



Legal Beat

By MICHAEL SEAN QUINN

An Agent's Nightmare Continues

Editor's Note: This is the second part of a story that appeared in our Sept. 25 issue. The first story described the facts of the case, up to the point of verdict and judgment. This column describes the verdict and judgment and what happened in the court of appeals.

Brief review

The case of *Reyna v. Safeway Managing General Agency*, decided in the San Antonio Court of Appeals on March 31, 2000, portrays an agent's nightmare.

Two insurance agents, a father and daughter, both named Reyna, owned an unincorporated insurance agency. They failed to forward suit papers to an insurance company. Stuff happens.

The insured didn't get a defense from the insurer. He had policy limits of \$40,000. A court entered a default judgment against him

for \$350,000. The insured assigned all claims he might have to the injured plaintiffs, and they sued both the insurer and the agency. The insurer settled with the plaintiffs for \$75,000 before the trial of the insurance case.

There were two lawsuits. First in time there was the underlying tort case. It was an auto accident case possibly involving drunk driving. After that there was a second insurance case. Remember this distinction. It's significant. It is mainly the insurance case that is discussed here.

It is also important to remember that in the underlying tort case, at one point, the parties agreed to set aside the default judgment. The victim-plaintiff successfully reneged on that agreement in that case. Indeed, that breach set up the second case.

Findings, verdict and judgment

In the insurance case, the trial court

found that there was a contract—a "Producer's Agreement"—between the agents and the insurer that required the agents to forward suit papers to the insurer. This finding was beyond dispute.

The jury found that the agents had failed to forward the suit papers, thereby breaching the contract, and that the Producer's Agreement contained an indemnity provision requiring the agents to indemnify the insurer fully if they failed to forward such papers, even if the insurer was relevantly negligent. The jury also found that the insurance agency had breached its fiduciary duties to the insurer and thereby caused injury to it.

On this basis, the trial court held that the insurer was entitled to recover from the agents the \$75,000 it paid in settlement, plus \$8,000 in attorneys' fees. This entitlement was a consequence of the indemnity agreement contained in the Producer's Agreement.

In addition, the jury said that the agents knowingly violated the Deceptive Trade Practices Act in various ways and violated art. 21.21 of the Insurance Code. These findings were based upon evidence that the agents tried to cover-up the fact that they didn't send the suit papers by creating phony

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records. Perhaps, this conduct was also why the jury said the agents breached fiduciary duties to the insurer.

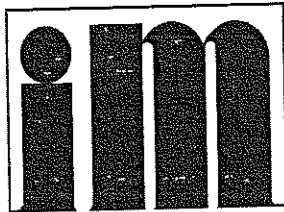
Remember, there were two agents. The jury assessed damages against one of them in the amount of \$10,000 for mental anguish, \$20,000 for the default judgment, and \$50,000 as a penalty for knowing misconduct. It assessed \$15,000 in mental anguish damages against the other agent, \$45,000 for permitting the default judgment to be taken, and \$50,000 for knowing conduct. These damages aggregate to \$190,000.

Finally, the trial court did something very odd. In addition to entering a judgment for the aforementioned damages, it awarded the victims-plaintiffs-assignees nearly \$850,000 on the basis of the default judgment itself. (Much of that sum was prejudgment interest, and some of it was attorneys' fees.)

The appeal

Naturally, the agents appealed. Their appeal was successful in part, and it failed in part. Both the failures and the successes are interesting.

Failed Appeals: From an insurance agent's point of view, there were two significant failures in the appeal. First, the appellate court held, in effect, that the assignment from the insured to the victims of any causes of action



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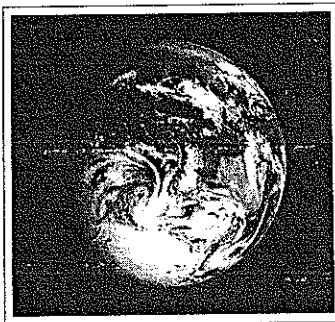


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he might have against the insurer or the agents was a valid assignment. Litigation assignments are invalid when they lead insureds to take positions inconsistent with their natural interests in order to "hook" insurance companies. Set ups often lead to lying, and that dishonors the legal system.

The appellate court said that did not happen here. Offensive assignments from insured-tortfeasors to victim-plaintiffs arise in a different context, according to the court. Sometimes, an insurer defends an insured subject to a reservation of rights. An insured sometimes demands that an insurer defend without any reservation. If an insurer refuses to do so, the insured may demand that the insurer relinquish control of the defense but continue to pay for it.

Sometimes, when this happens, a plaintiff and a defendant engage in a sham trial. The hope is that the defendant will be hit with big damages, which it will never have to pay. Some judges accommodate parties on this score. The defendant won't have to pay them, because the plaintiff has agreed not to pursue collection from him in exchange for an assignment against the insurer. In that circumstance, defendant insureds may be counted upon to take positions contrary to their natural interests. They can be counted upon not to oppose huge damage awards, for example.

