

in the future.

- c. *Bodily injury* as that term is used in liability policies does not include purely emotional injuries, and unambiguously requires an injury to the physical structure of the human body.²⁹⁸

- 7) **Recommendations relating to coverage issues.** Insurers should continue to: 1) carefully review all claims that are in any way related to an insured's defective work or service for coverage defenses; 2) for claims involving injury or damage caused by exposure to a condition over a period of time, remember that multiple policy periods may be invoked and that any exposure during your policy period will be an occurrence under the policy; 3) when coverage issues are apparent, timely send out a thorough reservation of rights letter to the insured that addresses all coverage defenses; 4) include in reservation of rights letter notice of any intent to seek reimbursement of defense costs for uncovered claims; 5) advise the insured to put all carriers on notice when dealing with a continuing tort over multiple policy periods; 6) engage and consult coverage counsel when significant claims arise.

- 13 **STOWERS LIABILITY.** *Stowers* is a Texas insurance term which refers to an insurance company's responsibility to an insured when responding to a settlement demand within policy limits. Since the 1929 case of *G.A. Stowers Furniture Co. v. American Indem. Co.*,²⁹⁹ Texas law has required an insurer, when confronted with a claim against an insured and a settlement demand within policy limits, to exercise that degree of care and diligence which an ordinarily prudent person would exercise in the management of that person's own business.³⁰⁰ If an ordinarily prudent person, as viewed from the standpoint of the insured, would have settled the case, but the insurer fails to do so, then the insurer may have liability for damages awarded against the insured, including damages in excess of the policy limits.³⁰¹ Although the *Stowers* concept is easy to understand, the task of analyzing the various *Stowers* issues for potential liability and response often proves difficult. Without a good understanding of the *Stowers* issues, insurers are prone to either overpay claims out of a mistaken fear of potential *Stowers* liability, or make themselves vulnerable to actual *Stowers* liability for failing to appreciate the true risk in a given case. Insurers do not need to leave the risk of *Stowers* liability up to a game of chance as to whether the insured is going to be found liable for damages in excess of policy limits at the underlying liability trial against the insured. A prompt and prudent analysis and response to the *Stowers* demand, can provide effective protection to an insurer even in cases where the *Stowers* demand is not accepted and the subsequent liability trial against the insured results in damages in excess of the policy limits. This section explores *Stowers* liability issues and Appendix G. is a worksheet to guide attorneys and adjusters in conducting a prudent analysis of the *Stowers* demand issues.

²⁹⁸ See *Trinity Universal v. Cowan*, 945 S.W.2d 819, 823 (Tex. 1997).

²⁹⁹ 15 S.W.2d 544, 547 (Tex. Comm'n App. 1929, holding approved).

³⁰⁰ See *American Physicians Ins. Exchange v. Garcia*, 876 S.W.2d 842, 848 (Tex. 1994);

³⁰¹ See *Stowers*, at 547.

A. **The *Stowers* Duty.** Just exactly what the *Stowers* duty entails has expanded and narrowed at different times since its inception.³⁰² The most expansive the duty ever became was after the 1987 Texas Supreme Court decision in the *Guin* case, which extended the insurer's duty to the "full range of the agency relationship," including investigation, preparation for the defense of the lawsuit against the insured, trial of the case, and reasonable attempts to settle.³⁰³ In 1994, the Texas Supreme Court began a subtle process of curtailing the *Guin* decision by re-characterizing *Guin*'s expansive duty language as dicta.³⁰⁴ Under the current *Stowers* duty, an insurer breaches the *Stowers* duty only by negligently failing to settle a claim made against its insured within policy limits.³⁰⁵ However, under the current duty, an insurer has no duty to make or solicit settlement proposals and evidence relating to an insurer's claim investigation, trial defense, and conduct during settlement negotiations is subsidiary to the ultimate *Stowers* issue.³⁰⁶ Some Texas courts refer to this as the duty to accept reasonable settlement offers within policy limits.³⁰⁷ When a carrier breaches this duty, the risk of a judgment in excess of the policy limits is shifted from the insured to the insurer.³⁰⁸ That is, if an insurer fails to honor its *Stowers* duty, and the insured suffers an adverse judgment above the policy limits, then the insurer can be liable for the entire amount of the judgment even if it exceeds policy limits.

