DUTY OF INSURER TO ADDITIONAL INSUREDS
NATIONAL UNION V. CROCKER

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NATIONAL UNION V. CROCKER – PERHAPS TEXAS INSURANCE LAW HAS NOT CHANGED AS MUCH AS WE THOUGHT?

I. INTRODUCTION

In *National Union Fire Insurance Company v. Crocker*, __ S.W.3d __, 2008 Tex. LEXIS 119 (Tex., Feb. 15, 2008), the Texas Supreme Court answered two of three certified questions from the Fifth Circuit Court of Appeals on the issue of whether an insurer has a duty to notify an additional insured of available liability insurance coverage. *See Crocker v. National Union Fire Ins. Co.*, 466 F.3d 347 (5th Cir. 2006) (certifying questions).

In short, the Texas Supreme Court held that, on the facts presented, Texas law imposes no such extracontractual duty on an insurer. *National Union*, 2008 Tex. LEXIS. 119 at *1. The Court also held, with respect to a late notice defense, that an insurer's actual knowledge that an additional insured has been served with process does not establish, as a matter of law, that the insurer has not been prejudiced by the by the additional insured's failure to comply with the notice-of-suit provision in the policy. *Id.*

Although the Texas Supreme Court held that the answers to the certified questions were governed by its 1978 opinion in *Weaver v. Hartford Accident and Indemnity Co.*, 570 S.W.2d 367 (Tex. 1978), the Fifth Circuit certified the questions because "changes in Texas insurance law since the *Weaver* opinion" led it "to question whether *Weaver* controls." *Crocker*, 466 F.3d at 354. The changes included a 1973 State Board of Insurance Order (No. 23080), which required a showing of prejudice by carriers invoking a late notice defense against the insured, as well as Texas case law interpreting that Board Order.

We examine below the labyrinthine history of the case, the various federal court opinions, and the Texas Supreme Court's ultimate decision, as well as its implications for future cases.

II. *CROCKER'S* PROCEDURAL HISTORY

A. State Court Personal Injury Lawsuit

The insurance issues arose out of a personal injury lawsuit by an elderly nursing home resident, Crocker, against a nursing home, Redwood Springs Nursing Home, and its employee, Richard Morris. Crocker alleged that Morris opened a swinging kitchen door that struck Crocker, knocked her down, and caused her significant injuries. *See Crocker v. National Union Fire Ins. Co.*, 2005 U.S. Dist. LEXIS 2806 at *2 (W.D. Tex. 2005) (not published) (original district court opinion in coverage case). Crocker alleged that she incurred more than $300,000 in medical expenses and that her injuries led to confinement in a wheelchair. *Id.* Redwood Springs terminated Morris shortly after the incident.

Crocker sued Morris and Redwood's owner, Emeritus Corporation, in May 2002 in Texas state district court. *Id.* at *3. Emeritus forwarded the suit papers and sought a defense from its liability carrier, National Union. *Id.* National Union provided a defense to Emeritus in the state court suit. *Id.* Crocker eventually served Morris in September 2002.

Because Morris never answered the state court suit, Crocker moved for default judgment in September 2003. *Id.* at *5. The case proceeded to trial in October 2003. Morris did not appear, attend the trial, or send counsel on his behalf. *Id.* at *6. Just before the case went to the jury, the trial court severed the claims against Morris into a separate suit.

The jury then rendered a defense verdict in favor of Emeritus, finding that Emeritus, acting through its agents (including Morris), was not negligent. *Id.* at *7. The trial court rendered a take-nothing judgment on Crocker's claims against Emeritus. *Id.* In November 2003, the trial court granted Crocker's motion for default judgment against Morris and rendered a default judgment in Crocker's favor for $1 million. *Id.*

Unbeknownst to Morris, Emeritus's liability policy also provided coverage (defense and indemnity) for employees of Emeritus, including Morris. *Id.* at *3. The policy terms required Morris, as an additional insured, to notify National Union of any claim or suit and to forward to the insurer copies of all demands, suit papers, or other legal documents received by Morris "before coverage will apply." *Id.*

During the pendency of the state court suit, Morris resisted attempts at contact by Emeritus's counsel (hired by National Union). *Id.* at *4. Morris also did not respond to contacts from the claims investigator hired by National Union (ProClaim America, Inc.). *Id.* Apparently, Morris believed Emeritus would not defend him because he had been fired after the incident, and Morris did not know that Emeritus owned Redwood Springs. *Id.* at *4-5. Importantly, Morris did not

forward the suit papers to National Union and did not request a defense in the state court suit. *Id.* at *5.[1]

B. Federal Court Coverage Lawsuit

In April 2004, Crocker sued National Union, as a judgment creditor of Morris and as a third-party beneficiary of National Union's liability policy covering Emeritus and Morris. *Id.* at *7. Crocker sued National Union for breach of the policy for failing to defend Morris, as well as some other claims relating to medical expense coverage. *Id.* at *7-8. Crocker sought to recover under the policy for the $1 million default judgment against Morris. *Id.* at *12.