The default judgment situation is entirely different. When there is a default judgment, all factual pleadings of the plaintiff are taken to be true, so that the only thing remaining to be proved is the amount of damages. In the default situation, according to the court of appeals, the insured-defendants do not help the plaintiff prove-up damages. As a result, the assignment is not invalid.

So much for the first major appellate failure. The second one pertained to the indemnity proviso in the Producer's Agreement. It is scandalous that these kind of indemnity agreements are imposed upon small economic entities by very large ones. Courts do not go nearly far enough to defend the weaker entities, like neighborhood, father-daughter insurance agencies. The courts do require that such indemnity agreements expressly say that the indemnitor will pay for the indemnitee's negligence. The Reyna's argued that the Producer's Agreement violated this rule.

Unfortunately, the appellate court didn't reach this important, substantive question. It said the error had not been preserved. (A litigant may not challenge the action of a trial court, unless it has explicitly given the trial court a chance to think about the matter first. Such an action is called "preserving error.") Thus, procedure triumphed over substance.

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There was a third appellate failure. The agent complained that the trial court that heard the insurance case should have enforced the agreement made in the underlying tort case to set aside the default judgment. The trial court in the insurance case and the appellate court both refused to do this. They reasoned that the agents were not parties to that agreement, which was enforceable in only two ways. (1) In the underlying tort case, it could have been enforced as a court order, e.g., by setting aside the default judgment. It could not be enforced simply as a court order outside the context of that lawsuit. (2) Since there was an agreement, it could be enforced as a contract outside the underlying litigation. But, the agents were not parties to that contract; nor were they its intended beneficiaries; consequently, they lacked standing to enforce it. The judgment of the trial court in the insurance case could not be reversed because of a breach of an agreement in a previous case.

Appellate successes: The agents had two significant appellate successes. Both involved substantial sums of money.

The first success involved \$75,000. The trial court had failed to give the agents credit for the amount the insurer paid victim-plaintiff-assignees. If the agents had to pay this sum again, there would have been a double recovery. That part of the judgment was therefore reversed. Thus, the obligations of the agents were reduced by \$75,000.

Second, and more importantly, the appellate court reversed the nearly \$850,000 award directly based upon the default judgment. This is the second most interesting feature of this case. The court held that the agent was not liable for the full amount of the default judgment awarded in the tort case, but only for the economic value of that judgment. The jury had found the default judgment to be worth only \$65,000.

Consequently, the face amount of the default judgment, interest, and related damages could not be awarded. By so holding, of course, the appellate court cut the value of the judgment in the insurance case by something approaching ten-fold.

Disappointing denouement

What the court of appeals did was controversial in several ways. There might have been something wrong with the assignment. There might have been something wrong with the indemnity agreement. There might have been something wrong with eliminating the default judgment in the tort case from the judgment in the insurance case. It is not clear the agent breached fiduciary duties it owed the insured. In truth, the opinion of the court of appeals made little sense. Perhaps it was poorly written. Often they are

written by law clerks (now called "Staff Attorneys") who are really just-graduated former law students looking for experience and resume entries.

Naturally, the parties sought review in the Supreme Court of Texas. A really important question was involved. The court of appeals held that the assignment from the insured to his tort victims is valid. It based this holding on the fact that the assignment followed a default judgment. Impliedly, the court distinguished the default judgment situation from the rejected reservation-of-rights situation. I am not inclined to embrace this argument. The argument is especially shaky in the unique facts of the Reyna case where the victim-assignee reneged on an agreement to set aside the default judgment in the underlying tort case.

Alas, the case has now totally fizzled. The agents themselves never had anything like the money it would have taken to pay even the reduced judgment. They were insured by an out of state carrier, moreover. That insurer went into receivership. As a consequence, the receiver's lawyers announced what it would be willing to pay—a paltry sum, one may be sure—and the offer was accepted. In other words, this tantalizingly interesting case was settled as it proceeded through the Supreme Court. Then perhaps the right sum was paid. Perhaps true justice was done amongst the parties.

Now for the most interesting part of the case. A condition of the settlement was that the decision of the court of appeals be reversed by agreement and that the unanimous opinion written by Chief Justice Hardberger never be certified for publication. In effect, the opinion was vacated. Nullified! The case can never be precedent for anything. Question: Who won and who lost? The agents? The insured? The victims?

The public?

In Italy, when the audience does not like an operatic performance, they yell, "Fiasco! Fiasco!" One feels like shouting this at the agents here. If they really tried to cover their negligence with fraud, fakery, forgery and falsification, then they deserve to be pilloried. In Italy, when members of the audience really don't like a performance, they throw soft things: tomatoes, bananas and the like. Of course, we can't do that here to the agents here. That would be battery, and there is no coverage for such conduct. ■

Quinn is an Austin shareholder in the law firm of Sheinfeld, Maley & Kay. He litigates and testifies on insurance related problems and is currently the chair of the Insurance Section of the State Bar of Texas. He also is a Visiting Professor of Law at the University of Texas-Austin.