

Court has held that this section does not create a private cause of action.¹⁴⁴

- 8 **BREACH OF THE DUTY OF GOOD FAITH AND FAIR DEALING.** Ever since the 1997 decision in the *Giles* case, when the Texas Supreme Court re-shaped the common law standard for establishing a carrier's bad faith by adopting the statutory standard, there has been more consistency and predictability in the judicial cases looking at the conduct required of a carrier to avoid bad faith. In *Giles*, the Court linked bad faith to the statutory prohibition against unfair claim settlement practices, specifically, "failing to attempt in good faith to effectuate a prompt, fair, and equitable settlement of a claim with respect to which the insurer's liability has become reasonably clear."¹⁴⁵ **In Texas, the tort cause of action for breach of the duty of good faith and fair dealing is now established when an insurer has no reasonable basis for denying or delaying payment of a claim, and the insurer knew or should have known that fact.**¹⁴⁶ Evidence that merely shows a bona fide dispute about the insurer's liability on the contract does not rise to the level of bad faith.¹⁴⁷ Bad faith is also not established if the evidence shows the insurer was merely incorrect about the factual basis for its denial of the claim, or about the proper construction of the policy.¹⁴⁸ When the underlying claim upon which an insured's bad faith or extra-contractual claims are premised is found to have been properly denied, the extra-contractual claims such as bad faith also necessarily fail.¹⁴⁹ That is, an insured cannot prevail on a bad faith or other extra-contractual claim without first proving that the insurer breached the insurance contract.¹⁵⁰ When an insurer proves it had a reasonable basis for denying a claim, even if the finder eventually determines that basis to be erroneous, that insurer is not subject to bad faith liability or liability under the Texas Insurance Code and the Texas Deceptive Trade Practices Act.¹⁵¹ Whether an insurer acted in bad faith because it denied or delayed payment of a claim after its liability became reasonably clear is a question for the fact-finder.¹⁵² The duty of good faith and fair dealing as to a particular claim ends when judgment has been rendered on the claim.¹⁵³ For example, when the insured obtains a judgment against the insurer on a claim, there is no longer a duty of good faith because the relationship of the parties at that point in time is that of

¹⁴⁴ *Universe Life Ins. Co. v. Giles*, 950 S.W.2d 48, 69 (Tex.1997); *Allstate Ins. Co. v. Watson*, 876 S.W.2d 145, 148-49 (Tex.1994); see also *American Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842, 847 n. 11 (Tex.1994) (Article 21.21-2 is "subject to enforcement only by the State Board of Insurance.").

¹⁴⁵ TEX. INS CODE ANN. § 541.060(a)(2)(A).

¹⁴⁶ *Universe Life Ins. Co. v. Giles*, 950 S.W.2d 48, 56 (Tex.1997) (citing *Aranda v. Insurance Co. of N. Am.*, 748 S.W.2d 210, 213 (Tex.1988)); *Betco Scaffolds Co. v. Houston United Cas. Ins. Co.*, 29 S.W.3d 341, 348 (Tex.App.--Houston [14th Dist.] 2000, no pet.).

¹⁴⁷ *State Farm Fire & Cas. Co. v. Simmons*, 963 S.W.2d 42, 44 (Tex.1998); *State Farm Lloyds v. Nicolau*, 951 S.W.2d 444, 448; *Transp. Ins. Co. v. Moriel*, 879 S.W.2d 10, 17 (Tex.1994); see also *Giles*, 950 S.W.2d at 54.

¹⁴⁸ *Moriel* at 18.

¹⁴⁹ *Chrysler Ins. Co v. Greenspoint Dodge of Houston, Inc.*, 297 S.W.3d 248, 254-255; *Republic Ins. Co. v. Stoker*, 903 S.W.2d 338, 341 (Tex.1995).

¹⁵⁰ *Id.*

¹⁵¹ *Lyons v. Millers Cas. Ins. Co. of Tex.*, 866 S.W.2d 597, 600 (Tex.1993); *Saunders v. Commonwealth Lloyd's Ins. Co.*, 928 S.W.2d 322, 324 (Tex. App.--San Antonio 1996, no writ).

¹⁵² *Giles*, 950 S.W.2d at 56.

