Insurer's Duties to Defend and Indemnify: Texas

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A Q&A guide to an insurer's duties to defend and indemnify claims and losses in Texas under commercial general liability (CGL) policies. This Q&A addresses state laws, court cases, and customs that impact the duties to defend and indemnify, when the duties are triggered and what they encompass, the scope of the duties, notice requirements, policy interpretation, defense and attorneys' fees, and duration.

Answers to questions can be compared across multiple jurisdictions (see Insurer's Duties to Defend and Indemnify: State Q&A Tool).

General

1. How does an insurer's duty to defend differ from the duty to indemnify in your jurisdiction? Specifically, please discuss:

- What the duties to defend and indemnify generally encompass.

- Whether the duty to defend is broader than the duty to indemnify.
- What the basis is for the duties to defend and indemnify. Is it contract law, common law, or statute?
- When each duty is triggered and when it arises.
- Whether the insured must tender the defense to the insurer and whether the insurer has the right to control the defense.

The duty to indemnify and the duty to defend are "distinct and separate duties" under Texas law:

- **The duty to indemnify.** The facts actually established in the underlying suit, whether by judgment or settlement, control the duty to indemnify.
- **The duty to defend.** The factual allegations in the complaint in the underlying suit, read together with the insurance policy, control the duty to defend (see When the Duties Are Triggered and When They Arise: Duty to Defend).

(*D.R. Horton-Tex., Ltd. v. Markel Int'l Ins. Co., Ltd.*, 300 S.W.3d 740, 743-44 (Tex. 2009); see *Pine Oak Builders, Inc. v. Great Am. Lloyds Ins. Co.*, 279 S.W.3d 650, 656 (Tex. 2009).)

As a general rule, the duty to indemnify cannot arise before a judgment in the underlying suit because facts proven at trial may differ slightly from the allegations in the complaint (*Hartford Cas. Ins. Co. v. DP Eng'g, L.L.C.*, 827 F.3d 423, 430 (5th Cir. 2016) (applying Texas law)).

What the Duties Encompass

In Texas,

- The **duty to defend** generally encompasses the obligation of the insurer to defend any lawsuit brought against the insured that alleges and seeks damages for an event potentially covered by the policy, even if it is groundless, false, or fraudulent, subject to the terms of the policy.
- The **duty to indemnify** generally encompasses the obligation of the insurer to pay all covered claims and judgments against the insured that are actually covered by the policy.

(See *D.R. Horton-Tex.*, 300 S.W.3d at 743.)

Which Duty Is Broader

Texas courts have traditionally considered the duty to defend broader than the duty to indemnify (see *Burlington Ins. Co. v. Tex. Krishnas, Inc.*, 143 S.W.3d 226, 229 (Tex. App.—Eastland 2004, no pet.)). The view comes mostly from the notion

that an insurer may have a duty to defend a lawsuit but may not have a duty to indemnify the insured (*Farmers Tex. Cnty. Mut. Ins. Co. v. Griffin*, 955 S.W.2d 81, 82 (Tex. 1997)).

However, the Texas Supreme Court has stressed that the duty to indemnify is **not** dependent on the duty to defend. They are separate and distinct duties. Therefore, an insurer may have a duty to indemnify its insured even if the duty to defend never arises. (*D.R. Horton-Texas*, 300 S.W. 3d at 741; see *Colony Ins. Co. v. Peachtree Const., Ltd.*, 647 F.3d 248, 254 (5th Cir. 2011).)

Basis for the Duties

Under Texas law, the basis for the duty to defend centers on:

- The allegations in the pleadings.
- The language of the insurance policy.

(*D.R. Horton-Tex.*, 300 S.W.3d at 743-44; see *Pine Oak Builders*, 279 S.W.3d at 654.)

The duty to indemnify, however, is determined by the actual facts eventually ascertained in the underlying lawsuit (*D.R. Horton-Tex.*, 300 S.W.3d at 744).

When the Duties Are Triggered and When They Arise

For purposes of triggering, which gives rise to the duties to defend and indemnify, US courts have taken either:

- **An "actual injury" or "injury-in-fact" approach** where the insurer must defend any claim of physical property damage that occurred during the policy term.
- **A "manifestation rule"** that imposes a duty to defend only if the property damage became evident or discoverable during the policy term.
- **An "exposure rule"** triggering coverage if the plaintiff is exposed to whatever agent ultimately results in property damage during the policy term.
- **A "continuous" approach** where the insurer must defend any claim of physical property damage from exposure to whatever agent ultimately results in property damage up to the time when the damage became evident or discoverable, if it did so during the policy term.

(*Don's Bldg. Supply, Inc. v. OneBeacon Ins. Co.*, 267 S.W.3d 20, 25-28 (Tex. 2008).)

In *Don's Bldg. Supply*, the Texas Supreme Court held that under an occurrence-based commercial general liability policy, an injury-in-fact trigger applies (267 S.W.3d at 27 (rejecting manifestation theory as a trigger of coverage)).

Duty to Defend

The duty to defend is established by the terms of the insurance policy. Texas courts compare the policy provisions against the allegations asserted in the third-party complaint regarding the insured to determine if a duty to defend exists. If a claim is potentially covered, the insurer has a duty to defend. (*GuideOne Elite Ins. Co. v. Fielder Rd. Baptist Church*, 197 S.W.3d 305, 310 (Tex. 2006); see *Burlington*, 334 S.W.3d at 219.) This process defines what is referred to as the eight-corners rule (see Question 3: Eight Corners and Extrinsic Evidence).

In applying the eight-corners rule, Texas courts:

- Resolve all doubts regarding coverage in favor of the duty to defend (*King v. Dallas Fire Ins. Co.*, 85 S.W.3d 185, 187 (Tex. 2002)).
- Find a duty to defend even if the allegations in the complaint do not state facts sufficient to clearly bring the case within the policy coverage if a claim potentially comes within the scope of coverage under the policy (*Heyden Newport Chem. Corp. v. S. Gen. Ins. Co.*, 387 S.W.2d 22, 26 (Tex. 1965)).

The duty to defend is **not** affected by:

- The facts ascertained before suit.
- The facts developed in the process of litigation.
- The ultimate outcome of the suit.

(*Trinity Universal Ins. Co. v. Cowan*, 945 S.W.2d 819, 829 (Tex. 1997).)

The duty to defend exists even if allegations in the complaint are fraudulent or groundless (see Question 4).

Duty to Indemnify

Under Texas law, a court generally cannot determine the duty to indemnify until there has been a judgment in the underlying suit. The primary reason for this is that the facts proven at trial may differ slightly from the allegations in the complaint. (*Hartford Cas. Ins. Co.*, 827 F.3d at 430; see *D.R. Horton-Tex.*, 300 S.W.3d at 744.)

The Texas Supreme Court has identified one situation when a duty to indemnify can be resolved solely on the pleadings in the underlying lawsuit: if the same reasons that negate the duty to defend also negate any possibility the insurer ever has a duty to indemnify (*Farmers Tex. Cnty. Mut. Ins. Co*, 955 S.W.2d at 84). In *Griffin*, a plaintiff alleged a drive-by shooting caused injuries, but the insurance policy only covered auto accidents. The court reasoned that no set of facts exist that a party may prove in the underlying lawsuit that may transform the shooting into an accident covered under the policy.

However, an insurer can seldom obtain resolution of the duty to indemnify based on the pleadings in the underlying lawsuit. An insurer generally must wait to resolve the duty to indemnify until after a trial in the underlying litigation. Facts established at trial nearly always determine the duty to indemnify. (*D.R. Horton-Tex.*, 300 S.W.3d at 744-45.)

Unlike the restrictions the eight corners rule applies to the duty to defend, parties may offer extrinsic evidence to prove or negate the insurer's duty to indemnify if either:

- The underlying lawsuit never goes to trial.
- The trial does not develop the facts necessary to determine policy coverage.

