

## Insurance Litigation Reporter

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### Underinsured Motorist Coverage

UNDER TEXAS LAW, UM/UIM POLICIES COVER PREJUDGMENT INTEREST RECOVERABLE FROM THE MOTORIST-TORTFEASOR, SINCE IT IS A TYPE OF DAMAGE, AND PREJUDGMENT INTEREST IS CALCULATED USING THE "DECLINING PRINCIPAL" FORMULA

*POLICYHOLDERS MAY RECOVER ATTORNEYS' FEES FROM CARRIERS WHICH BREACH UM/UIM INSURANCE CONTRACTS, BUT ONLY AFTER THE TORTFEASOR'S LIABILITY HAS BEEN LEGALLY ESTABLISHED*

***BRAINARD V. TRINITY UNIVERSAL INSURANCE COMPANY***, \_\_ S.W.3D \_\_, 2006 WL 3751572

(TEX. DECEMBER 22, 2006), *STATE FARM MUTUAL AUTOMOBILE INSURANCE COMPANY V.*

*NORRIS*, \_\_ S.W.3D \_\_, 2006 WL 3751580 (TEX. DECEMBER 22, 2006), AND *STATE*

*FARM MUT. AUTO. INS. CO. V. NICKERSON*, \_\_ S.W.3d \_\_, 2006 WL 3754824 (TEX. DECEMBER 22, 2006)

### Cases at a Glance

The governing Texas statute provides that uninsured/underinsured (UM/UIM) policies cover damages recoverable from an uninsured or underinsured tortfeasor. Under Texas law, prejudgment interest is a form of damage. Consequently prejudgment interest for which the tortfeasor would be liable is covered. How to calculate this interest is complicated when there have been some payments, e.g., from the tortfeasor's insurer or from the UM/UIM carrier's policy, say, for PIP. Prejudgment interest is paid only on principal, since prejudgment interest is simple interest and not compounded, i.e., there is no prejudgment interest on prejudgment interest. The policyholder's right to prejudgment interest can begin quite early in the claims process. (The *Brainard* case provides a chart for calculation. Among the three cases, it and *Norris*

concern prejudgment interest, and *Norris* simply follows *Brainard*.)

The same is not true with respect to attorneys' fees. A breaching insurer is liable for attorney's fees under Texas statutes. There can be no right to attorney's fees, however, until the insurance policy-contract has been breached by the carrier. Under Texas law, this cannot happen until the UM/UIM insured obtains a judgment establishing the liability and under insured status of the tortfeasor motorist. All three of the cases listed above discuss the recovery of attorney's fees by insureds from UIM carriers.

### Summary of the *Brainard* Decision

*Facts.* On July 1, 1999, Edward H. **Brainard** II was killed. His vehicle was struck head-on by a rig owned by Premier Well Service, Inc. **Brainard** had a wife and five children. They brought a wrongful death action against Premier and sought UIM benefits from Trinity, under a policy issued to the family business. Trinity timely paid the **Brainard** family ("**Brainard**") \$5,000 under the PIP provision of the policy; with respect to the UIM coverage, however, Trinity asked for further information. **Brainard** alleges this information was submitted and otherwise complied with all condition precedent to receiving benefits but that Trinity never paid.

Trinity was thereafter joined to the wrongful death action as a defendant. The allegations against Trinity were for breach of the insurance contract, common law bad faith, statutory bad faith, violations of the Texas Deceptive Trade Practices-Consumer Protection Act.

*Procedural History.* On December 7, 2000, **Brainard** and Premier settled for Premier's \$1 million liability insurance policy limit. This was Premier's policy limit. Premier was dismissed from the suit. **Brainard** then demanded that Trinity tender the \$1 million UIM policy limit. Trinity countered with an offer of \$50,000. (Keep this in mind. It was a sensible offer, and **Brainard** mistakenly refused it.)

The trial court severed the extra-contractual claims, and the case proceeded to trial on the UIM contract. The jury found that Premier was negligent and that its negligence caused the accident. It awarded **Brainard** \$1,010,000 in actual damages. This award included pecuniary loss, funeral expenses, loss of companionship in society, and mental anguish. The jury also awarded \$100,000 in attorney's fees. There was, of course, no award of punitive damages.

The trial court applied a credit involving the payment by Premier and Trinity's PIP payment. This amounted to \$1,005,000, and signed a judgment against Trinity for \$5,000 in damages plus \$100,000 in attorney's fees.

