NICHOLAS E. ZITO AND LAURA L. KEMP

An Update On Uninsured and Underinsured Motorist Coverage in Texas: *Brainard* and Other Cases of Interest

The Texas underinsured/uninsured motorist statute[1] has been in effect now for more than three decades. We continue to see, however, several cases each year which interpret the coverage available under Texas auto policies and the statute. In the past two years we have seen several notable opinions, the most important of which are from three cases all decided by the Texas Supreme Court on the same day. Those cases, of course, are *Brainard*,[2] *Nickerson*[3] and *Norris*[4]. The Court finally addressed two important questions involving UIM coverage: claims for attorney fees under Chapter 38 of the Civil Practices and Remedies Code and claims for *Cavnar*[5]-type prejudgment interest.

We have also seen interesting opinions regarding former Article 21.55 of the Insurance Code, a new "hit and run" case, a case precluding coverage for bystander claims, and a recent case out of the Houston 14th Court of Appeals involving offsets allowed for liability payments against UIM coverage under the same policy.

THE CURRENT STATE OF THE LAW ON PREJUDGMENT INTERESTS AND ATTORNEY FEE CLAIMS

The Texas Supreme Court has now written another chapter on claims for attorney fees and prejudgment interest in UIM suits. As a general rule, prejudgment interest will be allowed, but attorney fees will not.

The *Brainard* trio of cases reached the Texas Supreme Court because of a conflict among the various Courts of Appeals on the issue of whether or not prejudgment interest (*Cavnar*-type interest) and attorney fees could be awarded on a UIM claim. It is interesting that *Norris* was an unpublished Court of Appeals opinion. It was the dissenting opinion in *Norris* that most closely mirrored the opinions announced by the Supreme Court on how to assess prejudgment interest in a case involving a claim for UIM benefits.

BACKGROUND OF *BRAINARD*

Brainard was the subject of three appellate court decisions. Edward H. Brainard, II sustained fatal injuries on July 1, 1999, when he was involved in a head-on collision with a vehicle owned and operated by Premier Well Service, Inc. Trinity Universal Insurance Company was the auto insurance carrier that issued a policy to the family business, Brainard Cattle Company. Trinity made a PIP payment of $5,000 on July 3, 1999. Suit was initially brought by the Brainard family[6] (hereinafter referred to collectively as "Brainard") against Premier and its employee. Through discovery, they learned that Premier's policy limit was $1 million. After settling with Premier for $1 million, Brainard made a written claim to Trinity for the $1 million UIM policy limits on April 18, 2000. Trinity responded with an offer of $50,000. On October 30, 2000, Brainard amended the petition to join Trinity as a defendant. Claims were asserted for contractual UIM benefits and various alleged Insurance Code violations, including a claim under 21.55 of the Texas Insurance Code, also known as the Prompt Payment of Claims Statute. A common law claim alleging a breach of the covenant of good faith and fair dealing was brought as well.

Trinity then filed a Motion for Severance and

Abatement, which the trial court partially granted. The good faith/unfair settlement practices and article 21.21 claims were severed, but the request to sever the article 21.55 claim was denied. A mandamus action was brought by Trinity and the Amarillo Court of Appeals conditionally granted the Petition for Writ of Mandamus.[7] The trial court ultimately severed the article 21.55 claim, as well.

The contract claim was subsequently tried, resulting in a jury verdict of actual damages of $1,010,000. The jury also awarded attorney fees to Brainard in the amount of $100,000. The trial court entered a judgment that Brainard recover from Trinity $5,000 in actual damages and $100,000 in attorney fees, but denied Brainard's request for prejudgment interest. The sole issue raised by Trinity on appeal challenged the trial court's award of attorney fees. Brainard raised one cross-point dealing with the court's failure to award prejudgment interest on the $1,010,000 in damages prior to offsetting settlement ($1,000,000) and PIP benefit payments ($5,000).

BACKGROUND IN *NICKERSON*

Nickerson involved a 1992 auto accident. Theresa Nickerson filed suit against the other driver in 1994 and, at some unknown point before October 1996, she accepted the third-party tortfeasor's policy limits of $25,000 and accepted $10,000 in PIP benefits under her own policy. She then sued her insurer, State Farm, on November 7, 1994 to recover underinsured motorist benefits. The case went to trial and resulted in a jury verdict of $225,000 in actual damages and $46,500 in attorney fees. After the verdict, but before the judgment was signed, State Farm tendered to Nickerson a check for damages, less the liability and PIP offsets of $35,000, but included postjudgment interest for a total amount of $191,294.52. State Farm excluded attorney fees from its check. The final judgment entered, however, included actual damages and prejudgment interest of $181,849.32 from the date suit was filed (November 7, 1994) for a total judgment of $371,849.32. The actual damages plus prejudgment interest less the offsets exceeded the policy limits of $300.000. Therefore, judgment was awarded for the UIM limits, and State Farm was also ordered to pay Nickerson's attorney fees and any postjudgment interest.