- 1) But just because an insurer refuses to pay a *Stowers* demand in a case where damages in excess of the policy limits are subsequently awarded against the insured, does not necessarily mean that the insurer will have liability for the damages in excess of the policy limits. Because a *Stowers* claim is a tort cause of action based on negligence, i.e., a negligent failure to accept a policy-limits settlement demand,³⁰⁹ if the insurer's failure to accept the demand was not negligent, then there will be no liability for any damages in excess of the policy limits. This is the only tort duty an insurer has in the

³⁰² See *Chancey v. New Amsterdam Cas. Co.*, 336 S.W.2d 763, 765 (Tex. Civ. App.—Amarillo 1960, writ ref'd n.r.e.) (duty to settle implies the duty to negotiate because the two duties cannot be separated); *Globe Indem. Co. v. Gen-Aero, Inc.*, 459 S.W.2d 205, 208 (Tex. Civ. App.—San Antonio 1970, writ ref'd n.r.e.) (numerous factors need to be considered in consideration of carrier's negligence including opportunities to settle, failure to carry on negotiations or make counteroffers, and failure to investigate); *Wood Truck Leasing, Inc. v. Amer. Auto Ins. Co.*, 526 S.W.2d 223, 225 (Tex. Civ. App.—San Antonio 1975, no writ) (Stowers liability can be based on negligent investigation).

³⁰³ See *Ranger County Mut. Ins. Co. v. Guin*, 723 S.W.2d 656, 659 (Tex. 1987).

³⁰⁴ See *American Physicians Ins. Exchange v. Garcia*, 876 S.W.2d 842, 848 (Tex. 1994).

³⁰⁵ See *Texas Farmers Ins. Co. v. Soriano*, 881 S.W.2d 312, 314 (Tex. 1994); *Stowers*, 15 S.W.2d at 547-48; see also *In the matter of Segerstrom*, 247 F.3d 218, 228 (5th Cir. 2001).

³⁰⁶ See *American Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842, 849 (Tex. 1994); *Birmingham Fire Ins. v. American Nat'l Fire*, 947 S.W.2d 592, 597 (Tex. App.—Texarkana 1997, writ denied) (insurer has no other duty to undertake actions often required for negotiation, such as making a counteroffer).

³⁰⁷ See *Insurance Corp. of America v. Webster*, 906 S.W.2d 77, 79 (Tex. App.—Houston [1st Dist.] 1995, writ denied).

³⁰⁸ See *id.* at 80; see also *American Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842, 849 (Tex. 1994).

³⁰⁹ See *Stowers* at 547; A *Stowers* claim requires both an insurer's negligent failure to settle, and subsequent harm or legal injury to the insured. *In re Davis*, 253 F.3d 807, 810-811 (5th Cir. 2001).

context of handling a third-party claim against an insured.³¹⁰ When an insurer breaches the *Stowers* duty, an insured has 2 years³¹¹ from the date the judgment in the underlying case becomes final, to assert a *Stowers* claim against the insurer.³¹² In such circumstances, it is not unusual for the insured's *Stowers* claim to be assigned to the prevailing plaintiff in the underlying case in exchange for Plaintiff's covenant not to execute on the judgment against the insured. However, a *Stowers* claim against an insurer belongs to the insured, and a plaintiff in the underlying case against the insured, has no standing to assert a *Stowers* claim absent an valid assignment of the claim from the insured.³¹³

B. When is the *Stowers* Duty Triggered? There are three primary elements to a settlement demand that triggers the *Stowers* duty: (1) the claim against the insured is within the scope of coverage; (2) the demand is within policy limits; and (3) the terms of the demand are such that an ordinarily prudent insurer would accept it, considering the likelihood and degree of the insured's potential exposure to an excess judgment.³¹⁴ Coverage is obviously an initial consideration because an insurer has no duty to settle a claim that is not covered under its policy.³¹⁵ Second, a demand above policy limits, even if reasonable, does not trigger the *Stowers* duty to settle.³¹⁶ Finally, a reasonable settlement is one that a reasonably prudent insurer would accept when considering solely the merits of the claim and the potential liability of its insured on the covered claim.³¹⁷

1) Other considerations may also affect whether the *Stowers* duty is triggered in a particular case. First, in order to trigger the *Stowers* duty, the settlement demand must propose to release the insured fully in exchange for a stated sum of money, but may substitute words such as "policy limits" for the sum certain.³¹⁸ Second, the demand must take into consideration and account for any liens that exist which might prohibit a full release from being obtained if the settlement demand is accepted, such as a hospital lien.³¹⁹ Under Texas

³¹⁰ See *Maryland Insurance Co. v. Head Industrial Coatings and Services, Inc.*, 938 S.W.2d 27, 28 (Tex.1996). Insurers are also subject to the duties of the insurance contract and statutory duties under the Texas Insurance Code.

