"The Down and Dirty on the Prompt Payment of Insurance Claims"

Mark L. Kincaid

University of Texas School of Law
32nd Annual Page Keeton Civil Litigation Conference

October 30, 2008

MARK L. KINCAID

KINCAID & HORTON, L.L.P.

106 E. 6th Street, Suite 500

Austin, Texas 78701

(512)499-0999 • (512)499-0816 *fax*

EDUCATION

- B.B.A. with honors, University of Texas (1980)
- J.D. with honors, University of Texas School of Law (1983)

EMPLOYMENT

- Kincaid & Horton, L.L.P. (2007–present)
- Kincaid, Horton & Smith (2004-2007)
- Kincaid & Horton (1997-2004)
- Law Office of Mark L. Kincaid (1991-1994, 1995-1997)
- Adjunct Professor, University of Texas School of Law (1995-present) (Insurance Litigation)
- Public Counsel, Office of Public Insurance Counsel, State of Texas (1994-1995) (appointed by Gov. Ann Richards to head agency advocating for the interests of Texas insurance consumers)
- Longley & Maxwell (1984-1991)
- Managing Editor, *Texas Consumer Law Reporter* (1985-1992)
- Briefing Attorney, Supreme Court of Texas, Justice Franklin S. Spears (1983-1984)

AWARDS & CERTIFICATIONS

- Board Certified in Consumer & Commercial Law (1993), Civil Trial Law (1993), and Civil Appellate Law (1991), Texas Board of Legal Specialization
- Fellow, Texas Bar Foundation
- "AV"-rated by Martindale-Hubbell Law Directory
- Named as *Super Lawyer* by Law & Politics Media and the publishers of Texas Monthly (2003, 2004, 2005, 2006, 2007 and 2008)

PROFESSIONAL & CONTINUING LEGAL EDUCATION ACTIVITIES

- Co-author, *Texas Practice Guide: Insurance Litigation* (West 2008)
- State Bar of Texas Pattern Jury Charges Committee – "Business, Consumer, Insurance & Employment"; Member (1995-2006); Vice Chair (2006-2008)
- Consumer Law Council, State Bar of Texas Consumer Law Section: Chair (1994-1995); Co-chair, Continuing Legal Education Committee (1992-1995); Member (1988-2002)
- Frequent Lecturer and Author, for State Bar of Texas, University of Texas School of Law, Southern Methodist University School of Law, St. Mary's University School of Law, Texas Tech University School of Law, University of Houston School of Law, and South Texas College of Law

Texas Practice Guide – Chapter 17 Prompt Payment of Claims Statute [1]

---

[1] Reprinted with permission from Kincaid & Martin, *Texas Practice Guide: Insurance Litigation* § 7:1 (West 2004).

Texas Practice Guide: Insurance Litigation
Database updated October 2008

Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute

Summary

Scope:

This chapter details the provisions of chapter 542, subchapter B of the Texas Insurance Code—the Prompt Payment of Claims statute. The statute imposes on insurers deadlines for responding to, investigating, and accepting or rejecting claims. The chapter covers standing to sue, potential defendants, duties imposed on insureds, duties imposed on insurers, and penalties and remedies for violations of the statute. Tex. Ins. Code §§ 542.051 to 542.061.

West's Key Number Digest

West's Key Number Digest, Insurance 3140 to 3201, 3334 to 3408, 3584, 3585

A.L.R. Library

A.L.R. Index: Insurance and Insurance Companies

Legal Encyclopedias

Tex. Jur. 3d, Insurance Contracts and Coverage §§ 1016 to 1042, 1106 to 1154, 1170 to 1194, 1202 to 1207

Treatises and Practice Aids

West's Texas Practice Series: Consumer Rights & Remedies § 5.16

Forms

Texas Jur Pleading and Practice Forms (2d ed.), Insurance § 144:10

TXPG-INS CH 17 SUM

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
I. Overview

Summary

Research References

West's Key Number Digest

West's Key Number Digest, Insurance 3140 to 3201, 3334 to 3408, 3584, 3585

Legal Encyclopedias

Tex. Jur. 3d, Insurance Contracts and Coverage §§ 1106 to 1154

Treatises and Practice Aids

West's Texas Practice Series: Consumer Rights & Remedies § 5.16

Forms

Texas Jur Pleading and Practice Forms (2d ed.), Insurance § 144:10

TXPG-INS CH 17 I REF

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
I. Overview

Summary References

§ 17:1. In general

West's Key Number Digest

West's Key Number Digest, Insurance 3140, 3141

The "Prompt Payment of Claims statute"—imposes certain deadlines for an insurer to acknowledge, investigate, and accept or reject a claim. An insurer that violates the statute is liable for attorney's fees and an additional 18% per annum in addition to the amount of the claim.

The statute sets out the steps an insurer must follow when presented with a "first party" claim by an insured.

To recover a penalty under the statute act, an insured must establish that:
(1) the insured had a claim under an insurance policy;
(2) the insurer is liable for the claim; and
(3) the insurer has failed to comply with a requirement of the Act.

Allstate Ins. Co. v. Bonner, 51 S.W.3d 289, 291 (Tex. 2001).

The statute was codified as article 21.55. Effective April 1, 2005, it was recodified as Texas Insurance Code §§ 542.051 to 542.061. Most authorities refer to the earlier version.

Comment:

The Texas Supreme Court considered in Allstate Ins. Co. v. Bonner, 51 S.W.3d 289 (Tex. 2001), whether an insurer that did not comply with the claim acknowledgment deadline could be held liable under the statute even though the insurer ultimately did not owe the claim. The insured was awarded less on her uninsured motorists claim than the insurer had already paid in personal injury protection benefits. Nevertheless, Bonner argued that Allstate's violation entitled her to recover attorney's fees under the statute. The Supreme Court rejected this argument and held that for an insurer to be held liable under Article 21.55, a party must establish the three elements listed above.

The *Bonner* decision raises questions whether an insurer can always disprove a claim and thereby avoid liability for violating the statute, or whether the court's holding is limited to the circumstance presented in that case. See also Wellisch v. United Serv. Automobile Ass'n, 75 S.W.3d 53, 56 to 59 (Tex. App.—San Antonio 2002, pet. denied); Menix v. Allstate Indem. Co., 83 S.W.3d 877, 883, 2002 WL 1726938 (Tex. App.—Eastland 2002, pet.

denied). This question is discussed in more detail below in § 17:43.

TXPG-INS § 17:1

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
I. Overview

Summary References

§ 17:2. Statutory origin and purpose

The statute's purpose is "to promote the prompt payment of insurance claims pursuant to policies of insurance." *Tex. Ins. Code Ann. § 542.054*; see also St. Paul Reinsurance Co., Ltd. v. Greenberg, 134 F.3d 1250, 1255 & n. 24 (5th Cir. 1998); Daugherty v. American Motorists Ins. Co., 974 S.W.2d 796, 798 (Tex. App.—Houston [14th Dist.] 1998, no pet.)

The statute replaced former Articles 3.62 and 3.62-1, which imposed penalties for an insurer's failure to pay a claim within thirty days.

Comment:

The new statute made several changes compared to the prior laws. It applies to more insurers and more kinds of insurance. It imposes more deadlines. It also imposes a bigger penalty—18% per annum, instead of a flat 12%. The statute was intended to enhance the protections for insureds and claimants, and strengthen the incentives for prompt claims handling by insurers.

TXPG-INS § 17:2

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
I. Overview

Summary References

§ 17:3. Statutory construction—Liberal construction

The statute provides:

This subchapter shall be liberally construed to promote the prompt payment of insurance claims.

Tex. Ins. Code Ann. § 542.054; see also Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 473 to 474 (Tex. App.—Tyler 1999, pet. denied); Bekins Moving & Storage Co. v. Williams, 947 S.W.2d 568, 583 (Tex. App.—Texarkana 1997, no pet.); Teate v. Mutual Life Ins. Co., 965 F. Supp. 891, 894 (E.D. Tex. 1997).

The meaning of "liberal construction" has been applied expansively under other consumer statutes. See Cameron v. Terrell & Garrett, Inc., 618 S.W.2d 535, 541 (Tex. 1981) (liberal construction mandates that court give statute most comprehensive application possible without doing violence to the statute's terms).

Example:

In Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467 (Tex. App.—Tyler 1999, pet. denied), the court relied on liberal construction to conclude that a claim was sufficient to trigger the statutory deadlines, even though it was presented through the claimant's attorney. Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 473 (Tex. App.—Tyler 1999, pet. denied). The *Dunn* court also relied on the liberal construction mandate to conclude that the statute applies to uninsured motorist claims. Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 474 (Tex. App.—Tyler 1999, pet. denied).

Example:

The court in Mid-Century Ins. Co. v. Barclay, 880 S.W.2d 807, 812 n. 4 (Tex. App.—Austin 1994, writ denied), relied on the liberal construction clause to reject the insurer's argument that the statute had to be strictly construed because it is penal in nature. Of course, even without a liberal construction mandate in the statute, this argument should have been rejected. The Legislature has generally provided that all statutes are to be liberally construed to achieve their purposes, and to promote justice. *Tex. Gov't Code Ann. § 312.006*.

Example:

On the other hand, the liberal construction mandate was not enough in Teate v. Mutual Life Ins. Co., 965 F. Supp. 891, 894 (E.D. Tex. 1997), to lead the court to allow compounding of the statutory damages. Nor was it

enough in Bekins Moving & Storage Co. v. Williams, 947 S.W.2d 568, 583 (Tex. App.—Texarkana 1997, no pet.), to cause the court to treat a violation of this statute as an unfair insurance practice.

TXPG-INS § 17:3

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
I. Overview

Summary References

§ 17:4. Statutory construction—Relation to prior law

Another tool for construing the statute is to consider precedents under its predecessor statutes, Articles 3.62 and 3.62-1.

Example:

The following illustrate the consideration of the predecessor statutes:

(1) Because good faith in denying a claim was no defense under the predecessor statutes, it is not a defense under this statute. See Higginbotham v. State Farm Mut. Auto. Ins. Co., 103 F.3d 456 (5th Cir. 1997);

(2) The court in Teate v. Mutual Life Ins. Co., 965 F. Supp. 891, 894 (E.D. Tex. 1997), relied on Article 3.62 precedents to conclude that a contingent fee was proper. Of course, a contingent fee stated as a percentage of recovery is no longer allowed (this is also discussed in § 17:36), but *Teate* does demonstrate the court's reference to precedents under the old statutes; and

(3) In Butler v. Group Life & Health Ins. Co., 962 S.W.2d 296, 301 (Tex. App.—Austin 1998, no pet.), the court held that the statute does not apply to insurance provided by the Employee Retirement System, because the prior statute did not.

Comment:

Referring to precedents under the predecessor statutes only applies when doing so is consistent with liberal construction of the statute to encourage prompt payment of claims. In Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467 (Tex. App.—Tyler 1999, pet. denied), the court declined to exclude uninsured motorist coverage from the purview of the statute, even though the prior statutes did not address this coverage. Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 473 (Tex. App.—Tyler 1999, pet. denied). Instead, the court held that the Legislature did not intend to limit the statute as the others had been. The Legislature excluded certain types of insurance from the statute, but UIM coverage was not among them. Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 473 to 474 (Tex. App.—Tyler 1999, pet. denied).

TXPG-INS § 17:4

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
II. Standing & Scope of Statute

Summary

Research References

West's Key Number Digest

West's Key Number Digest, Insurance 3140, 3153 to 3156, 3244 to 3246

Legal Encyclopedias

Tex. Jur. 3d, Insurance Contracts and Coverage §§ 1106 to 1154

Treatises and Practice Aids

West's Texas Practice Series: Consumer Rights & Remedies § 5.16

Forms

Texas Jur Pleading and Practice Forms (2d ed.), Insurance § 144:10

TXPG-INS CH 17 II REF

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
II. Standing & Scope of Statute

Summary References

§ 17:5. Standing—In general—“Claims" and "claimants"

West's Key Number Digest

West's Key Number Digest, Insurance 3140

The protections of the statute apply to a “claimant,” who is defined as “a person making a claim.” *Tex. Ins. Code § 542.051(3)*.