While initially appealing the award of prejudgment interest and the award of attorney fees, State Farm later withdrew the issue of prejudgment interest based upon the Supreme Court's denial of petition in *Menix v. Allstate Indem. Co.*[8] Therefore, the only issue remaining for the Appellate Court to decide was the award of $46,500 in attorney fees. Both sides treated the fees as being sought and awarded pursuant to Section 38.001 of the Texas Civil Practices and Remedies Code. In a footnote, it was stated that a claim for attorney fees under article 21.55 of the Insurance Code appeared not to have been asserted.[9]

BACKGROUND IN *NORRIS*

The third case in the UIM trilogy is *Norris*. *Norris* was initially decided by the Waco Court of Appeals in April of 2004.[10] Norris was in an accident on December 8, 1997. The underinsured motorist, Johnston, had policy limits of $50,000. Norris settled his claim against Johnston for $40,000 and then sued State Farm to collect under the UIM provisions of his policy. Norris' case proceeded to trial and the jury found that his damages were $51,200 and attorney fees were awarded. State Farm had previously paid $5,000 in personal injury protection benefits. State Farm also received credit for Johnston's $50,000 policy limits – the amount recoverable. Therefore, the total credits amounted to $55,000. The trial court found that the credits exceeded the amount of the damage verdict and, therefore, entered a Take Nothing Judgment in favor of State Farm. Norris appealed claiming he was entitled to prejudgment interest on $51,200 before applying the credits, as well as his attorney fees. The Waco Court of Appeals agreed on both counts.

Where there is no contractual duty to pay, there can be no "just amount owed."

THE SUPREME COURT'S HOLDINGS

The opinions in *Brainard*, *Nickerson*, and *Norris* were all authored by Chief Justice Jefferson. In each case, Chief Justice Jefferson found that attorney fees were not recoverable from the UIM insurer under Chapter 38 of the Civil Practices and Remedies Code. The circumstances under which an insured may recover attorney fees under Chapter 38 were described and the UIM policies were held to cover prejudgment interest on the damages attributable to the underinsured motorist. The Court also held that credits were to be applied using the "declining principle" formula which was derived from the Court's earlier opinion in *Battaglia v. Alexander*,[11] a case involving healthcare liability claims.

ATTORNEY FEES

In *Brainard,* the Court reiterated that attorney fees were only recoverable where authorized by statute or by contract. Attorney fees were only sought under Chapter 38 because no other "statutory scheme" applied. The Court noted that in order for Brainard to recover attorney fees, three things must be shown: they were represented by counsel; they presented a claim to Trinity; and Trinity failed to pay the "just amount owed" within 30 days of presentment. It was Brainard's position that their suit was like any other breach of contact suit and, therefore, the presentment occurred in February of 2000 when they made a demand for the UIM policy limits. Trinity argued that UIM policies are different because the carrier's duty to pay does not arise until the underinsured motorist's liability and the insured's damages are legally determined. The Court stated that under article 5.06-1(5) of the Insurance Code, the UIM insurer is only obligated to pay damages which the insured is "legally entitled to recover" from the underinsured motorist. Therefore, the UIM carrier was under no contractual duty to pay benefits until the insured obtained a judgment establishing the liability and the underinsured status of the other motorist, which required a determination of the amount of damages. Therefore, the filing of suit or demand for UIM benefits is insufficient to trigger a contractual duty to pay on the part of the insurer. In other words, where there is no contractual duty to pay there can be no "just amount owed." The Court, therefore, found that when UIM benefits are involved, the claim is not presented until there is a judgment entered by the trial court that establishes both fault and the underinsured status of the other motorist, which necessarily requires a determination of the amount of the insured's damages.

The Court stated that the insured was not required to obtain a judgment against the tortfeasor, but instead could settle with the tortfeasor. The Court held, however, that neither a settlement nor an admission of liability from the tortfeasor would establish UIM coverage.[12] Under the insuring agreement, Trinity had no obligation to pay UIM benefits before the negligence and underinsured status of the tortfeasor (Premier) was established. Therefore, a contact claim was not actually presented until the trial court had rendered its judgment,[13] and Brainard was not entitled to recover attorney fees under Chapter 38.

COMMENT ON CLAIMS FOR ATTORNEY FEES

There are instances, however, when a presentment can be deemed to have occurred without an actual trial of a UIM case. For example, should the carrier consent to the suit against the underinsured motorist, any default judgment or jury verdict obtained against the underinsured motorist would be binding upon the carrier, thereby triggering the 30-day time period set forth in Chapter 38 for payment of claims after presentment.