³¹¹ See *Amer. Centennial Ins. Co. v. Canal Ins. Co.*, 810 S.W.2d 246, 254 (Tex. App.--Houston [1st Dist.],1991, *aff'd in part, rev'd in part on other grounds*, 843 S.W.2d 480 (Tex. 1992).

³¹² See *Street v. Hon. Second Ct. of Apps.*, 756 S.W.2d 299, 301 (Tex. 1988).

³¹³ See *Whatley v. City of Dallas*, 758 S.W.2d 301, 307 (Tex. App.--Dallas 1988, writ denied); *Becker v. Allstate Insurance Company*, 678 S.W.2d 561 (Tex. App.--Houston [14th Dist.] 1984, writ ref'd n.r.e.). Note that an assignment of a *Stowers* claim is invalid if: 1) it is made prior to an adjudication of plaintiff's claim against the insured in a fully adversarial trial; 2) the insurer has tendered a defense; and 3) either (a) the insurer has accepted coverage, or (b) the insurer has made a good faith effort to adjudicate coverage issues prior to the adjudication of plaintiff's claim. See *State Farm Fire & Cas. Co. v. Gandy*, 925 S.W.2d 696, 714 (Tex.1996).

³¹⁴ See *State Farm Lloyds Ins. Co. v. Maldonado*, 963 S.W.2d 38, 41 (Tex. 1998); see also *American Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842, 849 (Tex.1994).

³¹⁵ See *American Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842, 848 (Tex.1994).

³¹⁶ See *Maldonado* at 41.

³¹⁷ See *Soriano* at 316.

³¹⁸ See *Garcia*, 876 S.W.2d at 848-49.

³¹⁹ See *Trinity Universal Ins. Co. v. Bleeker*, 966 S.W.2d 489, 491 (Tex. 1998).

law, when a hospital lien exists, a release is not valid unless: (1) the hospital's charges were paid in full before the execution and delivery of the release; (2) the hospital's charges were paid before the execution and delivery of the release to the extent of any full and true consideration paid to the injured individual by or on behalf of the other parties to the release; or (3) the hospital is a party to the release.³²⁰ In such a case, if the plaintiff's settlement demand does not include consideration for payment of, or settlement of, the hospital lien, then a full release is not being offered, and no *Stowers* duty arises.³²¹ Third, the demand must also be an unconditional offer of settlement, such that it is not conditioned on some other event or occurrence, and gives the insurer a reasonable opportunity to accept the offer.³²² Finally, the insurer must be given a reasonable amount of time to consider and respond to the offer. Exactly how much time is required is an open question, but fourteen days has been held to be an adequate period of time.³²³

- C. **Importance of Resolving Coverage Issues.** Over the last several years, the Texas Supreme Court has made clear that when an insurer is asked to defend an insured against a liability claim, the insurer must either accept coverage or make a good faith effort to resolve coverage before resolution of the Plaintiff's claim against the insured.³²⁴ Because the insurer is in the business of analyzing and allocating risk, the insurer is in the best position to assess the viability of its coverage position. The risk is on the insurer to resolve all coverage issues promptly.³²⁵ Accordingly, in a recent case, the Texas Supreme Court held that absent a specific policy provision or agreement to the contrary, an insurer who had not resolved coverage issues before funding a settlement, cannot later assert a claim against the insured for reimbursement of the settlement monies paid on behalf of the insured.³²⁶ The duty placed on an insurer because of a *Stowers* demand makes the early resolution of coverage issues even more critical. In cases where a *Stowers* demand is possible or anticipated, the insurer usually has an opportunity to resolve coverage issues before actually receiving the demand. Leaving a serious coverage issue unresolved until a *Stowers* demand is received, usually means that it is too late to obtain a judicial determination of the insurer's obligations to the insured before a response is due on the Plaintiff's demand. In such a case, the insurer can only rely on, and at a minimum should have already requested and received, an attorney's written coverage opinion as to whether a particular claim is covered. In cases where significant limits are involved, the failure to resolve coverage issues early, unnecessarily adds another element of uncertainty to an insurer's already complicated task of responding to a

³²⁰ TEX. PROP CODE § 55.007(a).

³²¹ See Bleeker, 966 S.W.2d at 491.

³²² See *Ins. Corp. of America v. Webster*, 906 S.W.2d 77 (Tex. App.–Houston [1st Dist.] 1995, writ denied).

³²³ See *Allstate Ins. V. Kelly*, 680 S.W.2d 595, 608 (Tex. App.–Tyler 1984, writ ref'd n.r.e.).

