The Weekly Update of Texas Insurance News
TEXAS INSURANCE LAW NEWSBRIEF
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TEXAS SUPREME COURT DENIES REHEARING ON LANDMARK RULING WHICH PERMITS APPLICATION OF TEXAS' PROMPT PAYMENT PENALTIES TO THIRD-PARTY LIABILITY CLAIMS

Last Friday, without issuing an opinion, the Texas Supreme Court denied the Motion for Rehearing in *Lamar Homes Inc. v. Mid-Continent Casualty Co.* In its original majority opinion delivered August 31, 2007 (and reported in the *MDJW Newsbrief* on September 4, 2007), the high court concluded that a general contractor sued for construction defects involving only damage to or loss of use of a home built by the insured contractor was an "accident" and "occurrence" resulting in "property damage" and was sufficiently pled so as to trigger the insurer's duty to defend. In *Lamar Homes Inc. v. Mid-Continent Casualty Co.*, 2007 WL 2459193 (Tex. August 31, 2007), the Texas Supreme Court refused to address the duty to indemnify observing: "that duty is not triggered by allegations but rather by proof at trial." But, the Court concluded that Texas Prompt Payment of Claims Act, formerly Article 21.55 (now Chapter 542), *did apply* to the duty to defend and is triggered when the insured submits a legal bill to the insurer for payment. The original opinion in its entirety can be found here.

The majority's silent denial of Mid-Continent's Motion for Rehearing drew a stern dissent from Justice Brister—who also authored the dissent to the original opinion, but did not initially address the prompt payment issue. The dissent on rehearing can be found here. The dissent noted: "Since Reconstruction, prompt-payment penalties applied to some insurance claims in Texas, but never to a liability carrier's duty to defend." After a brief history of the 1991 legislative amendments to the Texas Insurance Code, the dissent set its sight on the primary issue: the characterization of the term "first-party claim." The dissent argued there are three reasons why Chapter 542 should not apply in this particular context.

First, the prompt payment statute is limited to claims "that must be *paid* by the insurer." A liability policy does not promise *payment*. Second, claims for reimbursement (like the one here) are not claims "under an insurance policy or contract," but a damages claim for breach of contract. Third, the prompt payment statute applies only to claims "that must be paid by the insurer directly to the insured." An insured who presents a property damage claim may demand direct payment under a first-party policy, but under a third-party liability policy an insured cannot demand that defense costs be paid to it directly.

In its original opinion, the majority noted that while the prompt payment statute does not define "first-party claim," the court previously has distinguished first-party and third-party claims on the basis of the claimant's relationship to the loss. Citing to a footnote in the plurality opinion in *Universe Life Ins. Co. v.*

Giles, the court wrote 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." *Universe Life Ins. Co. v. Giles*, 950 S.W.2d 48, 54 n. 2 (Tex. 1997). Based upon this distinction, the majority concluded in its initial decision that a claim for reimbursement of its defense costs is a "first-party claim" because it relates solely to the insured's own loss.

The dissent to the rehearing issued lat Friday addressed this argument (and the entire majority opinion) stating that the decision to penalize insurers that refuse to defend a claim is a decision to be left for the people of Texas to make through the legislative process and not for "this Court to make out of whole cloth." There was no majority opinion on the motion to reconsider. The Court simply denied the motion for rehearing. Judge Brister and two of his fellow Justices authored this dissent.

Editor's Note: The majority decision on the applicability of Texas' Prompt Payment Statute is going to be a nightmare to apply and will inevitably lead to more litigation. The impact of the court's decision to apply Chapter 542 penalties in the third-party liability context will significantly complicate some claims decisions regarding defense-costs to the point of near impossibility. The majority decision raised many more questions and provides few answers. The lower courts of Texas will be left to figure out how to apply the 18% penalty statute to liability claims for which the Texas Legislature never intended them to apply. But, for now, that is the law of the state and the insurers and their counsel doing business here will have to work through the myriad of unanswered questions regarding just how the statutory framework can and will apply to a liability insurers' duty to defend.

NEWSBRIEF TO RESUME JANUARY 7, 2008
MDJ&W WISHES ALL OF OUR READERS A VERY MERRY CHRISTMAS AND A HAPPY AND PROSPEROUS NEW YEAR!

Our offices will be closed next Monday and Tuesday, December 24th and 25th, for the Christmas Holiday, as well as Monday and Tuesday, December 31st and January 1st, for the New Year's holiday. Our Texas Insurance Law Newsbrief research and writing staff will also be taking those days off to spend time with family and friends. The Newsbrief will resume publication January 7, 2008 and will continue weekly in 2008 as we have for the past 8 years. As we have done before, if the courts of Texas (particularly the Texas Supreme Court) issue any *significant* decisions before January 7th, we will issue a special report to keep our readers updated on any ground-breaking developments. Otherwise, we will resume our weekly reporting on January 7th. Until then, we want to offer our special thanks to our clients and friends in the insurance industry who contributed in many different ways in making 2007 successful on many different judicial, appellate, legislative, regulatory and business fronts. We want to wish all of our readers a very Merry Christmas and a Happy and Prosperous New Year!