The statute provides:

• a "claimant" is a person making a claim, *Tex. Ins. Code § 542.051(3)*

• a "claim" is a first party claim that is made by an insured or a policyholder under an insurance policy or contract or by a beneficiary named in the policy or contract, and that must be paid by the insurer directly to the insured or beneficiary, *Tex. Ins. Code § 542.051(2)*

• "notice of claim" means any written notification by a claimant to an insurer that reasonably apprises the insurer of the facts relating to the claim, *Tex. Ins. Code § 542.051(4)*

• the statutory deadlines begin once the insurer receives notice of a "claim," from a "claimant." *Tex. Ins. Code § 542.055(a)*

The term "claimant" does not limit the statute to those claims where the insurer is dealing directly with the insured. The insured's retention of legal counsel does not cause the insured to lose their "claimant" status under the statute. In *Dunn v. Southern Farm Bur. Cas. Ins. Co.*, the court held:

> Thus, the logical conclusion is that Dunn remains a "claimant" under the statute even though her claim was presented by an attorney … The impact on insurance claimants by the practices condemned in Article 21.55 is the same whether the claimant is represented by counsel or not.

Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 473 (Tex. App.—Tyler 1999, pet. denied). A judgment creditor of an insured is not a claimant entitled to relief under Article 21.55. Hartman v. St. Paul Fire & Marine Ins. Co., 55 F. Supp. 2d 600, 604 (N.D. Tex. 1998).

Comment:

Uninsured motorist claims, plumbing leak claims, life insurance claims, and business interruption claims are just a few examples of "first party" claims governed by this statute. An insured's claim for a defense under a liability policy may also be considered a first party claim under this statute. See *infra* § 17:7.

Comment:

By focusing on first party claimants, these definitions would exclude persons making a claim against another person's policy. Allstate Ins. Co. v. Watson, 876 S.W.2d 145, 147 (Tex. 1994) (claimant had no standing to sue other party's insurer under Article 21.21 for unfair insurance practices).

TXPG-INS § 17:5

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
II. Standing & Scope of Statute

Summary References

§ 17:6. Application to "third party" liability insurance claims

West's Key Number Digest

West's Key Number Digest, Insurance 3244 to 3246

On its face, the statute applies only to "first party" claims. The statute defines "claim" to mean "a first party claim that: (A) is made by an insured or a policyholder under an insurance policy or contract or by a beneficiary named in the policy or contract; and (B) must be paid by the insurer directly to the insured or beneficiary." *Tex. Ins. Code Ann. § 542.051*. This would exclude liability insurance claims for coverage that must be paid to an injured third party.

Nevertheless, in State Farm Fire & Cas. Co. v. Gandy, 925 S.W.2d 696 (Tex. 1996), the Supreme Court stated that the statute does apply to third party liability insurance. The court was discussing a liability insurer's ability to seek a declaratory judgment when issues of coverage and the duty to defend arise. The court stated that if the insured were successful, the insured should be entitled to recover attorney's fees and penalties under the statute. See State Farm Fire & Cas. Co. v. Gandy, 925 S.W.2d 696, 714 (Tex. 1996).

Comment:

Many corporate liability policies contain a self-insured retention or a deductible that results in the reimbursement of defense or indemnity benefits directly to the policyholder. Similarly, some "indemnity only" liability policies only pay benefits after the insured has paid money in settlement of a claim and then submitted the claim to the liability carrier for reimbursement. In either of these situations an argument exists that the statute should apply to the claim because the policy benefit is being paid directly to the insured.

The Texas Supreme Court has found that a “first-party claim” is not synonymous with a first-party insurance policy. Lamar Homes, Inc. v. Mid-Continent Cas. Co., 50 Tex. Sup. Ct. J. 1162, 2007 WL 2459193 (Tex. Aug. 31, 2007). In other words, whether a claim falls within the ambit of the statute depends not on the type of policy but on the claimant’s relationship to the loss: “a first-party claim is stated when ‘an insured seeks recovery for the insured’s own loss,’ whereas a third-party claim is stated when ‘an insured seeks coverage for injuries to a third party.’” Lamar Homes, Inc. v. Mid-Continent Cas. Co., 50 Tex. Sup. Ct. J. 1162, 2007 WL 2459193 (Tex. Aug. 31, 2007) (quoting Universe Life Ins. Co. v. Giles, 950 S.W.2d 48, 45 n. 2 (Tex. 1997)). Therefore, the statute may apply to claims brought under third-party insurance policies, including claims for a defense under a liability policy. See *infra* § 17:7.

TXPG-INS § 17:6

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
II. Standing & Scope of Statute

Summary References

§ 17:7. Application of statute to demand for defense under liability insurance policy

The Texas Supreme Court addressed the issue of whether the prompt payment statute applies to an insured's demand for a defense under a liability policy or to the insured's demand for reimbursement of defense costs when the insurer has wrongly denied a defense, in Lamar Homes, Inc. v. Mid-Continent Cas. Co., 50 Tex. Sup. Ct. J. 1162, 2007 WL 2459193 (Tex. Aug. 31, 2007). Prior to this decision, courts were split on the issue. A number of courts had concluded that the statute applied to the denial of a claim for a defense. See, e.g., Northern County Mutual Ins. Co. v. Davalos, 84 S.W.3d 314, 318-19 (Tex. App.—Corpus Christi 2002), rev'd on other grounds, 140 S.W.3d 685 (Tex. 2004). Other courts had reached the opposite conclusion that the statute does not apply to the denial of a claim for a defense. See, e.g., TIG Ins. Co. v. Dallas Basketball, Ltd., 129 S.W.3d 232, 239-241 (Tex. App.—Dallas 2004, pet. denied). The Texas Supreme Court agreed with the former position, and held that the statute does apply to a demand for a defense under a liability policy.

In *Lamar Homes*, a construction builder sold a new home that later developed problems due to defects in the foundation. The buyers sued the builder, which forwarded the lawsuit to its insurance company seeking a defense and indemnification under a commercial general liability (CGL) insurance policy. The insurer denied coverage and refused to defend. Consequently, the builder sought a declaration of its rights under the CGL policy and recovery under the prompt payment statute. The district court held that the insurer had no duty to defend. Lamar Homes, Inc. v. Mid-Continent Casualty Co., 335 F. Supp.2d 754, 760 (W.D. Tex. 2004). The builder then appealed to the Fifth Circuit, which noted a split among the Texas Courts of Appeals and certified to the Texas Supreme Court the question whether the prompt payment statute applies when an insurer wrongfully refuses to pay the insured's claim for defense costs. Lamar Homes, Inc. v. Mid-Continent Cas. Co., 428 F.3d 193, 199-201 (5th Cir. 2005).

The Texas Supreme Court held that the prompt payment statute applies "when an insurer wrongfully refuses to promptly pay a defense benefit owed to the insured." Lamar Homes, Inc. v. Mid-Continent Cas. Co., 50 Tex. Sup. Ct. J. 1162, 2007 WL 2459193 (Tex. Aug. 31, 2007). First, the court found that claims for a defense were first-party claims, and not third-party claims, because of the claimant's relationship to the loss:

> Without the defense benefit provided by a liability policy, the insured alone would be responsible for these costs. Unlike the loss incurred in satisfaction of a judgment or settlement, this loss belongs only to the insured and is in no way derivative of any loss suffered by a third party. The claim for defense costs then is a first-party claim because the insured is the only party who will suffer the loss of benefit from the claim.

Lamar Homes, Inc. v. Mid-Continent Cas. Co., 50 Tex. Sup. Ct. J. 1162, 2007 WL 2459193 at *12 (Tex. Aug. 31, 2007). Accordingly, claims for defense fall within the scope of the prompt payment statute.

Second, the court found that the language of the statute supports its application to defense claims. Specifically, the court rejected the argument that the statutory language "first party claims" means claims brought under first-party insurance policies. Lamar Homes, Inc. v. Mid-Continent Cas. Co., 50 Tex. Sup. Ct. J. 1162, 2007 WL 2459193 at *12 (Tex. Aug. 31, 2007). According to the court, the language "first party" modifies "claim" and does not, therefore, place any limitations on the types of policies or insurers to which the statute applies. Furthermore, the statute expressly states that it applies to "any insurer" and does not exempt liability or third-party insurance. Thus, the court found no support in the statutory language for exempting a claim for a defense under a liability policy.

Third, the court considered irrelevant the fact that payment of a defense claim is ordinarily paid to the service provider rather than to the insured. Many other types of claims — including health insurance claims and property damage claims — are paid directly to service providers and yet fall within the statute's scope. Additionally, to distinguish between whether an insured or his attorney is paid contradicts the legislative intent that the statute be "liberally construed." Lamar Homes, Inc. v. Mid-Continent Cas. Co., 50 Tex. Sup. Ct. J. 1162, 2007 WL 2459193 at *12-13 (Tex. Aug. 31, 2007).

Finally, the court rejected the argument that the prompt payment statute is unworkable with respect to claims for a defense. The court explained:

> [W]hen the insurer wrongfully rejects its defense obligation, the insured has suffered an actual loss that is quantified after the insured retains counsel and begins receiving statements for legal service. These statements or invoices are the last piece of information needed to put a value on the insured's loss. And when the insurer. . . fails to pay within the statutory deadline, the insured matures its right to reasonable attorney's fees and the eighteen percent interest rate specified by the statute.

Lamar Homes, Inc. v. Mid-Continent Cas. Co., 50 Tex. Sup. Ct. J. 1162, 2007 WL 2459193 at *13 (Tex. Aug. 31, 2007) (citations omitted). In this way, the prompt payment statute's procedures are workable in the context of defense claims.

The court held that "the Legislature did not intend to limit the prompt-payment statute to first-party insurance, but rather intended that it apply to claims personal to the insured," including claims for a defense under liability policies. Consequently, Texas jurisprudence now recognizes that the prompt payment statute applies to an insurer's wrongful refusal to promptly pay a defense benefit owed to an insured. Lamar Homes, Inc. v. Mid-Continent Cas. Co., 50 Tex. Sup. Ct. J. 1162, 2007 WL 2459193 at *14 (Tex. Aug. 31, 2007).

TXPG-INS § 17:7

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
III. Potential Defendants—Who Can Be Sued?

Summary

Research References

Legal Encyclopedias

Tex. Jur. 3d, Insurance Contracts and Coverage §§ 1202 to 1207

Treatises and Practice Aids

West's Texas Practice Series: Consumer Rights & Remedies § 5.16

TXPG-INS CH 17 III REF

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
III. Potential Defendants—Who Can Be Sued?

Summary References

§ 17:8. Potential defendants—Statute applies to insurers

The statute applies only to insurers. See *Tex. Ins. Code Ann. §§ 542.052*, *542.055*, *542.056*, *542.058*, *542.060*. Section 542.052 entitled "Applicability of Subchapter" provides the new definition of "insurer" by stating the following: "This subchapter applies to any insurer authorized to engage in business as an insurance company or to provide insurance in the state, including: " Section 542.052 then provides a list of various insurance companies that would constitute an "insurer" under the former Article and, under the new Chapter 542.

Comment:

This is in contrast to the unfair insurance practices prohibitions in chapter 541, which apply to any "person." Those prohibitions, therefore, also include insurance agents and others engaged in the business of insurance. See Liberty Mut. Ins. Co. v. Garrison Contractors, Inc., 966 S.W.2d 482, 485 (Tex. 1998).

TXPG-INS § 17:8

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
III. Potential Defendants—Who Can Be Sued?

Summary References

§ 17:9. Potential defendants—Types of insurers

The statute applies to all insurers, except those specifically exempted. The statute provides:

(1) a stock life, health, or accident insurance company;

(2) a mutual life, health, or accident insurance company;

(3) a stock fire or casualty insurance company;

(4) a mutual fire or casualty insurance company;

(5) a Mexican casualty insurance company;

(6) a Lloyd's plan;

(7) a reciprocal or interinsurance exchange;

(8) a fraternal benefit society;

(9) a stipulated premium company;

(10) a nonprofit legal services corporation;

(11) a statewide mutual assessment company;

(12) a local mutual aid association;

(13) a local mutual burial association;

(14) an association exempt under Section 887.102;

(15) a nonprofit hospital, medical, or dental service corporation, including a corporation subject to Chapter 842;

(16) a county mutual insurance company;

(17) a farm mutual insurance company;

(18) a risk retention group;

(19) a purchasing group;

(20) an eligible surplus lines insurer; and

(21) except as provided by § 542.053(b), a guaranty association operating under Article 21.28-C or 21.28-D.

Tex. Ins. Code Ann. § 542.052. The statute encompasses almost all insurers and covers almost every type of insurance policy.

The prior "statutory interest" provision—Article 3.62, repealed in 1991, did not apply to certain types of coverages such as UM/UIM claims. The Tyler Court of Appeals has held that the statute is broader than the old Article 3.62 and does apply to UM/UIM claims. Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 473 to 474 (Tex. App.—Tyler 1999, pet. denied).

