The Weekly Update of Texas Insurance News
TEXAS INSURANCE LAW NEWSBRIEF
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WHETHER 1991 CHANGES TO THE TEXAS INSURANCE CODE AND PROMPT PAYMENT OF CLAIMS STATUTE CONTINUE TO EXEMPT INTERPLEADER ACTIONS

Last week, in *State Farm Life Insurance Company v. Martinez*, 2007 WL 431043 (Feb. 9, 2007), the Texas Supreme Court determined that the Legislature's 1991 changes to the Texas Insurance Code no longer support an exception for interpleader actions pursuant to the Prompt Payment of Claims statute. However, nothing in those changes suggested that statutory penalties should apply after the interpleader occurs.

In *Martinez*, State Farm received competing claims to a life insurance policy. One of the claims was received on September 11th, and the 60th day elapsed on November 10th. State Farm did not interplead the funds until twelve (12) days later. After a bench trial, the trial court assessed against State Farm prejudgment interest at 6% ($25,506.73), penalty interest at 18% ($76,520.19), and attorney's fees for the trial court of $37,089.91. State Farm appealed, but its argument that penalty interest should apply only to the 12-day delay was rejected by the Court of Appeals.

On appeal, State Farm argued that the prompt payment statute did not apply when rival claims required an insurer to file an interpleader. The Supreme Court noted that since at least 1874 there have been Texas statutes punishing an insurer's failure to pay promptly. Until 1991, those statutes generally provided that if a life insurance claim was not paid within 30 days, the insurer had to pay penalty interest of 12% and attorney's fees to the policy beneficiary. Throughout this same period, Texas common law provided that an insurer faced with rival claims to policy proceeds could interplead the funds, join the rivals who claimed the funds, and be discharged from further liability. Under the common law, a stakeholder is entitled to recover its attorney's fees from the deposited funds unless there were no rival claimants or the interpleader was unreasonably delayed.

The Supreme Court noted that Texas statutes have long punished insurers for delays beyond 30 days, while the common law punished them only for unreasonable delays – an unspecified period that depended on the facts of each case. Generally, the two rules operated in harmony – insurers interpleading within 30 days were protected and those who unreasonably delayed interpleading paid penalties. However, the Supreme Court noted circumstances in which the different standards inevitably overlapped. For example, the rules would overlap if an insurer waited more than 30 days but the delay was not "unreasonable." Thus, for many years, Texas court held that the prompt payment statute must yield to the common law – that an interpleader filed within a reasonable time did not subject the insurer to the statutory penalties regardless of the statutory deadlines.

However in 1991, the Legislature changed the prompt payment statute, raising the penalty interest to 18% and the deadline for payment to 60 days. For several reasons, the Supreme Court held that the common law interpleader exception to the prompt payment statute did not survive the 1991 changes: "Continuing to recognize an interpleader exception to the prompt payment statute would frustrate its purpose in some cases, while removing the exception would allow the purposes of both the statute and interpleader to be fulfilled."

Further, the Supreme Court noted that while assessing penalties before interpleader is consistent with both the statutory and common law rules, assessing penalties after interpleader is not. Assessing penalty interest and attorneys' fees after an interpleader is filed would punish insurers for doing exactly what Texas law encourages. Notably, an insurer's delay beyond the statutory 60 days may bar recovery of attorneys' fees and incur the statutory penalties, only the absence of rival claims justifies continuing statutory penalties ***after*** interpleader occurs.

Finally, the Supreme Court noted that once funds are deposited into the registry of the court, they are held in trust for the litigant who establishes his right thereto and interest accrues to its ultimate owner. Allowing the prevailing party to recover interest on proceeds in the court's registry and interest from the insurer at the same time would constitute a double recovery. Accordingly, interpleader should halt prejudgment interest.

SEVERANCE AND ABATEMENT OF EXTRA-CONTRACTUAL CLAIMS

On February 8, 2007, the Beaumont Court of Appeals issued an interesting opinion on the severance and abatement of extra-contractual claims. In *In Re Progressive County Mutual Insurance Company*, 2007WL 416553, the Beaumont Court strictly followed *United States Fire Insurance Company v. Millard*, 847 S.W.2d 668 (Tex. App. – Houston [1st Dist.] 1993, orig. proceeding). The Beaumont Court held that when a policyholder asserts claims against the insurer for both breach of contract and for extra-contractual bad faith, and the insurance company has previously made a settlement offer on the disputed contract claim, severance and abatement "are required" to avoid undue prejudice to the insurer in its defense of the contract dispute.