What We Have Learned From Menchaca

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Chapter 3

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EDUCATIONAL BACKGROUND

- **Southern Methodist University** J.D. - 1983; **Texas A&M University** 1980 (G.P.A. - 4.0) B.A. - Summa Cum Laude

PROFESSIONAL ACTIVITIES

- **Recipient of the 2017 Thomas Segalla Award,** American College of Coverage and Extra-Contractual Counsel.
- **Texas Lawyer "Go To" Lawyer in Insurance Law** 2012; Texas Lawyers "Top Notch Lawyer" (one of five nominees for the "Go To" Lawyer Award in 2007
- **Best Lawyers Lawyer of the Year** in Insurance Law for Dallas, Texas
- **Chambers & Partners, Chambers USA, "America's Leading Lawyers for Business, Leading Individuals in the field of Insurance Law," (2003-2017)**
- **American College of Coverage and Extra-Contractual Counsel**
  Member of Board of Directors
- **Insurance Section of the State Bar of Texas, a** founding officer and past-chair
- **Dallas Bar Association Tort & Insurance Practice Section,** past-chair, received "Oustanding Section" Award from the DBA.
- **Dallas Bar Association Appellate Section,** Founding Officer and Past-Chair
- **Master, Mack Taylor Inn of Court, American Inns of Court**
- **D Magazine Best Lawyer in Dallas**
- **Best Lawyers in America** (2006-2017)
- **Texas Monthly Magazine – Texas Super Lawyer** (2003-2017)

LAW RELATED PUBLICATIONS AND SEMINARS

- American College of Coverage and Extracontractual Counsel, "Bad Faith Trial Tactics From the Best, For the Best" (May 2017)
- Dallas Bar Association Tort & Insurance Section, "The Duty to Settle in Texas" (March 2017).
- The Knowledge Group, "Insurance Coverage Litigation: Tools & Tactics for 2017," Live Webcast (February 2017)
- Dallas Bar Association Tort & Insurance Section, "*Stowers* Update" (August 2016).
- American College of Contractual and Extra-Contractual Counsel, Annual Meeting, "Discovery and Admissibility of Evidence of Other Claims" (May 2016).
- American Bar Association, Insurance Coverage Litigation Committee CLE Seminar, "Settlement Without The Carrier: Dealing With Sweetheart Deals and Mary Carter Traps", (March 2016)
- State Bar of Texas, Legal Issues in the Texas Hospitality Industry, "Liability Insurance-Ten Things You Need to Know", (November 2015)

- The University of Texas School of Law, 20th Annual Insurance Law Institute, "How to Get Dough Out of Insurance Companies: Tactics and Tricks of the Trade", (November 2015)
- State Bar of Texas, 12th Annual Advanced Insurance Law, "Independent Counsel: When The Facts to be Adjudicated in the Liability Lawsuit are the Same Facts Upon Which Coverage Depends", (June 2015)
- The University of Texas School of Law, 19th Annual Insurance Law Institute, "Pattern and Practice in Claims Handling" (November 2014)
- The University of Texas School of Law, 38th Annual Page Keeton Civil Litigation Conference, "Insurance Update" (October 2014)
- The Seminar Group, 3rd Annual Insurance in the Construction Industry, "Coverage Allocation: Horizontal Versus Vertical Allocation; Towers of Coverage Including Multiple Years for a Single Insured; Priorities between Additional Insured and Named Insured's Own Coverage Disputes" (October 2014)
- Dallas Bar Association, Senior Lawyers Committee, "Anatomy of An Insurance Claim", (February 2014)
- The University of Texas School of Law, 18th Annual Insurance Law Institute, "What's In a Name: Making Sure You Have Insurance for the Right Entities and Individuals and What to Do If You Don't" (November 2013)
- State Bar of Texas, 10th Annual Advance Insurance Law Course, "*Stowers*" (April 2013)

SIGNIFICANT APPELLATE DECISIONS

- *State Farm v. Gandy* (Tex. 1996)(eliminating "sweetheart" liability insurance deals)
- *Christophersen v. Allied-Signal* (5th Cir. 1990)(en banc)(adopting test for expert testimony pre-*Daubert*)
- *Rose v. Doctors Hospital* (Tex. 1990)(holding statutory med-mal caps constitutional)
- *St. Paul Fire v. Convalescent Services* (5th Cir. 1999)(no duty to settle based on uncovered claims)
- *State Farm v. Williams* (Tex. App.--Dallas 1990, writ denied)(proof of prejudice to establish waiver and estoppel)
- *Pennsylvania Nat. v. Kitty Hawk Airways* (5th Cir. 1992)(same).