(*Peachtree Const.*, 647 F.3d at 254-55; see *D.R. Horton-Tex.*, 300 S.W.3d at 744-45.)

Tendering and Control of the Defense

Most primary CGL insurance policies provide that the insurer has both the right and the duty to defend the policyholder. Accordingly, in Texas, if an insurer has a duty to defend its insured, typically it also has the right to control the insured's defense. The duty to defend, however, only arises after an insured has requested coverage.

Obligation to Request Coverage

An insurer has no duty to defend or indemnify an insured unless the insured forwards suit papers and requests a defense in compliance with the policy's notice-of-suit conditions (see *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Crocker*, 246 S.W.3d 603, 606-10 (Tex. 2008); *Harwell v. State Farm Mut. Auto. Ins. Co.*, 896 S.W.2d 170, 174-75 (Tex. 1995)). Courts reason that notice and delivery-of-suit-papers provisions in insurance policies serve two essential purposes:

- They facilitate a timely and effective defense of the claim against the insured.
- They trigger the insurer's duty to defend by notifying the insurer that a defense is expected.

(*Crocker*, 246 S.W.3d at 608.)

An insurer not only has no duty to defend, but also has no liability under a policy unless and until the insured complies with the notice-of-suit conditions and demands a defense (*Jenkins v. State & Cnty. Mut. Fire Ins. Co.*, 287 S.W.3d 891, 897 (Tex. App.—Fort Worth 2009, pet denied); see *Weaver v. Hartford Acc. & Indem. Co.*, 570 S.W.2d 367, 370 (Tex. 1978)). Therefore, an insured bears the threshold obligation to request a defense to invoke coverage (*Crocker*, 246 S.W.3d at 610).

Right to Control the Defense

Whether an insurer has the right to conduct its insured's defense is a matter of contract, which nearly all insurance policies grant. As part of the duty to defend in the policy, an insurer generally has the right to control the defense of claims against the insured. This right includes the authority to make defense decisions as if it were the client. (*Unauthorized Prac. of Law Comm. v. Am. Home Assur. Co.*, 261 S.W.3d 24, 26, 42 (Tex. 2008).)

The insurer's authority typically includes:

- The authority to select the attorney to defend the claim.

- The ability to make other decisions that are normally vested in the insured as the named party in the case.

(*N. Cnty. Mut. Ins. Co. v. Davalos*, 140 S.W.3d 685, 688 (Tex. 2004).)

Other decisions, for example, may relate to the right to:

- Appoint counsel.
- Determine reasonable claims expenses.
- Control any settlement.
- Determine whether the matter is litigated or arbitrated.

(*Darwin Select Ins. Co. v. Laminack, Pirtle & Martines, L.L.P.*, 2011 WL 2174970, at *3 (S.D. Tex. 2011) (applying Texas law).)

For more information on the right to independent counsel, including potential conflicts of interest, see Question 13.

Duty to Defend: Notice

2. Does the duty to defend require notice of claim or loss by an insured in your jurisdiction? Specifically, please discuss:

- Who may provide notice.
- Who the notice must be delivered to.
- When the insurer has not received notice, but has actual or constructive knowledge of a claim or loss.
- The effect of failure to provide notice.

In Texas, the required notice that generally triggers the duty to defend involves two conditions:

- The service of process on the insured.
- The insured relaying that information to the insurer and requesting a defense.

(*Moreno v. Sentinel Ins. Co., Ltd.*, 35 F.4th 965, 975 (5th Cir. 2022) (applying Texas law).)

Who Can Provide Notice

Notice may typically be provided by:

- The insured.
- A representative of the insured.

The insurer has no duty to determine when or if a party served the insured with process (*Harwell*, 896 S.W.2d at 174; see *Crocker*, 246 S.W.3d 603 at 610 (insurers owe no duty to provide an unsought, uninvited, unrequested, or unsolicited defense)). For example, in *Harwell*, the policy required notice of suit from the insured or its representative. While the insurer had notice of suit, the notice came from another party suing the insured, which the court considered insufficient. (896 S.W.2d at 175.)

Courts examine the policy language closely to determine who has authority on behalf of an insured to provide notice (see *White v. Transit Cas. Co.*, 402 S.W.2d 212, 215 (Tex. App.—Houston 1966, writ ref'd n.r.e.) (notice by attorney was not on behalf of insured for purposes of insurance policy)).

Where there are multiple insureds, written notice by the named insured inures to the benefit of any additional or omnibus insureds if it is timely and sufficient to place the insurer on notice regarding the extent of its possible liability and omnibus coverage under the policy (*Emps. Cas. Co. v. Glens Falls Ins. Co.*, 484 S.W.2d 570, 575 (Tex. 1972)).

If a policy does not specify who can provide notice, Texas courts have recognized exceptions to the general rule requiring only the insured to provide the notice (see *Superior Lloyds of Am. v. Boesch Loan Co.*, 130 S.W.2d 1036, 1037 (Tex. App.—Fort Worth 1939, no writ) (where a mortgagor failed to comply with provisions of automobile collision policy requiring furnishing of notice of loss and proofs of loss, mortgagee of automobile may furnish the proofs)).

Who Must Notice Be Delivered To

An insurance policy generally states to whom an insured must deliver notice of claim or loss for purposes of defense and indemnification. In the absence of that information, any duly authorized agent typically suffices.

Unless stated otherwise in the policy, Texas courts generally consider an insurance broker an agent of the insured, not the insurer (*Duzich v. Marine Office of Am. Corp.*, 980 S.W.2d 857, 865 (Tex. App.—Corpus Christi–Edinburg 1998, pet. denied)). Therefore, reporting a claim to a broker generally does not satisfy providing notice to an insurer.

While the Texas Insurance Code uses the term "broker" throughout, insurance professionals are licensed as agents, not brokers. Whether referred to as agents or brokers, they typically have agreements with insurance companies that define whether they have authority to accept claims. For example, a court found a party's notice to an insurance broker of a lawsuit did not suffice to notify the insurer where the agency agreement between the broker and insurer was silent regarding whether the broker had authority to accept notice of claims on behalf of the insurer. The court also noted that the broker:

- Did not procure the insured's policy directly from the insurer.

- Lacked implied authority to accept notice of claims because claims processing was distinct from policy brokering.

(*Berkley Reg'l Ins. Co. v. Philadelphia Indem. Ins. Co.*, 600 Fed. Appx. 230, 235-36 (5th Cir. 2015).)

A court may estop an insurance company from denying that a broker is its own agent if it finds the broker had implied or apparent authority. For example, a court may treat a broker as the insurer's agent where the broker has a history of transmitting claims or providing notice of claims to the insurer that are later paid by the insurer (see *Duzich*, 980 S.W.2d at 865).

For an insurance agent to have the necessary apparent authority from an insurer, the insurer must confer that apparent authority by committing actions that, either intentionally or negligently, induce a third person to believe the agent to have the claimed authority. A court determines apparent authority by looking to the acts of the insurer, not the agent, to see if those acts are likely to lead a reasonably prudent person using diligence and discretion to suppose that the agent had the purported authority the agent purported to exercise. For example, the insurer must have either:

- Affirmatively held the agent out as having the authority.
- Knowingly and voluntarily permitted the agent to act in an unauthorized manner.

(*Guthrie v. Republic Nat. Ins. Co.*, 682 S.W.2d 634, 637 (Tex. App.—Houston [1st Dist.] 1984, writ ref'd n.r.e.).)

Knowledge of Insurer

Actual Knowledge

In Texas, an insurer need not provide a defense to an insured even though it both:

- Knew of its possible status as an insured.
- Was aware that it had been sued.

(See *Crocker*, 246 S.W.3d at 606-10).)

