PROFESSIONAL LIABILITY CLAIMS AND COVERAGE ISSUES

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Mr. McCoy has expertise in insurance coverage and related matters. During his over 30 year career, he has been involved in complicated and sophisticated insurance coverage disputes involving multi parties, multi lines of insurance, reinsurance, retail and wholesale insurance brokers, managing general agencies, and various syndicates from the overseas market.

Mr. McCoy has been involved in insurance coverage litigation involving almost every type of insurance policy imaginable, in both first and third party insurance cases, and in respect to both primary and excess insurance. Additionally, he has represented insurance brokers in almost every type of dispute over the brokering and producing of insurance policies, has represented other professionals in liability and malpractice actions, including lawyers, and has defended numerous insurance carriers and third party claims administrators in "bad faith" and extra-contractual litigation, and has been involved in countless general insurance defense matters ranging in scope from premises liability to sophisticated machinery products cases.

Mr. McCoy writes and lectures frequently in the insurance coverage, insurance "bad faith" and insurance broker errors and omissions area, is active as an affiliate member of Independent Insurance Agents and Brokers Organization, and additionally serves as an expert witness with respect to coverage, and insurance broker errors and omissions. Further, Mr. McCoy is also actively involved in employment litigation on behalf of employers, and is active as an affiliate member in certain HR organizations.

Born Houston, Texas, October 12, 1955. Admitted to Texas Bar, 1979. Also admitted to practice before U.S. Court of Appeals, Fifth Circuit; U.S. District Court, Northern, Eastern, Southern and Western Districts of Texas. Preparatory education, University of Texas (B.A., with high honors, 1976); legal education, Baylor University (J.D., 1979); Fraternity: Phi Delta Phi. Associate Editor, Baylor Law Review, 1977-1979. Member: State Bar of Texas; American Bar Association; Houston Bar Association; Texas Association of Defense Counsel; Defense Research Institute; Texas Bar Foundation. Lecturer and Author: *Representing an Insurance Company at Trial and Overcoming Jury Bias*; State Bar of Texas Lecture Series: Spring, 1993; Summer, 1993; Spring, 1994; and Summer, 1994. Lecturer: *Insurance Concerns*; Houston Claims Association; 1992 and 1993. Lecturer: Conducting Depositions; Houston Association of Independent Insurance Agents; 1994 and 2000. Lecturer: *Disputes Among Insurance Carriers*; University of Houston Law Center and Advanced Personal Injury Seminar or Advanced Insurance Seminar: Summer, 1996; Summer, 1997; Summer, 1998; Summer, 1999; Summer, 2000 and Spring, 2001. Lecturer and Author: *Appraisal and Arbitration*; Texas Insurance Law Symposium at South Texas Law School; Fall, 1997. Lecturer and Author: *Overview of Agents' and Brokers' Errors and Omissions Liability*; Houston Association of Independent Insurance Agents; Summer, 1998 and Fall, 1998; Texas Insurance Law Symposium; Summer, 1998 and 1999. Lecturer: *Recent Trends in Employment Law*; Association of Hospital Human Resource Managers, 1998. Director and Participant. Mock Trials: Houston Association of Independent Insurance Agents, 1994 and 1997; Tarrant County Association of Independent Insurance Agents, 1994; Houston Claims Association, 1994; Association of Human Resource Managers, 1996 and 1998. AV Rated by Martindale-Hubbell Law Directory. Texas Super Lawyer in 2006, 2007, as named by Texas Monthly Magazine in insurance coverage area; Top Lawyer as named by H Magazine, 2008, 2009.

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I. HISTORICAL REFERENCE

A. The Composition of Professional Liability Policies.

1. To insure professionals for the rendering of professional services, typically as defined in the policy per the specific profession.
2. Generally limited to "Wrongful Acts," as usually defined in the policy.
3. Claims made.
4. Sometimes claims made and reported.
5. Retroactive dates.
6. Limits reduced by defense costs and expenses.
7. Various professional liability policies included:
   a. lawyers;
   b. doctors;
   c. accountants;
   d. engineers;
   e. surveyors;
   f. real estate brokers and agents;
   g. insurance brokers and agents;
   h. directors and officers;
   i. architects;
   j. other medical related professionals and entities.

