held that the insurer can obtain reimbursement of settlement funds if the insured has authorized the settlement and agreed to reimburse the insurer in the event the insurer prevails on the coverage issue, or if the insurer has notified the insured of a reasonable offer and given the insured the opportunity to assume the defense. See, e.g., *Mt. Airy Ins. Co. v. Doe Law Firm*, 668 So. 2d 534 (Ala. 1995); *Johansen v. California State Auto. Ass'n Inter-Ins. Bur.*, 15 Cal. 3d 9, 538 P.2d 744, 750, 123 Cal. Rptr. 288 (Cal. 1975); *Val's Painting and Drywall, Inc. v. Allstate Ins. Co.*, 53 Cal. App. 3d 576, 126 Cal. Rptr. 267, 273-74 (Ct. App. 1975); *Medical Malpractice Joint Underwriting Ass'n v. Goldberg*, 425 Mass. 46, 680 N.E.2d 1121, 1127-29 (Mass. 1997); *Matagorda County v. Texas Ass'n of Counties County Gov't Risk Mgmt. Pool*, 975 S.W.2d 782 (Tex. Ct. App. 1998), review granted (June 29, 1999). This, however, is not inconsistent with the analysis, developed in the text, that the insured's express agreement to the insurer's claim of right to reimbursement of defense costs is not needed. As with reimbursement of defense costs, see supra note 45, a specific policy provision authorizing reimbursement of settlement funds in the event the insurer prevails on the coverage issue is enforceable. See *National Cas. Co. v. Lane Express, Inc.*, 998 S.W.2d 256, 1999 WL 219437 (Tex. Ct. App. 1999).

"We agree with this approach." [48]

Two statements in *Matagorda County* did not, however, fully set forth the "approach" taken by three of the four authorities relied upon. Those two statements in *Matagorda County* were that "the few courts that have considered the settlement-reimbursement question have generally opted to recognize a reimbursement right only if the insured has authorized the settlement and agreed to reimburse the insurer should the insurer prevail on its coverage defense," [49] and when coverage is disputed and the insurer is presented with a reasonable settlement demand within policy limits, the insurer may fund the settlement and seek reimbursement only if it obtains the insured's clear and unequivocal consent to the settlement and the insurer's right to seek reimbursement. See *Goldberg*, 680 N.E.2d at 1129. [50]

To the extent *Matagorda County* indicated that the only circumstance under which an insurer may obtain reimbursement from an insured for settlement payments when there is no coverage is when there is an express agreement that there is a right to seek reimbursement, we **clarify** that there are additional circumstances that will give rise to a right of reimbursement. Those include the circumstances in the case presently before us.

Part III "Louisiana Law"

Opinion: By Justice Owen
Joined by: Jefferson, Hecht, Medina and Green

The Louisiana courts have not considered whether an insurer is entitled to reimbursement from its insured when it pays to settle claims against its insured that are not covered. However, it appears that under Louisiana law there would be a right to reimbursement in this case.

The Louisiana Civil Code provides a remedy when a person "has been enriched without cause at the expense of another person." [51] The Code says, A person who has been enriched without cause at the expense of another person is bound to compensate that person. The term "without cause" is used in this context to exclude cases in which the enrichment results from a valid juridical act or the law.

The remedy declared here is subsidiary and shall not be available if the law provides another remedy for the impoverishment or declares a contrary rule.

The amount of compensation due is measured by the extent to which one has been enriched or the other has been impoverished, whichever is less.

The extent of the enrichment or impoverishment is measured as of the time the suit is brought or, according to the circumstances, as of the time the judgment is rendered. [52]

This section was enacted in 1995. The commentary to this section notes that "it expresses the principle of enrichment without cause that was inherent but not fully expressed in the Louisiana Civil Code of 1870. The formulation of the principle accords with civilian doctrine and jurisprudence." [53]

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[48] 52 S.W.3d at 135.

[49] Id. at 134.

[50] Id. at 135.

[51] LA. CIV. CODE art. 2298.

[52] Id.

[53] Id. revision cmts. (1995).

A decision of the Supreme Court of Louisiana that preceded the promulgation of this provision illuminates the principles of Louisiana law it embodies. In *Edmonston v. A-Second Mortgage Co. of Slidell, Inc*., Edmonston and her husband obtained a loan from Standard Life Insurance Company [54]. To secure the loan, Edmonston mortgaged her separate property. Standard also required the couple to insure their lives and assign the policies to Standard. The assignment provided that any proceeds of the policy would be used to discharge the mortgage or would be paid to the beneficiary, at the survivor's option. The couple later obtained a loan from A-Second Mortgage Company, and Edmonston gave that company a second mortgage on her property. Thereafter, the couple deeded the property to A-Second in satisfaction of its mortgage as well as the outstanding debt to Standard. Instead of immediately paying off the debt to Standard, A-Second agreed to make all payments on the Standard loan as they became due. Edmonston's husband subsequently died. Although A-Second had assumed the couple's obligation to repay the Standard loan, Standard had never released Edmonston or her husband from liability. She and Standard agreed that the proceeds of her husband's life insurance policy, $16,000, should be applied to pay off the Standard loan, which had a balance of about $14,500, with the remainder to be paid to Edmonston. Edmonston then sued A-Second to recover the $14,500, apparently realizing she had discharged a debt that she had already paid A-Second to discharge on her behalf. The Louisiana Supreme Court recognized that Edmonston had no obligation to A-Second to pay Standard's note and that "A-Second received a benefit they had never bargained for, the discharge of its obligation to Standard." [55] The court held that Edmonston was entitled to restitution, reasoning, "she has, in effect, paid the debt of another and the actual benefit to A-Second cannot be questioned." [56]

Under the rationale of Edmonston and the provisions of article 2298, it appears that Louisiana law would permit the excess underwriters to obtain reimbursement from Frank's Casing. Accordingly, the result under Louisiana and Texas law would be the same, and we need not engage in a conflict of laws analysis to determine which state's law applies.