Also, the statute applies to transit insurance provided by a moving company. See Bekins Moving & Storage Co. v. Williams, 947 S.W.2d 568, 581 (Tex. App.—Texarkana 1997, no pet.) The court reasoned that the moving company called the coverage insurance, its representative called it insurance, the coverage was paid for as insurance, and both parties believed the mover was providing insurance. Thus, the coverage came within the scope of the statute.

TXPG-INS § 17:9

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
III. Potential Defendants—Who Can Be Sued?

Summary References

§ 17:10. Exemptions—Certain insurers are exempted

Exemptions are found in § 542.053, which provides:

(a) This subchapter does not apply to:

(1) workers' compensation insurance;

(2) mortgage guaranty insurance;

(3) title insurance;

(4) fidelity, surety, or guaranty bonds;

(5) marine insurance other than inland marine insurance governed by Article 5.53; or

(6) a guaranty association created an operating under Chapter 2602.

(b) A guaranty association operating under Article 21.28-C or 21.28-D is not subject to the damage provisions of § 542.060.

(c) This subchapter does not apply to a health maintenance organization, except as provided by § 1271.005(c) a claim governed by § 3A, Article 3.70-3C, of this code.

(d) This subchapter does not apply to a claim governed by subchapter C, Chapter 1301 (which relates to preferred provider benefit plans). § 542.053.

Comment:

The exemptions that relate to certain health care providers, are not complete exemptions. Other statutes apply timelines for paying claims and penalties, *Tex. Ins. Code Ann. §§ 1301.101 to 1301.109; Tex. Ins. Code Ann. Ch. 1301*.

In addition to the exemptions expressly set out in the statute, courts have recognized other exemptions.

• In Butler v. Group Life & Health Ins. Co., 962 S.W.2d 296, 301 (Tex. App.—Austin 1998, no pet.), the court held that Article 21.55 does not apply to insurance provided by the Employees' Retirement System.

Those claims are governed by Article 3.50-2, which the court found did not grant a right to recover under this statute.

• The statute is preempted by ERISA, with respect to claims against an employee benefit plan subject to that federal statute. Salameh v. Provident Life & Acc. Ins. Co., 23 F. Supp. 2d 704, 718 (S.D. Tex. 1998).

• Another court held that a claim under the statute was preempted by the federal Carmack Amendment, which applies to claims against interstate shippers. Simmons v. United Parcel Serv., 924 F. Supp. 65, 66 (W.D. Tex. 1996).

TXPG-INS § 17:10

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
IV. Duties Imposed on Claimants

Summary

Research References

West's Key Number Digest

West's Key Number Digest, Insurance 3142 to 3199

Treatises and Practice Aids

West's Texas Practice Series: Consumer Rights & Remedies § 5.16

TXPG-INS CH 17 IV REF

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
IV. Duties Imposed on Claimants

Summary References

§ 17:11. Duties imposed on claimants—In general

West's Key Number Digest

West's Key Number Digest, Insurance 3142 to 3199

A claimant has two duties: (1) to give the insurer notice of the claim; and (2) to give the insurer all items the insurer reasonably requests as necessary to secure final proof of loss. Section 542.055(a) starts the deadlines for the insurer to act, once the insurer receives notice of the claim. Section 542.056(a) imposes other deadlines once the insurer receives all information required to secure final proof of loss.

TXPG-INS § 17:11

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
IV. Duties Imposed on Claimants

Summary References

§ 17:12. Duties imposed on claimants—Form of "claim"

No particular content is required, as long as the claim "reasonably apprises the insurer of the facts relating to the claim." See *Tex. Ins. Code Ann. § 542.051(4)*.

The statute requires that the claim be in writing. The statute provides that "notice of claim" means “any written notification provided by a claimant to an insurer that reasonably apprises the insurer of the facts relating to the claim." *Tex. Ins. Code Ann. § 542.051(4)*. One court has strictly applied the requirement of written notice, holding that a phone call was not sufficient. McMillin v. State Farm Lloyds, 180 S.W.3d 183 (Tex.App.—Austin, 2005, no pet.)

Practice tip:

Because the statute requires written notice, but insurer’s routinely accept notice of claims by phone, a potential trap exists. If an insured calls to give notice of a claim, the insurer may commence its investigation, but be able to argue, as in *McMillin* that the statutory protections do not apply. Lawyers for insureds should try to make sure written notice was given, to avoid this argument. Often the lawyer does not become involved in time to influence the form of the notice, so it may be necessary to argue that by proceeding with the investigation the insurer waived this right. Alternatively, any assurances or conduct by the insurer leading the insured to believe oral notice was sufficient could support an estoppel argument. Of course, an attorney for the insurer should determine if written notice was not given and, if not, argue that the statutory deadlines were not triggered. Requiring the insured to later give written notice could give the insurer a “do over” chance to meet deadlines that were blown before.

It is sufficient to present a claim through an attorney. Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 471 to 472 (Tex. App.—Tyler 1999, pet. denied).

Example:

In Mid-Century Ins. Co. v. Barclay, 880 S.W.2d 807, 810 (Tex. App.—Austin 1994, writ denied), the court rejected the insurer's argument that an insured giving notice of a claim must identify the specific elements of the policy and expressly state an intent to assert a claim under each.

Comment:

Although the statute calls for written notice, oral notice may be sufficient. For example, in Mid-Century Ins. Co. v. Barclay, 880 S.W.2d 807, 810 (Tex. App.—Austin 1994, writ denied), the court held that a phone call from the insured was sufficient notice to the insurer.

Comment:

If the insurer receives oral notice or written notice that is deficient, but the insurer proceeds to investigate anyway, the insurer may be held to have waived any complaint. Insurers are aware of the requirement that notice of the claim be in writing. If they proceed without written notice, that is conduct inconsistent with assertion of a known right—i.e., waiver. See Massachusetts Bonding & Ins. Co. v. Orkin Exterminating Co., 416 S.W.2d 396, 401 (Tex. 1967).

Example:

In Daugherty v. American Motorists Ins. Co., 974 S.W.2d 796, 798 n. 3 (Tex. App.—Houston [14th Dist.] 1998, no pet.), the court held that the insurer waived any complaint about the insured's notice, because the insurer investigated the claim anyway. See also Bekins Moving & Storage Co. v. Williams, 947 S.W.2d 568, 576, 581 to 582 (Tex. App.—Texarkana 1997, no pet.) (insurer waived asserted condition precedent by proceeding to handle claim despite noncompliance).

TXPG-INS § 17:12

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
IV. Duties Imposed on Claimants

Summary References

§ 17:13. Duties imposed on claimants—Providing insurer with materials reasonably requested by insurer

Although the insured has a duty to respond to an insurer's request for material as are necessary to secure final proof of loss, the insured need only respond with material that is reasonably necessary to secure the final proof of loss to start the clock running. In *Colonial County Mut. Ins. Co. v. Valdez*, the Corpus Christi Court of Appeals held that the failure of the insured to supply all materials pursuant to a broad blunderbuss request even after he supplied what was truly necessary did not operate to prevent the statutory clocks running. Colonial Mut. Ins. Co. v. Valdez, 30 S.W.3d 514, 522 to 523 (Tex. App—Corpus Christi 2000, no pet.) (to secure proof of loss that a vehicle was stolen, it was unnecessary to provide, for example, copies of all vehicle service records and all sets of keys).

TXPG-INS § 17:13

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary

Research References

West's Key Number Digest

West's Key Number Digest, Insurance 3334 to 3408

A.L.R. Library

Liability insurance: third party's right of action for insurer's bad-faith tactics designed to delay payment of claim, 62 A.L.R. 4th 1113

Treatises and Practice Aids

West's Texas Practice Series: Consumer Rights & Remedies § 5.16

TXPG-INS CH 17 V REF

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:14. Duties imposed on insurer—After insurer receives notice of claim

West's Key Number Digest

West's Key Number Digest, Insurance 3334 to 3408

Once the insurer receives notice of a claim, four duties are triggered:

(1) **Acknowledge the claim.** The insurer must acknowledge receipt of the claim. *Tex. Ins. Code Ann. § 542.055(a)(1)*.

(2) **Record the acknowledgment.** If the acknowledgement is not in writing, the insurer shall make a record of the date, means, and content of the acknowledgment. *Tex. Ins. Code Ann. § 542.055(c)*.

(3) **Commence the investigation.** The insurer must commence any investigation of the claim. *Tex. Ins. Code Ann. § 542.055(a)(2)*.

(4) **Request information from the claimant.** The insurer must request from the claimant all items, statements, and forms that the insurer reasonably believes, at that time, will be required from the claimant. *Tex. Ins. Code Ann. § 542.055(a)(3)*.

Most insurers must perform these duties "not later than the 15th day after receipt of notice of a claim." Eligible surplus lines insurers have longer, until "the 30th business day." *Tex. Ins. Code Ann. § 542.055(a)*.

Practice Tip:

Note the different use of "days" and "business days." This distinction appears at several points in the statute. "Business day" is defined to exclude weekends and state holidays. *Tex. Ins. Code Ann. § 542.051(1)*. Because of this distinction, most insurers have about two weeks, but eligible surplus lines insurers have six weeks.

Comment:

In *Lamar Homes Inc. v. Mid-Continental Casualty Co.*, the Texas Supreme Court found that in the context of an insured's claim for a defense, the insured needs to provide the insurer with the statements or invoices for legal services that the insured receives in order to trigger the statutory deadlines. Lamar Homes, Inc. v. Mid-Continent Cas. Co., 50 Tex. Sup. Ct. J. 1162, 2007 WL 2459193, at *12 (Tex. Aug. 31, 2007).

TXPG-INS § 17:14

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:15. Duties imposed on insurer—After insurer receives required information

No additional deadlines are triggered until the insurer receives all items, statements, and forms reasonably required by the insurer. Once the insurer receives that information, seven new duties arise:

(5) **Accept or reject the claim.** By the 15th "business day," the insurer must notify the claimant that it accepts or rejects the claim. *Tex. Ins. Code Ann. § 542.056(a)*. The deadline extends to 30 "days" if the insurer reasonably suspects arson. *Tex. Ins. Code Ann. § 542.056(b)*. Also, the insurer can get a 45 day extension of these deadlines. *Tex. Ins. Code Ann. § 542.056(d)*.

(6) **State reasons for any rejection.** If the insurer rejects the claim, the notice must state the reasons. *Tex. Ins. Code Ann. § 542.056(c)*.

(7) **Ask for more time and tell why it is needed.** If the insurer is unable to accept or reject the claim by the regular deadlines, the insurer may notify the claimant and state the reasons the insurer needs more time. *Tex. Ins. Code Ann. § 542.056(d)*.

(8) **Accept or reject the claim by the extended deadline.** If the insurer gives this notice, the insurer must accept or reject the claim within 45 additional days. *Tex. Ins. Code Ann. § 542.056(d)*.

(9) **Pay claim after accepting.** If the insurer accepts the claim, the insurer must pay within five business days (twenty for surplus lines insurers). *Tex. Ins. Code Ann. § 542.057(a), (c)*.

(10) **Pay the claim after the claimant performs any condition.** If the insurer conditions payment on some act by the claimant, the payment deadline is five business days after the act is performed. A surplus lines insurer has 20 business days. *Tex. Ins. Code Ann. § 542.057(b), (c)*.

(11) **Pay the claim within 60 days after receipt of information.** The insurer must pay the claim within 60 days after receiving the items requested from the claimant. *Tex. Ins. Code Ann. § 542.058(a)*.

Note: If it is determined as a result of arbitration or litigation that a claim is invalid and should not be paid, this requirement does not apply. *Tex. Ins. Code Ann. § 542.058(b)*.

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:16. Duties imposed on insurer—Acknowledge claim

Each separate claim requires written acknowledgment. See Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 472 (Tex. App.—Tyler 1999, pet. denied). It is arguable that separate acknowledgments are required for separate claims arising from the same accident.

TXPG-INS § 17:16

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:17. Duties imposed on insurer—Commence investigation of claim

An insurer must commence any investigation within 15 days after receiving notice of a claim—within 30 days for surplus lines insurers. *Tex. Ins. Code Ann. § 542.055(a)(2)*.

Comment:

The statute does not regulate the scope of an insurer's investigation, only the timeliness of such investigation.

TXPG-INS § 17:17

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:18. Duties imposed on insurer—Requests from claimant for items required to evaluate claim

The statute provides that the insurer must request from the claimant items reasonably believed to be necessary to evaluate the claim. "Additional requests may be made if during the investigation of the claim such additional requests are necessary." *Tex. Ins. Code Ann. § 542.055(a)(3).*

Comment:

Multiple requests are permitted only when "necessary." Multiple incremental requests may be an unfair insurance practice.