B. Differences with Occurrence Based Policies.

1. Occurrence based claims determined by whether the incident happened/arose during the pendency of the policy, regardless of when reported; if the incident was outside of the policy period, then typically no coverage.

2. Claims made policies require both the claim to have been made and reported; however, if a retroactive date existed, and the incident took place after the retroactive date, but was made during the year of coverage, and was reported as a claim, then assuming the claim comports with the insuring terms and conditions, without the application of other exclusions, there would be coverage.

C. Older case law made clear the differences between occurrence based policies and claims made policies regarding the importance of such notice.

1. *Members Mutual Ins. Co. v. Cutaia*, 476 S.W.2d 278 (Tex. 1972).

2. *Hirsch v. Texas Lawyers Ins. Exchange*, 808 S.W.2nd 561 (Tex.App.—El Paso 1991, writ denied).

3. *Hernandez v. Gulf Group Lloyds*, 875 S.W.2d 691 (Tex. 1994).

4. *Matador Petroleum Corp. v. St. Paul Surplus Lines Ins. Co.*, 174 F.3d 653 (5th Cir. 1999) (interpreting Texas law).

5. *Fed. Ins. Co. v. CompUSA, Inc.*, 319 F.3d 756 (5th Cir. 2003).

6. Distinctions were not really made historically in the claims made area between claims made, and claims made and reported.

D. Insurance Agency Issues with Respect to Notice of Claims.

1. Insurance agents are typically dual insurance agents, meaning that such agents can bind both the insured and the insurer with respect to representations, though numerous exceptions exist.

2. Generally, a wholesale insurance agent does not owe duties to the client, excepting certain circumstances. *North American Shipbuilding v. So. Marine & Aviation Underwriting*, 930 S.W.2d 829 (Tex.App.—Houston [1st Dist.] 1999, no writ).

3. *Lexington Ins. Co. v. Buckingham Gate, Ltd.*, 993 S.W.2d 185 (Tex.App. - Corpus Christi 1999, no writ).

4. *Celtic Life Ins. Co. v. Coats*, 885 S.W.2d 96 (Tex. 1994), in which the Texas Supreme Court held in general that an individual who performs at least some of the acts listed in Section 4001.051 of the Texas Insurance Code, is an agent of the insurer; it is important to note that this was a life insurance policy, and only involved an agent of the direct insurer, as opposed to a wholesale broker, or surplus lines broker.

5. Retail agent typically not the agent of surplus lines broker/underwriter unless is admitted carrier, or agent is written into the policy as the agent for claim loss notices.

II. TYPICAL BATTLEGROUND PREVIOUSLY IN COVERAGE ISSUES UNDER PROFESSIONAL LIABILITY POLICIES

A. Misrepresentations in the Application.

1. Controlled by Chapter 705 of the Texas Insurance Code, specifically § 705.004.
2. Essentially a five-prong test for determining if a misrepresentation allows the insurer to invalidate a policy of insurance.
3. *Mayes v. Mass. Mutual Life Ins. Co.*, 608 S.W.2d 612 (Tex. 1980).
4. Steep burden of proof. However, *see Legion Ins. Co. v. Texas Timber Group*, 2000 U.S. Dist. LEXIS 14488 (N.D. Tex. September 29, 2000).
5. Condition precedent and warranties. Traditionally, warranties which cause forfeiture, or policy coverage avoidance, have been disfavored under Texas law. *Gourverne v. Care Risk Retention Group*, 2008 U.S. Dist. LEXIS 38869 (S.D. Tex. May 13, 2008).
6. *Allied Bankers Life Ins. Co. v. De La Cerda*, 584 S.W.2d 529 (Tex.Civ.App.—Amarillo 1979, writ refused n.r.e.).
7. See however, *Riner v. Allstate Life Ins. Co.*, 131 F.3d 530 (5th Cir. 1997).

B. Reliance on Policy Language.

1. Conditions precedent or warranties, as noted above.

2. Prior wrongful acts.

3. Part of a continuing wrongful act or incident.

4. Claim reported after the expiration of either the policy or even the extended reporting date.

C. Issues When Consecutive Policies Exist.

1. Claim arguably is covered under one or both policies.

2. Impact on issues regarding deductibles, aggregates, etc.

3. Analysis if claim was not made and reported under first year policy, yet the "wrongful" act was known or should have been known at the time of application or inception of the second year policy.

