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Gandy/Seger - Assignments / Actual Trials

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I. INTRODUCTION

Very few topics in the area of insurance have created or caused as much confusion as the actual trial requirement. One only has to look at the plethora of cases attempting to interpret the requirements of an actual trial to understand the difficulty that both insurers, insureds, attorneys and judges have had in understanding and applying this document. In most cases, where the issue is raised in coverage and/or bad faith litigation, one side will latch on to one line of cases and argue that these cases support the proposition that there is or is not an actual trial requirement while the other side will latch on to a separate line of cases arguing just the opposite. The question to be addressed in this article is whether the cases truly are that confusing and inconsistent. Many of the cases cited are from the Texas Supreme Court. In order for these cases to be that inconsistent, the supreme court would normally have to take positions in one case that were contrary to its earlier cases. This is not the case. Rather, like many issues in law, this issue is sensitive not only to the particular facts of the case, but also sensitive to the public policy to which the courts are trying to provide support. This paper will attempt to examine the cases focusing on the actual trial requirement and provide some guidance and logic to them.

II. ACTUAL ISSUE

In trying to create a framework for these cases, the first issue that must be examined is what is the actual issue being addressed by the court? Is the actual issue a question of law, i.e., what is the measure of damages in these cases? Or rather, is the issue an evidentiary issue, i.e., what evidence can be admitted and what evidence cannot be admitted on the issue of damages which are sustained by the insured? One of the earliest cases to address this issue was *Hernandez v. Great American Insurance Company of New York*, 464 S.W.2d 91 (Tex. 1971). *Hernandez* was technically a decision determining whether Texas would cling to the prepayment rule. However, the court noted that the existence of the judgment itself resulted in some injury to the insured. In that case the court treated the existence of the judgment as evidentiary which could be considered by the jury.

The next case to address this issue was *Montfort v. Jeter,* 567 S.W.2d 498 (Tex. 1978). One of the issues in the case was whether there was evidence of damage on the part of the plaintiff. When the defendant was arguing that the plaintiff had failed to present sufficient evidence of damages, the court held that:

> [T]he existing judgment against Montfort is some evidence of actual damages. Therefore, the court of civil appeals erred in holding that there was no evidence to support the jury finding of actual damages.

In essence, the supreme court in Montfort held that the existence of a judgment, though not conclusive, was some evidence of damages. Again the court viewed the issue as an evidentiary one.

It was against this backdrop that the court in *State Farm Fire & Cas. Co. v. Gandy*, 925 S.W.2d 698 (Tex. 1996) was decided. In *Gandy* there was an assignment with agreement not to execute in return for an agreed judgment. The question before the court of appeals was whether the agreed judgment was going to be binding as some evidence of damages. The supreme court in Gandy held:

> In no event, however, is a judgment for plaintiff against defendant, rendered without a fully adversarial trial, binding on defendant's insurer or admissible as evidence of damages in an action against defendant's insurer by plaintiff as defendant's assignee.

The court in *Gandy* again treated the issue as an evidentiary one, holding that under these circumstances not only was the judgment not binding, it was not even admissible in evidence as evidence of damages on the part of the insured.

The most recent case where the Texas Supreme Court to address this issue is *Evanston Ins. Co. v. Atofina Petrochemicals, Inc.,* 256 S.W.3d 660 (Tex. 2008). In *Atofina,* there was no judgment but rather a settlement. The court held that the settlement was admissible as evidence of damages and that the factors relating to trust worthiness, etc., in *Gandy* were not applicable in this case.

Based upon the foregoing cases from the supreme court, it is apparent that the court has consistently treated this issue as an evidentiary one. There is no hard and fast rule that applies in every single case. Another common thread, the court has adhered to factors on indicia of reliability to determine whether the judgment or settlement is binding and/or admissible.