HOBBIES

- **Father of two**
- **Book-collector (Churchill and Lloyd George)**
- **Jazz/Rock saxophonist**
- **Journeyman Golfer**

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What We Have Learned From *Menchaca*

I. Introduction and Dedication

We recently celebrated the 30th anniversary of the decision in *Vail v. Texas Farm Bureau Mut. Ins. Co.*, 754 S.W.2d 129 (1988). This paper and its discussion of *Vail* and its recent affirmation in *USAA Texas Lloyds Company v. Menchaca*, 2017 WL 1311752 (Tex. April 7, 2017) is dedicated to two of the best insurance lawyers this author has had the privilege of working with on numerous cases, Mark Kincaid (for the Vails in the Supreme Court) and Sidney Davis. How strange that two such fine lawyers would be on the same critical case and both be gone from us too soon? A nod as well to Roger Sanders and Joe Longley who played critical roles in the *Vail* case as well.

The journey to *Menchaca* began with a morass of seemingly conflicting decisions from the courts of appeals, the Supreme Court, and the Fifth Circuit. Many believed the issue of whether policy benefits were "actual damages" recoverable under the Insurance Code would finally be answered in *In re Deepwater Horizon*, 807 F.3d 689 (5th Cir. 2015). The Fifth Circuit in its certification decision observed:

> [W]e find it prudent to obtain clarity from Texas itself. The parties' arguments regarding whether *Vail* remains good law "illuminate the magnitude and wide ramifications . . . for insurance law" that this issue presents. *In re Deepwater Horizon*, 728 F.3d 491, 500 (5th Cir.2013), *certified question answered*, 470 S.W.3d 452 (Tex.2015), *reh'g withdrawn* (May 29, 2015). We thus conclude that certification is appropriate here.

Id. at 693. But, Deepwater settled and the issues remained unresolved. With *Menchaca*, we finally have answers, for good or for ill.

A. Facts

The case revolves around a homeowner's insurance claim resulting from Hurricane Ike. USAA inspected twice, once of being given notice and again five months later. Both investigations concluded that there were some covered damages, but they were less than the deductible. *Id.* at *1. Suit was filed by the insured, urging only " insurance benefits under the policy, plus court costs and attorney's fees" as damages. *Id.*

At trial, the jury answered the following questions:

1. "Question 1 of the jury charge, which addressed Menchaca's breach-of-contract claim, asked whether USAA failed 'to comply with the terms of the insurance policy with respect to the claim for damages filed by Gail Menchaca resulting from Hurricane Ike.'"

"The jury answered 'No.'" *Id.* at 2.

2. "Question 2, which addressed Menchaca's statutory claims, asked whether USAA engaged in various unfair or deceptive practices, including whether USAA refused 'to pay a claim without conducting a reasonable investigation with respect to' that claim."

   "As to that specific practice, the jury answered 'Yes.'" *Id.*

3. "Question 3 asked the jury to determine Menchaca's damages that resulted from either USAA's failure to comply with the policy or its statutory violations, calculated as 'the difference, if any, between the amount USAA should have paid Gail Menchaca for her Hurricane Ike damages and the amount that was actually paid.'"

   The jury answered "$11,350."

The trial court was asked by USAA to disregard all of the findings and enter judgment for it based on the lack of a finding of a breach of contract by USAA. The policyholder asked for the trial court to disregard the answer to question 1 and enter judgment for the policyholder based on the jury answers to questions 2 and 3. The trial court agreed with the policyholder. *Id.* The court of appeals affirmed. *USAA Texas Lloyd's Co. v. Menchaca*, 2014 WL 3804602 (Tex. App.-Corpus Christi 2014)(affirmed as modified).