¹⁵³ *Mid-Century Ins. Co. of Texas v. Boyte*, 80 S.W.3d 546, 549 (Tex. 2002).

judgment creditor and judgment debtor and not insurer and insured.¹⁵⁴

- A. **Failure to Investigate.** An insurer may also breach its duty of good faith and fair dealing when it fails to reasonably investigate a claim in order to determine whether its liability is reasonably clear.¹⁵⁵ An insurer will not escape liability merely by failing to investigate a claim so that it can contend that liability was never reasonably clear.
- B. **Subsequent Investigations.** Evidence that an insurer preformed subsequent additional assessments of a claimed condition at the request of the insured is not alone evidence of bad faith, even if it results in additional payments being made to the insured.¹⁵⁶
- C. **Use of Experts as Basis for Denial.** Evidence of the insurer's investigation, including the preparation of an objective, expert report, may demonstrate the existence of a reasonable basis for denying a claim.¹⁵⁷ Even a simple disagreement among experts about whether the cause of the loss is one covered by the policy will not alone support a judgment for bad faith.¹⁵⁸ But the mere fact that an insurer relies on an expert's report will not shield the insurer from liability if there is evidence that the insurer's reliance was "merely pretextual,"¹⁵⁹ or if there is evidence that the expert's report was not objectively prepared, or if there is evidence that the insurer's reliance on the report was unreasonable.¹⁶⁰ Such evidence raises concerns that the carrier's investigation was an "outcome-oriented investigation," and in such a case, the Court must consider in detail the circumstances surrounding the carrier's reliance on the expert's report.
 - 1) One piece of evidence that can assist the insured in showing a result oriented investigation is the connection and past history between the carrier and any expert retained by the carrier to give an opinion on a coverage issue. For example, has the expert been used previously by the carrier to deny a claim; has the expert been overused by the carrier? How much business does the carrier give that expert? Other factors that may affect the reasonableness of the carrier's reliance on the expert's report include the reliability of the experts' methodology and investigation. Did the expert conduct an objective investigation to determine causation?
 - 2) These issues are especially prominent in property damage claims, where experts are routinely retained to determine whether the claimed

¹⁵⁴ *Id.*

¹⁵⁵ *Giles*, 950 S.W.2d at 56 n. 5.

¹⁵⁶ *Spicewood Summit Office Condominiums Ass'n., Inc. v. America First Lloyd's Ins. Co.*, 287 S.W.3d 461, 470 (Tex. App. – Austin 2009, pet. denied).

¹⁵⁷ *Lyons*, 866 S.W.2d at 601.

¹⁵⁸ *Id.*

¹⁵⁹ *Nicolau*, 951 S.W.2d at 448.

¹⁶⁰ *Id.*

damage was the result of a covered peril or not. An example of this type of claim is a residential foundation claim. In Texas, the HO-B homeowner's insurance policy has been determined to cover foundation damage caused by an underground plumbing leak.¹⁶¹ Because of the shifting sands in several areas of Texas, foundation movement is not unusual, even without any plumbing leak. Carrier's hire engineers to investigate these claims and determine if an underground plumbing leak caused the claimed foundation damage. Not surprisingly, the carrier-retained engineer frequently opines that the foundation damage was not caused by a covered peril, and the carrier uses that opinion to deny the claim. If the insured decides to challenge the denial of the claim, they usually find an engineer that will say the opposite and attribute the foundation movement to a covered peril such as a plumbing leak. When these claims go to trial, it is the insured that prevails most of the time on the coverage issue, and the insured recovers the costs of repair, attorneys' fees, costs, plus the penalties under §542.060 of the Texas Insurance Code. On some occasions, Plaintiffs even obtain judgments against the carrier for knowing violations of the Insurance Code and DTPA, and recover treble and mental anguish damages.

- 3) **Recommendations.** Carriers should strive to do a thorough and objective investigation of every first party claim. Carriers need to be aware of the use and overuse of experts in the determination of coverage issues. Carriers should not give all of their investigation work to the same engineer, but should actively try to retain multiple independent and competent engineers in a particular area. Insurers need to make sure that their retained engineers and experts have the skill and experience necessary to render an opinion on the matter, and should be suspect of engineers, who routinely provide reports that are not objectively based. If an expert loses his objectivity on claims issues, the expert should not be used.

