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THE TEXAS SUPREME COURT REVERSES EARLIER 7-0 DECISION IN *FRANKS CASING*

On February 1, 2008, the Texas Supreme Court handed down a long awaited decision reversing its earlier ruling in *Excess Underwriters at Lloyd's London et al. v. Franks Casing Crew & Rental Tools Inc.* On rehearing, the Supreme Court held 5-3 that excess insurers that dispute policy coverage, but settle a claim against an insured, do not have a right to reimbursement unless the policyholder's contract specifically provides for reimbursement. This landmark decision has come as a surprise to many, since the reconsideration and reversal of a previously 7-0 ruling is extremely rare.

FACTS OF THE CASE

Frank's Casing built a drilling platform for ARCO. When the platform collapsed, ARCO sued Frank's Casing and several others. Frank's Casing had a \$1 million primary liability policy, and excess coverage up to \$10 million written by several carriers. After Frank's Casing notified Excess Underwriters of ARCO's claims, they issued reservation-of-rights letters asserting that coverage for ARCO's claims was "limited or negated" under the policy's terms.

As trial began, it quickly became clear that Frank's Casing was ARCO's primary target, prompting Frank's Casing's in-house counsel to contact ARCO and request a settlement demand. ARCO responded with a \$7.5 million demand. Frank's Casing forwarded ARCO's demand to Excess Underwriters with a letter suggesting that they should accept. The letter reiterated Frank's Casing's disagreement with their coverage position, and stated that Frank's Casing was looking to Excess Underwriters to fund the settlement.

In their response, Excess Underwriters agreed that the case should be settled, but noted that coverage issues remained. They offered to fund the entire settlement if Frank's Casing would agree to reserve those issues for resolution later. Frank's Casing rejected the proposal.

In response, Excess Underwriters advised Frank's Casing that they would pay \$7.5 million to settle the claim, less any contribution from the primary carrier, and then seek reimbursement from Frank's Casing. Within hours, Excess Underwriters contacted ARCO and orally accepted its settlement offer, and the primary carrier tendered its remaining policy limits of approximately \$500,000. Excess Underwriters subsequently filed suit against Frank's Casing in 1998.

PROCEDURAL HISTORY

Both Frank's Casing and Excess Underwriters filed a series of cross motions for partial summary judgment. The trial court initially granted Excess Underwriters' motions on their right to reimbursement. It also granted their motions for partial summary judgment on coverage, and another concluding that Excess Underwriters was entitled to \$7,013,612 in damages on their reimbursement claim.

In 2000, and before final judgment in the trial court was entered, the Texas Supreme Court issued their opinion in *Tex. Ass'n of Counties County Gov't Risk Mgmt. Pool v. Matagorda County*, 52 S.W.3d 128, 135 (Tex. 2000), declining to recognize an implied-in-fact, an implied-in-law, or an equitable reimbursement right outside of the insurance policy's provisions. In light of the Court's decision, the trial court ordered Frank's Casing to file a motion for new trial only on the reimbursement issue. Frank's Casing filed the motion and the trial court granted it, withdrew its prior order, and signed a take-nothing judgment in Frank's Casing's favor.

The 14th Court of Appeals in Houston affirmed the trial court's decision. The Texas Supreme Court granted Excess Underwriters' petition for review to decide whether the decision in *Matagorda County* allowed underwriters to assert a reimbursement right when the insured consented to the settlement, but not to the excess insurer's asserted reimbursement right. In May of 2005 the Supreme Court issued its decision, holding 7-0 that in certain circumstances an insurer has a right to reimbursement for the settlement of uncovered claims.

After the May 2005 decision, the Supreme Court received a number of amicus curiae briefs that opposed the insurer's implied right to reimbursement. Two amicus briefs submitted by insurance trade organizations supported it. The Supreme Court granted a rehearing on the issue.

HOLDING ON REHEARING

In the majority opinion, Justice O'Neill explained:

"An insurer that settles a claim against its insured when coverage is disputed may seek reimbursement from the insured should coverage later be determined not to exist if the insurer obtains the insured's clear and unequivocal consent to the settlement and the insurer's right to seek reimbursement. *Tex. Ass'n of Counties County Gov't Risk Mgmt. Pool v. Matagorda County*, 52 S.W.3d 128, 135 (Tex. 2000).

In this case, which involves excess coverage, the insured consented to the settlement but not to the excess insurer's asserted reimbursement right. We must decide whether to recognize an exception to the rule in *Matagorda County* and imply a reimbursement obligation when the policy involves excess coverage, the insurer has no duty to defend under the policy, and the insured acknowledges that the claimant's settlement offer is reasonable and demands that the insurer accept it. Because none of these distinctions alleviates the concerns that drove the Court's analysis in *Matagorda County*, we decline to recognize such an exception."

However, this was not a unanimous decision and in his dissenting opinion, Justice Hecht stated: "By refusing to apply to insurers the same law of unjust enrichment that applies to everyone else, the Court hands Frank's Casing Crew & Rental Tools Inc. \$7 million for which it paid nothing and to which it has no contractual right."

WHAT THIS MEANS

The recent decision in *Frank's Casing* has many people speculating about what this will mean for the future. On one hand, this decision removes the potential fear of liability that might discourage an insured when trying to make a decision about a settlement and accompanying potential liability, and it allows defense counsel to be forthright about settlement recommendations. On the other hand, many people predict that this will increase litigation by insurers against their insureds because they will be forced to determine coverage rights prior to settlement.

Whatever the outcome, one thing is clear from the Texas Supreme Court's decision: If an insurer intends to seek reimbursement, the reservation of the reimbursement right must be expressly agreed to by the insured and should be clearly delineated in the policy agreement.

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