II. The Supreme Court—Framing The Issue/s

The court framed the issue before it as follows:

> The primary issue is whether the insured can recover policy benefits based on jury findings that the insurer violated the Texas Insurance Code and that the violation resulted in the insured's loss of benefits the insurer "should have paid" under the policy, even though the jury also failed to find that the insurer failed to comply with its obligations under the policy.

Id. at *1. The court characterized its opinion's mission as follows:

> In resolving this appeal, we seek to clarify our precedent by announcing five rules that address the relationship between contract claims under an insurance policy and ***tort claims*** under the Insurance Code.

Id. (emphasis added). Of course, Insurance Code claims are statutory claims, not tort claims. As we will note below, this terminology and its purpose could be of great importance to the scope of the decision.

A. Endorsement and Restatement of Duty of Good Faith

With respect to the common law duty of good faith, the court states:

> An insurance policy, however, is a unique type of contract because an insurer generally "has exclusive control over the evaluation, processing[,] and denial of claims," and it can easily use that control to take advantage of its insured. *Arnold v. Nat'l Cty. Mut. Fire Ins. Co.*, 725 S.W.2d 165, 167 (Tex. 1987). Because of this inherent "unequal bargaining power," we concluded in Arnold that the "special relationship" between an insurer and insured justifies the imposition of a common-law duty on insurers to "deal fairly and in good faith with their insureds." *Id.*

Id. at 4. That is interesting, but the issue is not whether a good faith claim can permit recovery contract benefits as "actual damages" under the Insurance Code. Nevertheless, the decision reaffirms the policy behind the common law duty of good faith.

B. Purpose of Insurance Code Unfair Claims Handling Provisions—"Supplements the Parties' Contractual Rights and Obligations"

The court observed: "Similar to th[e] common-law duty, the Insurance Code ***supplements the parties' contractual rights and obligations*** by imposing procedural requirements that govern the ***manner in which insurers review and resolve*** an insured's claim for policy benefits. *See, e.g.*, TEX. INS. CODE § 541.060(a) (prohibiting insurers from engaging in a variety of "unfair settlement practices")." *Id.* at *3.

C. The Five Rules Explaining the Relationship of Tort and Contract

The court announced, as distilled from prior opinions, "five distinct but interrelated rules that govern the relationship between contractual and extra-contractual claims in the insurance context." *Id.* at *4. The five rules are as follows:

1. MUST HAVE COVERAGE TO RECOVER UNDER STATUTE: "[A]s a general rule, an insured cannot recover policy benefits as damages for an insurer's statutory violation if the policy does not provide the insured a right to receive those benefits."

2. CONTRACT BENEFITS CAN BE STATUTORY DAMAGES IF THE CARRIER ACTION HAS A CAUSAL NEXUS TO THE LOSS OF THE BENEFITS:"[A]n insured who establishes a right to receive benefits under the insurance policy can recover those benefits as actual damages under the Insurance Code if the insurer's statutory violation ***causes the loss of the benefits***. The court added: "[A]n insured who sues an insurer for statutory violations can only recover damages 'caused by' those violations." *Id.* at *5

3. CONTRACT BENEFITS MAY BE RECOVERED ABSENT COVERAGE IF THE INSURED CAUSED THE BENEFITS TO BE LOST:"[E]ven if the insured cannot establish a present contractual right to policy benefits, the insured can recover benefits as actual damages under the Insurance Code if the insurer's statutory violation caused the insured to lose that contractual right." *Id.* at *4. The court explained that what it had really held in *Castañeda* was that where only policy benefits are sought, they cannot be recovered under an

Insurance Code claim unless the policyholder pleads and obtains a "determination [that the insurer] was liable for breach of the insurance contract." *Id.* at 201.

4. **INDEPENDENT INJURIES MAY BE RECOVERED REGARDLESS OF WHETHER THERE IS COVERAGE:** "[I]f an insurer's statutory violation causes an injury independent of the loss of policy benefits, the insured may recover damages for that injury even if the policy does not grant the insured a right to benefits" and

5. **ABSENT COVERAGE OR INDEPENDENT INJURY, NO RIGHT TO RECOVERY:** "[A]n insured cannot recover any damages based on an insurer's statutory violation if the insured had no right to receive benefits under the policy and sustained no injury independent of a right to benefits." Thus, the court explained that in *Provident American Insurance Co. v. Castañeda*,: 988 S.W.2d 189, 198 (Tex. 1998), it had held that "failure to properly investigate a claim is not a basis for obtaining policy benefits."