For the reasons set forth, we reverse the court of appeals' judgment and remand this case to the trial court to render judgment in favor of the excess underwriters consistent with this opinion.

CONCURING OPINION: JUSTICE HECHT

I join fully in the Court's opinion and write separately only to say that while I agree distinctions can be found between this case and *Texas Association of Counties County Government Risk Management Pool v. Matagorda County,* [1] **in fact those distinctions are immaterial, and the rule in** *Matagorda County* **cannot survive today's decision for the reasons** *Matagorda County* **was wrongly decided** [2].

The question in both cases is this: may a liability insurer accept a reasonable offer within policy limits to settle a claim for which coverage is disputed and, if the claim is later determined not to have been covered, obtain reimbursement from the insured. In the present case, we answer "yes;" in *Matagorda County*, the Court said "no." The Court sees two distinctions in the cases. In the present case, the insured (1) had the right to consent to any settlement and (2) demanded that the insurer accept the claimant's settlement offer. **Neither of these things was true in** *Matagorda County***, but neither distinction matters to the decision in either case**.

The insured's right to consent to settlement does not matter because neither case is about a settlement forced on

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[54] 289 So. 2d 116, 118 (La. 1974).

[55] Id. at 121.

[56] Id. at 122.

[1] 52 N.W.3d 128 (Tex. 2000).

[2] Id. at 136-141 (Owen, J., joined by Hecht, J., dissenting).

an insured. The insureds in both cases wanted the insurer to settle. The insured in *Matagorda County* "advised [the insurer] that the proposed settlement was reasonable and prudent, given the facts and circumstances of the case"; [3] it simply refused to contribute to the settlement or to agree to reimburse the insurer's contribution if the claim were determined not to be covered. The insured never argued that it would have withheld consent to the settlement had it had that right under the policy. Right or no right, the insured in each case viewed the proposed settlement exactly the same way. The insureds' desire in both cases to "have their cake and eat it, too" has nothing whatever to do with a right to consent to settlement.

Nor does it matter to either case that the insured did or did not demand that the insurer accept the settlement offer. The insurer's duty to settle is triggered by a reasonable offer from the claimant [4] -- which was made in each case -- regardless of whether the insured demands that the offer be accepted. It is the existence of this duty and the severe consequences for its breach that forced the insurer in each case to accept the settlement offer and seek reimbursement from the insured. Now granted, it is harder to sympathize with an insured that, instead of sitting mute, demands that its insurer settle a claim and then denies its responsibility to fund the settlement when it is later determined that there was no coverage, but the insurer's responsibilities in both cases were exactly the same.

Since the present case cannot be distinguished from *Matagorda County* **on any ground that matters, this case effectively overrules** *Matagorda County***, as it should.** "An insurer has no duty to settle a claim that is not covered under its policy." [5] But to deny an insurer the option of accepting a reasonable settlement though coverage is doubtful and then seeking reimbursement from the insured if the claim is determined not to be covered forces on the insurer this choice: either fund the settlement and abandon all arguments that the claim is not covered, or refuse to fund the settlement and if the claim is determined to be covered, face liability for the full amount of the claim, even above policy limits, [6] plus statutory damages and attorney fees [7]. Since the cost of the latter option will almost certainly exceed the cost of settlement many times over, an insurer cannot afford to gamble. In both the present case and *Matagorda County*, the insurer ultimately prevailed on its arguments of no coverage. Yet the insurer in *Matagorda County* paid $300,000, and the insurer in the present case paid over $7 million, hoping for reimbursement, rather than take the chance that they were wrong about coverage. When insurers are forced to pay doubtful claims, the premiums paid by policyholders who have purchased coverage must be used to satisfy claims against policyholders who have not purchased coverage. The rule in *Matagorda County* thus allows a non-covered policyholder to extort payments not only from the insurer but from the insurer's other policyholders. The result in *Matagorda County* was especially egregious because it fell on the public: in effect, the Court allowed the *Matagorda County* Commissioners' Court to force the innocent and unknowing taxpayers of the risk pool's other member counties to pay for damages the members had not agreed to cover.

Justice Wainwright's concurring opinion argues that when "the insurer gives notice of its intention to recoup [a settlement] payment in a timely reservation of rights letter or makes reimbursement a term or condition of a subsequent agreement", an agreement for the insured to reimburse the payment is implied in fact [8]. I agree with this, of course, and

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[3] Id. at 129.

[4] *American Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842, 848-849, 37 Tex. Sup. Ct. J. 561 (Tex. 1994); G.A. *Stowers* Furniture Co. v. Am. Indem. Co., 15 S.W.2d 544, 547-548 (Tex. Comm'n App. 1929, holding approved).

[5] *American Physician*s, 876 S.W.2d at 848.

[6] Id. at 849.

[7] See TEX. INS. CODE art. 21.21, § 16A, art. 21.55, § 6.

[8] Post at ___.

said so in *Matagorda County*, [9] but the Court in *Matagorda County* expressly rejected that view [10]. *Matagorda County* cannot survive reasoning in JUSTICE WAINWRIGHT's concurring opinion.

Justice O'Neill's concurrence argues that "absent a consent-to-settlement clause or the opportunity for the insured to assume its own defense, an insured [does not] necessarily assume[] a reimbursement obligation merely by expressing agreement with the insurer's decision to settle a case." [11] Why an insured should assume an obligation to reimburse an insurer's settlement of a non-covered claim when the insured has the right to consent to settlement and does so, but not when he consents though he has no right to do so, is baffling. What possible difference can the right to consent make if the insured in fact consents? The insured's obligation to reimburse an insurer's settlement of a non-covered claim depends entirely on the reasonableness of the settlement.

