Insurer's Duty to Settle: Understanding and Working with Stowers Issues

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A *Stowers* cause of action is a negligence claim that arises when a third party claimant offers to settle a disputed claim within the policy limits and the insurer refuses to settle. *G.A. Stowers Furniture Co. v. American Indemnity Co.*, 15 S.W.2d 544, 547 (Tex. Comm'n App. 1929, holding approved). If a jury finds that a person of ordinary care and prudence in the insurance company's position would have accepted the settlement offer, the insurance company's refusal of such an offer is negligent and the insurance company is liable for the judgment that exceeds the policy limits. *Id.*

A. *Stowers* History

The *Stowers* doctrine was born on a "dark, rainy night" in 1920 when Mamie Bichon drove into the side of a parked furniture truck. *G.A. Stowers Furniture Co. v. Bichon*, 254 S.W. 606, 609 (Tex. Civ. App.—Galveston 1923, writ dism'd w.o.j.) ("That appellee was injured . . . on a dark, rainy night . . . is shown by the undisputed evidence."). Bichon sued Stowers Furniture Company for leaving its delivery truck, disabled after its own collision with a wagon, on the side of the road "without a light and without any one to watch it." *G.A. Stowers Furniture Co.*, 15 S.W.2d at 545. Bichon initially sought $20,000 in damages, but later offered to settle her claim for $4,000. American Indemnity had issued an auto insurance policy covering Stowers Furniture Company, with policy limits of $5,000. American Indemnity refused Bichon's offer and proceeded to trial. The jury rendered a verdict in Bichon's favor and awarded damages, including interest and costs, totaling just over $14,000. American Indemnity tendered the policy limits of $5,000, but refused to pay the excess. Stowers Furniture Company subsequently paid the full amount of the judgment and sued American Indemnity.

American Indemnity argued that it could only be responsible up to its $5,000 policy limit. Stowers Furniture Company argued that because the claim could have been settled within policy limits, the insurer should pay the entire judgment. The Texas Commission of Appeals agreed with Stowers Furniture. The court found that because the terms of the policy gave American Indemnity exclusive control of the case, including settlement, it owed a duty of ordinary care to Stowers Furniture in deciding whether to accept a settlement offer. *Id.* at 547. The court based this broad principle on the insurer's nearly exclusive control of the suit against its insured:

> [T]he indemnity company had the right to take complete and exclusive control of the suit against the assured, and the assured was absolutely prohibited from making any settlement, except at his own expense, or to interfere in any negotiations for settlement or legal proceeding without the consent of the company....Certainly, where an insurance company makes such a contract; it, by the very terms of the contract, assumed the responsibility to act as the exclusive and absolute agent of the assured ... and, as such care and diligence which an ordinarily prudent person would exercise in the management of his own business.

Id. at 547. Thus the *Stowers* doctrine was born – an insurer could thereafter be liable to pay

more than its policy limits for refusing to settle a claim that a reasonable insurer would have settled.

B. Evolution of the *Stowers* Doctrine

Far from being a static rule of law, the *Stowers* doctrine has expanded and contracted over the years as courts have grappled with its elements and limits. At its core, *Stowers* requires only that an insurance company accept reasonable demands within the policy limits, but over its 80-plus years it has sometimes been held to include more expansive but less defined duties, such as the duty to negotiate, the duty to solicit demands, or the duty to investigate. *See Chancey v. New Amsterdam Cas. Co.*, 336 S.W.2d 763, 764-65 (Tex. Civ. App.—Amarillo 1960, writ ref'd n.r.e.) (holding that duty to settle includes duty to negotiate). In its modern form, the more expansive duties are no longer a part of the doctrine.

The most significant, albeit short-lived, expansion of the *Stowers* doctrine occurred in *Ranger County Mutual Ins. Co. v. Guin*, 723 S.W.2d 656 (Tex. 1987). *Guin* extended the duty to settle "to the full range of the agency relationship." The Supreme Court refused an argument that an offer to settle within policy limits was a prerequisite to a *Stowers* breach, holding instead that the *Stowers* duty included the duty to investigate, prepare for the defense of the lawsuit, trial of the case, and to make reasonable attempts to settle. *Id.* at 659. Following *Guin,* the appellate courts adopted and applied the more expansive view of the *Stowers* doctrine *Guin*. *See e.g., USAA v. Pennington*, 810 S.W.2d 777 (Tex. App.—San Antonio 1991, writ denied); *Wheelways Ins. Co. v. Hodges*, 872 S.W.2d 776 (Tex. App.—Texarkana 1994, no writ).

