

TEXAS SUPREME COURT RECOGNIZES INSURANCE COMPANY'S RIGHT TO RECOUP SETTLEMENT PAYMENTS FROM POLICYHOLDER

A recent decision of the Texas Supreme Court will have a tremendous impact on the respective rights and obligations of insurance companies and their insureds when it comes to the settlement of third-party claims against the insured. In *Excess Underwriters at Lloyd's, London v. Frank's Casing Crew & Rental Tools, Inc.*, the Court examined a situation that is extremely common in the world of insurance coverage:

- An insured is sued by a third party.
- The insurance carrier issues a reservation of rights letter contesting coverage.
- Before the coverage issue is resolved, the insured receives a settlement offer from the third party that is within the policy limits.
- The carrier must then make a decision whether to accept the settlement offer and fund the settlement, even though the question of coverage is still undetermined. If the carrier is wrong on the coverage question, then a refusal to settle will subject it to liability.

The critical question is this: May the carrier pay the settlement and then recoup that money from the insured if it is subsequently determined that no coverage exists? In *Frank's Casing*, the Texas Supreme Court answered that question "Yes."

The facts in *Frank's Casing* are instructive and may provide guidance for insureds faced with this situation. The carrier issued a reservation of rights asserting that certain of the plaintiff's claims against the insured were not covered. On the eve of trial, the insured received a settlement offer within the policy limits and promptly sent a *Stowers* letter to the carrier demanding acceptance of the offer. The carrier initially agreed to fund the settlement if the insured would agree that the coverage issues would be resolved at a later date. When the insured refused and again demanded that the carrier accept the settlement offer, the carrier advised the insured that it would pay the settlement and seek reimbursement from the insured if the coverage litigation was resolved in the carrier's favor. This, in fact, occurred when the trial court in the coverage suit subsequently held that the claims asserted against the insured in the underlying lawsuit were not covered. In *Frank's Casing*, the Texas Supreme Court held that, under these circumstances, the insurance carrier was entitled to recoup the settlement payments from the insured.

The *Frank's Casing* holding signals a dramatic shift in the Court's position on this issue, as reflected in its previous decision in *Texas Assoc. of Counties County Gov. Risk Mgmt. Pool v. Matagorda County*. In *Matagorda*, the carrier settled a lawsuit against the insured after notifying the insured that it would seek reimbursement of the settlement funds if it was determined in the coverage suit that the claims were not covered. The insured did not respond to the carrier's letter, and the carrier then settled the claim without the insured's consent as was permitted by the policy. It was subsequently determined that the claims were not covered, and the carrier sought reimbursement from the insured for the settlement payment. In holding that the insurance carrier was *not* entitled to reimbursement, the Supreme Court noted that there was no express agreement between the parties for reimbursement, and held that no such agreement would be implied. Thus, *Matagorda* came to be viewed for the principle that, absent an express agreement between the parties permitting reimbursement, the carrier simply could not recoup settlement payments from the insured, even if it was subsequently determined that the settled claims were not covered.

The Court in *Frank's Casing*, however, indicated that its holding in *Matagorda* was not that clear cut, and was limited to the facts of that case. More specifically, the Court held that even absent an express agreement authorizing reimbursement, the circumstances may give rise to a right of reimbursement. Those circumstances include *at least* the following:

1. When the insured has demanded that the insurer accept a settlement offer within the policy limits; and
2. When the insured expressly agrees that the settlement offer should be accepted.

The Court held that, in these circumstances, an agreement by the insured to reimburse the carrier is implied at law. According to the Court, if the insured demands that the carrier accept a settlement offer within policy limits, it is deemed to have viewed the offer as reasonable, and whether the insured or the carrier ultimately bears the cost of a reasonable settlement with the third party should depend on whether there is, in fact, coverage.

Obviously, the *Frank's Casing* decision dramatically changes the settlement landscape and will have a significant impact on the way settlement discussions and decisions are approached by the insurance company and the insured. Under the Court's holding, an insured who demands that the carrier accept a settlement within policy limits or otherwise indicates that it wants the carrier to accept such a settlement offer will be deemed to have consented to the carrier's right to recoup that settlement payment if it is subsequently determined that there is no coverage. Further, the Court's decision leaves open the possibility that there may be even more circumstances under which an agreement to reimburse the carrier will be implied.

An insured faced with this situation should exercise caution and consult with insurance counsel to determine the appropriate course of action. As always, Haynes and Boone stands ready to assist in any way possible.

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