Justice O'Neill's concurrence argues that the reasonableness of a settlement depends on the availability of insurance or the defendant's ability to pay. It is true, of course, that a claimant is often willing to settle his claim for less than its fair value when there is no insurance coverage and the defendant's assets are limited, although that is certainly not always the case. From this observation, Justice O'Neill's concurrence concludes that it is somehow wrong to saddle an insured with an obligation to reimburse a settlement paid by the insurer when coverage was in doubt, because the claimant might have agreed to a lesser settlement, and one within the insured's means, had coverage been determined not to exist. Even if one accepts that a claimant would take less to settle a non-covered claim than to settle a claim for which coverage was disputed, Justice O'Neill's concurrence cannot explain how the insured is disadvantaged by an obligation to reimburse the settlement in the latter instance. Suppose P's claim is worth $10X but P is convinced that he can extract only $1X from D, who is not covered by insurance, so P settles with D for $1X. D pays $1X. But suppose D's liability might be covered by insurance, so the insurer decides to pay P the reasonable value of the claim, $10X, and seek reimbursement from D if coverage issues are later resolved in the insurer's favor, rather than face liability for much more than $10X if coverage issues are resolved in D's favor. How much does D pay the insurer if there is found to be no coverage? $1X -- that's all D has. Justice O'Neill's concurrence seems to imagine -- one cannot tell for sure -- a defendant of limited means who can negotiate a settlement with the claimant that is less than his ability to pay, but there is no reason to suppose that a claimant would demand less in settlement from a defendant, known to be uninsured, than the insurer would demand in reimbursement from the defendant for settling a claim later determined not to be covered. A defendant who cannot pay the claimant more than $1X cannot reimburse his insurer more than $1X. Justice O'Neill's concurrence states: "I just do not believe that an insured that calls upon its insurer to settle a disputed claim necessarily agrees it is willing and able to pay the same amount in the event the insurer ultimately prevails in its coverage dispute." [12] The statement is, of course, correct; the would-be insured agrees to nothing regarding his willingness and ability to pay. But it is also irrelevant. The exposure of the defendant of limited means to his insurer is no greater than it would be to the claimant.

Perhaps it is necessary to stress, again, that no one suggests that an insurer may unilaterally settle a claim for an unreasonable amount, or in circumstances that actually (rather than hypothetically) prejudice the insured, and then force reimbursement from the insured. Neither the present case nor *Matagorda County* involved such a situation. The Court has never been cited to a case involving such a situation. **In the off-chance that such a situation could arise, statutory prohibitions against unfair practices by insurers offer full relief: actual damages, additional damages, and attorney fees**. [13]

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[9] *Matagorda County*, 52 S.W.3d at 140 (Owen, J., joined by Hecht, J., dissenting) ("If in the case before us, the County had demanded that the Association settle the Coseboon litigation after receiving the reservation-of-rights letter, I would hold that an implied-in-fact agreement arose, even if the County maintained that there was no obligation to reimburse."). [*34]

[10] Id. at 129, 131-133.

[11] Post at .

[12] Post at .

[13] See TEX. INS. CODE art. 21.21, § 16A, art. 21.55, § 6.

An insured should not be allowed to unreasonably withhold consent to settlement to force the insurer to pay a claim and abandon coverage issues at the risk of incurring stiff statutory liabilities. An insurer's right to recoup from its insured the amount paid to settle a claim depends on two things: the reasonableness of the settlement, and coverage. That is the essence of today's decision.

CONCURRING OPINION: JUSTICE O'NEILL

I agree that the excess underwriters are entitled to reimbursement under the circumstances presented in this case. As the Court notes, the insurers could not settle without their insured's consent under the parties' insurance agreements, and Frank's Casing not only consented to the settlement, but initiated it. For this reason, I join Part I and Part II, C and D, of the Court's opinion. I cannot join the remainder, however, for in my view the Court's opinion is unduly broad and based at least in part upon faulty assumptions.

The Court holds that an insured may be required to reimburse its insurer for settling claims that are ultimately determined to be outside the scope of coverage if the insured expressly agrees to the settlement. ___ S.W.3d at ___. In discussing that justification, the Court emphasizes that the underwriters in this case could not settle without Frank's consent and distinguishes our decision in *Texas Association of Counties County Government Risk Management Pool v. Matagorda County*, 52 S.W.3d 128, 44 Tex. Sup. Ct. J. 215 (Tex. 2000), on that basis. ___ S.W.3d at ___. I agree because, when the insurance policy requires the insured's consent before a settlement may be reached, the insured has at least some control over whether to settle for the offered amount or continue the litigation, unlike the situation presented in *Matagorda County*. In *Matagorda County*, we expressed agreement with the approach other courts had taken in recognizing a reimbursement right when the insurer conveys a reasonable offer to the insured and gives the insured an opportunity to assume the defense. 52 S.W.3d at 134. In that instance, the insured retains a level of control similar to that which a consent-to-settlement clause confers. Because in *Matagorda County* the insurer had not given its insured the opportunity to assume its own defense, we did not expand on this approach. But it is analogous to the situation presented here, in which control of Frank's Casing's defense did not lie with the underwriters, and the underwriters had to obtain Frank's Casing's consent before settling the case. The implied reimbursement right that we recognize in Part II, C and D, is entirely consistent with our decision in *Matagorda County*.

