AN UPDATE ON RECENT INSURANCE COVERAGE DECISIONS

THE POLICYHOLDERS' PERSPECTIVE

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I. *Yorkshire Insurance Co., Ltd. v. Seger*, 2013 WL 3821748 (Tex. App.—Amarillo July 19, 2013, pet. filed)

On July 19, 2013, the Amarillo Court of Appeals issued an important ruling touching on two long-standing principles of Texas insurance law: the *Stowers* doctrine and the application of *Gandy*. *See Yorkshire Ins. Co., Ltd. v. Seger*, 2013 WL 3821748 (Tex. App.—Amarillo July 19, 2013, pet. filed).

A. Background Facts

The facts surrounding the underlying lawsuit that led to *Seger* are extensive. The lawsuit arises out of the death of a man in 1992 while working on an oil rig owned by Diatom Drilling Co., L.P. The man, Randall Jay Seger, did drilling work for both Diatom and Employer's Contractor Services, Inc. ("ECS") and, on the day in question, he was employed by ECS and providing services to Diatom. Diatom was insured by a Lloyd's of London-type commercial general liability insurance policy at the time of the accident, and the subscribing insurers were notified of the accident. Then, after Seger's parents filed suit against Diatom, its partners, and ECS, the Insurers were notified, but they ultimately refused to provide a defense, "contending that Randall's death was not a covered occurrence and that Diatom failed to provide timely notice of suit." *Id.* at *1.

Seger's parents made two policy-limits settlement demands and then a $250,000 settlement demand, but all them were refused by the Insurers. The underlying lawsuit proceeded to trial after the plaintiffs non-suited all the defendants except for Diatom. At the trial, Diatom's principal, Cynthia Gilliam, was subpoenaed to attend and did attend as a witness, but she did not appear in a representative capacity on behalf of Diatom. According to the court of appeals, her participation was consistent with that of a witness and not a party. Diatom was not represented by counsel in any way. After the trial, the court entered judgment in favor of each parent to the tune of $7.5 million plus interest.

Thereafter, Gilliam contacted Diatom's Insurers about satisfying the judgment, but she did not receive a response. Accordingly, Diatom assigned its rights against the Insurers to the Segers (save and except for the right to recover Diatom's attorneys' fees incurred in defending the underlying suit). The Segers then filed a *Stowers* action against the Insurers for their wrongful failure to settle the underlying case within policy limits.

The Segers ultimately settled with all the Insurers except Yorkshire and Ocean Marine. By way of pretrial summary judgment, the trial court found that the parties in the underlying suit were in a "fully adversarial relationship" and that the proceeding was a "trial." Thus, all that remained to be determined in the *Stowers* case was the Insurers' negligence, causation and damages. The court ordered a directed verdict on damages based on the underlying judgment and submitted the other issues to the jury, which returned a verdict in favor of the Segers. *Id.* at *2. In the court of appeals' first bite at the case, the court agreed that the underlying plaintiffs had made a sufficient demand within policy limits. However, the court reversed the judgment in all other respects and remanded the case for a new trial. *Id.*

On retrial, the case was submitted to a jury. "Based on the jury's findings, the trial court entered a judgment that recites that the Segers' claims were covered by the CGL insurance policy, and that the underlying judgment was the result of a fully adversarial trial and, therefore, establishes the Segers' damages as a matter of law." *Id.* Each parent was awarded more than $35 million, which was the current amount of the previously issued underlying judgment. *Id.* The Insurers then appealed again, raising seven issues. The court of appeals addressed only the first issue, which it found to be dispositive, and that issue was that the evidence was legally and factually insufficient to establish that Diatom was damaged by the insurers. *Id.*

B. A "Fully Adversarial Trial"

According to the Insurers, the Segers' only evidence of their damages was the underlying judgment that had been issued. However, because that judgment was not obtained through a fully adversarial trial, the Insurers argued that was insufficient evidence of the damages. *Id.* at *3 (citing *State Farm Fire & Cas. Co. v. Gandy*, 925 S.W.2d 696, 714 (Tex. 1996)). In response, the *Segers* contended that, under *Evanston Insurance Co. v. ATOFINA Petrochemicals, Inc.*, 256 S.W.3d 660, 671–72, 674 (Tex. 2008), the *Gandy* requirement of a fully adversarial trial is inapplicable where an insurer wrongfully fails to provide a defense to its insured or wrongfully denies coverage.

Addressing the *ATOFINA* decision, the Amarillo Court of Appeals noted that the Supreme Court in *ATOFINA* discussed the effect of *Gandy* on another of its decisions, *Employers Casualty Co. v. Block*, 744 S.W.2d 940, 943 (Tex. 1988), where the Court held that an insurer cannot challenge the reasonableness of a settlement amount as part of an agreed judgment if the insurer wrongfully denied coverage. The Court ultimately held that *Gandy* did not apply to the settlement agreement in *ATOFINA* because of two key distinctions: (1) there was no assignment; and (2) there were no *Gandy* concerns. More specifically, ATOFINA had not assigned its claim against Evanston to anyone and sued Evanston directly. As to the concerns raised in *Gandy*, the Court found that preventing insurers from litigating the reasonableness of a settlement shortens a dispute rather than extending it, and no risk of distorting litigation or settlement motives existed because, at the time of the settlement, ATOFINA did not know whether coverage ultimately would exist or not. Thus, *Block* was applied to bar Evanston from challenging ATOFINA's settlement agreement and found *Gandy* wholly inapplicable.

Relying on that holding, the Segers argued that the Insurers could not challenge the underlying judgment because they failed to defend Diatom and denied coverage. The Amarillo Court of Appeals disagreed, however, concluding "that the arrangement between Diatom and the Segers does not meet *ATOFINA's* exception to *Gandy*." *Seger*, 2013 WL 3821748 at *5. First, Diatom had assigned its rights against its Insurers to the Segers so, unlike in *ATOFINA*, that key factual predicate of *Gandy* existed. *Id.* Second, the concerns of *Gandy* also were present because the assignment by Diatom specifically was made to prolong the litigation and allow the Segers to pursue the Insurers, as Diatom was judgment-proof and each of its principals had been non-suited. *Id.* Moreover, the assignment also distorted the litigation. "Because neither Diatom nor its principals had any financial exposure in the underlying trial, unlike ATOFINA, Diatom had no incentive to contest its liability or to attempt to limit the assessment of damages after it was found liable." *Id.* (citations omitted). Moreover, as assignee of the *Stowers* claim, the Segers had to argue that they would not have recovered more than policy limits against Diatom if Diatom

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