D. Loss or Incident Known or Should Have Been Known.

1. The “known” loss doctrine.

2. Failure to disclose “incidents” which could give rise to a claim, and whether that is sufficient to void coverage at a later date.

3. “Fortuitous” loss doctrine.

4. “Reasonably should have been known” or “reasonably could have been foreseen” standard.

5. Verbal or written loss or incident; important distinctions in policy forms.

E. Limitation of Coverage to Designated Premises or Project, or Specified Operations Endorsement.

1. Designated premises or project may limit coverage to professional services being rendered at a designated premise or for a particular project.

2. Little case law in Texas interpreting limitation of coverage to designated premises or project.

3. Specified operations may attempt to limit coverage to the described operations in the policy itself.

4. Policy occasionally contains classified operations or description of operations, with limitations on coverage to those so described.

5. Classification limitations endorsement—ties back into the classification of both various premises and types of operations as noted in the declaration page.

III. NEW BATTLEGROUND IN COVERAGE ISSUES UNDER PROFESSIONAL LIABILITY POLICIES

A. Consent to Settle Clause, Cooperation Clause, and Prejudice by Settlements to which Insurer Does Not Agree.

1. The consent clause had been used favorably by insurers to deny professional liability claims where the insured settled without consent of the insurer. *Dairyland Co. Mutual Ins. Co. v. Roman*, 498 S.W.2d 145 (Tex. 1973); *Ford v. State Farm Mutual Automobile Ins. Co.*, 550 S.W.2d 663 (Tex. 1977); *Guaranty Co. Mutual Ins. Co. v. Kline*, 845 S.W.2d 810 (Tex. 1992);
2. Denials previously based on by insurers' reliance on consent to settle clauses, cooperation clauses, or conditions precedent requiring consent by an insurer to a settlement for coverage to exist.
3. Notice of claim provisions handled similarly; *Members Mutual Ins. Co. v. Cutaia, supra*, in which Texas Supreme Court did not require insurer prejudice as to claim denial where late notice took place.
4. Notice of claim provisions for occurrence based policies changed, requiring prejudice, in Texas State Commission Board Order No. 23080.
5. Texas law regarding consent to settle clauses, and the requirement of prejudice, changed in *Hernandez v. Gulf Group Lloyds Ins., supra.*
6. Attempts by insurer coverage counsel to distinguish the Hernandez decision requiring prejudice on the consent to settle provision if such constituted an actual policy requirement, as opposed to timely notice of a claim, was soundly rejected by Texas Supreme Court in *Lennar Corp. v. Markel*

B. Claim Notices Today, Prejudice Required Even in Claims Made Policies?

1. *PAJ Inc. v. Hanover Ins. Co.*, 243 S.W.3d 630 (Tex. 2008).

   a. *PAJ* actually involved an occurrence based policy.

   b. Notice prejudice rule had been adopted by the Fifth Circuit in *Hanson Prod. Co. v. American Ins. Co.*, 108 F.3d 627 (5th Cir. 1997) and *Ridglea Estate Condo. Assoc. v. Lexington Ins. Co.*, 415 F.3d 474 (5th Cir. 2005).

2. As defined by the Fifth Circuit in the above-referenced cases, appears to have been immaterial under the notice prejudice rule in an occurrence based policy whether such would be considered a material breach of an insurance contract provision, or a condition precedent under the policy with respect to coverage itself.

3. PAJ established that the insurer would have to prove prejudice, which would establish a material breach of the policy condition or precedent to coverage, either way, and that a notice of claim provision stating, "as soon as practicable," would generally not give rise to prejudice.

C. Evolution of *Prodigy* and *Financial Industries/XL Specialty*.

1. *Prodigy Communications Corp. v. Agric. Excess; Surplus Ins. Co.*, 288 S.W.3d 374 (Tex. 2009), involved a claims made policy, where the insured was required to give written notice of the claim to the insurer as soon as practicable.
2. There was a temporal provision as well, namely requiring claim notice no later than 90 days.
3. Admission by the insurer that the claim was reported within 90 days, but contention not, "as soon as practicable."
4. Texas Supreme Court in *Prodigy* noted the distinction between "as soon as practicable" and "in no event later than 90 days" requirement as to its decision that the claim could not be denied under the facts.
5. *Financial Indus. Corp. v. XL Specialty Ins. Co.*, 285 S.W.3d 877 (Tex. 2009) was a claims made policy that contained a condition precedent to coverage that the insured give the insurer written notice of any claim "as soon as practicable."
6. No temporal deadline.
7. Was a claims made policy, but not a "claims made and reported policy."
8. Texas Supreme Court in *XL Specialty* required a showing of prejudice by the insurer to allow denial of coverage, regardless of the "claims made" nature of the policy, where notice was indeed given within the policy period.

