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TEXAS SUPREME COURT UPHOLDS COMMON-LAW INTENT-TO-DECEIVE RULE FOR MISREPRESENTATIONS IN INSURANCE APPLICATIONS

The Supreme Court of Texas recently held that Section 705.051 of the Texas Insurance Code does not displace the common-law intent-to-deceive rule because the statute prescribes necessary, not exclusive or sufficient, conditions for denying recovery under a contestable policy. In American National Ins. Co. v. Bertha Arce, No. 21-0843, 2023 WL 3134718 (Tex. 2023), American National Insurance Company ("ANIC") issued a life insurance policy to Sergio Arce. Thirteen days later, Sergio died from injuries sustained in an automobile accident. Sergio's mother, Bertha, submitted a claim under the policy as his designated beneficiary. However, ANIC denied the claim and refunded the premium because Sergio's medical records indicated he had incorrectly answered "no" to an application question inquiring about certain prior medical diagnoses. Consequently, Bertha sued ANIC for policy benefits and other extra-contractual claims.

The century-old Texas common-law rule regarding misrepresentations in insurance applications is that insurers cannot avoid liability under an insurance policy based on a misrepresentation unless, among other things, the insurer pleads and proves that the insured intended to deceive or induce the insurer to issue the policy. On the other hand, Section 705.051 of the Texas Insurance Code, which dates back to 1909, provides that a misrepresentation in an application does not defeat recovery under the policy unless the misrepresentation (1) is of a material fact, and (2) affects the risks assumed (i.e., the statute does not include the intent-to-deceive requirement).

On appeal, ANIC argued that the intent-to-deceive requirement was incompatible with section 705.051's plain language, and an insurer could avoid an obligation to pay on an insurance policy based on an innocent, unknowing, or careless misstatement in an insurance application, so long as the misstatement was of a material fact and either induced the policy's issuance or affected the premium charged. Bertha argued that section 705.051's language did not conflict with the common law and the two have coexisted for more than a hundred years without any substantive modification to the statute.

The Supreme Court of Texas began its analysis by noting that it granted ANIC's petition for review "to resolve an incipient conflict between Texas state cases, which consistently apply the common-law rule, and a handful of federal district court cases that have recently departed from it." The Court then framed the issue as follows: "the issue here is not whether the common law alters the statutory language but whether the Legislature's enacted language expressly or effectively forecloses the common law." The Court held that "section 705.051 is not discordant with the common law, either expressly or by necessary implication." The Court reasoned that "section 705.051 states conditions that are necessary, not sufficient, to defeat recovery."

"Section 705.051 does not guarantee that the insurer can 'defeat recovery under the policy' if both of the stated conditions are satisfied; it only guarantees that recovery cannot be defeated if one or the other is not." "The statute does not inherently or necessarily conflict with settled law requiring pleading and proof of intent to deceive in addition to the statutorily mandated conditions." "In over a hundred years, there has been no indication that the Legislature disagrees with the common-law approach to enforcement of insurance contracts. Adhering to our precedent, we therefore hold that insurers must plead and prove intent to deceive to avoid contractual liability based on a misrepresentation in an application for life insurance, whether the policy is contestable or not. Proof of a material inaccuracy is not enough."

FIDUCIARY DUTY IS NOT CONTRACTUAL, FIFTH CIRCUIT HOLDS

The Fifth Circuit Court of Appeals recently re-examined the scope of a contractual liability exclusion in a liability insurance policy. In Windermere Oaks Water Supply Corp. v. Allied World Specialty Ins. Co., No. 22-50218, 2023 WL 3313593 (5th Cir. May 9, 2023) (slip op.), a municipal utility company sought coverage for a suit a filed against it alleging that it sold a valuable tract of land to a company board member "for pennies on the dollar." The suit alleged violations of the Texas Business Organizations Code, including unauthorized conveyance of property, improper use of the cooperative's assets, improper disbursement of the cooperative's assets to benefit the directors, and failure to recover loss, as well as for common-law breach of fiduciary duty.

The insurer denied the claim, leading to this suit, in which the trial court ordered the insurer to defend. This appeal resulted. The appellate court's summary of its holding was refreshingly simple: "This insurance dispute turns on a simple principle of law: A claim for breach of fiduciary duty is not a claim for breach of contract, and is therefore not subject to exclusion from coverage under a contractual liability exclusion. That's what the district court found here in granting summary judgment in favor of the insured. We

accordingly affirm."

In its analysis, the court was mindful of Ewing Const. Co. v. Amerisure Ins. Co., 420 S.W.3d 30 (Tex. 2014) [link to our summary at https://www.mdjwlaw.com/newsroom-news-TIN-20140121-item1.html], in which the Supreme Court of Texas limited the scope of contractual liability exclusions. Although a contract for the sale of land was the subject of the underlying suit against Windermere, the actual claims asserted against Windermere were not contractual in nature and did not depend on a contractual relationship between Windermere and the plaintiffs. They were the types of claims that grew out of duties imposed by law, not contract, and therefore were beyond the scope of the Contractual Liability exclusion.