Accordingly, I do not read the Court's opinion to decide that, absent a consent-to-settlement clause or the opportunity for the insured to assume its own defense, an insured necessarily assumes a reimbursement obligation merely by expressing agreement with the insurer's decision to settle a case. Those situations contrast with the allocation of power set out in the standard homeowner's or automobile liability policies, under which the insurer generally exercises exclusive control over settlement decisions. See, e.g., *Texas Personal Auto Policy*, available at http://www.adcusa.com/bain/F15.html (last visited May 26, 2005); *Rodriquez v. Tex. Farmers Ins. Co.*, 903 S.W.2d 499, 509 (Tex. App.-Amarillo 1995, writ denied); *G.A. Stowers Furniture Co. v. Am. Indem. Co.*, 15 S.W.2d 544, 547 (Tex. Comm'n App. 1929, holdings approved); *Syverud, The Duty to Settle*, 76 VA. L. REV. 1113, 1118-19 (1990). Under those policies, the insurer may not unilaterally impose a right of reimbursement that does not appear in the policy with its insured. See *Matagorda County*, 52 S.W.3d at 134.

Although the case could be resolved on the basis I have just discussed, the Court ventures beyond. The Court also holds that a reimbursement obligation is implied "when an insured has demanded that its insurer accept a settlement offer that is within policy limits." ___ S.W.3d at ___. Citing *Stowers*, the Court reasons that an insured that has demanded that its insurer settle "is deemed to have viewed the settlement offer as a reasonable one." Id. at ___. But the Court's application of *Stowers*'s reasoning to this situation makes no sense. The *Stowers* test was designed to define the standard of care an insurer must abide by in deciding whether to accept a third-party claimant's settlement demand--it measures whether "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." *Am. Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842, 849, 37 Tex. Sup. Ct. J. 561 (Tex. 1994) (emphasis added). In sum, the *Stowers* test presumes coverage and simply has no application in determining an insurer's reimbursement right when coverage is disputed. Id. ("The *Stowers* duty is not activated by a settlement demand unless . . . the claim against the insured is within the scope of coverage . . . .").

Further, the Court's application of *Stowers* presumes that a settlement's reasonableness is measured solely by the insured's potential liability exposure irrespective of the insured's ability to pay. While that premise is certainly true when coverage is presumed, as *Stowers* contemplates, it doesn't square with reality when coverage doesn't exist. See *Syverud*, supra, at 1114 (noting that "most tort suits would be significantly less attractive to plaintiffs and their attorneys" without liability insurance). When a defendant lacks coverage, the uninsured's ability to pay becomes the paramount concern driving settlement discussions. If the uninsured has assets totaling $100,000, surely it would not behoove an injured plaintiff to seek a considerably larger but uncollectible judgment against him. Rather, the case will likely settle in the range of what the uninsured can pay irrespective of the amount of damages that the injured plaintiff sustained. I just do not believe that an insured that calls upon its insurer to settle a disputed claim necessarily agrees it is willing and able to pay the same amount in the event the insurer ultimately prevails in its coverage dispute. Accordingly, I would not hold, as the Court seems to, that an insured assumes a reimbursement obligation merely by asking its insurer to accept a settlement demand within policy limits.

On this disposition, at least, JUSTICE WAINWRIGHT and I are in agreement. However, I disagree with JUSTICE WAINWRIGHT's conclusion that Frank's Casing assumed a contractual reimbursement obligation in this case by acquiescing to the settlement of the underlying lawsuit. In settling the ARCO suit, both Frank's Casing and the excess carriers expressly sought to preserve their positions in the coverage dispute; in effect, they agreed to disagree on the reimbursement question and let the trial court decide the legal effect. This is a far cry from impliedly consenting to reimbursement under the common-law contract principles JUSTICE WAINWRIGHT purports to follow, and ignores the parties' written agreement preserving "any claims that presently exist" between them. As JUSTICE WAINWRIGHT recognizes, the excess carriers benefitted from the settlement by eliminating potential *Stowers* liability in the event ARCO's claims were later determined to be covered, just as Frank's Casing benefitted by eliminating the possibility of a large verdict that might turn out not to be covered. Given the parties' explicit efforts to preserve their positions, it makes no more sense to say that Frank's Casing impliedly agreed to reimburse the excess carriers than it would to say that the excess carriers impliedly agreed to waive their coverage position. Just as an insured's acceptance of a defense the insurer proffers with a reservation of rights implies the insured's consent to the reservation, the excess underwriters' agreement to accept the settlement in light of Frank's Casing's reimbursement contest implied the insurers' consent to Frank's Casing's reservation of the reimbursement question.

Finally, I disagree with JUSTICE WAINWRIGHT's implication that our decision in *Matagorda County* eschewed common-law contract principles in determining reimbursement rights. Nothing could be further from the case. In *Matagorda County*, we acknowledged those principles would apply if their well-established elements were met. According to the seven justices who comprised the majority (JUSTICE O'NEILL delivered the opinion of the Court joined by CHIEF JUSTICE PHILLIPS, JUSTICES ENOCH, BAKER, ABBOTT, HANKINSON, and GONZALES), they were not met in that case. 52 S.W.3d at 129.

I agree that Frank's Casing had an implied-in-law reimbursement obligation because it consented to the settlement and the underwriters could not have settled without that consent. For this reason, I join Part I and Part II, C and D, of the Court's opinion and concur in the court's judgment of reversal.

CONCURRING OPINION: JUSTICE WAINWRIGHT

When an insurer seeks reimbursement from its insured after paying to settle claims later determined not to be covered under the insurance policy, may contract and quasi-contract principles be considered in determining whether a right to seek reimbursement of the settlement payment arises? [1] n1 In Texas, prior to today, the answer was "no" under almost all circumstances, even though the insurer had timely reserved its right to contest coverage.

This rule was established in *Texas Ass'n of Counties County Government Risk Management Pool v. Matagorda*

[1] The insurance policy in this case is silent as to the insurer's right to reimbursement.