National Union removed the coverage suit to federal district court in San Antonio, and the parties filed cross-motions for summary judgment on the coverage issues. *Id.* at *7. National Union urged that its duty to defend Morris never arose because Morris never forwarded suit papers and never requested a defense. *Id.* at *8. Crocker countered that National Union had actual knowledge that Morris had been served and failed to defend him, in violation of its policy duties. *Id.* at *9. Crocker also argued that National Union had to show prejudice to succeed on its late notice defense. *Id.*

III. THE FEDERAL DISTRICT COURT OPINIONS

A. Original Opinion on Cross-Motions for Summary Judgment

The federal district court in San Antonio initially granted Crocker's motion for summary judgment on the coverage issues. The court recognized that the insured generally must take certain actions to trigger an insurer's duty to defend, referred to as the "tender" of the defense. *Id.* at *15. These are, the court said, conditions precedent to the insured's recovery of benefits under the policy. *Id.* The insured has the burden to prove all conditions precedent have been satisfied. *Id.* at *16.

The federal district court, without much discussion, effectively held that Morris had failed to comply with the notice provision in the policy by failing to forward the suit papers to National Union. *See id.* at *17. The court then focused on the prejudice requirement for the late notice defense. *Id.* at *18. The court discussed Board Order 23080 (the prejudice endorsement), which had been included in an endorsement to the National Union policy. *Id.* at *20-22. The court held that National Union had to show prejudice from Morris's failure to comply with the notice condition. *Id.* at *23.

After surveying Texas and federal law analyzing the prejudice requirement and the proof required for an insurer to show prejudice, the district court stated it could find no Texas case "clearly holding that an insurer could avoid liability when its insured failed to submit pleadings and formally request a defense in a suit falling under its liability policy when the insurer had actual knowledge of the suit." *Id.* at *28. The cases the district court discussed, however, all involved late notice by a named insured, rather than a complete lack of notice by an additional insured. *See id.* at *28-32.

The court found that National Union had actual knowledge that Morris had been sued and served at least 14 months prior to the trial. *Id.* at *33. The court found this case distinguishable from others where the insurer did not receive notice of the suit against its insured until after default judgment had been rendered. *Id.* at *34. Accordingly, the court held that Morris's failure to forward the suit papers and request a defense did not prejudice National Union as a matter of law, given that it had actual notice of the suit and the impending default judgment. *Id.* Therefore, National Union had a duty to defend Morris, breached that duty by failing to defend, and owed indemnity for the $1 million default judgment against Morris. *Id.* at *38.

B. Opinion on Motion for Reconsideration

The federal district court wrote a second opinion after National Union filed a motion for reconsideration. *See Crocker v. National Union Fire Ins. Co.*, 2005 U.S. Dist. LEXIS 9377 (W.D. Tex. 2005) (not published).

1. Affirming its Prior Ruling and Applying the "Prejudice Rule"

The district court rejected National Union's argument that it misapplied Texas insurance law. The court said it was "confident" in applying the "Prejudice Rule" because of Texas Supreme Court and Fifth Circuit opinions applying it, as well as opinions from other states. *Id.* at *11.

The district court affirmed its prior ruling on coverage, stating that "Texas courts also hold that evidence of actual knowledge of a lawsuit against an insured negates the prejudice suffered by an insurer." *Id.* at *14 *(citing *Liberty Mut. Ins. Co. v. Cruz*, 883 S.W.2d 164 (Tex. 1993) (per curiam)). Thus, because

[1] In his deposition in the coverage suit, Morris confirmed these facts. *Id.* at *8.