A case may arise in which the liability of the underinsured motorist may be so clear that it may be established by a summary judgment motion brought in the action against the UIM carrier. This, of course, would not result in establishing damages unless there was a stipulation as to the amount of damages or the damages exceeded a certain threshold limit. Also, situations could arise where the economic damages are so clearly established that the underinsured status of the other motorist could be deemed to have been found. This, of course, would be a rare circumstance where a court would be willing to make such a finding as a matter of law (*i.e.*, on a summary judgment basis). Absent exceptional circumstances, it appears that *Brainard* would foreclose a recovery of attorney fees from a UIM carrier under Chapter 38, as long as any judgment is paid within 30 days of entry.

RECOVERY OF PREJUDGMENT INTEREST

The Supreme Court's opinions in *Brainard* and *Norris* make it clear that prejudgment interest is now recoverable in a case involving a claim for UIM benefits. The issue of prejudgment interest first reached the Texas Supreme Court in another context in *Henson v. Southern Farm Bureau Casualty Ins. Co.*[14] *Henson* was a case where the insured's damages were in excess of $133,000, but the policy limits were $25,000 under a Texas Farm Bureau UIM policy and $20,000 under a Southern Farm Bureau UIM policy, for a total of $45,000. The question before the Court was not whether prejudgment interest could be added to the award against the tort defendant, but instead whether prejudgment interest could be awarded on the contract claim, *i.e.*, on top of the UIM policy limits. The specific question posed to the court was "whether an insurer, obligated to pay uninsured/underinsured benefits, owed on top of those benefits prejudgment interest to be computed either from 180 days after demand for those benefits has been made, or from the day a suit is filed for those benefits."[15] The Supreme Court held that prejudgment interest does not begin running on this type of a claim until the date that liability of the uninsured/underinsured motorist is established (*i.e.*, the date of judgment). The rationale was that the carrier would owe prejudgment interest on top of the policy benefits only if they had wrongfully withheld those benefits.

Since the carrier's contractual obligation to pay does not arise until the judgment was rendered, a claim for prejudgment interest on the policy benefits was properly denied. This type of claim could only earn prejudgment interest if the insurer wrongfully withheld benefits after a judgment was obtained establishing the necessary elements of a UIM claim.

The Court, in dictum, gave a hint of what it would do if it had been faced with a claim for "tort" or *Cavnar*-type interest. The Court stated that:

> there is no doubt that if *Henson* were recovering directly from *Contreras*, the judgment would include prejudgment interest. And the insurers do not dispute that had the trial court awarded prejudgment interest against the tort defendants, the insurers would be obligated to pay the entire judgment including that portion awarded for prejudgment interest, to the extent of policy limits.[16]

Brainard and *Norris*, therefore, presented a different prejudgment issue to the Supreme Court. The issue was whether prejudgment interest could be added to the tort award so as to obligate the carrier to be responsible for that amount up to the respective policy limits. The second question raised in both *Brainard* and *Norris* involved the issue of how and when credits to an award should be applied. *Brainard* sets forth rules on when prejudgment interest accrues and how settlement credits and/or advanced payments are to be credited. *Brainard* also incorporates statutory requirements for tolling the accrual of prejudgment interest once a written settlement offer has been made.

In addition to addressing the issue of prejudgment interest, *Norris* addressed a point that earlier cases had not. It had previously been held that the UIM carrier was entitled to a credit for the amount recovered or recoverable (which ever sum was greater) from the alleged underinsured tortfeasor.[17] *Norris* dealt with how the trial court should handle a claim for prejudgment interest when the insured accepts a settlement amount from the alleged underinsured tortfeasor which is less than the tortfeasor's policy limits.

BRAINARD'S HOLDING ON PREJUDGMENT INTEREST

Brainard claimed that prejudgment interest should be calculated on the entire $1,010,000 jury award before applying credits. Therefore, it was argued that the plaintiff should recover $263,430 in prejudgment interest. Trinity, however, argued that Brainard should not continue to earn interest on $1,010,000 in damages since they had already recovered $1,005,000 in compensation. The Supreme Court agreed with Trinity. The Court looked for guidance in its earlier opinion in *Battaglia v. Alexander*[18] where the Court held it was error to calculate prejudgment interest on total damages before deducting payments that plaintiff had received from other settling parties. Prejudgment interest was only to be awarded for loss of use of money as damages. Where there was a settlement or other payment, there could be no loss of use of money and, therefore, to allow an award of interest would be a windfall to a party and would result in a penalty to a defendant. Therefore, in *Battaglia*, the Court held that settlements must be credited according to the date they are received.[19] The Court adopted the "declining principal" formula as the method to be used in calculating prejudgment interest in UIM cases. Therefore, credits should be applied first to accrued interest and then to principal. In instances where payments were made (*e.g.*, PIP) prior to prejudgment interest accruing, the credit would be applied to principal only.

The relevant dates in *Brainard* are as follows:

(a) July 1, 1999, date of accident;

(b) July 31, 1999, Brainard receives $5,000 PIP payment;

(c) January 19, 2000, prejudgment interest period begins when Brainard files suit;

(d) December 7, 2000, Brainard receives $1,000,000 settlement; and

(e) March 9, 2001, Trinity offers Brainard $50,000.