The court made clear that where the statutory or tort claims are predicated on the right to coverage, a determination that there is no coverage defeats the dependent extra-contractual claims as well. For example, deprivation of contractual benefits because of "failing to promptly pay [the] claim, failing to fairly investigate the claim, and denying the claim in bad faith" cannot exist where it is determined THAT no coverage was owed from the outset. *Id.* at *6 (discussing and quoting *Progressive County Mutual Insurance Co. v. Boyd*, 177 S.W.3d 919, 920, 922 (Tex. 2005) (per curiam)).

D. Must Coverage or a Breach of Contract Be Shown?

The court held this was a meaningless distinction. If there is coverage, failure to pay is a breach. If there is no coverage, failure to pay is not a breach.

E. The Battle—Can Policy Benefits Ever Be Recovered As "Actual Damages" For A Statutory Violation

1. *The Entitled-To-Benefits Rule*

The court rejected the argument of USAA that "*an insured can never recover policy benefits as damages for a statutory violation.*" *Id.* at *7. The court could not have been more clear that "if the jury finds that the policy entitles the insured to receive the benefits and that the insurer's statutory violation caused the insured to not receive those benefits, the insured can recover the benefits as 'actual damages … caused by' the statutory violation." *Id.* at *7. The corollary is that "an insured cannot recover policy benefits as actual damages for an insurer's statutory violation if the insured has no right to those benefits under the policy." *Id.* at *7-*8.

2. *Vail Controls*

The court followed its very specific holding in *Vail* that "the insureds could elect to recover the benefits under the [Insurance Code] even though they also could have asserted a breach-of-contract claim." Quoting *Vail*, the court explained:

> The insurer argued that the insureds could not recover policy benefits as damages for statutory violations because "the amount due under the policy solely represents damages for breach of contract and does not constitute actual damages in relation to a claim of unfair claims settlement practices." [*Vail*, *supra*] at 136. We rejected that argument and held that "an insurer's unfair refusal to pay the insured's claim causes damages as a matter of law in at least the amount of the policy benefits wrongfully withheld." *Id.* We explained that the insureds "suffered a *loss* … for which they were entitled to make a claim under the insurance policy," and that loss was "transformed into a legal *damage*" when the insurer "wrongfully denied the claim." *Id.* "That damage," we held, "is, at minimum, the amount of policy proceeds wrongfully withheld by" the insurer. *Id.*

Menchaca, *supra*, at *8.

The court further explained that it did not "not reject the *Vail* rule in [*Republic Ins. Co. v. Stoker*, 903 S.W.2d 338, 341 (Tex. 1995)] or in [*Provident American Insurance Co. v. Castañeda*,988 S.W.2d 189, 198 (Tex. 1998)]." The court emphasized:

> The rule we announced in *Vail* was premised on the fact that the policy undisputedly covered the loss in that case, and the insurer therefore "*wrongfully* denied" a "*valid* claim." *Id.* at 136–37 (emphases added).[18] If an insurer's "wrongful" denial of a "valid" claim for benefits results from or constitutes a statutory violation, the resulting damages will necessarily include "at least the amount of the policy benefits wrongfully withheld." *Id.* at 136. We confirmed this reading of *Vail* and reaffirmed the general rule in *Twin City*, 904 S.W.2d at 666. There, we explained that "*Vail* was only concerned with the insurer's argument that policy benefits *improperly withheld* were not 'actual damages in relation to a claim of unfair claims settlement practices.' " *Id.* (emphasis added) (quoting *Vail*, 754 S.W.2d at 136). We further explained that the Court rejected the insurer's argument in *Vail* because "policy benefits *wrongfully withheld* were indeed actual damages" under the statute." *Id.* (emphasis added).

Id. at *9.

As to *Castaneda*, the court again emphasized that there was no determination of coverage or not and no pleading of liability for contract damages. The court observed:

> On that issue, we held that an insurer's "failure to properly investigate a claim is not a basis for obtaining policy benefits," but we did not assume that coverage existed when deciding that separate issue. *Id.* Instead, we relied on the fact that the insured

> "did not plead and did not obtain a determination [that the insurer] was liable for breach of the insurance contract." [*Castaneda*, *supra*,] at 198, 201.