FIFTH CIRCUIT AFFIRMS CLASS CERTIFICATION AGAINST GEICO

The Fifth Circuit Court of Appeals recently affirmed a district court's approval of class certification in favor of a group of GEICO policyholders seeking to represent all similarly situated policyholders, claiming GEICO had failed to fully compensate them for the total loss of their vehicles. The plaintiffs alleged GEICO had consistently failed to include title fees, registration fees, and sales tax in its calculation of ACV payments due under the collision or comprehensive coverage to policyholders who had suffered total loss of their vehicles. Among the claims they sought to certify as a class was a claim for violation of Chapter 542 of the Texas Insurance Code, a/k/a the Texas Prompt Payment of Claims Act.

The court concluded the plaintiffs had standing to bring the claims, and all of the types of costs involved amounted to the same legal injury – breach of contract – even though the three types of costs accrue in different ways. The court rejected GEICO's arguments that the damages claimed were too individualized to be susceptible to class certification because recalculating the correct payment for each vehicle would be a fact-intensive process. But Plaintiffs presented simple formulas and tables by which GEICO's previous value determinations could be adjusted for most class members.

The Fifth Circuit also agreed with the lower court's inclusion of Chapter 542/TPPCA claims in the class certification, noting it is a strict liability statute, and if the actual damages of the class members could be easily calculated, so too could the interest due under Chapter 542.

APPEALS COURT UPHOLDS DISMISSAL OF INSURED'S LAWSUIT AGAINST INSURER IN COVERAGE DISPUTE

An appeals court in San Antonio recently ruled in favor of an insurer and upheld the dismissal of an insured's claims in a coverage dispute. Jones v. Allstate Vehicle and Property Ins. Co., NO. 04-22-00010-CV, 2023 WL 3733917 (Tex. App.—San Antonio May 31, 2023) involved claims for breach of contract and unfair settlement practices against an insurer when the insurer concluded the insured's roof did not sustain covered damage, and it refused to pay for the roof's replacement.

After a hailstorm hit his property, the insured filed a property damage claim with his insurer. The insurer then inspected the house and issued an estimate for the damages it considered covered under the policy. The insured, who was also an attorney, requested a second inspection. The insurer again inspected the property and issued an additional payment. The insured, dissatisfied with the insurer's position, filed suit against the insurer for breach of contract and violations of the Texas Insurance Code.

During the jury trial, the insured and his wife testified that the storm was severe, and the hail was large, but they did not observe water leakage in their roof after the storm. The insured's expert adjuster further opined that the storm damaged the roof and parts of the house and that it would cost over $45,000 to repair the property. The insured also only produced one photograph of the damage to his house.

The jury returned a verdict in favor of the insurer, a take-nothing judgment was entered, and the insured appealed—claiming that he had conclusively established his breach of contract claim and that the jury's rejection of his claims was factually insufficient.

Because the jury charge did not define the term "loss," the court applied its commonly understood meaning: "the state or fact of being destroyed or placed beyond recovery." With that in mind, the court reviewed the record. Although the court held that the record conclusively established that a storm hit the insured's home in April 2016, there was no evidence that the insured's roof and siding was "destroyed or placed beyond recovery" solely by the storm in excess of the insurer's damage estimate.

The Court further held that the insured's expert did not explain how the storm destroyed or placed the roof or siding beyond recovery and made conclusory statements that the entire roof and other items needed to be completely replaced. Consequently, the Court held that the insured failed to conclusively establish the elements for breach of contract and the elements of his bad faith claim. As the court noted, "the jury may have determined that [the insurer's] second inspection and supplemental payment constituted a 'reasonable investigation.'" As such, the Court upheld the jury's verdict and the trial court's judgment.

COURT OF APPEALS CONCLUDES THAT SURPLUS LINES INSURERS ARE "INSURERS" FOR PURPOSES OF CHAPTER 4001 OF THE TEXAS INSURANCE CODE

The Fort Worth Court of Appeals recently concluded that surplus lines insurers are "insurers" for purposes of Chapter 4001 of the Texas Insurance Code which regulates licensure and activities of agents and other persons engaged in the business of insurance in Texas. In HOF Partners LLC v. Nautilus Ins. Co., No. 02-22-00175-CV, 2023 WL 3114309 (Tex. App-Fort Worth, April 27, 2023, mem. op.), HOF Partners LLC ("HOF"), through its retail agent Summit Insurance Group, LLC ("Summit"), obtained property and casualty insurance from Nautilus Insurance Company ("Nautilus") for HOF's commercial building. Under the parties' agency billing plan, Summit was responsible for collecting the premiums from HOF and transmitting them to Nautilus via its broker. However, although HOF timely made its premium payments to Summit, Summit failed to forward them to Nautilus, who then, unbeknownst to HOF, canceled the policy and, based upon this cancellation, subsequently refused to cover a loss claimed by HOF. Consequently, HOF filed suit.