Pursuant to statute, prejudgment interest begins on the 180th day after the defendant receives written notice of the claim or the date suit is filed, whichever occurs first. Since suit was filed on January 19, 2000 (180 days had not yet elapsed from the date of the accident), prejudgment interest began to accrue on the date of suit.

In addition, where there is a settlement offer, prejudgment interest cannot accrue on the judgment where the damages do not exceed the amount of the settlement offer where the offer is left open. *See* Section 304.105(a)

of the Finance Code which states that: "[I]f judgment for a claimant is equal to or less than the amount of a settlement offer of the defendant, prejudgment interest does not accrue on the amount of the judgment during the period that the offer may be accepted."

Because the $5,000 PIP payment was made prior to the date that prejudgment interest would begin to accrue, it reduced the principal before prejudgment interest was assessed. In the interim, from the date that suit was filed up to the date of the $1,000.000 settlement, prejudgment interest accrued on $1,005,000. Then the $1,000,000 credit would be applied first to accrued prejudgment interest and then to the remaining principal. Interest would then continue to run on the remaining principal up to March 9, 2001, which was the date of Trinity's $50,000 offer.

Since Trinity had made a settlement offer, which was kept open and which exceeded the net jury award, no prejudgment interest accrued on the remaining principal due Brainard.

NORRIS' HOLDING ON PREJUDGMENT INTERESTS

Norris brought a claim against State Farm as a result of injuries he sustained in a December 8, 1997 accident. He first sued the underinsured motorist Johnston on March 29, 1999 and settled with Johnston for $40,000 (a sum $10,000 less than Johnston's $50,000 limit). State Farm paid Norris $5,000 in PIP benefits, but did not make an offer on Norris' UM claim. The jury in the trial of the UIM case found past damages of $51,200. Since there was nothing in the record to show the dates of settlements and/or PIP payments, the Supreme Court remanded the case to the trial court to establish the payment dates so that prejudgment interest could be properly calculated.

In addition, although Norris settled with Johnson for $40,000, State Farm was entitled to a full $50,000 credit, the amount of Johnson's policy limits as of the date that Johnson remitted the settlement amount. Although Norris only received $40,000, the Court held that Norris had forfeited the difference between the settlement amount and Johnson's policy limits. Norris had not lost the use of $10,000 and had released any entitlement to it. Therefore, he waived and/or forfeited his right to receive prejudgment interest on the settlement gap. Prejudgment interest could only be awarded then on the amount of the settlement ($40,000) up to the date of payment, plus whatever amount was in excess of Johnston's policy limits ($1,200).

Norris gives us a refined statement by the Court: (1) the written notice that counts is the written notice received by the underinsured motorist carrier[20] and not the notice received by the underinsured motorist; and (2) settlement with the underinsured motorist for an amount less than their policy limit results in a forfeiture of a right to claim prejudgment interest on the "gap" between the settlement amount and the actual policy limits available.

From *Brainard* and *Norris* (as well as other opinions) we now have the following rules to apply in regards to prejudgment interest on UIM claims.

Rule 1: **You apply settlements to past damages first, then to future damages.**

Rule 2: **By statute, no prejudgment interest is allowed on future tort damages.**

Rule 3: Prejudgment interest begins to accrue 180 days after written notice to the UIM carrier of the accident/claim or the date that suit is filed,[21] whichever occurs first.

Rule 4: **Payments, such as PIP payments, that were made prior to prejudgment interest accruing are applied directly against principal.**

Rule 5: **In order to properly credit a settlement, it should be applied:**

(a) first to accrued prejudgment interest as of the date the settlement was made;

(b) then to the principal (past damages) thereby reducing or perhaps eliminating prejudgment interest from that point forward.

Rule 6: **The insured forfeits any right to claim prejudgment interest on any settlement gap (where the insured settles for an amount less than the underinsured motorist's policy limits).**

Rule 7: **Settlement offers which are in writing result in a suspension of prejudgment interest up to the amount of the settlement offer and the suspension is effective from the date of the written offer.**

QUESTIONS RAISED BY THESE DECISIONS

Question 1: Who has the burden to prove when payment was made?

The Supreme Court did not address this issue, although it was addressed by the Court of Appeals in *Norris*. In *Norris,* the dissenting opinion written by Judge Gray suggests that the burden of proof should be on the party seeking to recover prejudgment interest. Until this issue is resolved, counsel representing the UIM carrier should be prepared to prove up the amount and date of each payment in order to receive a proper credit and/or offset.

Question 2: Can creative drafting of settlement documents circumvent a carrier's right to assert a claim for a credit?

Note that in *Battaglia*, the case that the Supreme Court relied heavily upon in adopting the declining principal formula, it was implied that the insured is not precluded from allocating the amount of a settlement to future damages as opposed to past damages, so long as the allocation is spelled out in the underlying settlement documents.

Question 3: Are 21.55 claims precluded in UIM cases?

