

The Fifth Circuit Holds that a Settlement Demand Made During Trial Triggers the Texas *Stowers* Doctrine

American Guarantee and Liability Ins. Co. v. ACE American Ins. Co., Cause No. 19-20779 on file in the Fifth Circuit Court of Appeals

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December 22, 2021

The Texas *Stowers* doctrine penalizes insurers for negligently failing to accept reasonable within limits settlement demands of covered claims by requiring the insurer to pay for resulting judgments in excess of their policy limits. On December 21, 2020, the Fifth Circuit Court of Appeals handed down an important opinion on the Texas *Stowers* doctrine holding that a settlement demand made during trial triggered the insurer's duties under *Stowers*.

Here, the insured, a national landscaping company, was sued for the wrongful death of a bicycle rider. It was defended in the wrongful death lawsuit by its primary insurer with \$2 million in limits. Above the primary policy, the insured also possessed a \$10 million excess policy. After the underlying wrongful death case ended with a \$42 million verdict (reduced to \$28 million due to the bicycle rider's contributory negligence), the primary insurer tendered its \$2 million limits and the excess insurer contributed approximately \$8 million to settle the underlying wrongful death case. Utilizing equitable subrogation, the excess insurer then sued the primary insurer to recover its payment under the Texas *Stowers* doctrine claiming that the primary insurer negligently failed to accept a settlement demand within its policy limits.

The case is remarkable for a few reasons.

First, the excess-primary *Stowers* case was tried to the bench, which in finding that the primary insurer breached the *Stowers* doctrine, issued an extensive opinion with 68 paragraphs of findings of fact and 17 paragraphs of conclusions of law. *American Guarantee and Liab. Ins. Co. v. Ace American Ins. Co.*, 2019 WL 4316531 (S.D. Tex. 2019). In this regard, the District Court opinion provides a unique analysis of the inner-workings of the *Stowers* doctrine.

Second, of three settlement demands at issue, it was the third demand made during the trial that triggered the primary insurer's duties under the *Stowers* doctrine. The District Court and the Fifth Circuit opinions provide guidance not only as to why the third demand satisfied *Stowers*, but also on the fallacies under *Stowers* of the first two demands.

Third, the settlement demand was made on behalf of multiple claimants and it did not parse out who would get what in the event that the demand was accepted.

The first settlement demand was made at a mediation about a week-and-a-half before trial and it was not considered by the Fifth Circuit. Instead, the Fifth Circuit limited its analysis to two demands; one oral and one in writing, that were made during the trial. The District Court analyzed the first demand in detail to rule that it did not invoke the *Stowers* doctrine even in the face of a "hammer" letter from the excess insurer, demanding

the settlement demand be accepted by the primary insurer. In this regard, the District Court ruled that in light of perceived liability defenses, an ordinarily prudent insurer could believe that the settlement value of the case was less than \$2 million, relying on what the judge found to be reasonable report assessing a reasonable settlement range between \$1.25 million and \$2 million.

At trial, however, there were adverse evidentiary rulings against the insured, which changed the District Court's mind about two demands made during trial. The second demand was oral demand for a high/low of "\$1.9 million to \$2.0 million with costs." For this demand, the Fifth Circuit disagreed with the District Court and ruled that this demand did not invoke the *Stowers* doctrine. On this point, the Fifth Circuit held that the inclusion of "costs" in the demand made that demand ambiguous. Here, the primary insurer believed "costs" included litigation expenses and court costs. In contrast, the excess insurer believed "costs" were limited to court costs, however, its case manager acknowledged that "costs" could have more than one meaning. Accordingly, the Fifth Circuit held that "the record reveals great confusion about that offer's terms" and, lacking the clear statement of a sum certain, the offer did not invoke *Stowers*."

Accordingly, the Fifth Circuit's focus was limited to the third settlement demand, made in writing during trial, which provided:

Please be advised that [Claimants] hereby make this unconditional offer to settle within the primary policy limits represented to us to be applicable to any judgment rendered in this case to settle any and all claims that were asserted or could be asserted in the above-referenced matter for the total sum of \$2,000,000.00.