³²⁴ See *Texas Ass'n. of Counties County Gov't Risk Management Pool v. Matagorda County*, 52 S.W.3d 128, 135 (Tex. 2000); *Farmers Texas County Mut. Ins. Co. v. Griffin*, 955 S.W.2d 81, 84 (Tex.1997); *State Farm Fire & Cas. Co. v. Gandy*, 925 S.W.2d 696, 714 (Tex.1996).

³²⁵ See *Texas Ass'n of Counties County Gov't Risk Management Pool v. Matagorda County* at 135.

³²⁶ See *id.*

Stowers demand. Therefore, anytime an insurer is faced with a potential policy limits case, the best course of action is to identify and resolve all coverage issues as early as possible.

- D. **Determining Policy Limits.** In many cases, the declarations sheet of the applicable insurance policy will indicate the policy limit for an occurrence in question. However, determining policy limits may prove more difficult in several situations, including: (1) when multiple claimants or claims arise from a single occurrence, (2) when claims from a single occurrence are made against multiple insureds under the same policy; (3) when a continuous occurrence invokes multiple policies; or (4) when previous unrelated claims are made under the same policy and policy period. One problem in determining the policy limit is where a single occurrence gives rise to multiple claims. **Texas law permits an insurer, when faced with a settlement demand arising out of multiple claims from the same occurrence and inadequate insurance proceeds, to enter into a reasonable settlement with one of the several claimants, even though such settlement exhausts or diminishes the insurance proceeds available to satisfy other claims.**³²⁷ Accordingly, the amount of available insurance for a subsequent claim arising out of the same occurrence may be reduced or even eliminated by the payment of a prior claim, and likewise, can effect the application of the *Stowers* duty. The same basic rule applies in a multi-insured case, when there are two or more insureds covered by the same policy and who face potential liability for the same incident.³²⁸ In this situation, an insurer can make a reasonable settlement on behalf of one of the insureds, even though such settlement reduces or eliminates coverage for another insured under the same policy.³²⁹ The general rule, therefore, is that each claim against each insured is to be evaluated on its own merits, and if it is reasonable for an insurer to accept a settlement demand, even though it reduces or eliminates coverage for other claimants or other insureds, then the insurer can do so without regard to such other claims.

- 1) Special rules apply to cases which involve a continuous occurrence that triggers multiple consecutive policies. The Texas Supreme Court has determined that consecutive policies covering distinct policy periods, cannot be stacked to multiply coverage for a single claim involving an indivisible injury.³³⁰ Simply because the occurrence of a claim extends throughout several policy periods, does not mean that the per occurrence indemnity cap of every policy period is implicated to satisfy the claim.³³¹ In a situation where a single occurrence triggers multiple policies over multiple policy periods, with differing per occurrence limits, the limit of insurance available to satisfy the claim is whatever limit applied at the single point in time during any of the covered periods under the triggered policies, when the coverage

³²⁷ See Soriano at 315.

³²⁸ See *American States Ins. Co. v. Arnold*, 930 S.W.2d 196, 202-03 (Tex. App.–Dallas 1996, writ denied); *Travelers Indem. Co. v. Citgo Petroleum Corp.*, 166 F.3d 761, 768 (5th Cir. 1999).

³²⁹ See *id.*

³³⁰ See *American Physicians Ins. Exchange v. Garcia*, 876 S.W.2d 842, 853 (Tex. 1994)

³³¹ See *id.*

limit available to the insured was the highest.³³² Once that applicable limit is identified, all insurers whose policies are triggered must allocate funding of the indemnity limit among themselves according to their subrogation rights.³³³ The one Texas appellate court that has considered this issue held that while an insured's indemnity amount may not be calculated by stacking, the allocation of each insurer's percentage of responsibility for the satisfaction of the Plaintiff's claim must be determined by dividing the policy limit of that insurer's policy by the sum of all implicated policies added together.³³⁴ For example, if insurer A has a policy with per occurrence limits of \$1,000,000 for year one, while insurer B has a policy B with per occurrence limits of \$100,000 for year two, the total of the policy limits is \$1,100,000. However, the limits available to satisfy a single continuous occurrence that implicates both policies is only \$1,000,000. Insurer B's percentage responsibility for satisfaction of the claim is determined by taking its policy limit and dividing by the sum of policies (\$100,000 divided by \$1,100,000 = 1/11) to get an overall percentage responsibility of 9% towards satisfaction of the claim.³³⁵

- 2) Finally, in some cases, the aggregate limit of a policy may be applicable. The aggregate limit is the most the carrier is obligated to pay for separate occurrences during one policy period. In cases where the aggregate limit is applicable, depending on what has previously been paid out for unrelated claims, the policy limit for the occurrence at issue may be less than the stated per occurrence limit.