Unfortunately, the issues that the court addressed in *Brainard, Nickerson* and *Norris* did not involve article 21.55 of the Insurance Code.[22] The Court's ruling on attorney fees dealt with what were presumed to be Chapter 38 attorney fees claims. Article 21.55 allows for attorney fees and an 18 percent interest penalty for instances where the carrier has failed to comply with the prompt payment of claims provision.

The Texas Supreme Court addressed article 21.55 in *Allstate Insurance Co. v. Bonner.*[23] In *Bonner,* Allstate had failed to timely acknowledge receipt of the claim. Bonner did not prevail on his suit seeking UIM benefits, as the jury award was less than the PIP payment made by Allstate. In order for Bonner to recover under the penalty provisions of article 21.55, he was required to establish: (1) a claim under a policy; (2) *the insurer was liable for the claim*; and (3) the insurer failed to follow one or more sections of article 21.55. Since Bonner could not establish Allstate's liability on the policy, he was precluded from recovering under article 21.55.

The court distinguished the situation in *Bonner* from that in *Dunn v. Southern Farm Bureau Case. Ins. Co.*[24] where Southern Farm Bureau was found liable on the contract claim. The insurer in *Dunn* was subject to the statutory penalties "as a consequence for delaying acknowledgement and payment of a claim for which it was liable."[25]

Brainard causes somewhat of a conflict with the Prompt Payment of Claims Statute. This is because a UIM claim is somewhat unique as liability on the policy (contract) is not established until the liability of the underinsured motorist is determined and damages are found by the jury which establishes the underinsured status of the third-party tortfeasor. Section 542.056 requires that the carrier give notice of acceptance or rejection of a claim within certain statutory deadlines. If the claim is accepted, the carrier must pay the claim not later than the fifth business day after the date notice is made. Another section involving delay of payment of a claim provides:

> ...if an insurer, after receiving all items, statements, and forms reasonably requested and required under Section 542.055, delays payment of the claim for a period exceeding the period specified by other applicable statutes or, if other statutes do not specify a period, for more than 60 days, the insurer shall pay damages and other items as provided by Section 542.060.

If the insurer delays payment of the claim, it is required to pay the 18 percent interest penalty and attorney fees set forth in Section 542.060.[26] The Insurance Code does not provide any exception for UIM claims. There is no other statute which specifies a time period for payment as the UM/UIM statute is silent on this point. In order to circumvent the application of the prompt payment statute, it must be implied by *Brainard* that there is no obligation to pay until liability and the underinsured status of the third party motorist is established. Hence, the inherent conflict between the caselaw and the plain meaning of the statute.

There are three decisions by lower courts that we can look to for guidance on this issue. In *Mid-Century Ins. Co. of Texas v. Daniel,*[27] the Amarillo Court of Appeals, on rehearing following the *Brainard* opinion, held that "Mid-Century's payment of [UIM benefits] within two days of the judgment against the third party precludes the award of attorney fees under article 21.55, §§ 4 and 6 or §38.002(s) of the Texas Civil Practice & Remedies Code." That Court also found the assessment of interest under article 21.55 would be triggered by the jury verdict

determining the insured's damages recoverable from the third party, and Mid-Century's payment within two days of that determination precluded interest penalties under article 21.55.

In *Delagarza v. State Farm Mutual Automobile Ins. Co.*,[28] the Dallas Court of Appeals held in an uninsured motorist case that State Farm had complied with the provisions of article 21.55. The record showed that State Farm had timely acknowledged the receipt of Delagarza's claim within 15 days and requested supporting documentation, including medical bills and requested a signed medical authorization. State Farm later received a letter enclosing Delagarza's medical bills and records, but no authorization was included. The letter demanded that State Farm tender payment of $25,000 in return for a release. State Farm had timely responded that it was unable to accept Delagarza's offer, but made a counter offer of $10,000 which it would agree to pay upon receipt of notice that Delagarza accepted the offer. State Farm had also learned that Delagarza had pre-existing degenerative back problems. Therefore, State Farm requested all prior records. Rather than forwarding the records, Delagarza filed suit. Within three weeks of the suit being filed, State Farm forwarded Delagarza a check for $10,000. After conducting discovery, State Farm sent a second check to Delagarza for $15,000 representing the balance of the benefits available under the policy. This left only the 21.55 claim remaining.

...it could be argued that the Prompt Payment of Claims Statute is not triggered if the carrier otherwise complies with all of the statutory deadlines...

The Court found that Section 4 of article 21.55 allowed an insurer to notify its insured that it was accepting only part of a claim and also allowed payment of part of the claim to be conditioned on the performance of an act by the insured, *i.e.*, such as signing a release or agreeing to settle for a lesser amount. *Delagarza,* therefore, stands for the proposition that Section 21.55 of the Insurance Code was not intended to eliminate an insurer's right to dispute all or part of an insured's claim. Instead, the purpose of 21.55 was to "merely establish deadlines by which the insurance company had to act."