National Union had actual knowledge of that Morris had been served in the state court suit, it was not prejudiced by Morris's failure to forward the suit papers. *Id.*

2. New Issues Raised and Rejected

On reconsideration, the district court rejected National Union's argument that, because the policy was issued in Florida, Board Order 23080 and the Prejudice Rule did not apply. *Id.* at *7. The court found that, under section 101.051 of the Texas Insurance Code, all insurance companies doing business in Texas are subject to Texas laws governing insurance. *Id.* Also, the court found that an insurance policy payable to a Texas citizen is governed by Texas law. *Id.*

Following *Hanson Production Co. v. Americas Ins. Co.*, 108 F.3d 627 (5th Cir. 1997), and *Hernandez v. Gulf Group Lloyds*, 875 S.W.2d 691 (Tex. 1994), the district court held that National Union had to show prejudice from Morris's lack of notice. *Id.* at *10-11. The court also held that Florida law (which National Union claimed applied) followed the Prejudice Rule and required a showing of prejudice. *Id.* at *11. Because National Union failed to show prejudice (given its actual knowledge), it owed a Morris a duty to defend and coverage.

Another argument raised by National Union on reconsideration was that it was not bound by the default judgment because it was rendered without a "fully adversarial trial" or an "actual trial," as required by *State Farm Fire & Casualty Insurance Company v. Gandy*, 925 S.W.2d 696 (Tex. 1996), and *State Farm Lloyds Insurance Company v. Maldonado*, 963 S.W.2d 38 (Tex. 1998), respectively. The district court also rejected these arguments, finding that Emeritus's counsel actively defended the case on behalf of both Emeritus and Morris and that, based on counsel's actions, the jury returned a defense verdict.

Thus, the district court found a "genuine contest of the issues" sufficient to bind National Union with regard to the default judgment. *Id.* at *17. The court distinguished *Gandy* on grounds it involved an assignment of claims not present in the case at bar. *Id.* at *20.

IV. THE FIFTH CIRCUIT OPINION

National Union appealed the district court's rulings to the Fifth Circuit. The Fifth Circuit opinion discusses in greater detail the facts surrounding both Morris's and National Union's actions in relation to the state court lawsuit. *Crocker*, 466 F.3d at 348-50.

The Fifth Circuit found it undisputed that (a) Crocker's claims against both Emeritus and Morris were covered by the policy, (b) National Union knew Morris was a named defendant in the lawsuit and knew or should have known Morris had been served, (c) Morris was unaware of the terms and conditions of the Emeritus policy, (d) Morris did not forward suit papers or request a defense in the state court suit, and (e) National Union did not inform Morris he was an additional insured and did not offer to defend Morris. *Id.* at *349-50.

A. Insurer's Duty to Notify Additional Insured of Potential Coverage

Unlike the district court, the Fifth Circuit gave considerable analysis to whether the insurer had any duty to notify Morris that he was an additional insured. The Court detailed the facts and holding of the *Weaver* opinion from the Texas Supreme Court. *Id.* at *351-52. The Court noted that the majority opinion in *Weaver* did not address two facts at issue before the Court: the insured's ignorance of the policy, and the insurer's actual knowledge of the suit. *Id.* at 352.

Nonetheless, the Fifth Circuit found "implied holdings" in *Weaver* that the insured's ignorance does not excuse failure to comply with policy conditions, and the insurer has no duty to cure such ignorance even if the insurer has actual knowledge of the suit. *Id.* The Court noted that the *Weaver* court focused on the fact that Hartford had no reason to think it was expected to defend the additional insured, absent compliance with the notice provision and a request for a defense. *Id.* at 353.

The Fifth Circuit stated that, if it applied *Weaver* to the facts of *Crocker*, Morris's ignorance of the policy would be no excuse for his failure to provide notice, and National Union would have had no duty to inform Morris of his rights and obligations as an additional insured. *Id.* at 353. Also, National Union's actual and timely knowledge of the suit against Morris would not have satisfied the purposes of the notice condition because National Union did not know it was expected to defend Morris. *Id.* at 353-54. However, the Court said, "changes in Texas insurance law since the *Weaver* opinion" caused the Court to question whether *Weaver* still controlled Texas law on the issue of the insurer's duty. *Id.* at 354.