The court in *Crocker* reasoned that the insured is free to trigger whatever policy it wants. Texas courts do not place a burden on the insurer to presume that the insured desires coverage under its policy. Actual knowledge of the claim against an insured does not equate to actual knowledge of suit against an insured (*Liberty Mut. Ins. Co. v. Cruz*, 883 S.W.2d 164, 165 n.2 (Tex. 1993)).

Constructive Knowledge

In Texas, constructive notice of a claim or loss is generally not sufficient to trigger the duty to defend. For example, Texas courts do not consider the insurer's **knowledge of the claim** against an insured the same as actual **knowledge of the suit**.

A party must provide both, even though an insurer may have constructive knowledge of the latter. (*Cruz*, 883 S.W.2d at 165 n.2; see *Hudson v. City of Houston*, 392 S.W.3d 714, 725 (Tex. App.—Houston [1st Dist.] 2011, pet. denied).)

Failure to Provide Notice

The duty to defend is generally triggered only when an insured has provided timely and reasonable notice to the insurer of the suit or claim according to the policy notification requirements (see Knowledge of Insurer). Texas courts, however, have qualified this right in various contexts by requiring the insurer to prove that the lack of notice prejudiced it (*Fin. Indus. Corp. v. XL Specialty Ins. Co.*, 285 S.W.3d 877, 878 (Tex. 2009); *PAJ, Inc. v. Hanover Ins. Co.*, 243 S.W.3d 630, 631, 636-37 (Tex. 2008)).

Texas courts recognize that often an insurer is not prejudiced at all concerning the untimely notice of a claim (*Hanson Prod. Co. v. Ams. Ins. Co.*, 108 F.3d 627, 631 (5th Cir. 1997) (applying Texas law)). The prejudice requirement is consistent with the general principle that an immaterial breach:

- Does not deprive the insurer of the benefit of the bargain.
- Cannot relieve the insurer of the contractual coverage obligation.

(*PAJ*, 243 S.W.3d at 631.)

Texas courts define prejudice as the loss of a valuable right or benefit (see *Hernandez v. Gulf Grp. Lloyds*, 875 S.W.2d 691, 693 (Tex. 1994)). They have described the loss as suffering a material adverse change in position due to the delay (*Coastal Refin. & Mktg., Inc. v. U.S. Fid. & Guar. Co.*, 218 S.W.3d 279, 288, 296 (Tex. App.—Houston [14th Dist.] 2007, pet. denied)).

Courts generally consider whether a delay prejudices an insurer as a question of fact. They may, however, determine the issue as a matter of law when the material facts are undisputed. (*St. Paul Guardian Ins. Co. v. Centrum G.S. Ltd.*, 383 F. Supp. 2d 891, 902 (N.D. Tex. 2003) (applying Texas law).) For example, a commercial general liability insurer was prejudiced as a matter of law when an additional insured:

- Failed to give notice of a lawsuit.
- Settled a lawsuit without the insurer's consent.

(*Md. Cas. Co. v. Am. Home Assur. Co.*, 277 S.W.3d 107, 117 (Tex. App.—Houston [1st Dist.] 2009, writ dismissed).)

An insurer's actual knowledge of a claim or suit does not preclude a showing of prejudice as a matter of law (*Crocker*, 246 S.W.3d at 609-10; *Jenkins*, 287 S.W.3d at 898).

For information on failure to provide notice relating to the duty to indemnify, see Question 7.

Policy and Complaint Interpretation

3. In your jurisdiction, in determining whether there is a duty to defend, how do courts typically construe the insurance policy and the complaint? Specifically, please discuss:

- How courts resolve ambiguities in the insurance policy.
- Whether courts apply the four- or eight-corners rule and whether they consider extrinsic evidence.
- Whether courts consider amendments to the complaint.

Interpretation of Insurance Policies

The provisions and the language of the insurance policy govern the duty to defend. Texas courts interpret an insurance policy under the well-established rules of contract construction (*Gilbert Tex. Const., L.P. v. Underwriters at Lloyd's London*, 327 S.W.3d 118, 126 (Tex. 2010)). Under the rules of contract construction, a court must interpret every contract both:

- As a whole.
- According to the plain meaning of its terms.

(*Crocker*, 246 S.W.3d at 606; *Don's Bldg. Supply, Inc.*, 267 S.W.3d at 23.)

This means in reviewing the policy language, they should **not**:

- Render any provision meaningless.
- Insert language or provisions the parties did not use or otherwise rewrite private agreements.

(*Gilbert*, 327 S.W.3d at 126; *Crocker*, 246 S.W.3d at 606.)

Courts try to determine the parties' true intent as expressed by the plain language used in the insurance policy (*Gilbert*, 327 S.W.3d at 126; *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. CBI Indus., Inc.*, 907 S.W.2d 517, 520 (Tex. 1995) (per curiam)). Courts consider "plain meaning" the watchword for contract interpretation, which means:

- The contract's plain language controls, not what one party or the other alleges they intended to say but did not.
- They assign terms their ordinary and generally accepted meaning unless the contract directs otherwise.

(*Gilbert*, 327 S.W.3d at 126-27; *Crocker*, 246 S.W.3d at 606.)

Policy Ambiguities

In Texas, if a court finds that the language of a policy lends itself to a clear and definite legal meaning:

- No ambiguity exists.
- It can construe the policy as a matter of law.

(*Am. Mfrs. Mut. Ins. Co. v. Schaefer*, 124 S.W.3d 154, 157 (Tex. 2003).)

Texas courts apply the normal rules of contract construction to insurance policies (see Interpretation of Insurance Policies). They do **not** find an ambiguity because a party offers an alternative conflicting interpretation. An ambiguity only exists when the contract is susceptible to two or more reasonable interpretations. (*State Farm Lloyds v. Page*, 315 S.W.3d 525, 527 (Tex. 2010).)

If a court finds the language and terms of the policy ambiguous and susceptible of more than one reasonable interpretation, it generally construes the policy:

- Strictly against the insurer as the drafter.
- Liberally in favor of coverage for the insured.

(*Pioneer Chlor Alkali Co., Inc. v. Royal Indem. Co.*, 879 S.W.2d 920, 929 (Tex. App.—Houston [14th Dist.] 1994, no writ); 45 Tex. Jur. 3d Insurance Contracts and Coverage § 137.)

Eight Corners and Extrinsic Evidence

Under Texas law, an insurer's duty to defend is determined by application of what is referred to as the eight-corners rule (*Richards v. State Farm Lloyds*, 597 S.W.3d 492, 494-95 (Tex. 2020); see *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Merchs. Fast Motor Lines, Inc.*, 939 S.W.2d 139, 141 (Tex. 1997) (per curiam)). Under the eight-corners rule, courts:

- Look to the facts alleged within the four comers of the complaint.
- Measure the facts against the language within the four corners of the insurance policy.
- Determine if the facts alleged present a matter that the insurance policy may potentially cover.

(*Ewing Const. Co. v. Amerisure Ins. Co.*, 420 S.W.3d 30, 33 (Tex. 2014).)

Courts focus on the factual allegations that show the origin of the damages, rather than on the legal theories advanced (*Hartford Cas. Ins. Co.*, 827 F.3d at 426-27). They consider the factual allegations without regard to their truth or falsity (*Ewing Const. Co.*, 420 S.W.3d at 33). The duty arises and remains where any allegation may potentially give rise to a claim

covered by an insurance policy in any proceeding (*Utica Nat'l Ins. Co. of Tex. v. Am. Indem. Co.*, 141 S.W.3d 198, 201-02 (Tex. 2004); *Rhodes v. Chicago Ins. Co.*, 719 F.2d 116, 119 (5th Cir. 1983) (applying Texas law)).

In terms of **burden of proof**:

- The insured bears the burden of showing that the claim against it is potentially within the policy's coverage.
- The insurer bears the burden of establishing that an exclusion in the policy is an avoidance of or **affirmative defense** to coverage.