On appeal, the issue was whether the statutory-agency provision of Section 4001.052 of the Texas Insurance Code applies to surplus lines insurers such as Nautilus (which if answered in the affirmative could characterize HOF's premium payments to Summit as payments to Nautilus and, thus, no proper cancellation of the policy). Section 4001.052 provides that a person who solicits an application for property or casualty insurance is considered the agent of the insurer issuing a policy on the application and not the agent of the insured in any controversy between the insurer and the insured. Nautilus argued that Section 4001.052 did not apply to surplus lines carriers such as itself because "insurer" is defined as "an insurance company or insurance carrier regulated by the department", and Nautilus, as a surplus lines insurer, was purportedly not regulated by the Texas Department of Insurance.

The Court of Appeals concluded that surplus lines insurers are "regulated" by the Department of Insurance and, thus, surplus lines insurers are "insurers" for purposes of Chapter 4001 of the Texas Insurance Code. The Court reasoned that the common and ordinary meaning of "regulated" was to be subject to rules or restrictions. "Accordingly, an entity that is subject to rules or restrictions promulgated or executed by a government agency is 'regulated' by that agency, and because surplus lines insurers are subject to certain rules and restrictions set forth in the Insurance Code and the Department is tasked with enforcing these rules and restrictions, surplus lines insurers are "regulated by the Department."

Nautilus argued that even if Chapter 4001 applied to surplus lines insurers, Summit did not qualify as Nautilus' agent because there was no evidence that Nautilus communicated with Summit or HOF regarding the policy. The Court remanded this issue to the trial court, concluding that the parties' agency billing plan was sufficient to create a genuine issue of material fact regarding whether Summit had actual or apparent authority to collect the premiums on Nautilus' behalf.

FEDERAL COURT DISMISSES HOMEOWNER'S CLAIMS IN COVERAGE DISPUTE INVOLVING FORCED-PLACED INSURANCE POLICY

A federal court in Houston recently granted an insurer's motion for summary judgment and dismissed claims by a homeowner that arose from a dispute over whether the insurer underpaid a claim made by the homeowner's lender under a "forced-placed" insurance policy. Peter Garcia v. Great American Assurance Co., Civil Action No. H-23-0090, 2023 WL 3262061 (S.D. Tex.—Houston May 4, 2023).

When the homeowner purchased his property, he did not purchase homeowner's insurance, so his lender purchased a "force-placed" policy for the property covering its interest as mortgagee and passed the cost of the policy to the homeowner through the mortgage payments. The homeowner was not a party to the policy and all payments for loss were to be made to the lender.

After the 2021 winter storm hit Texas, the property was damaged. The lender submitted a claim under the policy, and the insurer paid some damages. The homeowner did not believe the amount paid by the insurer was adequate, so he filed suit against the insurer and alleged breach of contract, bad faith, violations of the Texas Insurance Code and Texas Deceptive Trade Practices Act, fraud, and civil conspiracy. The insurer then removed the case to federal court and filed a motion for summary judgment, arguing that the homeowner was not a party to the policy and not a "third-party beneficiary," so the homeowner could not recover under any of the theories of liability he alleged.

The Court reviewed the language of the policy and found that it did not provide coverage for the interest or equity of the [homeowner] and that the homeowner was not a named insured under the policy. Although the homeowner argued that he was a third-party beneficiary because he lived in the home and paid the premiums, the Court concluded that neither of those factors, standing alone, supporting a finding of third-party beneficiary status because they do not indicate anything about the contracting parties' (i.e., the lender's and the insurer's) intent to confer any such status on the homeowner. Consequently, the Court ruled that the homeowner's breach of contract claim failed as a matter of law.

In turn, the Court summarily dismissed the homeowner's bad faith claim (because the homeowner provided no evidence that the insurer owed a duty of good faith and fair dealing to someone who was not a party to the policy or a third-party beneficiary), as well as the homeowner's claims for violations of the Texas Insurance Code (because the Code requires a plaintiff to be either a named insured or a third-party beneficiary) and the Texas Deceptive Trade Practices Act (because the homeowner was not a "consumer" under the Act due to not being the party who sought and acquired the insurer's services). The Court also dismissed the homeowner's claims for fraud and civil conspiracy because he failed to cite any evidence to support his claims and instead relied on conclusory statements. As a result, the Court granted the insurer's motion for summary judgment and dismissed all of the homeowner's claims against it.