B. Perceived Changes in Texas Law that Might Affect *Weaver* as Continuing Precedent

The principal changes in Texas law cited by the Fifth Circuit were the 1973 Board Order, No. 23080 (which, notably, predated the *Weaver* opinion), and subsequent Texas cases discussing the prejudice requirement imposed by the Board Order, such as *Liberty Mutual v. Cruz*, *Hernandez v. Gulf Group Lloyds*, and *Harwell v. State Farm Mutual Automobile Insurance Company*, 896 S.W.2d 170 (Tex. 1995). *Crocker*, 466 F.3d at 354-56. In a lengthy discussion of *Harwell*, the Court noted that the Texas Supreme Court reiterated in *Harwell* many of its statements from *Weaver*, including the purposes of the notice-of-suit provision and the fact that insurers do not have to gratuitously subject themselves to liability if the insured does not request a defense. *Id.* at 356.

The Court also noted a split among Texas intermediate courts of appeals as to whether the insurer's actual knowledge of the suit affected its ability to show prejudice from an insured's late notice of suit. *Id.* at 356-58. In discussing these cases, the Court seemed to question whether Texas law would hold that, under those circumstances, the existence of prejudice to the insurer from the insured's late notice was a fact issue for a jury (as opposed to the knowledge negating any prejudice, as a matter of law). *See, e.g., id.* The Court seemed troubled by the fact that some of the opinions rejected the insurers' arguments for prejudice as a matter of law, without addressing whether the insurer had a reason to believe the insured expected it to defend him. *Id.* at 357-58. In other words, if the carrier had not been notified that the insured expected a defense, how can its mere knowledge of the suit negate any prejudice from the late notice as a matter of law? Such a thought process, the Court said, "derogated the second prong of the notice of suit . . . requirement's "basic purpose" . . . – to notify the insurer that it is expected to defend the suit." *Id.* at 358.

The Fifth Circuit also mentioned a distinction among the cases finding no prejudice to the insurer when the insurer has actual knowledge of a suit, noting that those finding that knowledge negated prejudice involved a named insured, while *Weaver* involved an additional insured. *Id.* at 358-59. The Court stated that "perhaps an insurer can safely assume his named insured would expect to be defended whereas such an assumption may be inappropriate with an additional insured as to whom the insurer normally has no direct contractual (or other) relationship." *Id.* at 358.

C. The Certified Questions

Therefore, given the changes in "the landscape of insurance law in Texas" since *Weaver*, the Fifth Circuit sought guidance from the Texas Supreme Court on "just how it has changed as applied to the present context." *Id.* Finding no controlling Texas Supreme Court precedent on the issues, the Fifth Circuit certified three questions to the Texas Supreme Court:

1. Where an additional insured does not and cannot be presumed to know of coverage under an insurer's liability policy, does an insurer that has knowledge that a suit implicating policy coverage has been filed against its additional insured have a duty to inform the additional insured of the available coverage?

2. If the above question is answered in the affirmative, what is the extent or proper measure of the insurer's duty to inform the additional insured, and what is the extent or measure of any duty on the part of the additional insured to cooperate with the insurer up to the point he is informed of the policy provisions?

3. Does proof of an insurer's actual knowledge of service of process in a suit against its additional insured, when such knowledge is obtained in sufficient time to provide a defense for the insured, establish as a matter of law the absence of prejudice to the insurer from the additional insured's failure to comply with the notice-of-suit provisions of the policy?

Id. at 359. The Fifth Circuit said it did not intend to confine the Texas Supreme Court to answering the precise form or scope of the questions certified.

V. THE TEXAS SUPREME COURT OPINION

In short, a unanimous Texas Supreme Court answered certified question no. 1 "no," did not answer certified question no. 2, and answered certified question no. 3 "no." The Court appeared to limit its holding to "the facts presented." *National Union*, 2008 Tex. LEXIS 119 at *1.

A. Question No. 1: Insurer Has No Duty to Additional Insured to Inform of Potential Coverage

On the first question, which inquired whether the insurer has a duty to inform an additional insured of coverage after receiving knowledge of a suit against the additional insured, the Texas Supreme Court held that

its decision in *Weaver* governed the issue. *Id.* at *7. The *Weaver* court held that "an insurer was not liable to an additional insured's judgment creditor when the additional insured failed to notify the insurer that he had been served with process, even though the insurer know about the suit and the additional insured knew nothing about the policy." *Id.* (citing *Weaver*¸ 570 S.W.2d at 368, 370 (Greenhill, C.J., dissenting)).

The facts of *Weaver* were very similar to the facts of *Crocker*. Weaver was the victim in an automobile accident, and he sued the driver, who was an employee of the named insured employer, for damages. Weaver then added the employer as a defendant. During the insurer's investigation, the employee acknowledged he had never notified the insurer of the lawsuit and had not filed an answer. Weaver then nonsuited the employer and took a default judgment against the employee. *Weaver*, 570 S.W.2d at 368.