(*Canutillo Indep. Sch. Dist. v. Nat'l Union Fire Ins. Co.*, 99 F.3d 695, 701 (5th Cir. 1996) (applying Texas law); Tex. Ins. Code Ann. § 554.002.)

Courts must apply the eight corners rule liberally and resolve any doubts in favor of the insured (*Standard Waste Sys. Ltd. v. Mid-Continent Cas. Co.*, 612 F.3d 394, 399 (5th Cir. 2010) (applying Texas law)). The eight-corners rule strictly limits a court's analysis of the duty to defend as it may not:

- Read facts into the pleadings.
- Look outside the pleadings.
- Speculate regarding factual scenarios that may trigger coverage or create an ambiguity.

(*Gilbane Bldg. Co. v. Admiral Ins. Co.*, 664 F.3d 589, 596 (5th Cir. 2011) (applying Texas law).)

The Texas Supreme Court has recognized two exceptions to the eight-corners rule. One exception is that courts may consider extrinsic evidence regarding collusion to make false representations of fact for invoking an insurer's duty to defend (*Loya Ins. Co. v. Avalos*, 610 S.W.3d 878, 882 (Tex. 2020)). The Fifth Circuit, along with federal district and Texas appellate courts, has also made an exception to the strict eight-corners rule in limited circumstances. They have permitted the use of extrinsic evidence only when both:

- It is initially impossible to discern whether coverage is potentially implicated.
- The extrinsic evidence goes solely to a fundamental issue of coverage that does not overlap with the merits of or engage the truth or falsity of any facts alleged in the underlying case.

(*Northfield Ins. Co. v. Loving Home Care, Inc.*, 363 F.3d 523, 529-31 (5th Cir. 2004) (applying Texas law).)

The Fifth Circuit sent a certified question to the Texas Supreme Court regarding whether the *Northfield* exception is "permissible under Texas law." (*Bitco Gen. Ins. Corp. v. Monroe Guar. Ins. Co.*, 846 Fed. Appx 248, 252 (5th Cir. 2021), certified question accepted (Mar. 19, 2021), certified question answered, 640 S.W.3d 195 (Tex. 2022)). The Texas Supreme Court adopted the second exception and held that Texas law permits the *Northfield* exception when the extrinsic evidence:

- Goes solely to the issue of coverage and does not overlap with the merits of liability.

- Does not contradict facts alleged in the pleading.
- Conclusively establishes the coverage fact to be proved.

(*Monroe Guar. Ins. Co. v. Bitco Gen. Ins. Co.*, 640 S.W.3d 195, 201-202 (Tex. 2022); *Pharr-San Juan-Alamo Indep. Sch. Dist. v. Tex. Pol. Subdivisions Prop./Cas. Joint Self-Ins. Fund*, 642 S.W.3d 466, 477 (Tex. 2022).)

Amendments to Complaint

When determining an insurer's defense obligation, Texas courts refer to the allegations in each party's last-filed petition (see *Atl. Cas. Ins. Co. v. Ramirez*, 651 F. Supp. 2d 686, 697 n.2 (N.D. Tex. 2009) (applying Texas law)). If a complaint does not initially state a cause of action under a policy but is amended to state a cause of action under a policy, this gives rise to the duty to defend. Similarly, amendment of a complaint can terminate the duty to defend (*Rhodes*, 719 F.2d at 119).

4. In your jurisdiction, will the duty to defend exist even if allegations in the complaint are fraudulent or groundless?

Under Texas law, the duty to defend does not depend on the truth or falsity of the underlying allegation. An insurer must defend the insured if the facts alleged in the petition, taken as true, potentially assert a claim for coverage under the insurance policy. (*GuideOne*, 197 S.W.3d at 308; see also Duty to Defend).

Therefore, the insurer must defend even if the allegations are:

- Groundless.
- False.
- Fraudulent.

(*Zurich Am. Ins. Co. v. Nokia, Inc.*, 268 S.W.3d 487, 491 (Tex. 2008).)

5. In your jurisdiction, who has the burden of proof in establishing the duty to defend?

Under Texas law, the insured bears the initial burden to establish that its claim falls within the scope of coverage provided by the insurance policy (*KLN Steel Prods. Co., Ltd. v. CNA Ins. Cos.*, 278 S.W.3d 429, 434 (Tex. App.—San Antonio 2008, pet. denied)). If the insured establishes a right to coverage, the burden shifts to the insurer to demonstrate that the claim is

subject to a policy exclusion. If the insurer can establish that an exclusion applies, the burden shifts back to the insured to show that an exception to the exclusion brings the claim back within the terms of the policy. (*Venture Encoding Serv., Inc. v. Atl. Mut. Ins. Co.*, 107 S.W.3d 729, 733 (Tex. App.—Fort Worth 2003, pet. denied).)

6. What are the consequences if an insurer fails to defend a claim that is covered under the policy in your jurisdiction?

An insurer that unjustifiably refuses to defend is liable to the insured for all reasonable and necessary expenses the insured has incurred in conducting the defense (see *Trammell Crow Residential Co. v. Va. Sur. Co., Inc.*, 643 F. Supp. 2d 844, 856 (N.D. Tex. 2008) (applying Texas law)). Reasonable and necessary expenses include:

- Attorneys' fees.
- Court costs and expenses.

For more information on unjustifiable refusal, see Wrongful Failure and Bad Faith. Attorneys' fees incurred involving litigation with a third party are recoverable as actual damages (*Am. Home Assurance Co. v. United Space All., LLC*, 378 F.3d 482, 490 (5th Cir. 2004) (applying Texas law)).

While an insured can recover all reasonable and necessary expenses it has incurred in conducting the defense, an insured generally cannot recover extra-contractual damages. This rule applies where the insured is not entitled to benefits under the policy at issue. (*Republic Ins. Co. v. Stoker*, 903 S.W.2d 338, 341 (Tex. 1995).)

Insurers wrongfully refusing to defend an insured or erroneously denying coverage under a policy also lose the benefit of the policy's procedural protections (*Gulf Ins. Co. v. Parker Prods., Inc.*, 498 S.W.2d 676, 679 (Tex. 1973)). For example, the insurer loses all procedural protections, including the ability to enforce:

- No action clauses.
- No voluntary assumption of liability clauses.

(*Willcox v. Am. Home Assurance Co.*, 900 F. Supp. 850, 856 (S.D. Tex. 1995) (applying Texas law).)

The Texas Prompt Payment of Claims Act (PPCA), which prohibits insurers from delaying the payment of first-party claims, also subjects an insurer to liability when it wrongfully rejects its defense obligations (Tex. Ins. Code Ann. §§ 542.051 to 542.061; *Lamar Homes, Inc. v. Mid-Continent Cas. Co.*, 242 S.W.3d 1, 20 (Tex. 2007)).

A first-party claim is one that:

- Is made by an insured or policyholder under an insurance policy or contract or by a beneficiary named in the policy or contract.
- Must be paid by the insurer directly to the insured or beneficiary.
- Can include defense costs incurred in connection with a third-party liability lawsuit.

(*Lamar Homes, Inc.*, 242 S.W.3d at 17-18.)

An insurer violating the PPCA must pay the insured not only the amount of the claim, but also:

- Interest on the amount of the claim of 18 percent a year as damages.
- Reasonable attorneys' fees.

(Tex. Ins. Code Ann. § 542.060.)

Wrongful Failure and Bad Faith

Processing Claims

The Texas Supreme Court has held that an insurer does not owe its insured a common law duty of good faith and fair dealing to investigate and defend claims by a third party against its insured (*Md. Ins. Co. v. Head Indus. Coatings & Servs., Inc.*, 938 S.W.2d 27, 27-28 (Tex. 1996) (superseded by statute on other grounds)).

