



The Weekly Update of Texas Insurance News

TEXAS INSURANCE LAW NEWSBRIEF



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January 26, 2009

FEDERAL COURT HOLDS DUTY TO DEFEND TRIGGERED IN UNDERLYING SUIT INVOLVING PROFESSIONAL LIABILITY DISPUTE BETWEEN LAW FIRM AND ITS FORMER CLIENTS

Recently, a Houston federal court concluded the duty to defend was triggered for an underlying action that involved a dispute between a law firm and its former clients. In *Am. Guarantee & Liab. Ins. Co. v. Hoeffner*, 2009 WL 130221 (S.D. Tex. January 16, 2009), former silicosis litigation clients filed three lawsuits against a law firm alleging the attorneys participated in a kickback scheme that caused the silicosis claims to be settled at arbitrary amounts resulting in millions of dollars in fees for the firm. The firm filed a claim under its professional liability policy and requested American Guarantee provide a defense for the three lawsuits.

American Guarantee agreed to provide a defense under a reservation of rights and then filed this suit seeking a declaration that it owed no duty to defend or indemnify the firm under the policy. After reviewing the individual allegations in the three lawsuits, the court then turned to analyze the policy language. The policy provides coverage for “damages” that an insured becomes obligated to pay because of a claim “based on an act or omission in the Insured’s rendering or failing to render Legal Services for others.” The policy excludes “any intentional, criminal, fraudulent, malicious or dishonest act or omission by an Insured, except that this exclusion shall not apply in the absence of a final adjudication or admission by an Insured that the act or omission was intentional, criminal, fraudulent, malicious or dishonest.”

The complaints in the underlying lawsuits contained claims for monetary relief based on an act or omission by the firm in the rendering of legal services as the plaintiffs’ attorneys in the silicosis litigation. American Guarantee argued engaging in a kickback scheme is not an act or omission “ordinarily performed as a lawyer” and, therefore, is not within the policy’s definition of “Legal Services.” The court found the claims in the underlying suit alleged acts committed in connection with the settlement of the silicosis lawsuits, and also found settling lawsuits was an act ordinarily performed by a lawyer. American Guarantee next argued the firm had prior knowledge that it was breaching a professional duty and this conduct could not result in a claim under the policy. Although it appeared clear from other sources that the firm’s alleged participation in the kickback scheme occurred before inception of the policy, the duty to defend is determined based on the factual allegations in the complaint in the underlying suit and is not affected by “facts ascertained before the suit, developed in the course of litigation, or by the ultimate outcome of the suit.”

Lastly, American Guarantee argued there was no duty to defend because the firm's conduct involved intentional, criminal, fraudulent, and dishonest acts. The "intentional acts" exclusion in the policy applies only where there has been a final adjudication or admission by the insured "that the act or omission was intentional, criminal, fraudulent, or dishonest." As was true for the prior knowledge analysis, the court concluded there was nothing in the complaints to indicate there had been a final adjudication or admission by an insured that the firm's conduct was intentional, criminal, fraudulent, or dishonest. As such, the claims against the firm triggered a duty to defend.

APPELLATE COURT AFFIRMS MOTION FOR DEFAULT JUDGMENT AGAINST WORKERS' COMPENSATION CARRIER EVEN THOUGH PLAINTIFF DID NOT SERVE AMENDED PETITION

Last week, addressing a bizarre situation, the San Antonio Court of Appeals affirmed a trial court's decision to grant a motion for default judgment against a workers' compensation carrier even though Plaintiff failed to serve his amended petition. In *Continental Casualty Co. v. Guzman*, 2009 WL 136926 (Tex. App.—San Antonio January 21, 2009), Guzman filed a workers' compensation claim and, after administrative hearings, the Texas Workers Compensation Commission (TWCC)^[1] determined he sustained a compensable injury for which Continental owed benefits.

Continental then appealed the TWCC decision to district court. A no-answer default judgment was awarded and the TWCC decision entitling benefits to Guzman was set aside. After discovering the default judgment, Guzman filed an "Original Petition for Bill of Review" seeking to set aside the default judgment. Guzman served Continental, but the carrier did not file an answer to the suit. Thereafter, Guzman filed an amended petition, but did not serve Continental. Guzman subsequently filed for default judgment on the amended petition and the court granted it. Upon discovering a default judgment against it, Continental filed this appeal.

First, Continental argued Guzman's failure to serve the amended petition amounted to reversible error. The appellate court concluded, although the amended petition contained new factual allegations, since it did not contain additional causes of action the amended petition did not seek a more onerous judgment than the original petition. Continental also argued Guzman's bill of review did not meet all the required elements. After a swift analysis, the court found no error and affirmed the trial court's judgment.