Both sides appealed. Trinity challenged the attorney's fee award. **Brainard** by cross-appeal alleged that the trial court erred in refusing to award prejudgment interest on the total actual damages of \$1,010,000. The court of appeals reversed with respect to attorney's fees and affirmed with respect to prejudgment interest. *Trinity Universal Ins. Co. v. Brainard*, [153 S.W.3d 508](#) (Tex App.--Amarillo, 200\_\_\_, rvd & rmd in the very case discussed here).

There are disagreements among Texas courts of appeals with respect to both of these points of law. Therefore, Texas Supreme Court granted **Brainard's** petition for review with respect to both of them.

*Prejudgment Interest Recovery.* This issue is partially controlled by [Art. 5.06-1\(5\) of the Texas Insurance Code](#). It mandates that UIM coverage shall apply for payment to the insured of "all sums which he shall be legally entitled to recover as damages from owners or operators of uninsured motor vehicles because of bodily injury[.]" Of course, the amount recoverable is controlled by policy limits, and it is "reduced by the amount recovered or recoverable from the insurer of the underinsured motor vehicle." Given this statute and given what had happened, Trinity did not dispute that it owed \$5,000. The central issue was whether it owed prejudgment interest on all or part of the \$1,010,000 of the actual damages. (Apparently the \$5000 had not been paid. It is difficult to see why not.)

The Texas Supreme Court ruled that Trinity was liable for prejudgment interest. The court's reasoning was straight forward: If prejudgment interest is a species of damage, then it is covered by the statute and, if it is covered by the policy, it is to be paid. The court, in effect, observed that the relevant statutes were clear, that the policy was clear, and that prejudgment interest had been classified as damages for over 20 years.

Trinity opposed this view. It argued that UIM policies required the insurers to pay only those damages which result from bodily injury or property damage. Trinity contended that "the essence of prejudgment interest is compensation for loss of use of money, not damages from bodily injury." Trinity further argued that if the statute created liability for prejudgment interest, it would create liability for "all damages assessed against the uninsured motorist, yet the courts of appeals have held that UIM insurance does not cover punitive damages."

The Texas Supreme Court rejected Trinity's arguments and the main reason for doing so was that its interpretation of the phrase *because of bodily injury* was unacceptably narrow, even if the phrase "because of bodily injury" is somewhat ambiguous. That phrase could mean either (a) *literally derived from bodily injury*, or (b) *as a results of bodily injury*. The court found that the phrase, fairly obviously, means the second of these. In addition, the court noted, "Trinity's rigid reading proves too much, for it would entail splitting hairs even among purely compensatory damages, such as those for mental anguish and loss of society." Furthermore, the relationship between a UIM insurer and the insured is not strictly and solely contractual; it also depends upon some third-parties' tort action. That feature of the relationship triggers the application of Texas's prejudgment interest statutes. If the strictly contractual vision of Trinity applied, the statutes would have no bearing.

*Prejudgment Interest Calculation.* Since Trinity owes prejudgment interest on the judgment against Premier, there are a number of questions. When did it start to run? How did the PIP-coverage payment affect the amount owed? How did the settlement payment from Premier affect the amount owed? How is this passage of time significant?

The parties agreed that there were credits for amounts paid. The only questions were how to calculate the credits. Naturally, different ways were conceptualized, and these different methods favored different parties.

[Texas Finance Code § 304.104](#) provides that in wrongful death cases, prejudgment interest accrues beginning on the earlier of two dates: (a) the 180th day after the defendant receives written notice of the claim or (b) on the date suit is filed. It ends on the day proceeding the date the judgment is rendered. In this case, the earlier of two dates was the date upon which **Brainard** filed suit against Premier, and that was in January 2000. The trial court signed its judgment on January 15, 2003, so **Brainard's** right to prejudgment interest ended on January 14, 2003. Under [§ § 304.103](#) and [304.104](#), prejudgment interest is computed as simple interest with a rate equal to the post judgment interest rate applicable when the judgment is rendered. Here, the trial court's judgment set that rate at 10%.

**Brainard** conceded that her net recovery was reduced by credits from the PIP and the settlement, but she wanted prejudgment interest on the entire

\$1,010,000 *before* applying any credits. She wanted 10% on the sum the jury awarded running from January 19, 2000 until August 29, 2002. Thus, as already stated, according to **Brainard**, the interest is added to the jury verdict before deducting the settlement and PIP credits. Thus, according to **Brainard**, the prejudgment interest calculation is not affected by the credits.