Settling Claims

Under the common law, an insurer generally had no obligation to either:

- Settle a third-party claim against its insured unless the claim was covered under the policy.
- Indemnify its insured for a third-party claim on which the insured is not liable.

(See *Rocor Int'l, Inc. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 77 S.W.3d 253, 261 (Tex. 2002).)

The primary common law authority for the duty of an insurer to protect an insured by accepting a reasonable settlement offer is *G.A. Stowers Furniture Co. v. Am. Indem. Co.* (15 S.W.2d 544 (Tex. Comm'n App. 1929)). The Texas Supreme Court has stated that an insured does not activate the *Stowers* duty by a settlement demand unless it meets all the following prerequisites:

- The claim against the insured is within the scope of coverage.

- The demand is within the policy limits.
- The terms of the demand are such that an ordinarily prudent insurer would accept it, considering the likelihood and degree of the insured's potential exposure to an excess judgment.

(*Am. Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842, 849 (Tex.1994).)

If a settlement demand meets those prerequisites, the insurer refuses to pay the policy limits, and a jury returns an amount that exceeds those limits, the insurer may have to pay the entire amount, regardless of the policy limits. This is commonly referred to as *Stowers* liability.

Texas courts have declined to extend the *Stowers* duty to recognize a cause of action for **tortious interference** with a **fiduciary duty** in handling third-party claims (see *Taylor v. Allstate Ins. Co.*, 356 S.W.3d 92, 100 (Tex. App.—Houston [1st Dist.] 2011, pet. denied)).

Apart from the common law, to trigger an insurer's statutory duty to reasonably attempt settlement of a third-party claim against its insured, regarding the law in force at the time, the Texas Supreme Court has held:

- An insurance policy must cover the claim.
- The insured's liability to the third party must be reasonably clear.

(*Rocor Int'l*, 77 S.W.3d at 261.)

The Fifth Circuit, applying Texas law, found a primary liability insurer improperly rejected a settlement offer within the limits of a primary insurer's coverage and was obligated to pay a judgment in excess of its policy limits in a suit brought by the excess liability insurer (*Am. Guarantee & Liab. Ins. Co. v. ACE Am. Ins. Co.*, 990 F.3d 842 (5th Cir. 2021)).

7. In determining whether a duty to indemnify exists, how does your jurisdiction interpret insurance policies? Specifically, please discuss:

- The general rules of contract construction that courts apply.
- How courts handle ambiguities in the insurance policy.
- If courts consider the reasonable expectations of the insured.
- Whether coverage will be denied if the insured does not provide timely notice of a loss or claim.

The provisions and the language of the insurance policy govern the duty to indemnify based on the actual facts determined at trial. For more information about how Texas courts interpret insurance policies, the general rules of contract construction, ambiguities in the insurance policy, and reasonable expectations, see Question 3.

Failure to Provide Timely Notice

Texas courts apply the same general rule of requiring an insurer to show prejudice to the duty to indemnify as they do to the duty to defend (see Question 2: Failure to Provide Notice).

An insured's failure to timely notify its insurer of a claim or suit does not generally defeat the insurer's duty to indemnify unless the delay prejudiced the insurer (*PAJ*, 243 S.W.3d at 636-37). The only exception relates to claims-based policies that require any claim to be reported to an insurer either:

- During the policy period.
- Within a specific number of days after the policy coverage ends.

In this situation, a policy defines the scope of coverage by providing a certain date after which an insurer knows it is no longer liable (*Prodigy Commc'ns Corp. v. Agric. Excess & Surplus Ins. Co.*, 288 S.W.3d 374, 380 (Tex. 2009)).

Outside of claims-based policies, an insurer must prove that a delay was prejudicial. For example, a substantive change in position for an insurer caused by a **default judgment** when an insurer had not received notice from its insured generally renders a default judgment prejudicial. Only before a default judgment can an insurer escape liability if the party filing suit fails to meet its burden of proof. (*Coastal Refin.*, 218 S.W.3d at 287-88.)

For the same reasons an insurer is prejudiced by a default judgment, the Texas Supreme Court recognized that when an additional insured settles a third-party claim made against it without ever notifying its insurer of the claim, the insurer may generally seem to suffer a substantive change in position and be prejudiced as a matter of law (*Md. Cas. Co.*, 277 S.W.3d at 117).

A delay may not be prejudicial where an insured's actions reduce the cost of coverage and damages. For example, the Texas Supreme Court found no prejudice to an excess liability insurer for remediation costs an insured incurred without notice to the insurer. Although the excess insurer did not consent to the remediation and the policy forbade the insured from incurring any expense without the insurer's consent, the court found damage was likely to have worsened and remediation costs would have increased had the insured not proceeded as it did (*Lennar Corp. v. Markel Am. Ins. Co.*, 413 S.W.3d 750, 755 (Tex. 2013)).

Duty to Defend: Scope and Duration

8. In your jurisdiction, is the insurer required to defend against all claims in a suit even if they are not all covered claims (also sometimes referred to as "mixed claims")?

In Texas, if the underlying complaint pleads facts sufficient to create the potential of covered liability, the insurer has a duty to defend the entire case. This is true even if:

- The allegations are demonstrably false, fraudulent, or groundless.
- Some of the injuries alleged:
  - are not covered; or
  - fall within the scope of an exclusion.

(*Zurich Am. Ins. Co.*., 268 S.W.3d at 491 (duty to defend is triggered by inclusion of claims that may be covered).)

However, an insurer has no duty to defend if the insurer can show that all the alleged liability either falls:

- Outside of the scope of coverage.
- Within the scope of an exclusion.

(*Nat'l Cas. Co. v. W. World Ins. Co.*, 669 F.3d 608, 616 (5th Cir. 2012) (applying Texas law).)

Therefore, the general rules are:

- An insured can trigger the duty to defend by a single alleged claim that falls within the scope of the policy coverage.
- An insurer can defeat a duty to defend when all the alleged claims fall outside the scope of coverage, or within an exclusionary provision.

(*Nat'l Cas. Co.*, 669 F.3d at 616.)

9. How is the insurer's duty to defend affected by a reservation of rights letter in your jurisdiction? Please discuss:

- The requirements for a valid reservation of rights letter.
- How a reservation of rights letter differs from a non-waiver agreement.
- Whether an insurer can reserve the right to be reimbursed for defense costs.

- Any relevant statutes and cases in your state.

In Texas, a valid reservation of rights letter allows an insurer to provide a defense to its insured while still preserving the option to later litigate and ultimately deny coverage (*Providence Wash. Ins. Co. v. A & A Coating, Inc.*, 30 S.W.3d 554, 556 (Tex. App.—Texarkana 2000, pet. denied)).

Requirements for a Valid Reservation of Rights Letter

Under Texas law, a reservation of rights letter is a proper action if the insurer believes, in good faith, that a complaint alleges conduct the policy may not cover. A reservation of rights does **not** breach the duty to defend if the letter:

- Sufficiently informs the insured of the insurer's position.
- Is timely.

(*Rhodes*, 719 F.2d at 120; *Providence Wash. Ins. Co.*, 30 S.W.3d at 556.)

While Texas imposes no formal requirements regarding the sufficiency of any reservation of rights letter, the key to be effective, like with any legal document, is to avoid ambiguity and clearly state the nature of the insurer's position. Texas courts have historically construed any purported reservation of rights strictly against the insurer and liberally in favor of the insured (see *Farmers Tex. Cnty. Mut. Ins. Co. v. Wilkinson*, 601 S.W.2d 520, 523 (Tex. Civ. App. 1980, writ ref'd n.r.e.), abrogated on other grounds by *Ulico Cas. Co. v. Allied Pilots Ass'n*, 262 S.W.3d 773, 787 (Tex. 2008)).