The Texas Supreme Court retreated from *Guin*'s expansive interpretation of the *Stowers* doctrine in *American Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842, 847 (Tex. 1994). The *Garcia* court rejected the proposition that *Stowers* included the duty to investigate, defend the lawsuit and make reasonable attempts to settle, labeling *Guin*'s contrary holding as dicta and holding that evidence about claim investigation, trial defense and conduct during settlement negotiations was "necessarily subsidiary to the ultimate issue" of the reasonableness of the demand." *Id*. at 849. The *Garcia* court found that the only duty imposed on insurers is that they are "required to exercise that degree of care and diligence which an ordinarily prudent person would exercise in the management of his own business in responding to settlement demands within policy limits." *Id.* at 848. The Texas Supreme Court recently reaffirmed that the *Stowers* duty is limited to accepting a reasonable settlement offer within policy limits, and rejected the contention that it includes a more expansive duty of reasonable negotiation and participation in settlement. *Mid-Continent Ins. Co. v. Liberty Mut. Ins. Co.*, 236 S.W.3d 765, 771, 776 (Tex. 2007); *see also St. Paul Fire & Marine Ins. Co. v. Convalescent Services, Inc.*, 193 F.3d 340, 343 (5th Cir. 1999) (concluding that *Garcia* "drastically curtailed the broad language" in *Guin*).

II. Elements Necessary to Trigger a *Stowers* Duty

The *Stowers* duty is triggered when a claimant makes a settlement demand on the insured that satisfies the following:

1) the claim is within the coverage of the policy;

2) the settlement demand is for policy limits or for a sum certain within the available policy limits; and

3) the settlement demand is reasonable; that is, it is on terms that an ordinarily prudent insurer would accept based on the insured's potential exposure to greater liability.

See Rocor International, Inc. v. National Union Fire Insurance Co., 77 S.W.3d 253, 262 (Tex. 2002); *Texas Farmers Insurance Co. v. Soriano*, 881 S.W.2d 312, 314 (Tex. 1994); *American Physicians Insurance Exchange v. Garcia*, 876 S.W.2d 842, 848-49 (Tex. 1994).[1]

A. The Claim Against the Insured Must Be Within the Scope of Coverage

The *Stowers* duty arises only when a claim is covered under the policy. *G.A. Stowers Furniture Co.*, 464 S.W.2d at 547; *see also St. Paul Fire & Marine Ins. Co. v. Convalescent Services, Inc.*, 193 F.3d 340, 343 (5th Cir. 1999). *Stowers* does not extend to a demand of policy limits for uncovered claims. *Convalescent*, 193 F.3d at 343. An insurer has no contractual or implied duty to settle a claim that is not covered under the policy. *Garcia*, 876 S.W.2d at 848; *Abe's Colony Club, Inc. v. C&W Underwriters, Inc.*, 852 S.W.2d 86 (Tex. App.—Fort Worth 1993, writ denied); *United Services Automobile Assoc. v. Pennington*, 810 S.W.2d 777, 783 (Tex. App. – San Antonio 1991, writ denied); *Stroman v. Fidelity & Cas. of New York*, 792 S.W.2d 257, 261 (Tex. App.—Austin 1990, writ denied); *see also HVAW v. American Motorists Ins. Co.*, 968 F. Supp. 1178 (N.D. Tex. 1997). Likewise, under common law, an insurer generally has no obligation to settle a third-party claim against its insured unless the claim is covered under the policy. *Rocor Int'l, Inc. v. Nat'l Union Fire Ins. Co. of Pittsburgh, P.A.*, 77 S.W.3d 253, 261 (Tex. 2003); *Farmers Tex. County Mut. Ins. Co. v. Griffin*, 955 S.W.2d 81, 82 (Tex. 1997). Accordingly, when there is no coverage under a policy, there is no duty to settle a claim against the insured for policy limits. *Id.*; *Emscor Mfg., Inc. v. Alliance Ins. Group*, 879 S.W.2d 894, 909 (Tex. App.—Houston [14th Dist.] 1994, writ denied).

When the claim asserts both covered and non-covered claims, there is an added level of complexity. The Fifth Circuit has held that the *Stowers* duty does not require the insurance company to consider non-covered claims. *St. Paul Fire & Marine Ins. Co. v. Convalescent Services, Inc.*, 193 F.3d 340, 343 (5th Cir. 1999). In *Convalescent*, the plaintiffs asserted a medical negligence claim that included a request for punitive damages that was specifically excluded from coverage. St. Paul rejected a demand of $250,000 that was well within its limits. The jury found negligence and gross negligence, and awarded $380,000 in actual damages and $850,000 in punitive damages. St. Paul paid the actual damages, but refused to pay the excluded punitive damages. The Fifth Circuit held that although *Stowers* permitted an insurer to be liable for amounts in excess of the limits, it did not extend the actual coverage of the policy, so St. Paul could not be liable for the non-covered punitive damages award. *Id.* at 343. It also rejected the insured's argument that the demand had been limited

[1] For a *Stowers* case to be actionable, the judgment must exceed the policy limits. *See, e.g., Hernandez v. Great American Ins. Co.*, 464 S.W.2d 91 (Tex. 1971).

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