With respect to this demand, the primary insurer argued that because the case involved minor children, any settlement would need court approval requiring the appointment of a Guardian Ad Litem to approve the settlement and bind the minor and was therefore impermissibly conditional. In this regard, the Fifth Circuit noted that whether the third offer was inherently conditional that depended on hindsight and held that:

There is no evidence that the settlement offer was more favorable to [the Mother] than her children or that [the Mother] was operating with interests adverse to those of her children. ACE offers nothing in the record suggesting that, had the third settlement offer been accepted, [the Mother] would have placed maximizing compensation for her own injuries above her children's claims.

Because the record is void of any specter of adverse interests between [the Mother] and her children had the third lump sum settlement offer been accepted, her children would have been bound by it. Accordingly, the offer generated a *Stowers* duty because it "proposed to release the insured fully" and it was not conditional.

Next, the primary insurer argued that the judgment in the underlying wrongful death case would have been reversed on appeal. As framed by the Fifth Circuit: "although the trial went poorly for ACE and its decision to reject the [Claimants'] final settlement offer may *appear* unreasonable, ACE was not actually negligent since the trial court's 'errors' likely rendered the judgment reversible on appeal." The Fifth Circuit initially rejected this argument because it was not raised in the District Court. Nonetheless, the Fifth Circuit conducted a *de novo*

evidentiary sufficiency review and found that based on adverse evidentiary rulings in the underlying wrongful death trial:

The evidence is clearly sufficient to support the bench trial verdict that “[a] reasonable insurer would have reevaluated the settlement value of the case [and accepted the Claimants’ third offer].

Considering all of the trial circumstances, an “ordinarily prudent insurer” in ACE’s position would have realized that the “likelihood and degree” of [the Defendants’] “potential exposure to an excess judgment” had materially worsened since the trial’s inception. When presented with the [Claimants’] third offer, an ordinary, prudent insurer would have accepted it. The evidence placed before the district court is sufficient to support that ACE violated its *Stowers* duty by failing to reevaluate the settlement value of the case and accept the [Claimants’] reasonable offer.

Accordingly, the Fifth Circuit affirmed the District Court’s ruling that the primary insurer violated the *Stowers* doctrine by failing to accept the in-trial written settlement demand.

There are many practical take-a-ways from the Fifth Circuit’s opinion.

First, it is extremely difficult for an oral settlement demand to invoke the *Stowers* doctrine, which is a highly criticized practice in the first place. There are enough technicalities about demands under the *Stowers* doctrine being clear, unequivocal and unconditional that oral demands are fraught with problems.

Second, the Fifth Circuit took a very practical approach to analyzing whether the presence of minors as releases made the in-trial policy limits demand conditional because the settlement was potentially conditioned on court approval with the need for a Guardian Ad Litem. In this regard, the Fifth Circuit held that:

Because the record is void of any specter of adverse interests between Michelle and her children had the third lump sum settlement offer been accepted, her children would have been bound by it. Accordingly, the offer generated a *Stowers* duty because it “proposed to release the insured fully” and it was not conditional.

Third, primary insurers can take some comfort in the District Court’s finding that the first within-limits settlement demand made at a mediation 11 days before the start of the trial did not invoke the *Stowers* doctrine based on what the District Court considered to be a reasonable report: “in light of perceived liability defenses, an ordinarily prudent insurer could believe that the settlement value of the case was less than \$2 million.” Many counsel for policyholders would argue that under this record, the first demand made at the pre-trial mediation invoked the *Stowers* doctrine.

Fourth, the opinion analyzes a demand made while the trial was ongoing. With all of the complexity of a trial, especially one that was not going well for the defense, insurers may also have to face the decision of whether to accept the settlement demand under a very tight deadline. Indeed, the Fifth Circuit cited with approval the District Court’s observation that: “[t]hese rulings, which exacerbated the known weaknesses in the case, should have changed ACE’s calculus A reasonable insurer would have reevaluated the settlement value of the case [and accepted the Claimants’ offer].

Finally, the opinion firmly re-establishes the Texas *Stowers* doctrine as the ultimate “hammer” in forcing insurers to face the harsh decision of whether to accept a settlement demand to cut-off any potential exposure above their policy limits.