Texas courts interpret timely to mean so as not to prejudice the insured (*Providence Wash. Ins. Co.*, 30 S.W.3d at 557; *W. Cas. & Sur. Co. v. Newell Mfg. Co.*, 566 S.W.2d 74, 77 (Tex. App.—San Antonio 1978, writ ref'd n.r.e.)).

When a reservation of rights is made, the insured may properly refuse the tender of defense and pursue its own defense (*Rhodes*, 719 F.2d at 120). However, courts may not bind the insurer to the amount of the agreed judgment or settlement and must allow the insurer to attack their reasonableness (*U.S. Aviation Underwriters, Inc. v. Olympia Wings, Inc.*, 896 F.2d 949, 954-55 (5th Cir. 1990) disapproved of by *State Farm Fire & Cas. Co. v. Gandy*, 925 S.W.2d 696 (Tex. 1996) (applying Texas law)).

Reservation of Rights Versus Non-Waiver Agreement

While a reservation of rights letter is a unilateral document issued by the insurer, a non-waiver agreement is a mutual document between the insurer and the insured. In a non-waiver agreement, the insured acknowledges that the insurer's investigation or defense of a claim against the insured does **not** waive the insurer's right to contest coverage of the claim later.

Non-waiver agreements are generally valid and enforceable in Texas (see *New Amsterdam Cas. Co. v. Hamblen*, 190 S.W.2d 56, 59 (Tex. 1945); *Provident Fire Ins. Co. v. Ashy*, 162 S.W.2d 684, 686 (Comm'n App. 1942)). As the lack of a reservation of rights letter does not waive or estop an insurer from asserting its coverage defenses, the same holds true without a non-waiver agreement (see *Ulico*, 262 S.W.3d at 775-87).

Reserving for Defense Costs

An insurer's unilateral reservation of rights letter cannot create rights that do not exist in the insurance policy. If a right of reimbursement is not created in the policy itself, the only other way an insurer may seek recoupment of defense costs paid towards the defense of noncovered claims is by obtaining the policyholder's "clear and unequivocal consent" to the insurer's right to seek reimbursement. (*Excess Underwriters at Lloyd's, London v. Frank's Casing Crew & Rental Tools, Inc.*, 246 S.W.3d 42, 45-46 (Tex. 2008).)

For more information on the right of recoupment, see Question 14.

10. In your jurisdiction, if there are multiple insurers covering the insured, which one will have the duty to defend? Please also discuss how courts allocate costs when more than one policy is triggered and whether excess carriers ever have a duty to defend.

Under Texas law, the duty to defend creates an obligation equally and concurrently due by all of an insured's insurers. This is because if even a single claim falls within the coverage of a policy, the insurer has a duty to provide a complete defense. (*Trinity Universal Ins. Co. v. Emps. Mut. Cas. Co.*, 592 F.3d 687, 695 (5th Cir. 2010) (applying Texas law).) Where a dispute exists between policies, Texas does not follow the majority rule. For example, if one policy contains a **pro rata** provision and the other an excess provision, Texas courts deem the two provisions mutually repugnant and cancel each other out (*Hardware Dealers Mut. Fire Ins. Co. v. Farmers Ins. Exch.*, 444 S.W.2d 583, 586-90 (Tex. 1969); *St. Paul Mercury Ins. Co. v. Lexington Ins. Co.*, 78 F.3d 202, 210 (5th Cir. 1996) (applying Texas law)).

In Texas, when a continuous occurrence triggers multiple policy periods:

- An insured can maximize its coverage by selecting the coverage period with the highest insurance limit.
- All insurers providing coverage during the multiple policy periods must allocate funding of the indemnity limit among themselves according to their **subrogation** rights.

(*Am. Physicians Ins. Exch.*, 876 S.W.2d at 855.)

11. When is the duty to defend terminated in your jurisdiction? Specifically, please discuss:

- Whether an insurer's tender of policy limits ends the duty to defend.
- Whether the insurer must defend through the finality of the action.

- Whether an insurer's settlement of the third-party claim against the insured terminates the duty to defend.
- Whether the duty to defend is terminated if the insured breaches a provision of the insurance contract.

In Texas, the duty to defend is generally controlled by the language in the insurance policy. Therefore, if the complaint giving rise to the duty changes in a way that eliminates coverage under the policy or the complaint is dismissed, the duty to defend is terminated (see *Consol. Underwriters v. Loyd W. Richardson Const. Corp.*, 444 S.W.2d 781, 784-85 (Tex. App.—Beaumont 1969, writ ref'd n.r.e.); *Travelers Ins. Co. v. Volentine*, 578 S.W.2d 501, 505 (Tex. App.—Texarkana 1979, no writ)). The duty may also terminate, for example, by:

- Reaching the limits of coverage that apply with the payment of judgment or settlement (see Tender of Policy Limits).
- Concluding the underlying lawsuit (see Finality of Action).
- Reaching a settlement (see Settlement of the Third-Party Claim).
- Breaching the contract (see Insured's Breach of Contract).

Tender of Policy Limits

One way for the duty to defend to terminate in Texas is when the insurer tenders the policy limits in payment of a judgment or settlement (see *Am. States Ins. Co. of Tex. v. Arnold*, 930 S.W.2d 196, 201-03 (Tex. App.—Dallas 1996, writ denied)). However, an insurer may not terminate its duty by paying the policy limits into the court or to an excess carrier before judgment or settlement (see *Cont'l Cas. Co. v. N. Am. Capacity Ins. Co.*, 683 F.3d 79, 89 (5th Cir. 2012) (applying Texas law)).

Texas courts recognize that an insurer may properly exhaust policy limits by accepting a settlement demand arising out of multiple claims and inadequate proceeds. The settlement must be reasonable to leave the insured to face the remaining claims without coverage. (*Tex. Farmers Ins. Co. v. Soriano*, 881 S.W.2d 312, 315 (Tex. 1994).)

Finality of Action

The duty to defend continues until:

- The underlying lawsuit is concluded or settled.
- A court determines no coverage under the policy exists.

(*Cont'l Cas.*, 683 F.3d at 89.)

For example, in *Aggreko, L.L.C. v. Chartis Specialty Ins. Co*, a primary carrier:

- Paid its remaining policy limits in a wrongful death action under a Covenant Not To Execute Agreement.
- Withdrew its defense of the insured upon exhaustion of its policy limits.

(942 F.3d 682 (5th Cir. 2019) (applying Texas law).)

Per the Covenant Not To Execute, the primary insurer exhausted its limits in exchange for the plaintiffs' promise not to collect from the insured any future judgment entered in the case. The primary insurer, however, did not obtain a full release of its insured, and the lawsuit continued against the insured to potentially collect under the various layers of excess coverage. The Fifth Circuit Court of Appeals nevertheless held that the Covenant Not To Execute constituted a "settlement" sufficient to relieve the primary insurer of its duty to defend the insured. (*Aggreko*, 942 F.3d at 693-94.)

In some circumstances, the duty to defend includes the duty to file an appeal. Unless an express policy provision states otherwise, an insurer's duty to defend encompasses a duty to appeal an adverse judgment against the insured if reasonable grounds exist to believe that the insured's interest is furthered by the appeal. (*Associated Auto., Inc. v. Acceptance Indem. Ins. Co.*, 705 F. Supp. 2d 714, 724-25 (S.D. Tex. 2010) (analyzing Texas law); *Gibbons-Markey v. Tex. Med. Liab. Tr.*, 163 Fed. Appx. 342, 346 (5th Cir. 2006) (analyzing Texas law) (reasoning that the word "defense" does not relate to only trial of the action)).

Settlement of the Third-Party Claim

In Texas, an insurer is relieved of its duty to defend on the settlement of a third-party claim (*Soriano*, 881 S.W.2d at 315). A settlement, however, need not release all claims against all insureds to terminate the insurer's duties under the policy (*Travelers Indem. Co. v. Citgo Petroleum Corp.*, 166 F.3d 761, 768 (5th Cir. 1999) (applying Texas law); *Arnold*, 930 S.W.2d at 202).