E. **Reasonable Settlement.** Perhaps the most difficult part of analyzing a *Stowers* demand, is determining whether it is reasonable to accept a given settlement demand. This determination must be made by considering solely the merits of the claim and the potential liability of the insured for the claim.³³⁶ Once a *Stowers* demand is received by an insurer, defense counsel should be asked to prepare an evaluation of the case against the insured, which includes opinions on the percentage chance of liability and the possible range of damages for each claim. Provided with this publication is The Texas "*Stowers*" Liability Worksheet which can be used as a guide in evaluating the *Stowers* demand. Side B of the Worksheet provides a framework for analyzing the reasonableness of accepting a settlement demand within policy limits. The completed worksheet can assist an adjuster in determining whether it is appropriate to settle a particular claim for the stated demand. The completed worksheet can also be maintained in the file as evidence of the prudent evaluation the insurer gave the demand, if and when the insurer's response to the demand is ever questioned in a subsequent *Stowers* case.

³³² See *id.* at 855.

³³³ See *id.*

³³⁴ See *CNA Lloyds of Texas v. St. Paul Ins. Co.*, 902 S.W.2d 657 (Tex. App.--Austin 1995, writ dismissed).

³³⁵ See *id.*

³³⁶ See Soriano at 316.

- F. **Excess Insurance and Self-insured Retention.** Despite the passage of over 70 years since the inception of the *Stowers* duty, several issues relating to excess insurance still remain unanswered, and therefore, special care should be taken in dealing with excess issues in the *Stowers* context. One of the only answered issues is the right of an excess insurer, under the principles of equitable subrogation, to bring a *Stowers* action against the primary carrier for breaching the *Stowers* duty and exposing the excess carrier to liability that would not have occurred had the primary carrier settled the case within policy limits.³³⁷ While a primary carrier has no duty to consider a demand that is not within its policy limits,³³⁸ no Texas court has yet answered the question of whether a *Stowers* duty arises if the primary and excess policies are issued from the same carrier and the demand is above the primary policy limits but within the limits of the excess policy. Similarly, a 1998 Texas Supreme Court opinion seems to have left open the question of whether a carrier has a *Stowers* duty when faced with a demand above policy limits and the insurer has actual knowledge that the insured has made an unconditional offer to pay the excess portion of any such demand above policy limits.³³⁹ Another area that can be problematic in the *Stowers* context is when the insured has a self-insured retention. Whenever insurers are confronted with problems involving these issues, consultation with legal counsel is usually advisable.
- G. **Recommendations.** Insurers can minimize the risk of *Stowers* liability by doing the following: 1) promptly identify and resolve all coverage issues as soon as possible in any potential policy limits case; 2) upon receipt of the *Stowers* demand, defense counsel should be asked to prepare a liability and damages evaluation as to all claims; 3) calendar response deadlines; 4) have defense counsel clear up, in writing, any ambiguities in the Plaintiff's demand letter; 5) if further discovery or information is needed to adequately evaluate claim, consider pros and cons of communicating such to Plaintiff's counsel; 6) communicate with insured regarding the demand review process and get the insured's input on value of claim and preference regarding acceptance of Plaintiff's demand; 7) carefully evaluate demand and consider possible responses through written evaluation of the claims or using a worksheet such as that provided in this article; 8) timely respond to Plaintiff's counsel with a formal courteous response to the settlement demand; 9) document in the claim file all efforts undertaken to evaluate and consider *Stowers* demand. For plaintiffs seeking to invoke the *Stowers* duty on an insurer the following should be done: 1) through written discovery identify policy limits applicable to case and all reservations of rights correspondences sent to the insured; 2) prepare thoughtful and unambiguous written demand for a stated sum within policy limits or for "policy limits" that involves at least one covered claim and which a reasonable insurer should accept; 3) offer full and complete release of all claims against insured; 4) do not make the offer conditional; 5) in personal injury actions, account for and include settlement of all hospital liens in demand, if applicable; and 6) provide Defendant reasonable time to consider and respond to the demand of not less than 14 days.

³³⁷ See *American Centennial v. Canal*, 843 S.W.2d 480, 483 (Tex. 1992).

³³⁸ See *Westchester Fire Ins. Co. v. American Contractors Ins. Co. Risk Retention Group*, 1 S.W.3d 872, 874 (Tex. App.--Houston [1st Dist.]1999, no writ).

³³⁹ See *State Farm Lloyds Ins. Co. v. Maldonado*, 963 S.W.2d 38, 41 (Tex. 1998)