Weaver then sued the insurer, Hartford, to collect on the default judgment. The Supreme Court reversed the trial court's judgment in favor of Weaver, finding that Hartford had no duty to "volunteer" to defend the additional insured. *Id.* at 370.

The *Weaver* court noted that one of the purposes served by the notice requirement in the liability policy was to "enable the insurer to control the litigation and interpose a defense." *Id.* at 369. A more basic purpose, however, was to advise the insurer that an insured has been served with process and that the insurer is expected to timely file an answer. *Id.* Under *Weaver*, an insurer's knowledge that a suit has been filed against an additional insured does not satisfy this "more basic purpose" or require the insurer to "gratuitously subject[ ] itself to liability." *Id.* at 370.

In *National Union*, the Supreme Court noted that the insured's ignorance of its rights or obligations under the policy did not affect its analysis in *Weaver*. *National Union*, 2008 Tex. LEXIS 119 at *9. "Put simply," the Court said, "there is no duty to provide a defense absent a request for coverage." *Id.*

The *National Union* court also set out the similarities between *Weaver* and the case before it:

1. Both Morris and the employee in *Weaver* were additional insureds under the liability policy at issue;

2. The injured party in each case sued both the named insured and the additional insured but did not recover against the named insured;

3. Both additional insureds failed to forward suit papers to the insurers and neither received a defense;

4. Both additional insureds lacked knowledge of the employers' liability policies and notice-of-suit provisions; and

5. Both insurers argued they had no duty to inform the additional insureds of the possibility of coverage.

Id. at *9-10. Acknowledging that *Weaver* did not expressly address the additional insured's ignorance of the policy, the *National Union* court said it "nevertheless held" in *Weaver* that the insurer had no duty to inject itself gratuitously into a lawsuit by defending an additional insured, who had not requested a defense and who failed to comply with the policy's forwarding conditions. *Id*. at *10.

The Court then recognized that it "unanimously reaffirmed" the holding of *Weaver* in *Harwell v. State Farm* some 18 years later. *Id.* at *11. *Harwell* also involved an additional insured. The Court confirmed in *Harwell* that *Weaver* remained the governing law and that the insurer did not have to gratuitously subject itself to liability by volunteering to defend if not requested to do so by the insured. *Id.* at *11-12.

Following both *Weaver* and *Harwell*, the *National Union* court stated that the notice-of-suit provisions in a liability policy serve two important purposes: (a) they facilitate a timely and effective defense of the claim against the insured, and, more fundamentally, (2) they trigger the insurer's duty to defend by notifying the insurer that a defense is expected. *Id.* at *12. The Court said, "Mere awareness of a claim or suit does not impose a duty on the insurer to defend under the policy; there is no unilateral duty to act unless and until the additional insured first *requests* a defense." *Id.* (emphasis in original).

The additional insured satisfies this "threshold duty" by notifying the insurer that he has been served with process and that the insurer is expected to answer on his behalf. *Id.* The *National Union* court again declined to subject the insurer to liability for failing to perform "'the sentry duty of tracking back and forth to the court house to keep a check on if or when . . . [the insured] may be served with process.'" *Id.* (citing

Harwell, 896 S.W.2d at 173, which cited *Weaver*, 570 S.W.2d at 369).

In one paragraph with potential implications, the *National Union* court said: "Of course, an insurer that is aware an additional insured has been sued *may, and perhaps should*, choose to inform the insured that a defense is available. . . ." *Id.* at *12-13 (emphasis added). If National Union had done so, the court said, it could have avoided the judgment against Morris and years of subsequent litigation. *Id.* at 13. However, an insurer that has not been notified that a defense is expected "bears no extra-contractual duty to provide notice that a defense is available to an additional insured who has not requested one."

Therefore, even if the carrier actually knows about the suit and service on an additional insured, it has no *legal* duty to advise the additional insured of the potential coverage. The Supreme Court suggests the carrier might, based on some other moral or ethical or business principle or code of conduct, choose to notify the additional insured when this situation arises. However, the carrier will not suffer *legal* liability if it chooses not to do so.

Because the Court answered "no" to Question No. 1, it did not answer Question No. 2 (which only applied on an affirmative answer to Question No. 1).