County. 52 S.W.3d 128, 44 Tex. Sup. Ct. J. 215 (Tex. 2000). *Matagorda County* precluded reimbursement to an insurer of settlement payments made to resolve claims that are later found not to be covered, and allowed reimbursement to be sought by the insurer "only if it obtains the insured's clear and unequivocal consent to the settlement and the insurer's right to seek reimbursement." Id. at 135 (emphasis added). *Matagorda County* erected this uncommon standard for contract formation even though the standard eschewed traditional common law contract principles on the tenets necessary to establish a right to recover. The Court further concluded that quasi-contract theories of quantum meruit and unjust enrichment would not support the insurer's claim of a right to reimbursement. Id. at 134-36. Quasi-contracts may be established under the common law, but *Matagorda County* precluded the normal application of these common law tenets. Id. at 135.

A contract is established when proven by a preponderance of the evidence that an offer is accepted, accompanied by consideration. See *Fed. Sign v. Tex. S. Univ*., 951 S.W.2d 401, 408, 40 Tex. Sup. Ct. J. 676 (Tex. 1997) ("A contract must be based upon a valid consideration, in other words, mutuality of obligation."); *Haws & Garrett Gen'l Contractors, Inc. v. Gorbett Brothers Welding Co.*, 480 S.W.2d 607, 609, 15 Tex. Sup. Ct. J. 321 (Tex. 1972) ("There must be shown the element of mutual agreement which, in the case of an implied contract, is inferred from the circumstances."). Unusual to Texas' common law of contracts, *Matagorda County* made a contractual agreement in this context subject to "clear and unequivocal" proof of acceptance. *Matagorda County* provides no reasoning to support its creation of that standard.

Matagorda County left open a very small window for insurers to seek reimbursement of settlement payments for claims later determined to be outside policy coverage. Although *Matagorda County* is not expressly overruled by the Court today, the small window *Matagorda County* left open to consider reimbursement is widened by the Court's decision in this case such that the law on reimbursement comports with principles of the common law. Hence, consideration by Texas courts of common law contract theories and quasi-contract theories (e.g., quantum meruit and unjust enrichment) is appropriate once again in determining the rights and obligations of the parties. I concur in the Court's result but join only one of the bases for its outcome, and write to further explain that basis. The parties reached an agreement on reimbursement and we should decide this case by enforcing their agreement. Therefore, I join Part II.C. of the Court's opinion. Although not inconsistent with precedent, the remainder of the opinion is based on equitable and policy considerations and concludes that the parties are bound by a contract implied in law.

Once upon a time, the relationship between insurer and insured was one of contract and was governed by the terms and conditions of the policy. See *Progressive County Mut. Ins. Co. v. Sink***,** 107 S.W.3d 547, 551, 46 Tex. Sup. Ct. J. 658, 46 Tex. Sup. Ct. J. 934 (Tex. 2003) (insurance policy is a contract to be interpreted according to contract principles); *Barnett v. Aetna Life Ins. Co.*, 723 S.W.2d 663, 665, 30 Tex. Sup. Ct. J. 191 (Tex. 1987) ("It is a fundamental rule of law that insurance policies are contracts and as such are controlled by rules of construction which are applicable to contracts generally."). Even after common law modifications of this common law relationship and legislative regulation of the parties' consensual relationship, see, e.g., TEX. BUS. & COM. CODE § 17.41-.63; TEX. INS. CODE § 541.001-.454; *Arnold v. Nat'l County Mut. Fire Ins. Co.*, 725 S.W.2d 165, 167, 30 Tex. Sup. Ct. J. 177 (Tex. 1987) (holding that insurers owe a duty of good faith and fair dealing toward insureds); *G.A. Stowers Furniture Co. v. Am. Indemn. Co.*, 15 S.W.2d 544, 547 (Tex. Comm'n App. 1929, holding approved) (creating a duty to accept reasonable settlement demands within policy limits), it still is fundamentally based on the agreement of the parties. See *Provident Life & Accident Ins. Co. v. Knott*, 128 S.W.3d 211, 216, 47 Tex. Sup. Ct. J. 174 (Tex. 2003) [*50] (as a type of contract, insurance policies are interpreted under rules of contract construction); *Barnett*, 723 S.W.2d at 665. In an insurance arrangement like the one at issue, the insured and insurer enter an agreement for the insurer to cover prescribed risks. Generally, the insured pays premiums to protect it against certain unrealized fortuitous costs or damages, up to an agreed limit, that it may suffer or be obligated to pay. See 1 HOLMES & RHODES, HOLMES'S APPLEMAN ON INSURANCE, 2D (1996).

In this case, Frank's Casing agreed to pay premiums for the provision by Excess Underwriters of excess insurance coverage in the amount of $10 million. ARCO/Vastar sued Frank's Casing and others after an offshore drilling platform partially fabricated by Frank's Casing for ARCO/Vastar collapsed in the Gulf of Mexico. Excess Underwriters issued a reservation of rights letter contesting coverage under its excess insurance policy with Frank's Casing. When settlement discussions were unfruitful, the case was tried to a jury. During the heat of trial, with a large verdict appearing increasingly likely, Frank's Casing entered another round of settlement discussions directly with the plaintiff ARCO and procured a settlement demand of $7.5 million. Frank's Casing then "Stowerized" Excess Underwriters asserting that

the settlement offered was reasonable and within policy limits and demanding that Excess Underwriters settle the case. Excess Underwriters agreed to pay $7 million (plus $500,000 from the primary insurer) to settle the case, conditioned on its intent to seek reimbursement if it were not required to extend coverage to Frank's Casing for claims at issue at trial and which it was about to resolve by settlement.

At the time the parties were considering the settlement, both believed they were in difficult positions. The record indicates that both parties believed a substantial verdict, possibly beyond the excess layer of insurance coverage, was likely. Both also knew that their original contract of insurance did not address the issue of the insurer's ability to obtain reimbursement of a settlement payment for uninsured claims. Under these circumstances, the following decision trees grew.