- D. **Good Faith Duty to Insureds For Third-party Liability Claims.** Courts employ an objective standard to determine whether a reasonable insurer under similar circumstances would have delayed or denied payment of the claim.¹⁶² An insurer will be liable if the insurer knew or should have known that it was reasonably clear that the claim was covered.¹⁶³ In the third-party claim context, liability may not be imposed against an insurer, and an insurer's liability is not reasonably clear unless it is shown that: 1) the policy covers the claim; 2) the insured's liability is reasonably clear; (3) the claimant has made a proper settlement demand within policy limits; and (4) the

¹⁶¹ *Balandran v. Safeco Ins. Co. of America*, 972 S.W.2d 738, 742 (Tex. 1998).

¹⁶² *Aranda v. Ins. Co. of N. Am.*, 748 S.W.2d 210, 213 (Tex.1988); *Vandeventer v. All Am. Life & Cas. Co.*, 101 S.W.3d 703, 722 (Tex. App.-Fort Worth 2003, no pet.).

¹⁶³ *Universe Life Ins. Co. v. Giles*, 950 S.W.2d at 56; *Vandeventer*, 101 S.W.3d at 722.

demand's terms are such that an ordinarily prudent insurer would accept it.¹⁶⁴ In establishing these guidelines for liability in this context, the Texas Supreme Court linked to, and borrowed from, the common law requirements to establish a Stowers claim, which is discussed later in this publication.¹⁶⁵

- 9 **EXTRA-CONTRACTUAL CLAIMS AGAINST THE INSURER.** Over the last decade the Texas Supreme Court has made a concerted effort to level the playing field for insurance carriers in litigation with policy holders. Insurers have always had to contend with anti-insurer bias at the trial court level which often times results in a lopsided judgment for the policy holder awarding extra-contractual damages for what was a simple breach of contract. Recent decisions have made clear that something more than a breach of contract is necessary to recover extra-contractual damages from an insurer. Two Texas Supreme Court decisions mark this trend.
- A. **Where there is no Coverage** - Lack of coverage precludes extra contractual claims, i.e. breach of duty of good faith, insurance code violations.¹⁶⁶ The one possible exception left open by the Court is where an insurer's denial of a claim it was not obliged to pay might nevertheless be in bad faith if its conduct was extreme and produced damages unrelated to and independent of the policy claim.¹⁶⁷ It is unclear from any case just exactly what conduct would fit under this exception, but it has been identified and left open by the Court.
 - B. **Where there is Coverage** – Conduct showing only negligence or breach of contract by insurer is not grounds for extra-contractual damages. Extra-contractual damages are only applicable in cases where the insurer knew its actions were false, deceptive, or unfair.¹⁶⁸
 - C. **No Claim for Negligent Claims Handling.** Texas does not recognize a claim for negligent claims handling.¹⁶⁹ Claims handling liability is based on the contract of insurance, the Texas Insurance Code, and the limited cases establishing a common law duty.
 - D. **No Duty to Notify Additional Insured of Coverage or Defend without a Request for Coverage.** Mere awareness of a claim or suit against an insured does not impose a duty on the insurer to defend the insured and there is no unilateral duty to act unless and until an additional insured first requests a defense.¹⁷⁰ Regardless of whether the insured is ignorant of any rights or obligations under the policy, notice is a threshold duty that the insured must fulfill by notifying the insurer that the insured has been served

¹⁶⁴ *Rocor Int'l Inc. v. Nat'l Union Fire Ins. Co.*, 77 S.W.3d 253, 261, 262 (Tex. 2002).

¹⁶⁵ *Id.*

¹⁶⁶ *Chrysler Ins. Co v. Greenspoint Dodge of Houston, Inc.*, 297 S.W3d 248, 254-255; *Progressive County Mut. Ins. Co. v. Boyd*, 177 S.W.3d 919, 922-923 (Tex. 2005).

¹⁶⁷ *Id.*

¹⁶⁸ *Minnesota Life Ins. Co. v. Vasquez*, 192 S.W.3d 774, 780 (Tex. 2006).

¹⁶⁹ *Northwinds Abatement, Inc. v. Employers Insurance of Wausau*, 258 F.3d 345, 352 (5th Cir. 2001).

¹⁷⁰ *Nat'l Union Fire Ins. Co. of Pittsburgh, P.A. v. Crocker*, 246 S.W.3d 603, 607-608 (Tex. 2008).