Id. at *9.

Importantly, the court summarized its conclusions:

> In short, *Stoker* and *Castañeda* stand for the general rule that an insured cannot recover policy benefits as damages for an insurer's extra-contractual violation if the policy does not provide the insured a right to those benefits. *Vail* announced a corollary rule: an insured who establishes a right to benefits under the policy can recover those benefits as actual damages resulting from a statutory violation. We clarify and affirm both of these rules today.

Id.

3. The Benefits-Lost Rule—Recovery of Benefits As Statutory Damages Even If No Actual Coverage

The court noted that our precedent recognizes "that an insured can recover benefits as actual damages under the Insurance Code ***even if the insured has no right to those benefits*** under the policy, *if the insurer's conduct caused the insured to lose that contractual right*." *Id.* The court gave three non-exclusive examples:

- Misrepresentation of a policy's coverage,
    - E.g., Agent for insurer represents there is coverage, but the policy issued says there is no coverage. *Id.* (citing *Royal Globe Ins. Co. v. Bar Consultants, Inc.*, 577 S.W.2d 688, 694 (Tex. 1979)).
- Waiver and/or estoppel as to the carrier's right to deny coverage
    - "[I]f the insurer's statutory violations prejudice the insured, the insurer may be estopped "from denying benefits that would be payable under its policy as if the risk had been covered." Under such circumstances, the insured may recover "any damages it sustains because of the insurer's actions, even though the policy does not cover the loss."
- Commission of a violation that caused the insured to lose a contractual right to benefits that it otherwise would have had.
    - The court explained by pointing to its decision in *JAW the Pointe, L.L.C. v. Lexington Insurance Co.*, 460 S.W.3d 597, 599, 602 (Tex. 2015).
        - The court stated it accepted arguments that the "insurer's statutory violations caused the insured to lose its contractual

right to the policy benefits by delaying the payments until after the limits had been reached."

- But, the court found an exclusion in fact barred all coverage and this resulted in no recovery under the statutory claims.

- The court concluded: "Put simply, an insurer that commits a statutory violation that eliminates or reduces its contractual obligations cannot then avail itself of the general rule." *Id.* at *10.

In each example, the benefits amount to, in the court's words, actual damages suffered as a result of the statutory violation. These examples will be welcome news to policyholders. They certainly appear to place the court's imprimatur on claims that were subject to some doubt previously. The waiver/estoppel example is particularly interesting, especially since timely and sufficient reservations and denials are required under the Insurance Code.[1]

F. Independent Injury Rule Redux?

The court includes a fifth and final analysis of what its prior decisions held. This time the focus is the "independent injury rule." The portion that has already caused confusion and stirred debate is the following:

> The second aspect of the independent-injury rule is that an insurer's statutory violation *does not permit the insured to recover any damages beyond policy benefits unless the violation causes an injury that is independent from the loss of the benefits.* Thus, we held in Twin City that an insured who prevails on a statutory claim *cannot recover punitive damages for bad-faith conduct in the absence of independent actual damages arising from that conduct.* 904 S.W.2d at 666; *see also Powell Elec. Sys., Inc. v. Nat'l Union Fire Ins. Co.*, 2011 WL 3813278, at *9 (S.D. Tex. Aug. 29, 2011) (granting summary judgment for the insured on its breach-of-contract claim but for the insurer on common-law and statutory bad-faith claims because the insured "failed to allege damage independent of the damages arising from the underlying breach of the insurance contract").

[1] Section 541.060(A) provides the following are unfair claims settlement practices:

. . . .

(3) failing to promptly provide to a policyholder a reasonable explanation of the basis in the policy, in relation to the facts or applicable law, for the insurer's denial of a claim or offer of a compromise settlement of a claim;

(4) failing within a reasonable time to:

(A) affirm or deny coverage of a claim to a policyholder; or

(B) submit a reservation of rights to a policyholder . . . .