During the trial, Excess Underwriters had to decide whether to pay for settlement of claims, which it asserted were not covered. It also knew that after being Stowerized, if it did not pay the settlement and did not prevail in a declaratory judgment action contesting coverage, it likely would face claims for bad faith insurance practices. These claims in Texas have on many occasions resulted in large verdicts against insurers which, with common law and statutory penalties, have far exceeded actual damages proven. On the other hand, if it paid to settle on behalf of its insured, Excess Underwriters' payment would be less than its policy limits, it would avoid a verdict that could exhaust its excess limits and it would halt the accrual of attorneys' fees. Effecting a settlement would also avoid a bad faith insurance lawsuit and the potential for a punitive damage award against it. Excess Underwriters would benefit from the proposed settlement.

Frank's Casing likewise believed that it was faced with the specter of a large jury verdict against it. It solicited a settlement offer within policy limits from ARCO. Armed with a potential way out, Frank's Casing demanded that Excess Underwriters pay the settlement. The settlement would end the trial and vanquish the risk of a large verdict and Frank's Casing's potential exposure for amounts above the excess limits or for the entire verdict if there were no coverage. Plus, by sending a *Stowers* letter, Frank's Casing upped the ante against Excess Underwriters for if it did not pay the settlement, and a large verdict were rendered for which coverage was found to exist, Excess Underwriters may have been liable for enhanced damages and substantial statutory penalties. In other words, the settlement would also benefit Frank's Casing.

Excess Underwriters decided to pay its portion of the settlement but conditioned its payment on its right to seek reimbursement if the claim were proven not to be a risk the parties had agreed to cover under their insurance policy. The insurer sent a letter on February 23, 1998, making this offer to Frank's Casing. The letter further stated that the insurer "will contact Arco/Vasta's attorney this morning" to settle the claims against Frank's in this case. Frank's Casing concurred that the settlement was reasonable and not only approved but demanded that Excess Underwriters consummate the $7.5 million settlement. Excess Underwriters sent a second letter on February 23 to confirm the settlement with ARCO and then filed a declaratory judgment action contesting coverage that same day. The next day at the hearing before the trial court, which had recessed trial to give the parties the opportunity to resolve the dispute, the parties dictated their settlement into the record. At the hearing after the parties had entered the settlement the prior day, Frank's Casing objected for the first time that Excess Underwriters did not preserve its ability to contest "coverage."

Hence, we come to the dispute before this Court. Did Frank's Casing obtain a windfall--i.e., payment by its insurer of millions of dollars to settle claims against it for which there was no coverage? Or did Excess Underwriters voluntarily pay a settlement to obtain the benefits of saving itself potentially millions of dollars from the expected verdict and millions more from a possible bad faith verdict in a subsequent lawsuit? Two sophisticated entities carefully exercised their rights and obligations in light of their potential exposure. Both made reasoned decisions they believed to be in their best interests under the circumstances. And but for the condition on reimbursement included in Excess Underwriters' offer accepted by Frank's Casing, I would conclude that there is no right to reimbursement. Absent the parties entering into a legally enforceable agreement, I do not believe that the equities of the parties' respective circumstances alone supports allowing a right to recoup the settlement payment.

I agree with the Court that by Stowerizing Excess Underwriters, Frank's Casing acknowledged the reasonableness of the settlement. See ___ S.W.3d at ___. But I disagree with the Court that the effect of that action supports allowing the insurer to seek reimbursement. If Frank's Casing's only conduct upon obtaining the $7.5 million settlement offer from ARCO was to make a *Stowers* demand on Excess Underwriters and acquiesce to a settlement that

did not include the term on reimbursement, Excess Underwriters should have no right to reimbursement. Threatening to sue does not change the contract between the parties. And such a threat should not serve as a sufficient basis to entitle Excess Underwriters to obtain reimbursement of its payment. Under these circumstances, it is difficult to conceive that Excess Underwriters was under any legally cognizable duress that undermined its will and forced it to pay the settlement. Neither the threat to exercise a legal right nor legally exercising that right can constitute duress. In re *FirstMerit Bank, N.A.*, 52 S.W.3d 749, 758, 44 Tex. Sup. Ct. J. 900 (Tex. 2001); *Ulmer v. Ulmer*, 139 Tex. 326, 162 S.W.2d 944, 947 (Tex. 1947). There were no allegations of fraud, collusion, or extortion to tilt the scale here.

However, I conclude that Frank's Casing, by its acquiescence in the settlement, bound itself under principles of contract law to the condition that Excess Underwriters would be able to seek reimbursement. Frank's Casing was not simply a beneficiary of its insurer's settlement, but demanded in a prior letter of February 19, 1998, that Excess Underwriters act in a "reasonably prudent" manner and accept the settlement offer from ARCO and do so "BEFORE a ruling by the court on the contract issues . . . [which] could occur at any time, but will occur, at the latest, by the beginning of court Tuesday of next week." Including the weekend, the following Tuesday (February 24) was five days away. Excess Underwriters agreed to pay the settlement but as a condition to doing so reserved the right to seek repayment from Frank's Casing if the declaratory judgment action determined there was no insurance coverage for the claims at issue in the prior trial. The February 23 letter to Frank's Casing in which Excess Underwriters agreed to settle the case on its behalf provided:

In order to ensure that the favorable settlement will not be lost to both Frank's and [Excess Underwriters], [Excess Underwriters] will fund the settlement up to $7,500,000 (less any contribution from the primary policy) and will continue to reserve all coverage issues under the Umbrella Policy. [Excess Underwriters] will hold Frank's responsible for and will seek reimbursement of all sums paid in settlement of claims for which no coverage exists under the Umbrella Policy." (emphasis added).