Comment:

This provision does not account for the insurer's need to obtain information or documentation from persons or entities other than the insured. The statute requires the insurer request from the claimant (i.e., the insured) all "items, statements, and forms" the insurer needs from the claimant to evaluate the claim. The statute does not address the insurer's need for expert reports, third party records (e.g., medical records), investigative reports from others (e.g., police accident report), and other information or documents available only from persons and entities other than the insured. Many insurers attempt to deal with this provision by informing the insured in writing that their claim cannot be processed until the insured provides needed documents or information from third parties or until the insured cooperates with the insurer's efforts to obtain such items.

TXPG-INS § 17:18

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:19. Duties imposed on insurer—Accept or reject claim

The statute requires the insurer to give written notice it is accepting or rejecting the claim. *Tex. Ins. Code Ann. § 542.056(a).* A telephone call from the insurer notifying the insured of the amount of the loss will not constitute "notice of payment of claim," because the statute requires that the acceptance or rejection be in writing. Daugherty v. American Motorists Ins. Co., 974 S.W.2d 796, 799 (Tex. App.—Houston [14th Dist.] 1998, no pet.) However, an insurer's written response acknowledging only that a claim has been received does not constitute an acceptance or rejection under the statute. Northern County Mut. Ins. Co. v. Davalos, 84 S.W.3d 314, 319 (Tex. App.—Corpus Christi 2002), rev'd on other grounds, 140 S.W.3d 685 (Tex. 2004).

The statute does not require that the insurer pay every claim, only that it promptly investigate, and accept or reject the claim. In Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467 (Tex. App.—Tyler 1999, pet. denied), the court stated:

> Article 21.55 does not require an insurer to pay every claim within a certain time. It simply requires steps to be taken within a specified time frame … Nothing in the statute suggests that the insurance company could not dispute and deny the claim. Indeed the statute is premised on the presumption that carriers have the right to dispute claims. It merely requires that they do so promptly.
>
> Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 474 (Tex. App.—Tyler 1999, pet. denied).

Comment:

Some insurers have attempted to comply with Chapter 542 by informing the insured their claim is "covered" during the required time period, but then taking a longer period of time to calculate the amount of benefits owed. It is doubtful whether this is sufficient to comply with the statute. Because a "claim" is more than a request for coverage, a decision on the claim, including its value, arguably must be made and communicated to the insured in the time required by the statute unless an extension is requested. Further, the term "claim" is not defined as "coverage"; it is a demand for policy benefits that must be paid.

TXPG-INS § 17:19

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:20. Duties imposed on insurer—State reasons for rejecting claim

"If the insurer rejects the claim, the notice required by Subsection (a) or (b) must state the reasons for the rejection." *Tex. Ins. Code Ann. § 542.056(c)*. Arguably, an insurer that fails to comply with this requirement could be held to have waived additional reasons that were not timely raised. However, this argument was rejected in Ridgelea Estate Condo. Ass'n v. Lexington Ins. Co., 415 F.3d 475, 478 n. 2 (5th Cir. 2005). The court stated that the insurer could raise an additional defense, where there was no allegation that the initial reason was unreasonable or made in bad faith.

Comment:

The phrase "rejects the claim" does not specifically address a situation where an insurer pays part, but not all, of a claim. It also does not specifically state whether a claim is "rejected" when the insurer refuses to pay, for a reason not related to coverage—e.g., if the claim is closed without payment because of noncooperation by the insured. Construing the statute liberally to promote its underlying purposes, it is reasonable to construe the term "reject" to mean any decision by the insurer not to pay the claim or not to pay a part of the claim. The insurer should state in writing the reason for any such decision. If the insurer pays part of the claim, the insurer should state in writing the reason it did not pay the rest.

TXPG-INS § 17:20

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:21. Duties imposed on insurer—Request additional time, state reasons, and accept or reject claim by extended deadline

If the insurer is unable to accept or reject the claim within the period specified, the insurer must notify the claimant, not later than the date specified. This notice must give the reasons the insurer needs additional time. *Tex. Ins. Code Ann. § 542.056(d)*.

The insurer shall accept or reject the claim within 45 days. *Tex. Ins. Code Ann. § 542.056(d)*.

Comment:

If the insurer requests a 45 day extension, it will then have 15 business days plus 45 calendar days to accept or reject a claim. This period is greater than the 60 day time period contained in § 542.058. This probably is reconciled through the "except as otherwise provided" language contained in § 542.058.

TXPG-INS § 17:21

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:22. Duties imposed on insurer—Pay claim within 60 days after receiving information

One of the most important provisions of the statute is found in § 542.058, is contained which states:
(a) except as otherwise provided, if an insurer, after receiving all items, statements, and forms reasonably requested and required under Section 542.055, delays payment of the claim for a period exceeding the period specified by other applicable statutes or, if other statutes do not specify a period, for more than 60 days, the insurer shall pay damages and other items as provided by Section 542.060; and
(b) this section does not apply in a case in which it is found as a result of arbitration or litigation that a claim received by an insurer is invalid and should not be paid by the insurer.

Tex. Ins. Code Ann. § 542.058.

Comment:

As discussed below, an insurer may automatically violate the statute by failing to pay a claim that is shown to be valid.

Comment:

The "60 day rule" is in addition to other deadlines in the statute. Under § 542.058, once all items are received pursuant to § 542.055 (i.e., from the insured), the insurer has 60 days to pay the claim (if it is valid). This could mean that within this time period, the insurer must evaluate the items received from the insured, secure any items needed from any third party, make and communicate a claims decision to the insured, and pay the claim.

Comment:

Even if the claim is not paid within 60 days of receiving all items under § 542.055, an insurer will arguably not violate the statute if it complies with the remainder of §§ 542.056 and 542.057. In other words, once all items are received from the insured, if the insurer requests a 45 day extension within one business day, makes a claims decision before the 45 day extension period expires, and then pays the claim within five days after the claims decision has been made, this should comply with the statute. Even though this is more than 60 calendar days, it is in compliance with the other deadlines. The language "except as otherwise provided" in the 60 day provision may allow this result. As currently worded, however, an insurer can violate the "60 day rule" even though it satisfies the "45 day rule."

TXPG-INS § 17:22

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:23. Duties imposed on insurer—Pay claim within five days after notice of acceptance

Section 542.057(a) requires payment by the fifth business day after the claim is accepted; surplus lines insurers have 20 business days. § 542.057(c).

One court has held that oral notice that the insurer intends to pay the claim is not sufficient. Daugherty v. American Motorists Ins. Co., 974 S.W.2d 796 (Tex. App.—Houston [14th Dist.] 1998, no pet.)

The *Daugherty* court also held that an insurer can withdraw its "notice of acceptance" and prevent the "five day payment rule" from triggering.

Example:

In Daugherty v. American Motorists Ins. Co., 974 S.W.2d 796 (Tex. App.—Houston [14th Dist.] 1998, no pet.), the insured's car was stolen. He claimed a loss of $68,000 as the anticipated cost of a replacement vehicle. The insurer responded by offering to pay about $62,000. The adjuster communicated this offer to the insured's bookkeeper. Before the insurer made the payment, and before the insured learned about the offer, the car was recovered. The insurer then revoked its offer and instead offered to pay only $1,900, which was the estimated cost of repair. The insured bought the replacement vehicle, which wound up costing about as much as the insurer had originally offered. The insured argued that the insurer notified him it would pay the claim when it made the original offer and that the insurer therefore had to pay within five days after the notification. The court rejected the insured's argument, and agreed that the insurer's communication was merely an offer, one that was rescinded before the insured accepted. Daugherty v. American Motorists Ins. Co., 974 S.W.2d 796, 798 to 799 (Tex. App.—Houston [14th Dist.] 1998, no pet.) In *Daugherty*, the court held: "We find nothing in the Insurance Code or the policy at issue which prevents the insurer from withdrawing its notice of payment if the facts and circumstances known to the insurer change significantly after the notice is given but before the claim is paid." Daugherty v. American Motorists Ins. Co., 974 S.W.2d 796, 799 (Tex. App.—Houston [14th Dist.] 1998, no pet.)

Comment:

The wording of this section does provide an additional argument to assist with the interpretation of the statute. Arguably, because the Legislature used the term "pay," a distinction can be made between "claim" and "coverage." In other words, under this section the duty to pay is conditioned upon the time when the "insurer notifies the claimant that the insurer will pay a claim]" Because payment is not conditioned upon acceptance of the claim, it may be permissible to argue that coverage must be determined within 15 business days, but a claim

does not need to be adjudicated until final proof of loss has been "secured."

TXPG-INS § 17:23

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:24. Duties imposed on insurer—Statutory requirement versus contract provisions

The statutory deadlines imposed by the statute are incorporated into most policies that are subject to the statute. Thus, a failure to meet the deadlines is both a violation of the statute, and a breach of the express terms of the contract. Sometimes, however, the policies do not incorporate the exact language. In Mid-Century Ins. Co. v. Barclay, 880 S.W.2d 807 (Tex. App.—Austin 1994, writ denied), the policy predated the effective date of the statute, so the notice requirement in the policy was different. The court concluded that the insured gave sufficient notice of his claim when he promptly notified the insurer of "how, when and where the accident or loss happened," as required by the policy. Because the policy did not require that notice be in writing, his telephone call was sufficient. Mid-Century Ins. Co. v. Barclay, 880 S.W.2d 807, 810 (Tex. App.—Austin 1994, writ denied).

In Daugherty v. American Motorists Ins. Co., 974 S.W.2d 796 (Tex. App.—Houston [14th Dist.] 1998, no pet.), the insurance policy incorporated the statutory language, including the deadlines for payment and acknowledgment of the claim. However, the policy did not require written notice of the claim. Daugherty v. American Motorists Ins. Co., 974 S.W.2d 796, 798 n. 3 (Tex. App.—Houston [14th Dist.] 1998, no pet.) The court concluded that the filing requirements of both the contract and the statute were satisfied when the insured notified the agent of the loss and later filed an affidavit. The court pointed out that the insurer acknowledged this notice and proceeded to investigate the claim.

TXPG-INS § 17:24

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:25. Duties imposed on insurer—Multiple claims

If the insured files multiple claims, the insurer must comply with the statutory deadlines for each claim. Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467 (Tex. App.—Tyler 1999, pet. denied).

Example:

In Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467 (Tex. App.—Tyler 1999, pet. denied), the insured filed claims for personal injury protection benefits, and underinsured motorist benefits. The court held that the insurer had to comply with the statutory requirements and deadlines for each claim. The court reasoned that these were two of five separate coverages offered by the automobile policy, and "each coverage has its own distinct insuring agreement, exclusion, limited liability, and other provisions applicable to that kind of coverage." Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 473 (Tex. App.—Tyler 1999, pet. denied). Complying with the statute for one claim did not show compliance for the other claim.

Comment:

A single demand for different types of coverage could still be treated as a single claim in some instances. For example, a homeowner might seek benefits for damages to the house as well as the cost of debris removal, all in one claim. *Dunn* appears correct based on the types of coverage at issue, but other types of coverage might lead to a different result.

TXPG-INS § 17:25

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:26. Actionable conduct—In general

An insurer that fails to comply with any of these statutory requirements faces liability for an 18% per annum damages, in addition to the amount of the claim, and attorney's fees. *Tex. Ins. Code Ann. § 542.060(a).*

Example:

Various violations were found in Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467 (Tex. App.—Tyler 1999, pet. denied). The insurer failed to properly document its acknowledgment. Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 471 (Tex. App.—Tyler 1999, pet. denied). The insurer failed to acknowledge in writing the claimant's second claim. The insurer also failed to record the date and means of its acknowledgement of the second claim. Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 472 (Tex. App.—Tyler 1999, pet. denied).

TXPG-INS § 17:26

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
V. Duties Imposed on Insurers—Actionable Conduct

Summary References

§ 17:27. Actionable conduct—Failure to pay claim within 60 days after receiving information

A particularly strict deadline for insurers is the requirement in § 542.058(a) that the insurer pay a valid claim within 60 days after receiving all required items requested from the claimant. This means that if the insurer ultimately loses on the coverage issue and has to pay the claim, then it necessarily has violated the 60 day payment provision and is subject to the 18% damage and attorney's fee provisions of the statute. This is true even if the delay on the part of the insurer was in good faith.

