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The Weekly Update of Texas Insurance News

TEXAS INSURANCE LAW NEWSBRIEF

A Service of Martin, Disiere, Jefferson & Wisdom L.L.P.

Principal Office 808 Travis, 20th Floor Houston, Texas 77002 713.632.1700 FAX 713.222.0101
900 S Capital of Texas Hwy, Suite 425 Austin, Texas 78746 512.610.4400 FAX 512.610.4401
16000 N Dallas Parkway, Suite 800 Dallas, Texas 75248 214.420.5500 FAX 214.420.5501

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COURT ERRS IN APPLYING "EIGHT-CORNERS" ANALYSIS BEFORE CONSIDERING REFORMATION CLAIM

Last Monday, the Fifth Circuit held that while a magistrate judge had constitutional authority to enter final judgment on state-law counterclaims, the judge erred in applying an eight-corners analysis to the insurer's duty to defend without first considering the insurer's equitable counterclaim for reformation based on mutual mistake. In *Technical Automation Services Corporation v. Liberty Surplus Insurance Corporation,* 2012 WL 688520 (5th Cir. (Tex.), March 5, 2012), an insured sought a defense under their commercial general liability policy for negligence claims after a chlorine leak caused bodily injuries at a chemical plant. The insurer sought reformation of the policy based on a mutual mistake wherein the wrong endorsement was inserted into the policy. The magistrate refused to consider parol evidence, found that the endorsement was ambiguous and applied the "eight-corners" rule in finding the insurer had a duty to defend. This appeal followed.

The Fifth Circuit held that the magistrate had the constitutional authority to enter final judgment on state-law claims and then turned its focus to the argument that the magistrate erred in interpreting the endorsement before determining whether its inclusion in the policy was the result of mutual mistake. The court observed that when "mutual mistake is alleged, the first task of the court is not to apply, perfunctorily, the "eight-corners" rule and then directly proceed to interpret the insurance policy. Instead, the first matter to address is whether the disputed provision results from an agreement between the parties." And, the court noted that the parol evidence rule does not apply to determinations of "mutual mistake, even when the contract is unambiguous or fully integrated." The Fifth Circuit held that the magistrate should have resolved the mutual mistake allegations before interpreting the contract and reversed, vacated and remanded the judgment for further proceedings.

FIFTH CIRCUIT FINDS FLOOD RENEWAL PREMIUM PAYMENT UNTIMELY

In a timely reminder to insureds as flood season comes upon us, last Tuesday the Fifth Circuit held that an insured's renewal premium was paid several hours too late and coverage was precluded as a matter of law. In *Worthen v. Fidelity National Property and Casualty Insurance Co.,* 2012 WL 715248(5th Cir. (Tex.) March 6, 2012), the insured's flood policy expired at 12:01 a.m. on August 10, 2008 and it was undisputed that all renewal notices and reminders were received. The policy provided a 30 day grace period to renew without a lapse in coverage. And on the morning of September 9, 2008, while Hurricane Ike was bearing down on the Texas coast, the insured called his agent to renew the policy and issued payment that same morning around 9:00 a.m. The residence was damaged by flood waters and the claim was denied based on the assertion that the policy lapsed at 12:01 a.m. September 9, 2008 and a 30 day waiting period applied to preclude coverage for the loss. This lawsuit followed.

The trial court granted judgment in favor of the insured finding that the premium payment was made on the 30th day after lapse and as a result, coverage was continuous under the policy. The insurer appealed and the Fifth Circuit examined the issue applying rules of insurance contract interpretation. The insured argued that the policy's grace period provision is ambiguous because it does not provide a specific date and time for the renewal premium deadline. In addressing the issue, the court examined FEMA's Flood Insurance Manual and based on the examples provided therein, concluded that the policy terms were not ambiguous and the policy lapsed at 12:01 a.m. on September 9, 2008 and no coverage was in force when Hurricane Ike damaged the insured property. Accordingly, judgment in favor of the insured was reversed.

COURT FINDS THIRD-PARTY HAS DIRECT ACTION AGAINST PHYSICIAN'S INSURER FOR STOWERS EXPOSURE UNDER MEDICAL LIABILITY ACT

Last Monday, the U.S. District Court for the Northern District of Texas held that an insurer's failure to exercise reasonable care in settling claims against an insured physician, were not capped by the now-repealed version of the Medical Liability and Insurance Improvement Act (MLIIA) and, the injured party had standing to bring a direct action against the insurer under the common law Stowers Doctrine exception to the MLIIA. In *Bramlett v. Medical Protective Co. of Fort Wayne, In.,* 2012 WL 692032 (N.D.Tex. March 5, 2012), an injured third-party obtained a judgment in excess of the physician's statutory liability cap and, also in excess of the insured physician's liability insurance policy limits. The injured third-party then sought to bring a direct-action against the insurer for the *Stowers* liability.

The court examined Texas case law applying the Stowers exception to the MLIIA and its purpose of encouraging insurers to resolve claims. The court also noted the distinction in the insurer's defenses applicable to the insured, differ from those applicable to third-parties. And, interpreting the exception, the court held that exception provided a direct third-party action against the insurer. *Editor's Note: Although the issue addressed in this case has been clarified by statutory changes and is unlikely to recur, the case remains significant in recognizing a direct third-party action against an insurer under Texas law. We continue to monitor this trend.*

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