



Legal Beat

By MICHAEL SEAN QUINN

Insurance for Arson

Every once in a while, people deliberately destroy their own property. Occasionally, they fake a theft. Sometimes, they do these things for the insurance money. As often as not, deliberate destruction is accomplished by arson.

Property insurance contracts do not usually explicitly exclude arson, other forms of deliberate destruction, or staged theft. Instead, insurers rely upon the well established Principle of Fortuity which pervades all property insurance and much of liability insurance. According to that venerable principle, insurance is for accidents and not for deliberate acts designed to enrich the insured. Insurance is not a gamble, where you buy the insurance, destroy the property, and then gamble that



the police will not put you in jail.

Lots of problems arise in arson, and similar cases. Special Investigation Units at

insurance companies—aka, “arson squads”—tend to see arson everywhere and veer dangerously towards the view that all insurance claims are phoney. Arson “scientists” are frequently bogus, and fire department investigators are often overworked, inarticulate and poorly trained.

Similar problems arise in theft cases. Recently, a high-end property insurer denied a semi-suspicious claim based on the misbegotten and overly aggressive analysis of a gun-toting, war-loving, cowboy lawyer who was also an ex-cop. This lawyer even tried to resolve the case by threatening criminal prosecution if the insured pressed his claim (but not otherwise). The insurer also (maybe) denied the claim because the policyholder was gay, and the insurer thought he wouldn’t come out of the closet. (Maybe the policy-

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holder's former friend stole the stuff.) The quite conservative jury was unphased. The insurer lost the case and paid bad faith damages in a settlement.

There is another quirky problem that has arisen in the area of arson over the last couple of generations. What should be done when two people insure the same property and one of them destroys it? Obviously, if a deliberate destruction entirely voids the policy, then the innocent coinsured cannot collect. This has never been the law.

For example, mortgagees have always been able to collect, even when the property owner burns down his own house, office building, warehouse, boat or what have you. The law has handled this situation by saying that these two coinsureds are insuring different interests. Sometimes, courts even say that a single insurance policy contains two contracts: one with the named insured and one with the mortgagee.

What must an insurance company do when a husband burns the property, and his wife is entirely innocent?

A more interesting problem arises when spouses own the same property. What must an insurance company do when Husband burns the property, and Wife is entirely innocent? (Interestingly, if there was ever a pattern to be found in reported cases, it is that H burns the property and W does not.) Obviously, H cannot collect insurance money when he torches the family home. Insurance isn't for the arsonist.

The problem has to do with W. If W is entirely innocent, why should she be denied insurance benefits simply because her miscreant husband did a rotten thing? On the other hand, if W gets the money, and is still somehow associated with H, then H is (indirectly or constructively) obtaining insurance proceeds, after he deliberately destroyed the property. That seems unjust and unwise.

In 1986, in *Kulubis v. Texas Farm Bureau Underwriters Insurance Company*, the Texas Supreme Court held that W could collect the insurance proceeds when the property was her separate property. *Kulubis* expressly declined to consider whether the

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same rule would apply to community property. *Kulubis* treated the issue as one of public policy.

Subsequently, courts have permitted W to recover where (1) W has divorced H, and (2) the divorce proceedings make it clear that H is not going to receive any of the insurance proceeds. Usually, this is done by H conveying all of his interest in the community property dwelling to W. (If there is a second fairly strong pattern in arson cases, it is that W divorces H. Frequently, the arson occurs during a pending divorce.)

On the other hand, not long ago, the

Supreme Court acquiesced in a decision by the Fort Worth Court of Appeals in *Kizer v. Chubb*. In that case, W had been found to be entirely innocent, but she had not divorced her husband. The Fort Worth appellate judges were concerned (among other things) with the fact that H would indirectly benefit if W received any money.

Now, finally, in mid-1999, the Texas Supreme Court has held that innocent spouses can "recover insurance proceeds when the other coinsured spouse has intentionally destroyed the covered community property." This decision came in *Texas*

Farmers Insurance v. Murphy, decided on July 1, 1999. One judge concurred in the judgment, though not the reasoning of the opinion, while two judges dissented.

Unlike previous decisions, the majority in *Murphy* based its decision on the language of the insurance policy, as opposed to public policy. The *Murphy* majority laid down the methodological principle that all insurance decisions should be based on contract language, before conflicting public policy considerations are evaluated.

Justice Gonzales, writing for the majority, began by observing that the 1991 "Texas Standard Homeowners Policy-Form B" does not include a clause barring or limiting recovery by others for losses intentionally caused by another insured. Thus contract language does not preclude recovery by W when H burns the house.