In Higginbotham v. State Farm Mut. Auto. Ins. Co., 103 F.3d 456 (5th Cir. 1997), the court held that by rejecting the claim, the insurer necessarily failed to pay within 60 days, in violation of the statute. As the court put it:

> A wrongful rejection of a claim may be considered a delay in payment for purposes of the 60 day rule and statutory damages. More specifically, if an insurer fails to pay a claim, it runs the risk of incurring this 18% statutory fee and reasonable attorneys' fees. In sum, State Farm took a risk when it chose to reject Higginbotham's claim. State Farm lost when it was found liable for breach of contract. Therefore, it must pay this 18% per annum interest and reasonable attorney's fees.

Higginbotham v. State Farm Mut. Auto. Ins. Co., 103 F.3d 456, 461 (5th Cir. 1997). Other courts have adopted this reasoning as well. See Protective Life Ins. Co. v. Russell, 119 S.W.3d 274, 286 (Tex.App—Tyler 2003 pet. denied); Oram v. State Farm Lloyds, 977 S.W.2d 163, 167 (Tex. App.—Austin 1998, no pet.); Teate v. Mutual Life Ins. Co., 965 F. Supp. 891, 893 (E.D. Tex. 1997).

TXPG-INS § 17:27

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VI. Remedies & Penalties

Summary

Research References

West's Key Number Digest

West's Key Number Digest, Insurance 3540, 3541, 3584, 3585

Legal Encyclopedias

Tex. Jur. 3d, Insurance Contracts and Coverage §§ 1034 to 1036, 1170 to 1194

Treatises and Practice Aids

West's Texas Practice Series: Consumer Rights & Remedies § 5.16

Forms

Texas Jur Pleading and Practice Forms (2d ed.), Insurance § 144:10

TXPG-INS CH 17 VI REF

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VI. Remedies & Penalties

Summary References

§ 17:28. Penalty for violation—18% damages

West's Key Number Digest

West's Key Number Digest, Insurance 3540

The statute provides for 18% per annum damages, in addition to the amount of the claim, and attorney's fees. Section 542.060 provides: (1) if an insurer that is liable for a claim under an insurance policy is not in compliance with this subchapter, the insurer is liable to pay the holder of the policy or the beneficiary making the claim under the policy, in addition to the amount of the claim, interest on the amount of the claim at the rate of 18 percent a year as damages, together with reasonable attorney's fees; and (2) if a suit is filed, the attorney's fees shall be taxed as part of the costs in the case.

Tex. Ins. Code Ann. § 542.058. Various decisions refer to the 18% as "statutory interest" or a "penalty," but the statute refers to it as "damages."

These damages are recoverable whenever the insurer fails to comply with any of the requirements of the statute. Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 472 (Tex. App.—Tyler 1999, pet. denied); Mid-Century Ins. Co. v. Barclay, 880 S.W.2d 807, 811 to 812 (Tex. App.—Austin 1994, writ denied).

Several courts have held that an insurer that denies a claim and is found liable necessarily violates the section that requires payment within 60 days after the insurer receives necessary information. See Oram v. State Farm Lloyds, 977 S.W.2d 163, 167 (Tex. App.—Austin 1998, no pet.); Higginbotham v. State Farm Mut. Auto. Ins. Co., 103 F.3d 456, 461 (5th Cir. 1997); Teate v. Mutual Life Ins. Co., 965 F. Supp. 891, 893 (E.D. Tex. 1997). As one court explained, "As long as the insurer is found to be liable under the policy, this fee attaches, even if the insurer had a reasonable basis for denying coverage." St. Paul Reinsurance Co., Ltd. v. Greenberg, 134 F.3d 1250, 1255 n. 21 (5th Cir. 1998).

Comment:

The Fifth Circuit decision in Higginbotham v. State Farm Mut. Auto. Ins. Co., 103 F.3d 456, 461 (5th Cir. 1997), is significant because it construed the statute as imposing as a "strict liability" for failing to pay a valid claim. Under *Higginbotham*, if the insurer is found at trial to have breached the contract, the 18% penalty under this statute can be awarded even if the insurer complied with all the other deadlines. Some insurers view this as an inaccurate construction of the statute. Insurers argue the statute only imposes penalties for delay in accepting

or rejecting a claim. They point out that the statute does not mention the imposition of the 18% penalty merely because the insurer is subsequently determined by a jury to have made a wrong decision on the claim. Insurers argue that wrong claim decisions are remedied by contractual damage awards, prejudgment interest, attorney's fees, and extra-contractual damage claims (i.e., violations of chapter 541, DTPA, bad faith, etc.). Insureds argue that *Higginbotham* is based on the plain language of the statute. Additional discussion of this issue may be found at § 17:27.

TXPG-INS § 17:28

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VI. Remedies & Penalties

Summary References

§ 17:29. Damage—Calculation method—18% per annum

West's Key Number Digest

West's Key Number Digest, Insurance 3584

The 18% penalty is calculated in the same manner as simple interest and should not be compounded annually. *Tex. Ins. Code Ann. § 542.060(a)*; Cater v. United Servs. Auto. Ass'n, 27 S.W.3d 81, 85 (Tex. App.—San Antonio 2000 pet. denied); Teate v. Mutual Life Ins. Co., 965 F. Supp. 891, 893 to 894 (E.D. Tex. 1997).

TXPG-INS § 17:29

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VI. Remedies & Penalties

Summary References

§ 17:30. Damage—Calculation method—Accrual date

The statute does not say when the penalty accrues. One approach would be to begin accruing the 18% damages from the date the claim was received. This focuses on the length of time the claimant has been without his or her money, instead of focusing on the length of the time the insurer has been in error. This approach encourages prompt payment of claims. As the claim proceeds toward payment, the insurer's incentive to pay the claim would increase. Any error, even at the last stage, would accrue damages of 18%, retroactive to the date the claim was filed. This approach has the benefit of making payment of the claim more important to the insurer, even as the passage of time makes payment of the claim more important to the insured.

Another approach is to begin the 18% damages accruing at the time of the violation. An insurer that errs later pays less. Those who err early pay more. In Teate v. Mutual Life Ins. Co., 965 F. Supp. 891, 894 (E.D. Tex. 1997), the court started the 18% damages accruing on the date of the insurer's violation. In that case, the violation was the insurer's failure to pay within 60 days after receiving proof of the claim.

A rather odd method was employed in Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 473 to 474 (Tex. App.—Tyler 1999, pet. denied), where the court of appeals started the accrual of the 18% damages 180 days after the insurer received notice of the claim. The court apparently did this by analogy to the prejudgment interest statute. Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 478 (Tex. App.—Tyler 1999, pet. denied). Other than establishing a parallel between the prejudgment interest statute and this statute, this approach has little to recommend itself. Nothing in the statute supports it.

TXPG-INS § 17:30

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VI. Remedies & Penalties

Summary References

§ 17:31. Damage—Calculation method—End date

The statute also does not say when the penalty stops accruing. No court has addressed this specific issue. Several courts have simply held that the penalty accrues from the date of the violation up to the date of judgment, without any analysis for choosing that end date. See Republic Underwriters Ins. Co. v. Mex-Tex, Inc., 150 S.W.3d 423, 427-28 (Tex. 2004); Texas Farmers Ins. Co. v. Cameron, 24 S.W.3d 386, 400 (Tex. App.–Dallas 2000, pet. denied); Oram v. State Farm Lloyds, 977 S.W.2d 163, 169 (Tex. App.–Austin 1998, no pet.); Mid-Century Ins. Co. v. Barclay, 880 S.W.2d 807, 813 (Tex. App.–Austin 1994, pet denied). Other courts have held that the penalty accrues until the insurer settled. See Cater v. United Services Automobile Ass'n, 27 S.W.3d 81, 85 (Tex. App.–San Antonio 2000, pet. denied); Southland Lloyd's Ins. Co. v. Tomberlain, 919 S.W.2d 822, 830 (Tex. App.–Texarkana 1996, pet. denied). One approach is to end the accrual of the 18% damages on the day of the judgment. Then the entire award would bear post-judgment interest. This is the approach taken in Mid-Century Ins. Co. v. Barclay, 880 S.W.2d 807, 813 (Tex. App.—Austin 1994, writ denied). The statute neither embraces nor rejects this approach.

Another approach would be to continue accruing the 18% damages until the insurer fully discharges its liability, including payment of the 18% damages and attorney's fees. An argument for this approach is that, presumably, the Legislature intended the 18% damages partially to compensate claimants for the delay and partially to punish insurers for violations. If the 18% damages accrue only up to the time of judgment, this would mean that while the insurer was contesting liability, perhaps even in good faith and reasonably, these extra damages would accrue, but once the claim is finally established, the incentive to pay would be removed. Arguably, it makes no sense to compensate the claimant when his claim is disputed, but once it is certain to no longer compensate him. Likewise, it makes no sense to punish the insurer for withholding a disputed claim, but to no longer punish it for withholding an established claim. The *Higginbotham* line of cases construing the statute recognizes that the insurer denies the claim at its risk. If the insurer gambles and loses, it pays these additional damages. Similarly, if the insurer wants to gamble on continuing to contest the claim once judgment has been rendered, that choice may bear financial consequences. Interestingly, in Cater v. United Services Automobile Ass'n, 27 S.W.3d 81, 85 (Tex. App.—San Antonio 2000, pet. denied), the court ended the penalty on the date the claim was paid, to shorten the time period, presumably as a reward or encouragement for the insurer to pay the claim. Conversely, the penalty should be extended when the insurer continues to refuse to pay, especially after judgment is rendered.

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VI. Remedies & Penalties

Summary References

§ 17:32. Damage—Calculation method—Amount of claim subject to 18% rate/Partial payments

The statute awards "interest on the amount of the claim at the rate of 18 percent a year as damages]" *Tex. Ins. Code § 542.060(a)*. But the statute does not say which amount. Is it the amount of the claim submitted by the claimant, or is it the amount of the claim paid by the insurer, or is it the amount of the claim as ultimately determined by the trier of fact? This matters, because the insured may "claim" too much, the "claim" paid by the insurer may be too small, and often no one knows the amount the notice of the "claim" is first given.

The Supreme Court answered this in Republic Underwriters Ins. Co. v. Mex-Tex, Inc., 150 S.W.3d 423, 426 (Tex. 2004). The court concluded that the "claim" is "the amount ultimately determined to be owed, which of course would be net of any partial payments made prior to that determination." Republic Underwriters Ins. Co. v. Mex-Tex, Inc., 150 S.W.3d 423, 426 (Tex. 2004). The court felt this would encourage insurers to pay the undisputed portion of a claim early, which was consistent with the statute's purpose to obtain prompt payment of claims. Republic Underwriters Ins. Co. v. Mex-Tex, Inc., 150 S.W.3d 423, 426 (Tex. 2004).

The court also held that the 18 percent would be assessed on the entire amount of the claim in the insurer's tender of partial payment was not unconditional. Otherwise, the court reasoned, the insurer could delay payment by insisting on a release to which it was not entitled. *Id.*

TXPG-INS § 17:32

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VI. Remedies & Penalties

Summary References

§ 17:33. Damage—Trebling

One court has directly addressed the issue of whether the 18% damages are subject to trebling, and it did so in a rather odd fashion. In Bekins Moving & Storage Co. v. Williams, 947 S.W.2d 568, 583 (Tex. App.—Texarkana 1997, no pet.), the court held that the damages recoverable under Article 21.55 could not be trebled under Article 21.21 unless the act was also listed as an unfair act or practice by a statute or rule of the Texas Department of Insurance.

The flaw in the court's analysis is that a violation of Article 21.55 was a violation of a rule of the Texas Department of Insurance, and was actionable as a violation of Article 21.21, prior to 1995. See Vail v. Texas Farm Bur. Mut. Ins. Co., 754 S.W.2d 129, 134 (Tex. 1988) (recognizing that prohibitions in rules were actionable under Article 21.21); *28 Tex. Admin. Code § 21.203(18)* (rule making it an unfair practice to violate the predecessor Article 21.55). The court's rationale was wrong, but there is another reason the result may be right.

The current statute, § 541.152(b), allows recovery of actual damages caused by the unfair practice and then allows trebling of those damages if the conduct was committed "knowingly." The same facts might establish a violation of chapter 542 and a violation of chapter 541, but one is not a per se violation of the other. Therefore, a plaintiff would have to show actual damages caused by the unfair insurance practice. It is unlikely that the 18% award could be shown to be damages caused by the unfair insurance practice. The violation does not cause the 18% damages; it just causes the insurer to be liable for those damages. Thus, it seems unlikely the 18% damages ever would be subject to trebling.