B. Question No. 3: Insurer's Knowledge Does Not Negate Prejudice as a Matter of Law

Certified question no. 3 inquired whether, if an insurer obtains actual knowledge that an additional insured has been served with process in time to provide a defense for the insured, this establishes – as a matter of law – the absence of prejudice to the insurer from the lack of notice. In responding to this question, the *National Union* court considered Board Order 23080 but did not give a lengthy discussion of its earlier opinions on prejudice, such as *Hernandez*, *Cruz*, or *Harwell*. Instead, the Court focused on its January 11, 2008 opinion in *PAJ, Inc. v. Hanover Ins. Co.*, __ S.W.3d __, 2008 Tex. LEXIS 8 (Tex. 2008), which addressed the prejudice requirement for a late notice defense.

The Court summarized its holding in *PAJ, Inc.* as: "tardy notice of a covered claim will not defeat coverage unless the insurer was actually prejudiced by the delay." *Id.* at *16. In *PAJ, Inc.*, the named insured did not notify the insurer of a suit against it "as soon as practicable," but waited about six months after litigation commenced to give notice and to request a defense. *PAJ, Inc.*, 2008 Tex. LEXIS 8 at *3.[2]

The *PAJ, Inc.* majority opinion (a 5-4 decision)[3] examined Board Order 23080 and its decision in *Hernandez v. Gulf Group Lloyds*, among others, and held that an immaterial breach of the policy by the insured (*i.e.*, late notice by a named insured that does not prejudice the insurer) does not deprive the insurer of the benefit of the bargain and, thus, does not relieve the insurer of its coverage obligations. *Id.* at *1. Therefore, for an insurer to successfully assert a late notice defense, it must establish it was prejudiced by the insured's late notice – which apparently constitutes a material breach. *See id.* at *10, 15.[4]

However, the *National Union* Court noted some distinguishing factors between *PAJ, Inc.* and the case before it. First, the Court said, the notice of suit by the named insured in *PAJ, Inc.* was late, but the insured did request coverage under the policy. In *National Union*, on the other hand, the additional insured's "notice" was not merely late, "it was wholly lacking" and "nonexistent." *Id.*

More importantly, the Court said, the requirement that an additional insured provide notice that it has been sued and served with process is driven by a purpose distinct from the purpose underlying the requirement for notice of a claim or occurrence. *National Union*, 2008 Tex. LEXIS 119 at *16. Notice of service of process, the Court said, lets the insurer know that the insured is subject to default and expects the insurer to interpose a defense. *Id.*

The Court said an insurer cannot necessarily assume that an additional insured, who has been served but has not given notice to the insurer, is looking to the

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[2] Interestingly, the insurer stipulated that it was not prejudiced by the late notice. *Id.* This stipulation did not appear to affect any court's analysis of the issues.

[3] Interestingly, Justice Willett disagreed with the opinion in *PAJ, Inc.* and wrote a dissenting opinion. Justice Willett was the author of the unanimous majority opinion in *National Union*.

[4] The Court also appeared to overrule several prior cases, including *Weaver*, *Cruz*, and *Harwell*, with a related holding that the notice-of-suit provision is a covenant rather than a condition precedent to coverage. *Id.* at *16-18. The earlier cases had expressly recognized that the notice-of-suit and suit-forwarding clauses were conditions precedent to coverage. *Harwell*, 896 S.W.2d at 173-74 (citing *Weaver*, 570 S.W.2d at 369); *Cruz*, 883 S.W.2d at 165. The consequences of treating the provision as a covenant, rather than a condition precedent, remain to be seen.

insurer to provide a defense. *Id.* For example, an additional insured may opt against invoking coverage because it wants to hire its own counsel and control its own defense. *Id.* at *17. In fact, the Court said, Emeritus's counsel believed that Morris had done just that, given Morris's statement at his deposition that he could not talk to Emeritus's counsel because he was waiting on a call from his attorney. *Id.*

Accordingly, the Court said, National Union did not incur a duty to inform Morris of available coverage or his entitlement to a defense, or a duty to sua sponte provide a defense, without any indication from Morris – either explicit or implicit – that he wanted or expected to be defended. *Id.* Neither the 1973 Board Order, nor the Court's recent decision in *PAJ, Inc.*, nor any other changes to Texas law since *Weaver* altered that conclusion. *Id.*