Wellisch v. United Services Automobile Assoc.[29] relied upon the holding in *Henson* in finding that an insurer "has the right to withhold payment of UIM benefits until the insured's legal entitlement is established."[30] The San Antonio Court of Appeals interpreted article 21.55 as not precluding a carrier from disputing or denying a claim, but only required that they do so promptly. "Nothing in article 21.55 precludes an insurer from awaiting a judicial determination of an insured's 'legal entitlement' to UIM benefits. It merely requires that the insurer notify the insured of its reasons for delaying the acceptance or rejection of a claim."[31]

Even in *Dunn,* which was discussed in *Bonner,* we find language in support of this point:

> Article 21.55 does not require an insurer to pay every claim within a certain time. It simply requires steps to be taken within a specified time frame....Nothing in the statute suggests that the insurance company could not dispute and deny the claim. Indeed the statute is premised on the presumption that carriers have the right to dispute claims. It merely requires that they do so promptly.[32]

Taking these cases into consideration, it could be argued that the Prompt Payment of Claims Statute is not triggered if the carrier otherwise complies with all of the statutory deadlines by acknowledging receipt of the claim and timely advising the insured if they have accepted or rejected the claim. Reasons must be specified for any delay in payment. The claim must then be paid on a timely basis after judgment. The question then is: when must payment be made? Must it be paid within five business days of the entry of the judgment? Can the carrier delay payment by stating that it will make payment if the insured obtains a judgment establishing liability and underinsured status? Can the insurer rely upon the statement by the Court in *Brainard* that payment must be made within 30 days of entry of judgment? Unfortunately, the answers to these questions have not been given to us by the Court. In *Brainard,* the 21.55 claim had been severed out. In *Norris* and *Nickerson,* it does not appear that a claim under 21.55 was raised as a point on appeal.

Question 4: Are bad faith claims now eliminated for UIM cases?

In ascertaining whether or not there has been a breach of the covenant of good faith and fair dealing, the Texas Supreme Court has held that:

> An insurer has a duty to deal fairly and in good faith with its insured in the processing and payment of claims. A breach of the duty of good faith and fair dealing is established when: (1) there is an absence of a reasonable basis for denying or delaying payment of benefits on other policy and, (2) the carrier knew or should have known that there was not a reasonable basis for denying the claim or delaying payment of the claim. The first element of this test required an objective determination of whether a reasonable insurer under similar circumstances would have delayed or denied the claimant's benefits. This assures that a carrier will not be subject to liability for an erroneous denial of a claim, as long as a reasonable basis for the denial of the claim exists.[33]

More recently, the Supreme Court held that the statutory standards and common law bad faith standard regarding the breach of the duty of good faith and fair dealing are the same. *See Mid-Century Ins. Co. v. Boyte*.[34]

Therefore, exposure may exist in regards to common law bad faith or statutory Insurance Code[35] claims where liability is found on the contract. In order to be successful on such a claim, however, it must be shown that the insurer delayed payment of a claim after its liability became reasonably clear. The current requirement that the liability of the underinsured motorist be established and that the third party's underinsured status be determined as well will certainly strengthen the insurer's position that there was a bona fide coverage dispute. Bona fide coverage disputes, standing alone, do not demonstrate bad faith.[36] Based upon the holding in *Brainard,* there generally can be no breach of contract if the insurer timely pays the claim after the entry of a judgment establishing liability on the part of the underinsured motorist and assessing damages.[37]

Question 5: Has the Court tacitly agreed that punitive damages are not covered by a UIM policy?

In *Brainard*, Trinity had argued that a UIM carrier was only obligated to pay those damages which the insured was legally entitled to recover "because of bodily injury or property damage." Trinity had also suggested the Brainard's interpretation of the UIM endorsement would result in all damages assessed against the underinsured motorist being covered. Trinity then pointed out that several courts of appeals have held that UIM insurance does not cover punitive damages. In *Brainard,* the Supreme Court chose to comment on that analysis. One of the cases discussed in the *Brainard* opinion was *State Farm Mutual Automobile Ins. Co. v. Schaffer*.[38] In *Schaffer,* the Court had conducted an analysis of the legislative intent behind article 5.06-1(5) of the Insurance Code. In *Schaffer,* it was concluded that the legislative intent was to "protect conscientious motorists from financial loss caused by negligent financially irresponsible motorists."[39]

In *Brainard,* the court stated that UIM insurance is compensatory in nature. Prejudgment interest was held to be additional compensatory damages for the insured's bodily injury and, therefore, would be covered under UIM insurance. Because of the lengthy discussion of *Schaffer* and the characterization of prejudgment interest as additional compensatory damages, it appears that the Supreme Court is, in fact, tacitly telling us that punitive damages will not be covered under a UIM policy.

OTHER RECENT CASES OF INTEREST: ARE BYSTANDER/MENTAL ANGUISH CLAIMS COVERED?