Comment:

Deciding the nature of the 18% award is significant in determining whether it can be trebled. The answer to this question may depend on whether the 18% is viewed as "damages," "interest," or a "penalty":

(1) The original statute called the 18% "damages." Republic Underwriters Ins. Co. v. Mex-Tex, Inc., 150 S.W.3d 423, 426 (Tex. 2004) (quoting *Tex. Ins. Code Ann. art. 21.55, § 6*);

(2) Several courts have called the 18% a "penalty." See State Farm Fire & Cas. Co. v. Gandy, 925 S.W.2d 696, 714 (Tex. 1996); Maryland Ins. Co. v. Head Indus. Coatings & Serv., Inc., 938 S.W.2d 27, 29 (Tex. 1996); Oram v. State Farm Lloyds, 977 S.W.2d 163, 167 (Tex. App.—Austin 1998, no pet.); Bekins Moving & Storage Co. v. Williams, 947 S.W.2d 568, 583 (Tex. App.—Texarkana 1997, no pet.); St. Paul Reinsurance Co., Ltd. v. Greenberg, 134 F.3d 1250, 1254 (5th Cir. 1998); Higginbotham v. State Farm Mut. Auto. Ins. Co., 103 F.3d 456, 461 (5th Cir. 1997); Teate v. Mutual Life Ins. Co., 965

F. Supp. 891, 893 (E.D. Tex. 1997).

(3) Other times the courts, sometimes the same courts, call the 18% "damages" or "statutory damages." See Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 471 (Tex. App.—Tyler 1999, pet. denied); Bekins Moving & Storage Co. v. Williams, 947 S.W.2d 568, 581, 584 (Tex. App.—Texarkana 1997, no pet.); Mid-Century Ins. Co. v. Barclay, 880 S.W.2d 807, 813 (Tex. App.—Austin 1994, writ denied); *Higginbotham*.

(4) Sometimes the 18% is referred to as "interest." Bekins Moving & Storage Co. v. Williams, 947 S.W.2d 568, 583 (Tex. App.—Texarkana 1997, no pet.); Oram v. State Farm Lloyds, 977 S.W.2d 163, 167 (Tex. App.—Austin 1998, no pet.). Inexplicably, in the nonsubstantive recodification to Tex. Ins. Code § 542.060(a) the word “interest” was inserted.

(5) Also, the 18% has been called a "statutory fee." Higginbotham v. State Farm Mut. Auto. Ins. Co., 103 F.3d 456, 460 to 461 (5th Cir. 1997); Oram v. State Farm Lloyds, 977 S.W.2d 163 (Tex. App.—Austin 1998, no pet.).

(6) Finally, the 18% has been referred to as "sanctions." Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 474 (Tex. App.—Tyler 1999, pet. denied).

It is not clear what the Legislature intended in calling the 18% "damages." If the award really is "damages" as the statute says, it may be subject to trebling. If the award is a "penalty," then trebling it would seem improper and would constitute double recovery. If the award is interest, the Supreme Court has already said interest is not subject to trebling. St. Paul Surplus Lines Ins. Co. v. Dal-Worth Tank Co., 974 S.W.2d 51, 54 to 55 (Tex. 1998) (per curiam).

Practice Tip:

This issue, while perhaps interesting academically, may not have much practical impact. Treble damages under § 541.152(b) for unfair insurance practices are discretionary. Thus, a litigant simply asks the jury to award an amount of additional damages, and the trial court imposes the upward limit of three times the actual damages. See *Tex. Ins. Code Ann. § 542.152(b)*. If the jury awards a large amount of additional damages, it may be desirable for the plaintiff to try to include the 18% damages under § 542.060(a) as damages subject to trebling, in order to increase the amount subject to trebling and preserve the jury's award. If the jury does not award an amount that exceeds three times the other damages, the issue is moot.

TXPG-INS § 17:33

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VI. Remedies & Penalties

Summary References

§ 17:34. Damage—Subject to prejudgment interest?

Courts have split on the issue of whether the 18 % award is subject to prejudgment interest.

Some courts do not analyze the issue; they simple deny prejudgment interest. See Marineau v. General American Life Ins. Co., 898 S.W.2d 397, 405-406 (Tex. App.–Fort Worth 1995, writ denied); Teate v. Mutual Life Ins. Co. of New York, 965 F. Supp. 891, 894 (E.D. Tex. 1997).

The cases that consider the issue and decline to award prejudgment interest do so based on their reasoning that the 18% award is punitive in nature. The courts then reason that because punitive damages are inherently penal they should not be enlarged by the imposition of pre-judgment interest. See Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 478-79 (Tex. App.–Tyler 1999, writ denied); Texas Farmers Ins. Co. v. Cameron, 24 S.W.3d 386, 399 (Tex. App.–Dallas 2000, pet. denied); J.C. Penney Life Ins. Co. v. Heinrich, 32 S.W.3d 280, 289 (Tex. App.–San Antonio 2000, pet denied).

On the other hand, in a case supporting the award of prejudgment interest on the 18% percent, the court considered the 18% to be an element of actual damages, subject to prejudgment interest like other elements of actual damages. Bekins Moving & Storage Co. v. Williams, 947 S.W.2d 568, 584-85 (Tex. App.–Texarkana 1997, no writ.)

The courts thus seem to have determined that the availability of pre-judgment interest depends on whether the 18% award is considered punitive or remedial.

The statute does not expressly say whether the 18 % is a penalty or compensation. No clear legislative history has been found, either.

As a practical matter, the statute has both effects. To encourage prompt payment of claims, it certainly has the effect of motivating an insurer by imposing a penalty. On the other hand, the whole reason to encourage prompt payment of claims is to make sure that insureds are compensated.

A respected commentator has recognized just this point. Statutes that impose penalties for denying or delaying payment of a claim are penal as to insurers and compensatory as to insureds. 14 Lee R. Russ & Thomas F. Segalla, 2 Couch on Insurance (3d ed.) §§ 204:57, 204:61, 204:62. As the Couch treatise explains, “Statutes imposing penalties on an insurer for its failure to meet its obligation on a contract of insurance have been described as ‘penal’ and ‘highly penal’ in character.” § 204:61 (footnotes omitted). Couch also notes:

> In contrast to jurisdictions which view a statutory penalty as punitive in nature, other jurisdictions regard such a statute as merely compensatory rather than penal. Thus, it has been said that damages allowed by statute for failure to comply with the contract of payment serve as compensation for the cost of collecting the debt. Otherwise stated, the penalty statutes, although penal in character insofar as the insurer is concerned, are compensatory with respect to the insured, the purpose being to create a cause of action in the insured in order to save him or her the amount of expense necessary to collect upon a policy, payment of which has been vexatiously refused, so that there will be no diminution of the recovery actually to be received.

§ 204:62 (footnotes omitted). Thus, the nature of the eighteen percent damages depends on the perspective. From the insurer's perspective it may seem penal; while from the insured's perspective it seems compensatory.

Another commentator makes the same point that such damages serve compensatory purposes. Prof. Robert Keeton recognizes that the threat of statutory relief may serve as a deterrent to irresponsible rejection of claims. Robert E. Keeton & Alan I. Widiss, *Keeton and Widiss' Basic Text on Insurance Law*, § 6.37.7(c), 870. The authors detail the compensatory purposes of such awards as follows:

> Second, imposing legislatively prescribed remedies whenever an insurer unsuccessfully contests a claim, even though the insurer acts reasonably in doing so, serves to compensate the insured for both the delay in the receipt of payment and the costs of engaging in the controversy with the insurer in order to recover (which in some circumstances are substantial). A denial of an insurance claim typically has several consequences for an insured. First, any time there is a denial of an insurance claim, that action obviously extends the period during which the insured must incur the adverse economic consequences of the loss without the benefit of being indemnified by the insurance. Second, an insured who is forced to litigate to recover insurance incurs legal expenses—which include, but are not limited to the fees charged by an attorney—to secure the insurance payments. Third, many insureds also sustain a variety of consequential problems, including harm to credit standing and loss of business. When an insured is compelled to resort to litigation to recover insurance benefits, the insured is denied indemnification for what, at least in many instances, is a very significant aspect of the economic risks incident to the hazards against which the insured sought protection when the insurance was purchased. Thus, when the payment of insurance benefits is only made after an insured has sought the assistance of an attorney and the legal process, the insured not only sustains added legal expenses but also is denied the right to prompt indemnification (which is one of the risks insureds seek to avoid through the acquisition of insurance). Third, most insureds have reasonable expectations that the net value to them of their insurance coverage, in the event of a loss, will not be reduced by a recalcitrant insurer. If, because the insurer is found to have acted reasonably in rejecting the claim, an insured's recovery is limited to an award of the amount of insurance benefits due, the amount provided by the insurance coverage—after the insurance recovery is reduced by the insured's payment of the lawyer's fee and other litigation expenses—is obviously diminished. The net amount actually received by such a claimant is then insufficient to indemnify the insured, often falling far short of that which the insured reasonably anticipated would be available as an insurance benefit to offset the economic loss that resulted as a consequence of the insured event. In such instances, it is surely a defensible legislative choice to determine that a layperson's reasonable view of insurance benefits should be protected by allowing the insured to recover full indemnification whenever an insured is compelled to resort to a lawsuit in order to recover the insurance benefits—that is, to receive a total recovery from the insurer that provides net to the insured no less than the insurance benefits the claimant reasonably anticipated would be paid in the event of a loss. Keeton & Widiss §

> 7.7 (c), 871. Professors Keeton and Widiss conclude:This is another situation in which contradictory canons of statutory construction potentially apply to a question of legislative interpretation: on the one hand, the canon of "strict" construction of "penal" statutes, and on the other hand, the canon of "liberal" construction to effectuate the apparent legislative purpose of protecting victims of wrongful denial of insurance benefits. Keeton & Widiss § 7.7 (c), 872–873. As these commentators recognize, damages under a statute like *Tex. Ins. Code Ann. § 542.060(a)* also serve to compensate.
>
> The statutory provisions establishing remedies for the late payment or nonpayment of insurance claims are often regarded, and sometimes are characterized by the legislation specifically, as penalties. Consequently, it is not surprising that some courts have adopted the view that because such legislation is "penal in nature," the provisions should be subject to strict construction. However, such awards may also appropriately be viewed as allowing an insured to recover compensation for consequential damages the claimant sustained (1) by having to pay an attorney (as well as other litigation expenses) to secure the insurance benefits and (2) by not having the use of the insurance benefits from the time when the insurance should have been paid. Even when such a statute provides for an additional recovery of an amount that is calculated as a percentage of the insurance benefit that was due to the insured, in many instances such an amount does not fully indemnify the claimants for all of the adverse consequences that have resulted from the insurer's wrongful denial of an insured's claim. Accordingly, in most circumstances, there is considerable justification for not according such statutory provisions a "strict" construction.

When an insurer withholds insurance benefits, it deprive the insured of those benefits. Arguably, that deprivation merits some form of compensation. When the insurer forces the insured to litigate to recover money that is due under the contract, it imposes additional expenses and aggravation on the insured. Those are elements the legislature reasonably could find deserve compensation.

Characterizing the 18% damages as penal in nature, while not entirely wrong, is not entirely correct either. Thus, simply applying the label does not provide a sufficient basis for deciding the question.

The reasoning of the decisions in *Cameron* and *Heinrich* is flawed for other reasons. Both courts reasoned that the eighteen percent damages must be exemplary damages, and not actual damages, because the award is made without reference to any harm suffered by the insured. Texas Farmers Ins. Co. v. Cameron, 24 S.W.3d 386, 400 (Tex. App.–Dallas 2000, pet. denied); J.C. Penney Life Ins. Co. v. Heinrich, 32 S.W.3d 280, 289 (Tex. App.–San Antonio 2000, pet denied). First, it is not clear at all that the legislature provided this relief without regard to the harm suffered by insureds. As the respected authorities quoted above point out, harm to the insured is a very important consideration. Absent legislative history either way, or express statutory language either way, these two courts simply assume the grant of the remedy was made without reference to harm suffered by the insured.

Second, the awards necessarily are made with reference to the harm suffered. An insured suffers harm in the amount of the benefits withheld. The 18% damages increases and decreases in direct proportion to that harm. The decisions are wrong, because the 18% is multiplied exactly by the "amount of harm" to the insured.

Third, the awards were also made without reference to any need to punish the insurer and without reference to its culpability. So, this supports the opposite conclusion. Since the award is made without reference to the need to punish the insurer, the damages must be actual damages. Because either proposition is equally plausible

under the statute, this provides no basis for deciding the issue.