When faced with a settlement demand arising out of multiple claims and inadequate proceeds, an insurer may enter into a reasonable settlement with one of the several claimants even though the settlement exhausts or diminishes the proceeds available to satisfy other claims (*Soriano*, 881 S.W.2d at 315).

Insured's Breach of Contract

An insurer in Texas is not relieved of liability by the failure of the insured to comply with a condition precedent in the policy. An insurer seeking to escape liability must instead establish that the failure to comply with the condition caused it to be prejudiced. (See *Cruz*, 883 S.W.2d at 165.)

The prejudice requirement is consistent with the general principle that an immaterial breach:

- Does not deprive the insurer of the benefit of the bargain.
- Cannot relieve the insurer of the contractual coverage obligation.

(*PAJ*, 243 S.W.3d at 631.)

Texas courts define prejudice as the loss of a valuable right or benefit (see *Hernandez*, 875 S.W.2d at 693). They have described the loss as suffering a material adverse change in position due to the delay or other breach (*Coastal Refin.*, 218 S.W.3d at 288, 294, and 296-98).

12. In your jurisdiction, when, if ever, are insurers permitted to withdraw their defense?

In Texas, the duty to defend ends when the covered portion of a petition or complaint is effectively dismissed by way of an amendment (see *Volentine*, 578 S.W.2d at 505 (holding insurer must defend until it can confine the claims to a recovery that the policy did not cover)).

Defense and Costs

13. In your jurisdiction, does an insured have the right to independent counsel?

In Texas, if an insurer has a duty to defend, the insurer also has the right to:

- Control the defense.
- Select counsel.

(*Unauthorized Prac. of Law Comm.*, 261 S.W.3d at 26; see *Davalos*, 140 S.W.3d at 688.)

For more information on the right to control the defense and what that includes, see Question 1: Right to Control the Defense.

An insurer may use staff attorneys to defend a claim against an insured, rather than a private firm, only if the insurer's interest and the insured's interest are congruent, which means:

- Their interests are aligned in defeating the claim.
- No conflict of interest exists between the insurer and the insured.

(*Unauthorized Prac. of Law Comm.*, 261 S.W.3d at 26-27.)

The insurer's right to appoint counsel only gives way when a disqualifying conflict of interest exists (*Davalos*, 140 S.W.3d at 688). Where a conflict exists, insureds may select their own, independent counsel (*Rx.com v. Hartford Fire Ins. Co.*, 426 F. Supp. 2d 546, 559-60 (S.D. Tex. 2006) (analyzing Texas law)).

A disqualifying conflict of interest exists where the facts to be adjudicated in the liability lawsuit are the same facts on which coverage depends. Adjudicated for purposes of this analysis means to rule on judicially. (*Davalos*, 140 S.W.3d at 688-89.) The Texas Supreme Court has not offered further clarity on:

- What is meant by *Davalos*' "same facts" requirement.
- How the requirement is to be applied.

Unless an insurer defends unconditionally, rather than under a reservation of rights letter, examples of a disqualifying conflict include:

- The existence of coverage.
- The scope of coverage.

(*Davalos*, 140 S.W.3d at 689.)

Therefore, broadly speaking, under Texas law, a conflict of interest exists that prevents the insurer from insisting on its contractual right to control the defense when both:

- The insurer has reserved its rights.
- The facts to be adjudicated in the liability lawsuit are the same facts on which coverage depends.

(*Davalos*, 140 S.W.3d at 688-89.)

However, reservation of rights letters do not necessarily create a conflict between the insured and the insurer. A reservation of rights letter instead only recognizes the possibility that a conflict may arise in the future. Otherwise, every disagreement about how the insurer conducts the defense may result in relinquishing that right. (*Unauthorized Prac. of Law Comm.*, 261 S.W.3d at 40.)

14. In your jurisdiction, can an insurer recover defense costs that are spent defending uncovered claims?

Most jurisdictions permit the insurer to recover defense costs when the insurer has:

- Timely and explicitly reserved its right to recoup the costs from the insured.
- Provided specific and adequate notice of the possibility of reimbursement.

For more information on the right to reserve defense costs, see Question 9: Reserving for Defense Costs.

In Texas, however, an insurer cannot issue a unilateral reservation of rights letter and reserve rights that do not exist in the insurance policy (*Matagorda Cnty.*, 52 S.W.3d at 131). If a right of reimbursement is not created in the policy itself, the only other way an insurer may seek recoupment of defense costs paid towards the defense of noncovered claims is by obtaining the policyholder's "clear and unequivocal consent" to the insurer's right to seek reimbursement (see *Frank's Casing*, 246 S.W.3d at 45-46).

Also, "other insurance" or "pro rata" clauses, which operate to ensure that each insurer is not liable for any greater proportion of the loss than the coverage amount in its policy bears to the entire amount of insurance coverage available, may restrict an insurer's ability to recover all defense costs. For example, a co-insurer paying more than its contractually agreed-on proportionate share:

- Does so voluntarily (without a legal obligation to do so).
- Cannot recover the excess from the other co-insurers.

(*Mid-Continent Ins. Co. v. Liberty Mut. Ins. Co.*, 236 S.W.3d 765, 772 (Tex. 2007).)

Duty to Indemnify: Causation

> 15. Do courts in your jurisdiction require a duty to indemnify if a loss has multiple causes, one or more of which is excluded from coverage? Please address whether a policy exclusion is effective whether or not there is any causal connection between the excluded risk and the loss.

An insurance policy may be drafted to specifically exclude coverage for losses with multiple causes or for concurrent causation. Otherwise, jurisdictions generally follow one of two approaches:

- **Efficient proximate cause rule**, which permits recovery under a policy for a loss caused by a combination of a covered risk and an excluded risk if the covered risk was the efficient proximate cause of the loss.
- **Concurrent cause rule**, which permits recovery under a policy for a loss caused concurrently by a combination of a covered risk and an excluded risk.

In Texas, courts apply the concurrent cause rule, but limit the application of the rule by requiring that the concurring causes be independent of each other for an insurer to have a duty to indemnify a party. An insured can only recover that portion of the damage caused solely by the covered loss. (*Wallis v. United Servs. Auto. Ass'n*, 2 S.W.3d 300, 302-03 (Tex. App.—San Antonio 1999, pet. denied.)

For example, where a vehicle accident was proximately caused both by a party's failure to stop in time and another party's negligence in maintaining the brakes, which contributed to the party's inability to stop, an insurer had no duty of indemnification. The negligent maintenance and negligent operation of the vehicle were not separate and independent causes of the accident. (*Bituminous Cas. Corp. v. Maxey*, 110 S.W.3d 203, 215 (Tex. App.—Houston [1st Dist.] 2003, pet. denied).)

This approach is consistent with Texas law requiring damages recited in either a judgment or a settlement to be apportioned between claims covered and not covered by a policy. The burden of apportioning damages between covered and non-covered claims rests on the insured (*Willcox*, 900 F. Supp. at 856).

Duty to Indemnify: Scope

16. Discuss whether your jurisdiction permits insurance companies to provide coverage and indemnification for:

- Punitive damages.
- Intentional damage or injury.

Punitive Damages

In Texas, insurance companies may provide coverage and indemnification for **punitive damages** if they pass a two-step analysis applied by Texas courts:

- The plain language of the insurance policy must cover the punitive damages sought in the underlying suit.
- The public policy of Texas must allow coverage in the circumstances of the underlying suit. Courts determine public policy by:
    - first looking to express statutory provisions regarding the insurability of punitive damages to see whether the legislature has made a policy decision; and
    - absent an explicit legislative policy decision, by considering the general public policies of Texas.