The defense bar is, in my opinion, selectively reading this portion of the opinion in a way that is fatally inconsistent with the (a) court's reaffirmation of *Vail* and (b) inconsistent with its interpretation and holdings that policy benefits are damages recoverable in contract or for statutory violations. This reading also creates a perversion of the court's references to *Twin City*.

The court in *Menchaca* reaffirmed commitment to *Vail: "Vail* announced [the rule that an] insured who establishes a right to benefits under the policy can recover those benefits as actual damages resulting from a statutory violation. We clarify and affirm both of these rules today." *Id.* at *8. The court rejected arguments that *Vail* was overruled by *Castaneda* or *Stoker*.

As the *Menchaca* court expressly recognized, *Vail* clearly held that the contract benefits were trebled.[2] *Vail. Supra*, at *7. The court noted: "Based on these findings, the trial court awarded benefits in the amount of the "full policy limit" plus treble ***that*** amount, attorney's fees, and prejudgment interest. Id. at 131. The court in *Vail* was even more explicit regarding the propriety of awarding treble damages where the only actual damages were lost policy benefits:

> Based on a jury verdict, the trial court rendered judgment for the Vails for treble the amount of the policy, prejudgment interest on the trebled amount, and attorney's fees. The court of appeals reversed that part of the trial court's judgment that trebled the actual damages and permitted the Vails to recover only the policy limit as actual damages, prejudgment interest on that amount, and attorney's fees. 695 S.W.2d 692. We reverse the judgment of the court of appeals in part and render judgment that the *Vails recover treble the amount of the policy*, prejudgment interest on the amount of the policy only, and attorney's fees.

Vail, *supra*, at 130 (emphasis added).

Ok. Let's break this down:

- "[A]n insurer's statutory violation does not permit the insured to recover any damages beyond policy benefits unless the violation causes an injury that is independent from the loss of the benefits."
    - The court's definition of what is (a) contract benefits and (b) what is truly independent is very peculiar. *Id.* at *11.
        - Policy benefits includes as well damages that "'are predicated on,' 'flow from,' or 'stem from' policy benefits." *Id.*

[2]Texas Farm Bureau's Response to the Vail's Reply and Supplemental Brief stated at page 17:

> In summary, the record in this case is devoid of any pleading, proof or finding of "actual damages" which are capable of being trebled under the DTPA.

        - Independent injury must be separate, different and "truly independent." Strangely, mental anguish damages are given as an example of an independent injury. *Id.*

        - The net result is that if you fail to show entitlement to contract benefits, you will not be saved by anything flowing from that loss.

    - Good news. If you establish a right to policy benefits, you can recover everything flowing from those benefits.

- "[W]e held in Twin City that an insured who prevails on a *statutory claim* cannot recover punitive damages for bad-faith conduct in the absence of independent actual damages arising from that conduct. 904 S.W.2d at 666; *see also Powell Elec. Sys., Inc. v. Nat'l Union Fire Ins. Co.*, 2011 WL 3813278, at *9 (S.D. Tex. Aug. 29, 2011)(granting summary judgment for the insured on its breach-of-contract claim but for the insurer on common-law and statutory bad-faith claims because the insured "failed to allege damage independent of the damages arising from the underlying breach of the insurance contract")." *Id.* (emphasis added).

    - Defense counsel are reading this as in effect reinstating the independent injury rule avoided by the court in holding contract benefits delayed by statutory violations were a form of "actual damages."

    - *Twin City* involved a judgment based on good faith and fair dealing findings, not statutory violations under the Insurance Code.

    - In *Twin City*, the parties agreed that tort and contract claims were wholly separate and distinct. That is certainly not what they held in determining the contract benefits could be recovered in both statutory and contract claims. The court noted in *Twin City*: "Likewise, the parties do not dispute that the insurer's failure to deal fairly and in good faith with its insured is a cause of action that sounds in tort, and is distinct from the contract cause of action for the breach of the terms of an underlying insurance policy" In *Menchaca, no claim for breach contract was made.*

    - Recovery in *Twin City* was for common law punitive damages, not additional damages under the Insurance Code. The legislature imposed no "independent injury" requirement in drafting the additional damages provision, which allows trebling of "actual damages."