We learned in *Trinity Universal Ins. Co. v. Cowan,*[40] that a claim for mental anguish was not a "bodily injury" and, therefore, would not be a covered claim under a liability policy. Since the language in the standard auto policy provides coverage for "bodily injury," a bystander bringing a UIM claim seeking recovery of mental anguish damages alone would not be covered. *See Southern Farm Bureau Casualty Ins. Co. v. Franklin.*[41] Also see earlier opinions cited in *Miller v. Windsor Ins. Co.*[42] which held that claims for mental anguish and loss of consortium by one not involved in the accident, standing alone, are not bodily injuries and, therefore, are not covered losses.

HIT AND RUN CASES

Elchehimi v. Nationwide Ins. Co.[43] involved an appeal of a summary judgment granted to Nationwide on a UIM claim. On appeal, Elchehimi had argued that the facts surrounding the collision were sufficient to meet the "actual physical contact" requirements of the UIM

Statute.[44] In *Elchehimi*, the insured vehicle was struck by an axle with attached wheels which broke away from a tractor trailer traveling in the opposite direction on a divided highway. The Waco court recognized that the San Antonio Court of Appeals had previously held that the "actual physical contact" requirement was not met when a component of a semi-trailer had detached immediately before striking an insured vehicle. *See Smith v. Nationwide Mutual Ins. Co.*[45] The Waco court sought to distinguish the San Antonio court's opinion by stating that the court had not given "adequate weight to the distinction between cargo which has fallen from an unidentified vehicle and an integral part of an unidentified vehicle which strikes an insured's vehicle in an unbroken chain of events."[46] We, therefore, have two divergent opinions on whether or not the actual physical contact requirement will have been met. Under *Elchehimi*, two requirements will need to be met: (1) a showing that the collision and resulting damages were caused by an integral part coming off an unidentified vehicle; and (2) a temporal proximity requirement; *i.e.*, there can be no intervening force to break the chain of causation.

As pointed out by the dissent in *Elchehimi*, a "host of questions" is now left by this opinion. If the reasoning in *Elchehimi* is adopted, courts will be faced with questions such as "What portion of a vehicle will be sufficient to constitute an 'integral part' of a vehicle so as to satisfy the actual physical contact test?" The *Elchehimi* case appears to be suspect, as a separated component from a vehicle cannot meet the definition of "vehicle." In a "hit and run" situation, our UM statute requires actual physical contact with a motor vehicle, not a component which is no longer part of that vehicle.

UNDERINSURED CLAIMS MADE AFTER PAYMENT OF LIABILITY LIMITS

In *Jankowiak v. Allstate Property & Case. Ins. Co.*[47] an insured was allowed to seek UM benefits after collecting the liability limits under the same policy. The Jankowiaks alleged in their suit that both drivers were at fault, and Allstate did not dispute this point in their summary judgment. After conducting a search of the legislative history of the UIM statute, the Houston 14th Court of Appeals determined that the statute was silent on combining coverages. This suggested that the insuring agreement should be analyzed to determine the issue. Both the liability and UM portions of the Allstate policy contained the following language:

> The limit of liability shown in the Declarations for 'each person' for bodily injury liability is our maximum limit of liability for all damages for bodily injury sustained by any one person in any one motor vehicle accident... This is the most we will pay regardless of the number of ... claims made...or vehicles involved in the accident.

Allstate claimed that it had satisfied both its liability and UM bodily injury obligations when it tendered its $25,000 limit. The court disagreed with Allstate because the "maximum limit of liability" language was repeated throughout the policy for each coverage. The court stated that a more reasonable interpretation of the offset language in the policy was that its purpose was to prevent a double recovery. Therefore, the amount of damages recoverable was reduced by the payments that were made, but the policy limits available under the UM coverage were not reduced by the payment made under the liability portion of the same policy.

The court also found the earlier opinion in *Hanson v. Republic Insurance Company*[48] was unpersuasive. *Hanson,* of course, involved a reverse situation, where UIM benefits were paid first and the carrier claimed that no liability payment could be due under the liability portion of the policy. The Houston 1st Court of Appeals agreed with Republic.

The typical Texas auto policy contains the following statement in the UM portion of the policy: "any payment under this coverage to or for a covered person will reduce any amount that person is entitled to recover for the same damages under the liability coverage of this policy." Following the logic in *Jankowiak*, if a UM payment is made to a passenger in a case where both drivers are at fault, and then a liability claim is subsequently made by the same claimant against the insured driver, the amount recoverable under the liability portion of the policy (the total damages) will be reduced by the amount of payment under the UIM coverage. *Hanson* states that this may not occur.

We already know that by law and by statute, under the UIM portion of an auto policy, the amount of actual damages is reduced by liability payments.[49] Once again, the deduction is taken from damages and not from the limits. *Jankowiak* takes this one step further, by holding that the source of the liability payment is not relevant, even when it is made under the same policy from which UIM benefits are being sought.