Excess Underwriters then settled the case against its insured the same day and faxed written confirmation to ARCO with a copy to Frank's Casing. Frank's Casing never asserts that it rejected the settlement offer or made a counteroffer. Instead, Frank's Casing acknowledged that it accepted the settlement offer from Excess Underwriters but argues that Excess Underwriters did not obtain "Frank's agreement nor its clear and unequivocal consent to seek reimbursement." [2]

The February 23 letter to ARCO confirming the verbal settlement also stated that Excess Underwriters continued to reserve all rights "against Frank's as to coverage" and, for a second time that day, affirmed that it would "hold Frank's responsible for and will seek reimbursement of all sums paid in settlement of claims for which no coverage exists under the Umbrella policy." Frank's Casing again did not reject but accepted the settlement. After entering the settlement, Excess Underwriters filed its declaratory judgment action contesting coverage that afternoon.

The next morning the trial court recessed the trial to enable the parties to dictate their settlement into the record. Frank's Casing stated that by the February 23 letter from Excess Underwriters to ARCO it had agreed to pay $7,500,000 to settle the case with the plaintiffs. Frank's Casing then asserted that "underwriters have either waived their right to reserve cover [sic] issues or alternatively [are estopped] from asserting any coverage issues since underwriters have agreed to the settlement." The court rendered judgment on the agreement dictated into the record. The Settlement Agreement and Release, signed later by the parties, including Frank's Casing and Excess Underwriters, confirmed that the covenants not to sue and the releases between the parties do not apply "to any claims that exist presently or may arise in the future between Defendant Frank's and Frank's Insurers arising from the claims asserted by Plaintiffs."

Frank's Casing has never disputed that Excess Underwriters' settlement offer was conditioned on a right to seek reimbursement. Frank's Casing argues that by its silence it accepted the part of the settlement offer providing for Excess Underwriters to make a $7 million settlement payment but did not accept the condition on that promise. The law and the facts do not support Frank's Casing's position.

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[2] Frank's Casing's also complains that it had only a few hours to study the proposed settlement from Excess Underwriters. This complaint carries little weight as it was Frank's Casing that imposed the February 23 deadline on the settlement negotiations in its February 19 letter.

A contracting party cannot accept the benefits of a contract and disclaim its obligations. *W.H. Putegnat Co. v. Fidelity & Deposit Co. of Md.*, 29 S.W.2d 1004, 1006 (Tex. 1930) ("Where one accepts the benefits of a contract, he must assume its burdens."). Nor can a party accepting an offer validly purport to accept the offer's benefits, acquiesce in the benefits from the offeror's performance of the contract, but later reject the detriments. *United Concrete Pipe Corp. v. Spin-Line Co.*, 430 S.W.2d 360, 364, 11 Tex. Sup. Ct. J. 495 (Tex. 1968) [*60] (noting that a party may have the right to withdraw his consent before a contract's performance but not after the promise is accepted or performed); see *Daniel v. Goesl*, 161 Tex. 490, 341 S.W.2d 892, 895, 4 Tex. Sup. Ct. J. 170 (Tex. 1960) (one who "receives and accepts benefits under the contract . . . is bound by the terms of the contract"); Jerry, The Insurer's Right to Reimbursement of Defense Costs, 42 ARIZ. L. REV. 13, 71-72 (2000) ("Acquiescence in and acceptance of the benefits of [the party's] performance constitute a manifestation of acceptance of the terms on which [the party's] performance was tendered."). To effectively decline an offer, some terms of which an offeree disapproves, the offeree must reject the offer or make a counteroffer. See *Ashford Dev., Inc. v. US Life Real Estate Servs. Corp*., 661 S.W.2d 933, 935, 27 Tex. Sup. Ct. J. 118 (Tex. 1983) (determining that supplemental provision of loan commitment was a counter-offer); *Komet v. Graves*, 40 S.W.3d 596, 601 (Tex. App.--San Antonio 2001, no pet.) (attempt to change offer before acceptance operates as a rejection and counter-offer). Neither occurred here before the settlement was consummated.

Frank's Casing accepted the settlement proposed by Excess Underwriters and thereby acquiesced in the terms of the offer, and bound itself to the settlement under the law of contracts. In practice in an insurance context, insureds often communicate acceptance of an offer by conduct, as in the case of an insured accepting a defense from an insurer which reserves its right to deny coverage. In such cases, the insured's acceptance of the defense is an implied consent to the insurer's reservation of the coverage issues, "even in the absence of an express consent or acceptance of the offer." *W. Cas. & Sur. Co. v. Newell Mfg. Co.*, 566 S.W.2d 74, 76 (Tex. Civ. App.--San Antonio 1978, writ ref'd n.r.e.); see *In re Halliburton Co.*, 80 S.W.3d 566, 568, 45 Tex. Sup. Ct. J. 720 (Tex. 2002) ("When an employer notifies an employee of changes to the at-will employment contract and the employee 'continues working with knowledge of the changes, he has accepted the changes as a matter of law.'") (citing *Hathaway v. General Mills, Inc*., 711 S.W.2d 227, 229, 29 Tex. Sup. Ct. J. 333 (Tex. 1986)); *Blue Ridge Ins. Co. v. Jacobsen*, 25 Cal. 4th 489, 106 Cal. Rptr. 2d 535, 22 P.3d 313, 317 (Cal. 2001).

Hence, during the trial the parties extended their contractual arrangement to address the risk of a large verdict by settlement and also agreed on a method to allocate the cost. The settlement vanquished the risk of a jury verdict against them. The allocation of the cost of settlement would be based on the outcome of the coverage suit. If the claims settled were found to be covered by the excess policy, Excess Underwriters' payment of the settlement would end the matter. The contractual relationship would function as intended as Excess Underwriters was paid premiums to protect Frank's Casing from covered risks within policy limits. If the claims settled were found not to be covered under the insurance policy, Excess Underwriters would have its contractual right to seek reimbursement of the settlement payment. The relationship of the parties is still one governed by contract.