As a number of courts have held, the damages are awarded despite the insurer's good faith. See Higginbotham v. State Farm Mutual Automobile Ins. Co., 103 F.3d 456, 461 (5th Cir. 1997). If the damages are awarded without regard to the insurer's good faith, or lack of good faith, how can they really be intended to punish? While they may have that effect, that is not a sufficient basis to characterize the award as punitive and hence outside the scope of prejudgment interest.

In contrast, another statute—section 541.152(b)—provides for additional damages if the insurer acted knowingly. See *Tex. Ins. Code Ann. § 541.152(b)*. At common law, punitive damages are available if the insurer's conduct was intentional, malicious, fraudulent, or grossly negligent. See Transportation Ins. Co. v. Moriel, 978 S.W.2d 10, 17 (Tex. 1994).

The damages awarded under the prompt payment statute are awarded simply for a failure to comply with a deadline. They are not based on any level of malfeasance by the insurer. Again, referring to the Couch treatise the authors make the following point:

> When the statute is silent on the matter, the determination of what kind of conduct of the insurer comes within the scope of the penalty statutes depends basically upon whether the statue is viewed as punitive or as compensatory. Where it is the latter, the only conduct of the insurer required is of the negative character that the insurer did not pay, and therefore, was sued by the insured, and successfully. Where, however, the statute is viewed as punitive as is generally the case, there must be some misconduct of the insurer to justify the imposition of the penalty. In general terms, these statutes apply to any improper conduct of the insurer with respect to delay in making payment, refusing to make payment, or stopping the making of payments.
>
> 2 Couch on Insurance (3d ed.) § 204:112.

With this analysis, the Texas prompt payment statute would fall within the "compensatory" group because the only conduct required of the insurer is the failure to pay or to timely process the claim, not other misconduct.

There is a final reason that the 18% award may be viewed as compensatory. Having stated that the issue is whether the 18% damages are penal or compensatory, for purposes of deciding whether or apply pre-judgment interest, the courts have overlooked one very clear and simple principle. There are two equally well-established rules of statutory construction. One is that penal statutes are strictly construed. See, e.g., Brown v. De la Cruz, 156 S.W.3d 560, 565 (Tex. 2004). The other is that if a statute is remedial, it is given a liberal construction. See, e.g., Burch v. City of San Antonio, 518 S.W.2d 540, 544 (Tex. 1975).

The legislature has provided the answer under the prompt payment statute. The statue is to be "liberally construed" as expressly stated in section eight. Therefore, the statute must be remedial, not penal.

There is one anomaly that confounds the analysis of whether the 18% is penal or remedial and thus subject to prejudgment interest or not. As originally enacted, section 6 or Article 21.55 simply referred to the award as "damages." In 2003, the statute underwent a "nonsubstantive" recodification. Effective April 1, 2005, article 21.55, section 6 was recodified as section 542.060. See 2003 *Tex. Sess. Law Serv. Ch. 1274 (H.B. 2922)*. Despite the nonsubstantive nature of this renumbering, the scriveners inserted the word "interest."

A court looking only at the current language could conclude that the 18% is itself interest and thus cannot

be subject to even more prejudgment interest. Unless that conclusion would be correct under the old language, it would be error for a court to reach that conclusion based on a nonsubstantive change.

TXPG-INS § 17:34

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VI. Remedies & Penalties

Summary References

§ 17:35. Damage—Effect of multiple violations

No case has yet decided whether multiple violations result in multiple penalties. In Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 471 to 472 (Tex. App.—Tyler 1999, pet. denied), the court found four separate violations by the insurer, but did not discuss whether this made a difference in the damages.

Comment:

Arguably, an insurer that violates the statute more than once ought to be more liable than an insurer that violates the statute only once. This view is consistent with liberal construction of the statute, and furthers the purpose of encouraging prompt payment of claims.

For example, if an insurer that fails to timely acknowledge the claim is just as liable as an insurer that violates every requirement, what incentive does the first insurer have to get on the right path and begin processing the claim properly? Arguably, if the penalty is as much for a single violation as for several, insurers may have no incentive for compliance with the remaining deadlines, once one violation occurs. Imposing multiple penalties for multiple violations cures this. An insurer that commits one violation has an incentive to be careful not to commit other violations.

TXPG-INS § 17:35

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VI. Remedies & Penalties

Summary References

§ 17:36. Attorney's fees

West's Key Number Digest

West's Key Number Digest, Insurance 3585

Attorney's fees under the statute are governed by the decision in Arthur Andersen & Co. v. Perry Equipment Corp., 945 S.W.2d 812, 817 to 818 (Tex. 1997). The court held that a reasonable fee must be based on the eight factors set out by the disciplinary rules. Fees cannot be awarded simply as a percentage of the recovery, but must be awarded as a dollar amount. The jury can consider the fact that the plaintiff has agreed to a contingent fee as one factor in deciding what fee is reasonable. See also Dunn v. Southern Farm Bur. Cas. Ins. Co., 991 S.W.2d 467, 474 to 475 (Tex. App.—Tyler 1999, pet. denied).

In light of Arthur Anderson, earlier cases allowing recovery of a percentage fee under the statute are no longer good law. See Mid-Century Ins. Co. v. Barclay, 880 S.W.2d 807, 812 (Tex. App.—Austin 1994, writ denied); Teate v. Mutual Life Ins. Co., 965 F. Supp. 891, 894 (E.D. Tex. 1997).

If fees can be segregated between the statutory claim and other claims, it is proper to do so, but the defendant needs to object. Otherwise an unsegregated award will be upheld. Allstate Ins. Co. v. Lincoln, 976 S.W.2d 873, 876 (Tex. App.—Waco 1998, no pet.).

TXPG-INS § 17:36

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VI. Remedies & Penalties

Summary References

§ 17:37. Cumulative remedy

West's Key Number Digest

West's Key Number Digest, Insurance 3541

The provisions of the statute are not exclusive, and the remedies are in addition to any other remedies or procedures provided by any other law or at common law. *Tex. Ins. Code Ann. § 542.061*; see also Bekins Moving & Storage Co. v. Williams, 947 S.W.2d 568, 582 (Tex. App.—Texarkana 1997, no pet.)

Comment:

Despite the cumulative remedy language of this provision, several courts have held that the statute does not create a separate cause of action. One federal court has explained:

> [A] claim for statutory penalties under Article 21.55 for failure to pay a claim under an insurance policy is not a separate cause of action. Instead, when an insured brings such a claim, the insurer's entire liability—both on the insurance policy and under Article 21.55—is put on issue as one cause of action.

Hartman v. St. Paul Fire & Marine Ins. Co., 55 F. Supp. 2d 600, 604 (N.D. Tex. 1998).

TXPG-INS § 17:37

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VII. Defenses

Summary

Research References

West's Key Number Digest

West's Key Number Digest, Insurance 3554

Legal Encyclopedias

Tex. Jur. 3d, Insurance Contracts and Coverage §§ 1016 to 1033

Treatises and Practice Aids

West's Texas Practice Series: Consumer Rights & Remedies § 5.16

TXPG-INS CH 17 VII REF

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VII. Defenses

Summary References

§ 17:38. Defenses—In general

West's Key Number Digest

West's Key Number Digest, Insurance 3554

The statute has several provisions that can be considered defenses:

(1) The defendant may be exempt. *Tex. Ins. Code Ann. § 542.053*. These exemptions are discussed above in § 17:10;

(2) There are preemption defenses, which are discussed above in § 17:10;

(3) There are defenses that deadlines were extended. These are also discussed below in § 17:39; and

(4) It is a defense to liability under § 542.060(a), based on the insurer's failure to pay within 60 days after receiving all necessary information, if the insurer proves through litigation or arbitration that it does not really owe the claim. *Tex. Ins. Code Ann. § 542.060(b)*. See §§ 17:42 to 17:43.

TXPG-INS § 17:38

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VII. Defenses

Summary References

§ 17:39. Defenses—Extensions of time

The statute contains several provisions by which insurers may extend the deadlines. While, technically, these are not "defenses," they may help insurers avoid liability. The following events or conditions can extend the deadlines:

(1) **Surplus lines insurers:** Being an eligible surplus lines insurer extends the deadlines for acknowledging receipt of the claim, commencing the investigation, and requesting information, from 15 days to 30 business days. *Tex. Ins. Code Ann. § 542.055(a)*;

(2) Also, being a surplus lines insurer extends the deadline for paying a claim from five business days to 20 business days after the insurer notifies the claimant that the claim will be paid, or after the claimant performs any condition imposed on payment of the claim. *Tex. Ins. Code Ann. § 542.057(c)*;

(3) **Request for information from claimant:** Waiting for information reasonably requested from the claimant effectively extends any additional deadlines until the insurer receives that information. *Tex. Ins. Code Ann. § 542.056(a)*;

(4) Making additional requests for information likewise extends the deadlines until that information is received, assuming those requests were timely. *Tex. Ins. Code Ann. §§ 542.055(b), 542.056(a)*;

(5) **Arson:** If the insurer reasonably suspects arson, that extends the deadline for accepting or rejecting the claim from 15 business days to 30 days after the insurer receives required information. *Tex. Ins. Code Ann. § 542.056(b)*. Because of the use of "days" and "business days" this gives the insurer one more week in arson cases;

(6) **Inability to accept or reject claim:** If the insurer cannot accept or reject the claim by the initial deadline, the insurer may notify the insured, and explain the reasons why the insurer needs additional time, and then the insurer has 45 more days to accept or reject the claim. *Tex. Ins. Code Ann. § 542.056(d)*;

(7) **Longer deadline in another statute:** Insurers may have more than 60 days to pay a claim after they receive all requested information, if some other statute provides for a longer period. *Tex. Ins. Code Ann. § 542.058(a)*;

(8) **Condition to be performed by claimant:** If the insurer agrees to pay the claim, the deadline for pay-

ment may be extended if the insurer conditions payment on the performance of some act by the claimant. In that case, the payment deadline is extended until five business days after the act is performed, or 20 business days for surplus lines insurers. §§ 542.057(b), (c);

(9) **Court extension:** A guaranty association may request an extension from the court. § 542.059(a); and

(10) **Catastrophe:** In the event of a weather-related catastrophe or major natural disaster, as defined by the State Board of Insurance (now the Texas Department of Insurance), the claim handling deadlines are extended for an additional 15 days. *Tex. Ins. Code Ann. § 542.059(b)*.

TXPG-INS § 17:39

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VII. Defenses

Summary References

§ 17:40. Defenses—Extensions of time—Insurer unable to accept or reject claim by deadline

If the insurer cannot accept or reject the claim by the initial deadline, the statute lets the insurer notify the claimant that it cannot accept or reject a claim by the deadline. *Tex. Ins. Code Ann. § 542.056(d)*. This notification has to be sent before the original deadline, and the notice must state the reason why the insurer needs additional time. The insurer then has 45 additional days to accept or reject the claim.

TXPG-INS § 17:40

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VII. Defenses

Summary References

§ 17:41. Good faith is not a defense

The insurer's good faith—or its lack of bad faith—is no defense. Higginbotham v. State Farm Mut. Auto. Ins. Co., 103 F.3d 456, 461 (5th Cir. 1997). In reaching this conclusion, the court noted that precedents under the predecessor statute, Article 3.62, held that an insurance company's good faith in denying a claim did not relieve the insurer of liability for penalties. The court concluded that an insurer that denies a claim takes the risk that it will have to pay the additional damages allowed by the statute.

TXPG-INS § 17:41

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VII. Defenses

Summary References

§ 17:42. Nonliability for claim as defense to violation of 60 day payment provision

The statute identifies one instance where the insurer may prove it does not owe the claim and thereby avoid liability under the statute for failing to comply with a deadline.

Except as otherwise provided, if an insurer, after receiving all items, statements, and forms reasonably requested and required under Section 542.055, delays payment of the claim for a period exceeding the period specified by other applicable statutes or, if other statutes do not specify a period, for more than 60 days, the insurer shall pay damages and other items as provided by Section 542.060.

Comment:

Section 542.058(a) requires the insurer to pay within 60 days after receiving all items requested from the claimant. If the insurer does not really owe the claim, and can prove it through litigation or arbitration, how can the insurer be faulted for not paying the claim after it received the necessary materials?

TXPG-INS § 17:42

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VII. Defenses

Summary References

§ 17:43. Nonliability for claim as defense to violation of other provisions

The statute does not provide that an insurer may avoid liability for any of the other violations by ultimately proving it does not owe the claim. Arguably, then, an insurer that violates one of these other provisions may still be liable under the statute, even if the insurer proves it does not owe the claim.