The holding in *Jankowiak* will not apply to a situation where the insured driver is solely at fault. By definition, an underinsured vehicle does not include a vehicle

owned by or furnished for the regular use of the insured. Therefore, where the liability policy limits are insufficient to cover passengers' claims against the insured driver, there is no recourse under the UIM portion of the same policy. If *Jankowiak* is followed, an insured will still be precluded from recovering UIM benefits for the damages which are attributable to the negligence of the operator of the insured's vehicle, except in circumstances where the third party tortfeasor's negligence exceeds 50 percent.[50]

CONCLUSION

Although the Texas Supreme Court resolved what had been some rather pressing questions as to UIM coverage, it is clear that many questions regarding this coverage remain unanswered. The recent decisions in *Brainard*, *Nickerson* and *Norris* did not involve article 21.55 of the Insurance Code[51] or "bad faith" claims. The holding in *Elchehimi*, if followed by other courts, will lead to further appellate court activity until the conflict raised by that decision is resolved. *Jankowiak* has already resulted in many claims, which carriers thought had been resolved, being reopened due to the assertion of UIM claims after liability limits have been paid. It is hoped that the author's analysis of these questions will give some guidance to practitioners in this area of insurance law.

... it is clear that many questions regarding this coverage remain unanswered.

[1] Article 5.06-1 TEX. INS. CODE (Vernon Supp. 2006).

[2] *Brainard v. Trinity Universal Ins. Co.* 50 Tex. Sup. Ct. J. 271 (Tex. December 22, 2006).

[3] *State Farm Mut. Auto. Ins. Co. v. Nickerson*, 50 Tex. Sup. Ct. J. 268, (Tex. December 22, 2006).

[4] *State Farm Mutual Automobile Ins. Co. v. Norris*, 50 Tex. Sup. Ct. J. 269, (Tex. December 22, 2006).

[5] *Cavnar v. Quality Control Parking, Inc.*, 696 S.W.2d 549 (Tex. 1985). *Cavnar* has now been superseded in part by statute. *See* Tex. Fin. Code §304.102 "a judgment in a wrongful death, personal injury, or property damage case earns prejudgment interest."

[6] Brainard's widow and five children were parties to the wrongful death suit.

[7] *See In re Trinity Universal Ins. Co.*, 64 S.W.3d 463 (Tex..App.-Amarillo 2001, orig. proceeding).

[8] 83 S.W.3d 877 (Tex. App.-Eastland 2002, pet. denied).

[9] *State Farm Mut. Auto. Ins. Co. v. Nickerson*, 130 S.W.3d 487, 489 n.2 (Tex. App.-Texarkana 2004), *rev'd*, 50 Tex. Sup. Ct. J. 268, 2006 WL 3754824 (Tex. December 22, 2006).

[10] *Norris v. State Farm Mut. Auto. Ins. Co.*, 2004 WL 811722 (Tex. App.-Waco 2004)(not designated for publication), *rev'd*, 50 Tex. Sup. Ct. J. 269, 2006 WL 3751580 (Tex. December 22, 2006).

[11] 177 S.W.3d 893 (Tex. 2005).

[12] The standard auto policy contains a provision which stands for the same proposition, absent express consent to the suit, any judgment obtained against the tortfeasor is not binding upon the carrier when it is not joined as a party to the suit.

[13] *See* fn. 3 in *Norris*. State Farm avoided liability for payment of attorney fees because a take nothing judgment had been entered against Norris and, hence, there had been no presentment of the "just amount owed" on the day of judgment.

[14] 17 S.W.3d 652 (Tex. 2000).

[15] *Id.* at 652.

[16] *Id.* at 653.

[17] *See Leal v. Northwest Nat. County Mut. Ins. Co.*, 846 S.W.2d 576 (Tex. App.-Austin 1993, no writ) and *Olivas v. State Farm Mut. Auto. Ins. Co.*, 850 S.W.2d 564 (Tex. App.-El Paso 1993, writ denied).

[18] 177 S.W.3d 893 (Tex. 2005.)

[19] *Id.* at 907-08.

[20] Since written notice of the accident was required in order for prejudgment interest to begin to accrue, the Court found that the earliest date in the record showing written notice of the accident was when State Farm had received a narrative from a physician.

[21] In *Brainard* this was held to be the date suit was brought against the underinsured motorist on January 19, 2000. Trinity was not joined as a party until an amended petition was filed on October 30, 2000. The record does not tell us when Trinity first received written notice of the accident. It is presumed that a different trigger date could apply if the insured were to bring a "new" suit against the insurer instead of bringing the carrier into the underlying action against the underinsured tortfeasor.

[22] Former article 21.55 is now codified under Section 542.051, *et. seq.* of the Insurance Code.

[23] 51 S.W.3d 289 (Tex. 2001).

[24] 991 S.W.2d 467 (Tex. App.-Tyler 1999, pet. denied).