On the issue of prejudice, the Court noted that National Union "was obviously prejudiced" in the sense that it was exposed to a $1 million judgment. *Id.* at *15. The question, however, was not whether National Union suffered exposure to a financial risk, but whether it should be estopped to deny coverage because it was aware that Morris had been sued and served and had ample time to defend him. *Id.*

The answer, the Court said, must be "no" based on its discussion of duty. *Id.* National Union had no duty to notify Morris of coverage and no duty to defend Morris until Morris notified National Union that he had been served with process and expected National Union to answer on his behalf. *Id.* Therefore, following *Harwell*, because the insurer had no duty to defend the insured at the time it received notice of the claim, the insurer was not estopped from asserting the insured's breach of the policy as a bar to its liability. *Id.* (citing *Harwell*, 896 S.W.2d at 175). The Court said, "Absent a threshold duty to defend, there can be no liability to Morris, or to Crocker derivatively." *Id.*[5]

The Court held that National Union's actual knowledge that Morris had been sued and served did not establish, as a matter of law, that the insurer was not prejudiced by Morris's failure to comply with the notice-of-suit clause. *Id.* at *18. However, the Court did not decide – and was not asked to decide – whether the prejudice requirement would even apply if the insured wholly failed to invoke the policy by forwarding suit papers and requesting a defense.

Nor did the Court decide whether, if the prejudice requirement does apply to National Union's complaint of lack of notice, the insurer should be deemed to suffer prejudice as a matter of law when the insured wholly fails to comply with the notice-of-suit provision – similar to its previous holdings in *Cruz* and *Harwell* that, when the insured's notice was so late that the insured had already suffered a final adverse judgment, the insurer was prejudiced as a matter of law. These issues still may be addressed by the Fifth Circuit when it issues its opinion applying the Texas Supreme Court's answers to the certified questions.

In conclusion, the *National Union* court stated:

> Insurers owe no duty to provide an unsought, uninvited, unrequested, unsolicited defense. Consistent with our decision in *Weaver*, we decline to impose an extra-contractual duty on liability insurers that would force them to keep track of potential litigants who may or may not be additional insureds, may or may not be entitled to coverage, and may or may not expect a defense to a claim. Accordingly, because insurers need not provide coverage to insureds who never seek it, National Union had no duty either to inform Morris of available coverage or to voluntarily undertake a defense for him, and its actual knowledge did not establish a lack of prejudice a s a matter of law.

Id. at *18. The Fifth Circuit will now, presumably, issue a second opinion applying the Court's answers to the certified questions in ruling on the appeal from the cross-motions for summary judgment. That opinion had not yet issued as of the presentation date of this paper.

VI. WHAT THE FUTURE HOLDS FOR *NATIONAL UNION V. CROCKER*, THE NOTICE-OF-SUIT PROVISION, AND THE PREJUDICE RULE

One constant in all the Texas Supreme Court opinions addressing the notice-of-suit provision in liability policies is that the insured – whether it is the named insured, omnibus insured, or additional insured – must forward the suit papers to the insurer and request a defense to satisfy the notice-of-suit covenant or condition. This is the act that triggers an insurer's duty

[5] Considering this language, the opinion could be interpreted as holding that, because the insurer's obligations under the policy were never triggered for the additional insured, the issue of prejudice was a moot point. This is certainly not clear from the opinion, however.

to defend and provide coverage. The fact that an insurer has various levels of knowledge of the occurrence or the claim or even the suit itself (as in *National Union*) will not satisfy a liability policy's notice-of-suit requirement.

As noted above, a thought-provoking issue left open by the Fifth Circuit's first opinion in *Crocker* and the Texas Supreme Court's opinion in *National Union* is whether the insurer, who has actual notice of a suit against and service of process on its insured, but no compliance with the notice-of-suit provision (*i.e.*, no forwarding of suit papers or request for a defense), must show prejudice before it is relieved of its policy obligations. The *National Union* court held only that the insurer's actual knowledge of the suit did not establish, as a matter of law, a *lack of* prejudice (which would theoretically negate the notice-of-suit defense and entitle the judgment creditor to indemnity).

Should we assume this means the carrier still has to show prejudice to avail itself of the additional insured's lack of notice, but the existence and extent of the prejudice is a question of fact for a jury? It seems after *PAJ, Inc.* that the lack of notice would be considered only an "immaterial breach" unless the insurer can show prejudice from the lack of notice.