This issue was partially addressed by the Supreme Court in Allstate Ins. Co. v. Bonner, 51 S.W.3d 289 (Tex. 2001). The insurer acknowledged an uninsured/underinsured motorist benefit claim late. The insured was then awarded damages less than the personal injury protection benefits the insurer had already paid, so the insurer was not liable for UM benefits. Nevertheless, Bonner argued that Allstate's violation entitled her to recover attorney's fees under the statute.

The Supreme Court rejected this argument and held that for an insurer to be held liable under the statute, a party must establish three elements:
(1) a claim under an insurance policy;
(2) that the insurer is liable for the claim; and
(3) that the insurer has failed to follow one or more sections of the statute with respect to the claim.

Allstate Ins. Co. v. Bonner, 51 S.W.3d 289, 291 (Tex. 2001). The court based this holding on the language of that provides an 18% penalty and attorney's fees "[i]n all cases where a claim is made pursuant to a policy of insurance and the insurer liable therefor is not in compliance that the requirements of this article." The court concluded that Bonner failed to satisfy the second element, because she could not show the insurer was liable for the claim.

In light of the *Bonner* holding, it is not clear whether defeating the insured's claim will always avoid liability for violating the statute, or whether the court's decision may be limited. There are many arguments for making an insurer that violates the statute liable for the claim. There are arguments the other way, as well. Because the *Bonner* court did not address these arguments, it was not certain under *Bonner* to what extent the debate had been resolved. See also Wellisch v. United Services Automobile Ass'n, 75 S.W.3d 53, 55 to 56 (Tex. App.—San Antonio 2000, pet. denied); Menix v. Allstate Indem. Co., 83 S.W.3d 877, 2002 WL 1726938 (Tex. App.—Eastland 2002, no pet. h.); Lundstrom v. United Services Auto. Ass'n-CIC, 192 S.W.3d 78, 97-98 (Tex. App.—Houston [14th Dist.] 2006, pet. denied) (holding that an insurer that was not liable under a homeowner's policy for mold damage also was not liable for failing to meet the deadlines imposed by the prompt payment of the claims statute).

These cases provide ammunition for both sides in the debate over whether an insurer should be found liable for Chapter 542 penalties should a claim which is initially rejected be later determined to be a valid claim which the insured is legally obligated to pay. According to the decisions in *Menix* and *Wellisch*, these penalties should not apply to any UIM claim that is initially disputed and rejected, if after a judicial determination renders the insurer liable for the claim, the insurer pays it promptly under the statute. These decisions, of course, can be easily limited to the fact that all involve only UIM claims under UIM policies with very specific language in the applicable policies of which the courts took careful note. One could argue that different rules should apply to non-UIM claims. Nevertheless, there is broad language in these decisions that suggests that a broader principle is at play, that insurers have a right to dispute a claim, and such language could be easily cited to argue that no disputed claim of any sort need be paid until a judicial determination has been made as to the insurer's liability to pay it and that penalties shouldn't apply if the claim is paid promptly after the judicial determination. Indeed, the distinction the court made in *Wellisch* between UIM claims, which need only be paid pursuant to a judicial determination that they must be paid, and those non-UIM claims that an insurer must pay in the event of an occurrence of a covered event under the policy, is not altogether convincing. For instance, one might consider that, in many instances, once a covered event occurs under a non-UIM policy, a valid defense can in many cases be interposed that an insurer could argue negates a legal obligation to pay the claim until there is a judicial determination of whether that obligation exists. Indeed, it is determining such legal obligations which is at the heart of these cases, and courts could easily construe them against the insured in the non-UIM benefits context just as it did in the UIM benefits context and hold the penalties do not apply to insurers whose claims do not meet the deadlines when that claim is initially disputed and a judicial determination of the liability for that claim is made. Such a result could very well encourage insurers, in many circumstances, to dispute and deny claims that they might otherwise pay if courts were to hold them liable for penalties for claims disputed and not paid and later found to be claims the payments for which the insurers are legally liable.

The fact that the statute makes proof of nonliability a defense in one instance but not others raises a question about the insurer's liability for a violation of one of the other provisions when the insurer ultimately proves it does not owe the claim.

Claimants may argue that an insurer that violates a deadline—other than the 60 day payment deadline—loses the ability to contest coverage for the claim. Insurers oppose this argument. Several arguments can be offered for each position.

First, on the claimant's side, the fact that the Legislature specifically addressed this issue arguably should control. The Legislature was aware of the issue whether an insurer should be able to avoid liability by proving it did not really owe the claim. The Legislature addressed this in § 542.058(b), and concluded that an insurer can prove non-liability on a claim to avoid statutory liability only under § 542.058(a)—the 60 day payment provision. This should mean that an insurer that can prove through litigation or arbitration that it does not owe the claim does not escape liability under the other sections.

Second, unless the insurer is held liable for both the amount of the claim, and the 18% penalty, there is no penalty. What would the 18% apply to? To give effect to the language that says the insurer is liable for the 18%, in addition to the amount of the claim, the insurer must be liable for both. Unless the insurer's violation means it has to pay the claim, there is no claim amount to which the 18% would apply.

Third, allowing an insurer to prove it really does not owe the claim, even after it has violated the statute, would undermine the statute. An insurer could ignore the duties to acknowledge the claim, commence the in-

vestigation, request items from an insured, and accept or reject the claim—as long as it could ultimately show it did not owe. This could give an insurer an economic incentive simply to ignore claims. For any claimant persistent enough to pursue the matter and litigate the claim, the insurer could then devote all its resources to disproving liability through litigation. Fighting a small subset of all claims, and losing a portion of those, could be much cheaper for the insurer than complying with the statute by promptly and properly handling all claims. To avoid this result, the statute arguably must be construed to mean that an insurer that violates the statute is precluded from contesting coverage. The Legislature could not have intended that an insurer could lay back, disprove liability at the eleventh hour, and thereby ignore all the deadlines with impunity.

Fourth, this construction is consistent with the purpose of the statute. The statute is to be liberally construed to promote its underlying purpose to promote prompt payment of claims. Facing a penalty of losing the right to contest coverage is certainly a great incentive for the insurer to remain focused on meeting the deadlines.

Fifth, this construction is consistent with the plain language of the statute. Section 542.060(a) provides:

> To successfully maintain a claim for the insurer's violation of settlement duties concerning first-party claims, a party must establish three elements: (1) a claim under an insurance policy; (2) the insurer's liability for the claim; and (3) the insurer's failure to follow one or more sections of the claims settlement statute with respect to the claim. V.A.T.S. Insurance Code, art. 21.55, § 6.

Tex. Ins. Code Ann. § 542.060(a) (emphasis added). The statute says that an insurer in violation is liable for the 18% "in addition to the amount of the claim." Necessarily, then, the insurer must be liable for the claim. In other words, a violation of the statute renders the insurer liable for both the amount of the claim and the 18%.

Sixth, a party that breaches its contract cannot demand compliance by the other party. These statutory deadlines are incorporated into many of the standard policies. A statutory violation is also a breach of contract. Therefore, an insurer that violates the statute should lose the right to assert any contractual defense or exclusion.

Seventh, the exemption for guaranty associations provides indirect support. Section 542.053(a)(6) says that a guaranty association is not subject to the damage provisions. Section 542.059(a) also says that a guaranty association may receive an extension of the time periods in the statute from a court, by showing good cause. Why would a guaranty association need an extension of time, when it is immune from the 18% penalty? There must be some other consequence for failing to meet the deadlines—perhaps forfeiture of the right to contest the claim.

There are arguments on the other side. One argument is based on the language of § 542.060. Insurers focus on the words referring to "an insurer that is liaable for a claim" to assert that the insurer has to be liable for the claim, first, before it can be liable "in addition" for the 18%.

Another argument that could be made is based on the definition of "claim," which refers to a claim that “must be paid by the insurer directly to the insured or beneficiary." *Tex. Ins. Code Ann. § 542.051(2)(B)*. It could be argued that a claim subject to liability for the 18% damages must be a claim that "must be paid by the insurer." Hence, if the insurer is not required to pay the claim, it is not a "claim" within the meaning of the statute.

This argument proves too much. If a "claim" is only one that must be paid by the insurer, that means the insurer would not have any obligation to acknowledge a "claim" or commence an investigation of a "claim" or re-

quest items to determine any "claim" that ultimately was not owed. The problem is, how would the insurer know? The insurer cannot know whether it owes a claim unless and until it acknowledges it and investigates. But if "claim" only means those the insurer owes, the process would never start. "Claim" has to include all demands submitted to the insurer—those that ultimately prove valid, and those that do not.

An insurer must timely accept or reject a "claim." *Tex. Ins. Code Ann. § 542.056(a)*. The word "claim" must encompass good ones and bad ones. The Legislature set deadlines for rejecting invalid claims, just as much as for accepting valid claims. Obviously, without a prompt and proper investigation, there is no way to tell to which category the claim belongs. These initial duties, to acknowledge, investigate, and accept or reject, apply to valid and invalid claims. A failure to comply must have consequences. It would make no sense to let an insurer ignore the deadlines and then escape responsibility by asserting that it did not owe the claim anyway. If the insurer wants to assert that it does not owe the claim, the statute imposes a timeline for that. If the insurer does not comply, arguably it should lose the right to deny the claim.

It makes more sense to assume that the phrase "must be paid by the insurer" is intended to designate claims that have to be paid to the insured or beneficiary, instead of claims that have to be paid to someone else.

A final concern is based on public policy. The argument over whether the insurer is barred from litigating coverage only matters when the insurer otherwise could disprove its liability. If the insurer is liable anyway, there is no need to rely on the statutory violation to preclude the issue. If the insurer really owes the claim, it will necessarily violate the 60 day payment provision in § 542.058(a). This issue preclusion argument matters only if the insurer doesn't otherwise "really" owe the claim. For example, this might come up after the insurer violated the statute, then denied the claim, but later discovered evidence that justified the denial.

This leads to a concern that some undeserving insured—for example, an arsonist—might reap a windfall from a minor blunder by the insurer. Perhaps courts could engraft a public policy exception and allow the insurer to contest coverage if the insured has engaged in criminal or fraudulent conduct that causes the loss. The same equitable concerns do not arise when other defenses, such as late notice, are precluded.

TXPG-INS § 17:43

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VIII. Other Issues

Summary

Research References

West's Key Number Digest

West's Key Number Digest, Insurance 3558

Treatises and Practice Aids

West's Texas Practice Series: Consumer Rights & Remedies § 5.16

TXPG-INS CH 17 VIII REF

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VIII. Other Issues

Summary References

§ 17:44. Insurer's need for information from third parties

If the insurer reasonably requests information from the claimant, deadlines are postponed until the insurer receives that information. See § 17:15.

In contrast, the statute does not expressly extend any deadlines while the insurer awaits information from third parties. However, if the insurer cannot accept or reject a claim because it is still waiting for such information, § 542.056(d) allows the insurer a one-time, 45 day extension.

Comment:

This 45 day extension may not provide the insurer sufficient time, for example, for an engineer to complete an inspection, conduct necessary studies, and write a report. The statute does not give insurers an answer to this dilemma, other than to deny the claim, at the risk of incurring the 60 day penalty, or pay the claim, based on an incomplete investigation.

On the other hand, insurers are normally in a better position to speed the claim investigation process than are insureds. In many cases, the statutory time limits will be sufficient. In those instances where an insurer must accept or reject a claim without sufficient time to receive all information, arguably, the statute is a legislative choice to put the risk of delay on the insurer, instead of the insured.

TXPG-INS § 17:44

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VIII. Other Issues

Summary References

§ 17:45. Insurer's unreasonable request for information

The statute allows the insurer to request information it reasonably believes will be required. Deadlines are then postponed while the insurer waits for this information from the claimant. An unreasonable request by the insurer would not postpone any deadlines and thus could lead the insurer to violate the statute by failing to meet a deadline. See Colonial Mut. Ins. Co. v. Valdez, 30 S.W.3d 514, 522 to 523 (Tex.App.—Corpus Christi 2000, no pet.)

TXPG-INS § 17:45

END OF DOCUMENT

Texas Practice Guide: Insurance Litigation
Database updated October 2008
Mark L. Kincaid and Christopher W. Martin

Chapter 17. Prompt Payment of Claims Statute
VIII. Other Issues

Summary References

§ 17:46. Amount in controversy for federal court jurisdiction

West's Key Number Digest

West's Key Number Digest, Insurance 3558

The amount of damages imposed by the statute should be included in calculating the "amount in controversy" for federal diversity jurisdiction purposes. St. Paul Reinsurance Co., Ltd. v. Greenberg, 134 F.3d 1250, 1252 to 1253 (5th Cir. 1998).

TXPG-INS § 17:46

END OF DOCUMENT