D. Claims Made and Reported Policies; Distinction?

1. Argument can be made that even under *PAJ*, *Prodigy*, and *XL Specialty*, prejudice is not required for "claims made and reported" policy if there is a temporal requirement with respect to the giving of notice, and it has not been met.

2. However, see concurrence in *Lennar* II, essentially stating that despite a "bright line" distinction between a condition precedent and insuring agreement language requiring consent to settle, that all insurance policies should be subject to a prejudice requirement as to notice provisions, consent provisions, cooperation clauses, and any other portion of the policy, regardless of the type of policy.

E. How Far Will the Courts Go?

1. Argument can be made that a prejudice requirement extends to a claims made policy where notice is even given outside of the policy period, at least where the lawsuit has not been settled and/or mediated, reached trial, or had important deadlines terminated, before notice is given; in other words, there will be an argument that prejudice must be shown in this situation, and it does not exist; thus, coverage would exist.

2. *See Eastex Medical Center Regional Healthcare System v. Lexington Ins. Co.*, 575 F.3d 520 (5th Cir. 2009).

a. Lexington had denied the claim because of the insured's alleged failure to comply with the notice provisions; Lexington received no formal "notice" of the claim.

b. However, Lexington was arguably aware of the claim because of a "loss run."

c. The Court found that providing notice of the claim and notice of the lawsuit were separate and distinct obligations of the insured under the policy.

d. The Court found that *Prodigy* and *XL Specialty* would not allow the insured to fail to satisfy a notice requirement as to the lawsuit itself.

e. Still, since notice of the underlying claim had been timely given per the temporal boundaries of the policy, then notice of the suit, even if provided outside of the policy period, would be subject to a prejudice showing.

f. *See Evanston Ins. Co. v. Keeway America, LLC.*, 210 U.S. Dist. LEXIS 66072 (N.D. Tex., June 29, 2010).

g. The subject policy was only claims made, and not claims made and reported.

h. Thus, it was considered permissible for the insured to report claims to Evanston even after the policy period had expired.

i. The Court indicated that if the subject policy had been a claims made and reported policy, Evanston would not need to show prejudice from the failure of the insured to provide notice within a specified and temporal time period.

F. Consecutive Insurance Policies in the Claims Made and Reported Area.

1. Next coverage battle in the professional liability insurance arena.
2. What if claim is made under one policy, but not reported until the following policy?
   a. Assuming a temporal notice requirement under the first year policy, arguably no coverage for failure to report at all during the policy period.
   b. However, second year policy would involve a claim being reported that actually took place before the inception of the policy coverage, and was known by the insured before the inception of the policy coverage.
3. Quandary as to coverage.
4. More confusing: what if consecutive policy years involve different insurers?
   a. First year insurer will argue claim was not timely reported within the policy period, or within the temporal deadline, so no coverage.
   b. However, second year insurer will argue that it was not a claim "made" under its policy, but was "known" to the insured at the time of policy inception, so no coverage.

IV. CONCLUSION

A. Foreseeable Next Battleground in Coverage Issues Under Professional Liability Policies.

1. Probable tightening of coverage defenses with respect to claims made, and claims made and reported policies.

2. Probable extension of prejudice requirement to conditions precedent, part of the insuring agreement, a definition that restricts coverage, an exclusion, or an endorsement that restricts coverage.

3. Expected additional “push back” from policyholder counsel over insured’s ability to choose counsel where any remotely potential coverage issues are raised in reservation of rights, despite current case law.

4. Possible tightening of policy language, including definitions and endorsements, to allow certain coverage defenses to continue to be raised.

B. Emerging Trends.

1. Despite “soft” market, possible increase in deductibles and self-insured retention programs.

2. Despite “soft” market, additional scrutiny as to underwriting.

3. Continued expansion into “new programs” as to “new professions.”

C. Finality.

1. May continue to be lacking, causing potential struggle between underwriters, agents and brokers, claims departments, and policyholders.