Or, should the prejudice to the insurer be deemed as a matter of law when the insured's notice to the insurer is "wholly lacking" and "nonexistent"? Some of the language in *National Union* can be interpreted as holding the insurer simply has no liability to the insured (or to a judgment creditor of the insured) because the policy obligations were never properly triggered. Therefore, how does the insurer's actual knowledge of the suit and service of process factor in when the insured has never requested that the insurer provide a defense and coverage under the policy?

Under previous Texas Supreme Court opinions dealing with the notice-of-suit requirement and the Prejudice Rule, the insurer has not had actual knowledge of the *suit* prior to the time the insured forwards the suit papers and requests a defense. In dicta in *Liberty Mutual v. Cruz*, the Court indicated that the existence of prejudice might be a fact issue *if* the insurer has actual knowledge of the suit. *Cruz*, 883 S.W.2d at 166 ("We agree that an insurer [who] is not notified of suit against its insured until a default judgment has become final, *absent actual knowledge of the suit*, is prejudiced as a matter of law.") (emphasis added).

Harwell v. State Farm involved a late notice defense against an additional insured who suffered a post-answer default judgment. However, in *Harwell*, the Supreme Court was very careful to show that the insurer had not obtained knowledge of the *suit*, as opposed to knowledge of the claim, so as to be consistent with its prior statement in *Cruz*.

In *Harwell*, the additional insured died in the accident, and the administrator of the additional insured's estate did not provide notice of the suit to State Farm at any time after she qualified as the administrator or became a party to the lawsuit. State Farm did know about the accident and the existence of the lawsuit via correspondence with the plaintiffs' counsel. The *Harwell* court held that, under its facts, State Farm had no duty to defend the administrator (she never forwarded suit papers or requested a defense) and suffered prejudice as a matter of law when it received notice of the default judgment after it was already final. *Harwell*, 896 S.W.2d at 174-75.

In *Cruz*, the insurer knew about the accident from a newspaper article but received notice of the suit only after a default judgment against the named insured had become final. The Court held the carrier suffered prejudice as a matter of law when it knew nothing about the suit until after a default judgment against the named insured had become final. *Cruz*, 883 S.W.2d at 165-66.

However, if the insurer has some actual knowledge of the suit, and the insured complies with the notice-of-suit provision after the insurer obtains this knowledge, most intermediate Texas courts of appeals have held that prejudice to the insurer is, essentially, a fact issue. *E.g.*, *Struna v. Concord Ins. Servs., Inc.* 11 S.W.3d 355 (Tex. App.–Houston [1st Dist.] 2000, no pet.) (record contained uncontroverted evidence of insurer's actual notice; thus, issue of whether insurer prejudiced by insured's late notice was fact issue for jury); *Ohio Cas. Group v. Risinger*, 960 S.W.2d 708 (Tex. App.–Tyler 1997, writ denied) (record contained sufficient evidence that insurer had actual notice of suit to support the fact finding of no prejudice); *Allstate Ins. Co. v. Pare*, 688 S.W.2d 680 (Tex. App.–Beaumont 1985, writ ref'd n.r.e.) (named insured notified insurer of claim, and plaintiffs' attorney sent insurer courtesy copy of petition before default judgment; thus, evidence sufficient to uphold jury's finding that insurer not prejudiced by insured's failure to forward suit papers); *but see Kim v. Farmers Ins. Exch., Inc.*, 2007 Tex. App. LEXIS 8533 (Tex. App.–Houston [1st Dist.] 2007, no pet. h.) (mem. op.) (insurer's summary judgment evidence conclusively established prejudice from summary judgment, and insured's evidence failed to raise fact issue); *Members Ins. Co. v. Branscum*, 803 S.W.2d 462

(Tex. App.–Dallas 1991, no writ) (insurer prejudiced as matter of law when insured did not comply with notice-of-suit provision and suffered default judgment, even though plaintiff's attorney told insurer's adjuster that suit had been filed; it is not just notice of suit, but service of citation on insured and forwarding of suit papers to insurer, that triggers duty to defend).

The Fifth Circuit already discussed some of these cases in its first opinion. Its discussion foreshadowed the holding of the Texas Supreme Court that an insurer's actual notice of the suit does not automatically negate prejudice as a matter of law. In other words (assuming the prejudice requirement applies to an insured who does not request a defense), if the carrier has some actual notice of the suit, the existence of prejudice to the insurer is likely to be a fact issue. We will have to wait and see how the Fifth Circuit addresses these issues in its second opinion applying the answers to the certified questions to the facts of *Crocker*.