One of the primary sources of confusion as evidenced in many opinions is the distinction between the evidentiary requirement of an actual trial that was imposed by *Gandy* versus the condition contained in most liability policies requiring an actual trial or a settlement agreed to by the company. One goes to the admissibility of the damage evidence; the other goes to whether there has been a breach of the policy by the insured. With respect to the condition actual trial notice, Texas courts and federal courts applying Texas statutory case law long and consistently have held that an insurance company cannot insist upon compliance with the "actual trial" condition within its insurance contract where the insurer has breached its duty to defend. *Scottsdale Ins. Co. v. Sessions*, 331 F. Supp. 2d 479, 488 (N.D.Tex. 2004); *Gulf Insurance Company v. Parker Products, Inc.*, 498 SW 2d 676, 679 (Tex. 1973); *see also Pioneer Casualty Company v. Jefferson*, 456 SW 2d 410 (Tex.App.—Houston [14th Dist.] 1970, writ ref'd n.r.e.) (finding that where the insurer refused to defend and the insured's attorney appeared at trial to admit liability on behalf of the insured who did not appear at the bench trial, witnesses were sworn and the trial court heard evidence and rendered judgment in favor of a third person, and all tendered testimony was in the record, judgment arose from "actual trial" and noting that an insurer who wrongfully refuses to defend its insured is barred from insisting upon compliance with the actual trial requirement.)

Likewise, with respect to the condition actual trial, there is a prejudice requirement. As a general rule, the failure of the insured to comply with the condition does not relieve the insurer from liability unless it was prejudiced by the noncompliance. *Harwell v. State Farm Mut. Auto. Ins. Co.*, 896 S.W.2d 170, 174 (Tex. 1995); *see also Texas Farmers Ins. Exchange v. Curosky*, 2015 WL 4043278 (Tex.App.—Fort Worth 2015).

A careful reading of the *Gandy* opinion demonstrates that in *Gandy*, the supreme court was not dealing with the condition actual trial. Rather, the court was dealing with a new requirement that was being imposed by this decision. The operative language from the *Gandy* decision states that:

> In no event, however, is a judgment for plaintiff against defendant, rendered without a fully adversarial trial, binding on defendant's insurer or admissible as evidence of damages in an action against defendant's insurer by plaintiff as defendant's assignee.

The issue in *Gandy* was not whether there had been a breach of a contract or breach of the conditions—rather, the issue was what was going to be admissible in as later suit by the insured or its assignee against the insurer.

Unfortunately, many courts have confused the two issues. However, they are distinct. One goes to breach of contract by the insured. The other goes to admissibility of evidence in a case by the insured or its assignee against the insurer.

III. POLICY ISSUES TO BE ADDRESSED

The resolution of the *Gandy/Seger* actual trial issue involves the resolution of competing policy interests by the courts. On the one hand, there is the policy interests that favors the insured. If the insurer denies coverage, the insured is left to its own devices. To require that the insured get permission of the insurer to settle or even to go through a full-blown trial in certain instances is unrealistic. In many cases, the insured does not have the assets to provide for its own defense and must make do as best it can with the circumstances.

On the other side of the equation is the public policy interest regarding the integrity of the legal system. These public policies were explored in great length by the court in the *Gandy* decision. The court there noted in many instances, the result is to make things appear as they really are not. The court was concerned about transparency not only on their part, but also on the judicial system. In some instances where there has been no breach of the policy by the insurer, the court is also concerned about preserving the right of contract. Because all circumstances are not the same, there is no one solution that fits every single circumstance. The supreme court has refrained from instituting a black-and-white rule but rather has focused on indicia of reliability regarding the settlement/trial. When dealing with a case involving the actual trial requirement, it is critical that the lawyer and/or judge pay specific attention to the facts and circumstances of the particular case. There are several factors that must be addressed when making this inquiry. A change in as little as one of these factors may result in a different outcome.

IV. FACTORS TO BE CONSIDERED:

A. Was there a breach of the policy?

One of the most important considerations in determining whether there has been an actual trial is whether there has been a breach of the policy. If there has been, then the needle moves toward the end of the

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