Trinity rejected this theory of calculating prejudgment interest. It argued that **Brainard** should not continue to received interest on the entire \$1,010,000 in damages after the date payments to be credited were made. If the law did otherwise, the plaintiff-insured would continue to earn interest even though she had already received \$1,005,000 in compensation. She would thus receive interest on money already paid, *after* she was paid. Trinity contended this is like being *paid twice* and that this essentially unjust.

The Texas Supreme Court agreed with Trinity. "[C]ompensation other than for loss of money is not interest but a windfall for the claimant and a penalty to the defendant.... [T]o satisfy the purpose of prejudgment interest, settlements must be credited periodically, according to the date they are received. This approach, known as the declining principal "formula, is the proper way to apply credits in the calculation of prejudgment interest." (Internal quotes omitted).

The Supreme Court observed it had already established the framework for resolving this type of issue. See [\*Battaglia v. Alexander\*, 177 S.W.3d 893, 908-09 \(Tex. 2005\)](#). Under the rules of the *Battaglia* case, settlement payments should be credited first to all ready accrued prejudgment interest as of the date the settlement payment is made. They should then be credited to the principal owed, "thereby reducing and perhaps eliminating prejudgment interest from that point in time forward." Thus, each credit establishes a new interval or a new time period for measuring prejudgment interest. During each of these new intervals, "prejudgment interest accrues only on the remaining principal [,]" since prejudgment interest is simple interest and therefore does not compound.

*Attorney's Fees.* In breach of contract cases, when the contract itself does not provide for recovery of attorney's fees, Chapter 38 of the Texas Civil Practices & Remedies Code controls. The relevant section under the conditions of this case is § 38.002, and it required that the claimant prove three propositions: (1) that the insured was represented by counsel, (2) that the insured presented a claim to the insurer, and (3) that the insurer failed to pay the just amount owed within 30 days of the presentation of the claim. Unfortunately,

the statutory word used for the presentation of the claim is "presentment."

The question here is this: What was the date of **Brainard's** presentment to Trinity. There are two possibilities. The first one is the first day upon which the insured presented a claim for UIM benefits. The second is much later "because the insurer's duty to pay does not arise until the underinsured motorist's liability, and the insured's damages, are legally determined."

The Texas Supreme Court opted for the second of these two choices. "[T]he UIM insurer is under no contractual duty to pay benefits until the insured obtains a judgment establishing the liability and underinsured status of the other motorists." Neither seeking UIM benefits from a carrier nor filing suit against the insurer, in the court's analysis, triggers a contractual duty to pay. Without a provable antecedent breach of contract, there can be no attorneys fees. When there is no contractual duty to pay, there is no just amount owed. Thus, under Chapter 38, a claim for UIM benefits is not presented until "a trial court [has] signed a judgment establishing the negligence and under insured status of the other motorist."

Similarly, neither an explicit admission of liability from the underinsured motorist nor a settlement with the underinsured motorist triggers a duty to pay. UIM policies, the court reasoned, are not to be treated like all other types of contracts. UIM contracts are "unique." According to the terms, "benefits are conditioned upon the insured's legal entitlement to receive damages from a third party." Thus, although a litigant like **Brainard** may be entitled to attorney's fees, there is no right to attorney's fees until a determinative judgment is rendered in a trial court. In the **Brainard** case, this rule deprived the insured-plaintiff of any right to attorney's fees.

### **Decision in the *Norris* Case**

This case was decided on the same day as the **Brainard** case. Together with the *Nickerson* case to be discussed presently, the three cases form a team. The **Brainard** case, of course is the captain thereof.

*Facts & Lower Court Proceedings.* Norris was injured in a car accident and sued the other driver. Norris settled with the other driver's insurer for \$40,000 of a \$50,000 policy. He then impleaded his own carrier, State Farm. That carrier paid \$5000 in PIP but never offered to settle the UIM claim.

There was a trial. The jury found the other driver negligent and that Norris had suffered only past damages of \$51,200. It assessed attorneys fees incurred at \$11,500, court of appeal fees at \$5000, and supreme court review fees at \$7500.