In her concurring opinion, JUSTICE O'NEILL contends that no such agreement was in fact reached, and under this contractual implied-in-fact analysis Frank's Casing may keep the benefit of the offer to pay $7,500,000 to settle the case but reject the reimbursement condition on the offer. As cited, infra, contract law does not allow her approach of "having my cake and eating it, too." A deal is a deal, and in Texas we enforce deals. If, as JUSTICE O'NEILL asserts, Frank's Casing really wanted to reject the offer's condition on reimbursement, it could have done so by refusing the $7,500,000 payment on its behalf and proceeding with trial, or making a counteroffer that excluded the reimbursement condition, or objecting to the reimbursement term before the settlement was entered with ARCO. (Frank's Casing likely did not want to do the latter because objecting to the condition would also have rejected the entire offer of settlement.) She further asserts that "Frank's Casing's reimbursement contest implied the insurers' consent to Frank's Casing's reservation of the reimbursement question." Again, neither the law nor the facts support her assertion. Only after the settlement with ARCO was entered verbally and confirmed in writing by Excess Underwriters did Frank's Casing assert that Excess Underwriters waived or was estopped from raising any coverage issues. Assuming the objection to raising coverage issues is an objection to the reimbursement condition, a party cannot make a deal and then later selectively

reject parts of it. See *W.H. Putegnat Co.*, 29 S.W.2d at 1006. [3]

Frank's Casing argues that such a result is unfair. I do not agree. A trial court decided that the claims against Frank's Casing, which Excess Underwriters agreed to pay to settle were not covered claims under Frank's Casing's insurance policy. Frank's Casing did not appeal that determination, and it is therefore settled. Frank's Casing is not entitled to insurance coverage for risks for which it paid no premiums. And Excess Underwriters is not obligated to pay for risks it did not agree to cover and for which it received no consideration. Should the parties have desired to cover such risks, they could have consented to such an arrangement by defining the scope of the coverage to include the claims at issue, and agreed on premiums to be paid for such insurance. But they did not.

The parties should sink or swim on the agreements they enter, unless the facts are such that they effect a change in the parties' agreement under principles of contract law, are validly affected by the Legislature, or involve fraud, extortion or other basis for altering a contract. Accordingly, the factors the Court cites as the basis for concluding that the right to reimbursement exists are not central to the reimbursement analysis. I disagree with the Court's reasoning that the weight and potential severity of a *Stowers* or bad faith insurance verdict can serve as a basis to alter the agreement of the parties. Insurance is a consensual arrangement not subject to change by the threat of a lawsuit. If *Stowers* or bad faith actions are skewing litigation and parties' legitimate incentives, then *Stowers* actions may need to be addressed by the appropriate branch rather than allow threat of such actions to serve as a basis for reimbursement.

In summary, I would hold that absent a provision in the insurance policy providing for the insured to reimburse the insurer for paying to settle a claim that is later held not to be covered, there is no right to reimbursement of the settlement payment. However, an insurer should be allowed the opportunity to prove a right to recoupment of a reasonable settlement under contract law, including under the theories of implied-in-fact contracts and quasi-contracts, if the insurer gives notice of its intention to recoup the payment in a timely reservation of rights letter or makes reimbursement a term or condition of a subsequent agreement.

This approach is straightforward and predictable. The current jurisprudence on this issue involves a convoluted set of tangled yet important interests and policy considerations that, with slight changes in the facts, can lead to widely varying results in cases that seem quite similar. Compare *Frank's Casing*, 93 S.W.3d 178 with *Matagorda County*, 52 S.W.2d 128. Under this Court's opinions, the adjudication of each case is based on the equities of the parties which will lead to a series of case-by-case adjudications or, at best, adjudications by category. Each case will involve the same plethora of questions with a different set of answers. Was a *Stowers* demand made? Did the insurer have the unilateral right to settle and was consent of the insured obtained to the settlement? Who controlled the defense? Who initiated and controlled the settlement discussions? Did the insurer give the insured the option to assume its own defense? Then the courts' balancing will begin. Instead, I believe the parties' contractual relationship should govern an insurer's right to reimbursement. These other factors may be central to other issues that arise between insurers and insureds, but should not be central to a right of reimbursement.

This case raises a tangled mound of considerations. The Court deftly traverses the multitude of policies, incentives, and equities to reach a decision. See, e.g., *Am. Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842, 37 Tex. Sup. Ct. J. 561 (Tex. 1994); *Arnold*, 725 S.W.2d 165, 30 Tex. Sup. Ct. J. 177; *Stowers*, 15 S.W.2d 544; see also *Blue Ridge Ins.*, 25 Cal. 4th 489, 106 Cal. Rptr. 2d 535, 22 P.3d 313. Frank's Casing acknowledges that decisions in reimbursement cases are "based on a balancing of policy considerations applicable to the relationship between an insurer and its

[3] Even accepting, arguendo, JUSTICE O'NEILL's position that Frank's Casing can reject a term of an accepted agreement, the facts still undercut her conclusion. Frank's Casing never asserted that it objected to the reimbursement term in Excess Underwriter's settlement offer. Even at the trial court hearing to enter the settlement on the record, Frank's Casing asserted only that Excess Underwriters waived or was estopped from contesting the insurance coverage issues. Its briefing is careful to only make the factual claim that it objected to a contest to coverage. Thus, contrary to JUSTICE O'NEILL's suggestion, Frank's Casing did not object to or reserve for court determination the reimbursement issue in the settlement. This issue is not a central part of my writing because it was not raised by the parties.

insured." If our analysis of this reimbursement issue were based on the agreements between the parties, the law in this area would be less perplexing and more predictable.