    - *Twin City* distinguished *Vail:* "We did not even discuss in *Vail* the argument Twin City makes here, that the policy benefits wrongfully

withheld will not alone support an award of punitive damages." *Id.* at 666.

- The independent injury concept was necessitated by the fact the claim in *Twin City* was for benefits payable under the Workers Compensation Act. Thus, unless the damages were wholly separate and independent from those benefits, the exclusivity provision would bar their recovery. *Id.* at 667 ("But, we said, because of the exclusivity provision, the employee must show that the claim for the breach "is *separate* from the compensation claim and produced an *independent* injury." *Id.* (emphasis added)."). The court held *Vail* was not the controlling case; instead, it was this case is controlled by our decision in *Aranda v. Insurance Co. of North America*, 748 S.W.2d 210 (Tex.1988), dealing with the exclusive remedy provision. This has absolutely nothing to do with claims such as that in *Menchaca.*

The simple fact is that section 541.152(b) of the Texas Insurance Code provides that "on a finding by the trier of fact that the defendant knowingly committed the act complained of, the trier of fact may award an amount not to exceed three times the amount of actual damages." This is the same "actual damages" found by the court to include policy benefits and that is made actionable in section 541.151.

In the end, the court's statements about the independent injury rule appear to be an artfully worded section attempting to explain that where there is no coverage, a truly independent injury must exist to allow recovery. If it stems from the contract claim, it is insufficient to support recovery of other "independent harms" under the statute. In other words, if there was no coverage for the claim, then there could be no extra-contractual recovery for bad faith, because there where there were no injuries independent of the contract damages.

G. Resolution of *Menchaca*

Because of the need for clarification of the law, the court remanded *Menchaca* in the interests of justice. The court observed: "[W]e conclude that the confusing nature of our precedent precludes us from faulting Menchaca for asserting throughout this litigation that she did not have to prove breach."

III. Post-*Menchaca* Decisions

In *State Farm Lloyds v. Webb*, 2017 WL 1739763 (Tex. App.—Corpus Christi, May 17, 2017), the court took the confusing and inconsistent language regarding the independent injury rule from *Menchaca*. The court held that the only damages were policy benefits. Thus, it concluded the statutory claims failed as a matter of law. It chose to treat those claims as "extra-contractual" claims. The court quoted *Menchaca* as follows:

> In *Menchaca*, the Supreme Court held that "if the policy does entitle the insured to benefits, the insurer's statutory violation does not permit the insured to recover any

> actual damages beyond those policy benefits unless the violation causes an injury that is independent from the loss of the benefits." *Id.* at *12.

Webb, *supra*, at *9. This purported holding is a mystery in light of the fact the court also held: "We conclude that the evidence does not enable reasonable and fair-minded people to find that State Farm engaged in a deceptive act or practice." *Id.*

The Houston 14th District Court similarly held that independent injury is required for any statutory violation to be actionable in *National Security Fire & Casualty Company v. Hurst*, 2017 WL 2258243 (Tex. App. 2017). The court stated:

> In order to recover any damages beyond policy benefits, the statutory violation or bad faith must cause an injury that is independent from the loss of benefits. *USAA Tex. Lloyds Co. v. Menchaca*, No. 14-0721, --- S.W.3d ----, ---- – ----, 2017 WL 1311752, at *11-12 (Tex. Apr. 7, 2017). The *Menchaca* court recognized that "a successful independent-injury claim would be rare, and we in fact have yet to encounter one." Id. at *12 (citing *Mid–Continent Cas. Co. v. Eland Energy, Inc.*, 709 F.3d 515, 521 (5th Cir. 2013)) (observing "[t]he *Stoker* language[8] has frequently been discussed, but in seventeen years since the decision appeared, no Texas Court has yet held that recovery is available for an insurer's extreme act, causing injury independent of the policy claim.") The *Menchaca* court explained that "[t]his is likely because the Insurance Code offers procedural protections against misconduct likely to lead to an improper denial of benefits and little else." Id. The court acknowledged that it has further limited the natural range of injury by insisting that an "independent injury" may not "flow" or "stem" from denial of policy benefits. Id. (citing *Provident Am. Ins. Co. v. Castañeda*, 988 S.W.2d 189, 198 (Tex. 1998)). And the court recognized that "although we reiterate our statement in Stoker that such a claim could exist, we have no occasion to speculate what would constitute a recoverable independent injury." *Id.*