The district court applied a \$55,000 credit to the recovery amount--\$50,000 for the other driver's liability policy and \$5000 for the PIP payment from State Farm. It also found that Norris could not recover attorneys fees and so signed a take-nothing judgment.

The court of appeals reversed as to both holdings. It found that Norris was entitled to both prejudgment interest and attorney's fees. The supreme court reversed and found that he was not entitled to attorney's fees but was entitled to prejudgment interest.

*Prejudgment Interest.* Norris gave the same argument **Brainard** used in the first case. State Farm argued that \$55,000 is larger than \$51,200, and so it owes nothing in the way of prejudgment interest. The supreme court rejected both views and applied the "Declining Principal Formula." Unfortunately, the underlying records do not reflect either when the settlement sum was paid or when the PIP was paid. Since this is not known, the Formula cannot be applied. What is certain, however, is that credits accumulated and applied before prejudgment interest begins to run apply to the principal. "Thereafter, each credit will apply first to the accrued prejudgment interest and second to the remaining principal."

Furthermore, Norris wanted prejudgment interest calculated on the whole \$50,000 in the other motorist's policy, and not simply what was not paid. The supreme court rejected this view, since the purpose of prejudgment interest is to--and only to-- compensate a plaintiff for the lack of use of other compensation money which is paid. If the plaintiff is paid a sum, then there is no interest due on that sum. Hence, Norris's right to interest on the \$10,000 remaining in the tortfeasor's auto liability policy did not exist, since he never had a right to that money, having released any claim for it, and so he never lost of the use of it.

*Attorney's Fees.* The supreme court here just follows **Brainard**, and not only reverses the decision in the court of appeals but disapproves a case upon which that court relied. The rule is here written pretty much as follows: A UIM insured may recover attorney's fees from its carrier under the applicable statute--Chapter 38 of the Texas Civil Practices and Remedies Code--"only if the [UIM] insurer

does not tender the UIM benefits within thirty days after the trial court signs a judgment establishing the liability and the underinsured status of the other motorist[,]" and this can happen only if the insured has presented a claim to the carrier. Usually with insurance companies, Chapter 38 imposes liability for attorney's fees if the insurer fails to pay the "just amount owed" within 30 days of the presenting of the claim, i.e., within 30 days of "claim presentment." UIM coverage is different: "there can be no 'just amount owed' until the trial court establishes liability and damages" against the underinsured tortfeasor motorist. That never happened in the *Norris* case. Hence, there was no right to fees.

### **Decision in the *Nickerson* Case**

On the same day the *Branard* case was decided, the Texas Supreme Court decided *State Farm Mutual Auto Ins. Co. v. Nickerson*. This is a very short opinion. The appellate issue in *Nickerson* was attorney's fees. It was a UIM case. Nickerson tried her case against the tortfeasor motorist in 2002. The jury awarded her \$46,000 in attorney's fees *incurred during that trial*.

The issue before the Texas Supreme Court was whether that award of attorney's fees was recoverable under the UIM policy. Given the decision in *Brainard*, the court held that it was not, since the fees were incurred before the fault of the underinsured motorist was determined by the court where the UIM case was pending. Given *Brainard*, it is difficult to see why this case was written upon by the supreme court at all.

### **Comment**

The Texas Supreme Court's ruling on prejudgment interest is a virtually perfect interpretation of statutes and contracts. It could not possibly be wrong, and given the function of prejudgment interest, it is conceptually and philosophically correct.

The court's resolution of the issue of attorney's fees is a bit different, at least philosophically. As an interpretation of the applicable statute, it is probably technically acceptable. From the point of view of social policy, the rule is not a very good idea and should be changed--if necessary, by altering the statute. Since UIM coverage is, according to the court, a unique type of contract, perhaps there should be a special section of the statute for attorney's fees in UM/ UIM cases.

The problem is this. The existing rule creates an incentive for UIM insurers to refuse coverage for as long as possible, to delay adjudication of the tortfeasor status of the underinsured motorist, and to proffer settlements substantially less than what could be adjudicatively determined. Although this was probably not a burden on the Bernard family, given their probable means, it would almost certainly be a burden on most citizens. Thus, when it is obvious that the underinsured motorist is a tortfeasor and when the size of the tort obligation is itself obvious, then attorney's fees should begin accumulating against the UIM carrier. Of course, this is sort of thing for which there must be an independent adjudication, if it is disputed, but this is a better system than the one created by the legal system and then imposed by the court. // **Quinn**

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