Moreover, Justice Gonzales observed that W was divorcing H in this case. However, divorce in partition should not be a necessary condition for W's recovery. Courts of Texas should not be encouraging divorce. Partition is a technical matter that could be fouled up. And besides, "[i]t is not the courts' business to superintend what innocent insureds may do with any insurance proceeds they are contractually entitled to recover."

Therefore, the rule to be preferred allows "innocent spouses to recover according to their contracts, regardless of petition or divorce." Thus, although the Supreme Court acquiesced in *Kizer* only two years ago, that case would have been decided differently, had it been presented to the current court.

The insurance company attempted to avoid coverage upon the grounds that the policy was subject to avoidance if an insured concealed an important fact or made a false statement in the claims process. The majority made short work of this view. Although concealment was pleaded, the insurance company failed to submit a jury issue on it, so the issue was out of the case.

One of the most significant lessons of the *Murphy* case for lawyers is always to get a jury issue on concealment or fraud in any arson case. I would have thought it was already legal malpractice to fail to do so. After all, questions submitted to the jury should follow the pleadings, just as evidence presented to the jury should also track the pleadings.

Justice Hecht merely concurred in the result. He thought that the majority went too far in its reasoning, however. W had argued that she was entitled to recovery because she had obtained a partition. Justice Hecht thought the matter should be put to rest there. In other words, "*Murphy* [the wife] is entitled to recover—on the argument she makes." I am not sure why this

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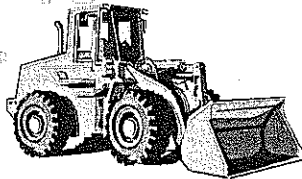
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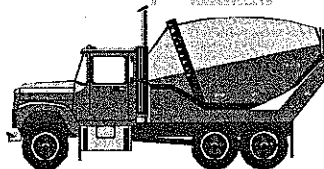
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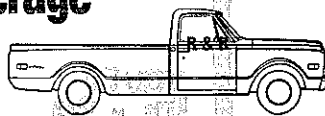
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principle should be true, if the court sees clearly that a different rule works better. One suspects that Justice Hecht wanted to decide the case on the narrowest possible grounds.

Justices Enoch and Owen dissented. The principal reason they dissented was because an arsonist can now profit from his own wrong doing indirectly through payments received by his wife. Moreover, they believed that the majority opinion represented too sharp a departure from the *Kizer* case, in which the Supreme Court acquiesced. In other words, the dissenters rejected

an about-face of the court after so short a time. According to Justice Enoch, "[t]he long-standing public policy of this state is that an arsonist cannot benefit from his or her crime. When a recovery benefits the arsonist's community estate, the arsonist benefits. An innocent spouse cannot avoid the application of this policy by a post-arson partition of the community estate."

The Texas Supreme Court is a conservative one. In general conservative courts are chary of any principle which benefits criminals. So how could they decide *Murphy* as they did? The reason is a deeper property

conservatism. W's interest was her property. It should not be forfeit because of H's conduct. She has a right to payment from the insurer if her property is destroyed by another. Once she has payment, it too is her property. She may not do with it as she sees fit. That is the nature of property. Courts have no business interfering, if she elects to give her money to a criminal. Now that's a full-blooded conception of individual property. Notice that it subtly weakens the idea of community property. ■

Quinn is a shareholder with Sheinfeld, Maley and Kay (Austin) and is currently teaching Insurance Law in the Law School at the University of Texas-Austin.

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Agent Pleads Guilty; Gets Seven-Year Term

Lubbock life insurance agent Gary Nicholas Ronck has pleaded guilty to charges that he stole \$1.6 million from an Austin woman, now 91, who gave him the money to buy annuities.

Ronck, 51, accepted a seven-year prison term as part of a plea agreement with Travis County District Attorney Ronald Earle's office. Sentencing is scheduled for September 13, 1999. Ronck also agreed to the revocation of his insurance license.

TDI's Insurance Fraud Unit investigated Ronck and turned its evidence over the district attorney's office, which obtained a first-degree felony theft indictment and prosecuted the case.

The Fraud Unit began its investigation after receiving an anonymous written tip that Ronck was using a client's money, possibly in excess of \$1 million, for personal expenses.

Ronck was indicted on charges that he stole \$1.6 million from Louise McElroy. The indictment lists seven occasions from December 1993 to March 1997 when Ronck misappropriated McElroy's money. In each case, she wrote checks to his "Senior Financial Services" insurance agency.

McElroy testified in a civil suit that she gave the money to Ronck for annuities. The civil suit against Ronck and several insurance companies seeks recovery of the money allegedly stolen by Ronck. In all, Ronck received about \$6.5 million from her between 1992 and 1997. In most instances, he actually obtained annuities or life insurance for her and received commissions from insurance companies for the sales. But, the indictment alleged, he pocketed \$1.6 million of the money she gave him for the purchase of annuities. ■