Id. Of course, this discussion is fractured and ignores the numerous holdings and explanations that if contract benefits are all that is lost, they are recoverable as actual damages under the Insurance Code. Two things are apparent: (1) the court decided all that was owed to the insured had been paid, and (2) the court concluded there were no statutory acts or omissions causing a loss of benefits. The court did not say that and is, in my opinion, dead wrong in its explanation and use of *Menchaca.* The court also blends and confuses discussions from *Menchaca* about *Stoker*, which clearly deal with the situation where no policy benefits are owed, i.e. there is no coverage, and the insured wants a statutory recovery anyway. That is the scenario that is rare.

IV. Conclusion

I still think Mark Kincaid explained it best in discussing a number of post-*Vail* decisions:

> It is hard to follow the [*Great American Insurance Co. v.*] *AFS/IBEX Financial Services*, [*Inc.*, 612 F.3d 800, 808 & n. 1 (5th Cir.2010)], court's reasoning that the attorney's fees damages were not recoverable yet could be the separate injury. What is more

> troubling, and clearly incorrect, is the court's conclusion that a separate injury is required for an insured to recover for unfair insurance practices. The court correctly quoted its prior holding in *Parkans* [*Int'l, L.L.C. v. Zurich Ins. Co.*, 299 F.3d 514, 519 (5th Cir. 2002)], but misapplied it. A number of cases have stated that there must be a separate injury for an insured to recover for unfair claims handling. This statement can be true when the insurer *does not* owe the claim.
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> . . . .
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> The statement that an independent injury is required is correct in that context, where the insurer *does not* owe the claim. The policy benefits cannot be damages, because the policy benefits are not owed. Thus, if there is no independent injury then there is no basis for extra-contractual liability.
>
> The Fifth Circuit's decision in *Parkans* was another example of this principle properly applied. In *Parkans*, the court first found there was no coverage for the claim and then found there could be no extra-contractual recovery for bad faith, because there were no injuries independent of the contract damages. Of course, since those contract damages were not recoverable, they could not serve as damages for the unfair insurance practices.
>
> The *Parkans* court relied on the Texas Supreme Court's decision in *Provident American Insurance Co. v. Casteneda*, 980 S.W.2d 189, 198-99 (Tex. 1998). In *Provident*, the supreme court did state that there was no evidence of an independent injury, but it did so after concluding that the insurer was not liable for unfair settlement practices. In *Provident*, the insureds did not sue for breach of contract, so the court was not considering whether they could or could not recover contract damages. What the court did consider was that the insurer had a reasonable basis to deny the claim, even if it is was wrong. Obviously, a reasonable denial of the claim could not cause any damages. The court found no evidence to support the claim for loss of credit reputation, and then concluded that there was no other independent injury. This statement regarding an independent injury made some sense in *Provident*. The policy benefits could not be damages for an unfair claim denial, when the court found there was no unfair claim denial. In other words, the insurer was not liable because it had not committed a violation – according to the court – not because the benefits wouldn't be damages if the insurer had committed a violation.

Mark L. Kincaid, et al., "Annual Survey of Texas Insurance Law 2010," JOURNAL OF CONSUMER & COMMERCIAL LAW, 59, 62-64 (2010). Mark added:

> The Texas Supreme Court expressly addressed this issue in the leading case of *Vail v. Texas Farm Bureau Mutual Ins. Co.*, 754 S.W.2d 129, 136 (Tex. 1988), rejecting the insurer's argument that damages for an unfair settlement practice had to be something more than the amount due under the policy. The supreme court held that damages for a wrongful refusal to pay are at least equal to the policy benefits, as a matter of law . . ***It would be exceedingly odd for the legislature to create a cause of action that says recovery of "actual damages" is allowed for failing to settle once liability is***

> ***reasonably clear, but to hold that the most common damages – policy benefits – were not recoverable and the insured had to establish some other bizarre "independent injury."*** The legislature could have done that, but the language it chose certainly does not disclose that it did. The supreme court's analysis and holding in *Vail* do not allow such a conclusion.

Id. at 64 (emphasis added).