(*Fairfield Ins. Co. v. Stephens Martin Paving, LP*, 246 S.W.3d 653, 655 (Tex. 2008).)

Courts determine coverage on a case-by-case basis depending on the severity of the underlying facts (see *Stephens Martin Paving*, 246 S.W.3d at 655, 660 (public policy did not exclude coverage for punitive damages in the context of a workers' compensation policy)). However, where a policy broadly obligated an insurer to indemnify an insured for all liability imposed on it by law, a federal court applying Texas law found that necessarily included both punitive and actual damages, which did not violate the public policy of Texas (*Ridgway v. Gulf Life Ins. Co.*, 578 F.2d 1026, 1029-30 (5th Cir. 1978)).

If an insured engages in particularly egregious conduct, at least one court applying Texas law held that it was against Texas public policy to insure that conduct (see *Am. Int'l Specialty Lines Ins. Co. v. Res-Care, Inc.*, 529 F.3d 649, 662-64 (5th Cir. 2008) (requiring the insured to bear the costs of punitive damages resulting from extreme conduct)).

Intentional Injury

The standard CGL policy contains an exclusion applicable to Coverage A for either of the following expected or intended from the standpoint of the insured:

- Bodily injury.
- Property damage.

Under Texas law, when determining the applicability of the intentional acts exclusion, courts focus on the insured's intent to cause the injury. The exclusion applies to intentionally caused injuries, not to intentional acts. (*State Farm Fire & Cas. Co. v. S.S.*, 858 S.W.2d 374, 377 n.2 (Tex. 1993)). Courts infer an intent to injure as a matter of law when a sufficiently great degree of certainty exists that the character of the act done will cause injury and that, therefore, the actor intended to do so. They are more likely to make this inference as a matter of law the more likely harm can result from the conduct. (*Com. Underwriters Ins. Co. v. Royal Surplus Lines Ins. Co.*, 345 F. Supp. 2d 652, 663 (S.D. Tex. 2004), order clarified, No. CIV.A. H-03-2922, 2004 WL 2733667 (S.D. Tex. Nov. 10, 2004) and aff'd sub nom. *N. Am. Specialty Ins. Co. v. Royal Surplus Lines Ins. Co.*, 541 F.3d 552 (5th Cir. 2008) (applying Texas law).)

17. How does your jurisdiction view policy provisions that limit coverage if the insured has other insurance available?

A minority of states, including Texas, disregard competing "other insurance" clauses, whether they are pro rata, escape, or excess clauses, and hold both insurers primarily liable. From this minority rule (also known as the "Oregon rule"), a pro rata provision is considered to be inconsistent with an excess provision in another policy and each is irreconcilable and repugnant as to the other, requiring the liability to be pro-rated. Addressing Texas law, the Fifth Circuit Court of Appeals addressed the issue of "other insurance" in *Royal Ins. Co. of Am. v. Hartford Underwriters Ins. Co.* (391 F.3d 639 (5th Cir. 2004)). The Fifth Circuit determined that an escape clause and a pro-rata clause conflict where both carriers are liable proportionally.

Excess Clauses in Primary Policies

The starting point for resolving most "other insurance" disputes is the Texas Supreme Court's decision in *Hardware Dealers Mut. Fire Ins. Co. v. Farmers Ins. Exch.* (444 S.W.2d 583 (1969)). "Other insurance" disputes refer to where an insured may be entitled to indemnification from more than one insurance policy. In *Hardware Dealers*, the Texas Supreme Court discussed the three types of "other insurance" provisions:

- **Pro rata clauses**, which restrict the liability of concurring insurers to an apportionment basis.
- **Excess clauses**, which restrict the liability of an insurer to excess coverage (that pays out only after the primary coverage is exhausted).
- **Escape clauses**, which avoid all liability if additional coverage exists.

Problems arise with these clauses when:

- More than one policy covers the same insured.
- Each policy has an "other insurance" clause that restricts its liability because of the existence of other coverage.

Traditionally, most courts have held that the contract with the escape clause provides primary coverage and the contract with the excess clause provides excess coverage (see ALCICC § 5:4). However, the Texas Supreme Court in *Hardware Dealers*, which involved a conflict between an escape clause and an excess clause, adopted the rule that Texas courts should ignore the conflicting provisions and instead apportion liability pro rata and require both insurers to indemnify (444 S.W.2d at 589-90).

Courts have generally applied the analysis of *Hardware Dealers* only to situations where the "other insurance" clauses directly conflict with one another (see *State Farm Fire & Cas. Co. v. Griffin*, 888 S.W.2d 150, 155 (Tex. App.—Houston [1st Dist.] 1994, no writ) (finding where two insurers have contracted to pay loss and each insurer's policy contains a competing pro rata clause, each insurer is liable to the insured only for its proportion of loss)). However, later Fifth Circuit cases call this conclusion into question (see *St. Paul Mercury Ins. Co.*, 78 F.3d at 209-210; *Royal Ins. Co. of Am.*, 391 F.3d at 643-44).

18. In your jurisdiction, can an insurer deny coverage of a settlement entered into by the insured on the grounds that the settlement was not authorized by the insurer?

Under Texas law, only a material breach of a voluntary payment provision of an insurance policy voids coverage (*Coastal Refin.*, 218 S.W.3d at 294). Otherwise, an insurer must have sustained actual prejudice, as opposed to theoretical or presumed prejudice, to deny coverage (*Coastal Refin.*, 218 S.W.3d at 288-89).

Other Issues

19. Are there any other statutes, rules, cases, or issues in your jurisdiction that insurers or insureds should be aware of in determining whether a duty to defend or duty to indemnify exists?

Number of Occurrences

Under Texas law, courts apply a "cause" analysis to determine whether a set of facts involves one or more "occurrences" for purposes of determining an insurer's limit of liability on its duty to indemnify. Under this analysis, the proper focus in interpreting "occurrence" under a liability policy is on the number of events that cause the injuries and give rise to the insured's liability, rather than the number of injurious effects. (*Lennar Corp. v. Great Am. Ins. Co.*, 200 S.W.3d 651, 682 (Tex. App.—Houston [14th Dist.] 2006, pet. denied), reversed on other grounds by *Gilbert Tex. Const., L.P. v. Underwriters at Lloyd's London*, 327 S.W.3d 118 (Tex. 2010)).

For example, federal courts applying Texas law have held that:

- Workers' injuries were caused by exposure to asbestos at three different work sites that involved three different occurrences (*Fina, Inc. v. Travelers Indem. Co.*, 184 F. Supp. 2d 547, 551-52 (N.D. Tex. 2002)).
- Faulty plumbing caused leaks to a hall bath shower and a master bath shower that involved two occurrences under an insurance policy because they were separate events (*Garza v. Allstate Tex. Lloyd's*, 284 Fed. Appx. 110, 114 (5th Cir. 2008)).
- 124 separate cases of food poisoning over a one-month period all arose from a single "occurrence" (the defendant's allegedly contaminated food), given that the insured restaurant's "ongoing preparation of contaminated food" supported a finding of a single occurrence, even where the exact source of the contamination was unknown (*Travelers Cas. Ins. Co. of Am. v. Mediterranean Grill & Kabob Inc.*, 499 F. Supp. 3d 371, 374-75 (W.D. Tex. 2020)).

In a case examining multiple occurrences from the perspective of a manufacturer of a defective product, a federal court applying Texas law stressed the determining factor is the number of causal events, and not the number of claims and claimants. Therefore, even though 800 water chambers failed multiple parties over a period of time, the injury still arose under one occurrence. (*Nat'l Union Fire Co. of Pittsburgh, Pa. v. Puget Plastics Corp.*, 649 F. Supp. 2d 613, 628-29 (S.D. Tex. 2009), aff'd, 454 Fed. Appx. 291 (5th Cir. 2011).)