APPELLATE COURT AFFIRMS SANCTIONS AGAINST S.O.R.M. FOR FRIVOLOUS LAWSUIT TO CHALLENGE TWCC DECISION ON COMPENSABILITY OF CORRECTIONAL OFFICER'S INJURY

Last Thursday, an appellate court concluded sanctions were appropriate against the State Office of Risk Management (SORM) for its frivolous lawsuit filed against a correctional officer to challenge a TWCC finding that her injury was compensable. In *State Office of Risk Management v. Foutz*, (Tex. App. — Eastland, January 22, 2009), Foutz, a Texas Department of Criminal Justice corrections officer, observed an inmate being stabbed by another inmate. TDCJ policies forbade Foutz to open the cell door to protect the inmate and, as a result, Foutz was required to watch the attack in order to identify the participants. Within a brief period after the attack, the injured inmate was pronounced dead.

Foutz then sought treatment from a licensed professional counselor because she experienced anxiety and questioned herself for not intervening to prevent the inmate's death. Foutz also filed a workers' compensation claim and SORM disputed it. At SORM's request Foutz saw a psychiatrist for an independent medical exam. The IME doctor confirmed Foutz suffered from post traumatic stress syndrome and recommended further treatment. Not surprising, a Texas Workers' Compensation hearing officer found Foutz suffered a compensable mental-trauma injury. SORM appealed and lost. It then filed suit for judicial review and lost a second time. The trial court sua sponte ordered SORM and its two trial attorneys to show cause why they should not be sanctioned for filing a frivolous suit.

The trial court conducted an evidentiary hearing and afterwards sanctioned SORM \$100,000, its lead counsel \$5,000, and co-counsel \$3,000 for filing a frivolous suit under TEX. R. CIV. P. 13 and TEX. CIV. PRAC. REM. CODE Ch. 10. No appeal was perfected as to the sanctions against SORM's attorneys; only the sanctions related to SORM was addressed in its appeal.

The appellate court analyzed the evidence provided at the show cause hearing and affirmed SORM's "position on the case was groundless, frivolous, in bad faith, and that it was unsupported by the facts and law." The Texas Supreme Court has held that trial courts must explain how a particular sanction will "deter repetition of the conduct or comparable conduct by others similarly situated." Because the court did not provide its reasons for assessing a \$100,000 sanction, the appellate court reversed the finding as an impermissible arbitrary fine. The court remanded the case for further proceedings and also issued a separate show cause order to afford SORM the opportunity to address the discrepancies between deposition testimony and SORM's description related to it.

Editor's Note: This case presents a good example why workers' compensation insurance providers must use careful discretion when deciding to challenge or otherwise pursue appellate remedies for adverse rulings at the administrative level. The Texas Supreme Court has instructed the Texas Workers' Compensation Act should be liberally construed in favor of injured workers, and a strained or narrow construction of that Act is improper. *See Kroger Co. v. Keng*, 23 S.W.3d 347, 349 (Tex. 2000). On the other hand, given the upward trend in bad faith lawsuits in workers' compensation cases, carriers need to promote a cautiously aggressive policy to dispute or challenge fraudulent or questionable workers' compensation claims.

ABA NATIONAL INSURANCE COVERAGE CONFERENCE IN TUCSON

Coverage lawyers might be interested in the American Bar Association's National Insurance Coverage Seminar which will be held in Tucson, Arizona on March 4-7, 2009. This is the 21st annual presentation of the ABA Section of Litigation [Insurance Coverage Litigation Committee CLE Seminar](#) March 4-7, 2009 in Tucson, Arizona at the [The Westin La Paloma Resort & Spa](#). Chris Martin from our office is one of the featured speakers this year.

This year's plenary sessions will address cutting edge coverage topics including creative coverage settlements, coverage mediation issues, written and oral advocacy errors, climate change litigation, and preparing an insurance coverage case for trial in the 21st century. In addition, this year the ABA will have a full complement of high level breakout sessions from Thursday through Saturday. There also will be receptions on Wednesday and Thursday nights, and a Friday night dinner, which will provide you with excellent opportunities to see old friends, and hopefully make new friends and contacts. Best of all, with a

particular emphasis on litigation skills and emerging substantive issues, this year's CLE conference will give each attendee new tools to apply to their coverage cases.

Important Conference Information: For conference details and activity guides, visit the [Insurance Coverage Litigation Committee CLE Seminar website](#). The [program brochure](#) is now also available online. Online registration closes **Friday, February 13, 2009**. [Register Now](#). Don't delay in booking your rooms! Hotel registration cut-off is **Tuesday, February 3, 2009**. For reservations, call 520-742-6000 and refer to the *ABA Section of Litigation 2009 Insurance Coverage Litigation Committee CLE Seminar*.

For additional information on this national coverage seminar, please contact [Jenny Langdon](#) with the ABA at 312-988-6247.

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