UPDATE ON INSURANCE CODE ON DECEPTIVE, UNFAIR, AND PROHIBITED PRACTICES

STEVEN R. SHATTUCK
COOPER & SCULLY, P.C.
900 JACKSON STREET, SUITE 100
DALLAS, TEXAS 75202

TELEPHONE: 214/712-9500
FACSIMILE: 214/712-9540

STATE BAR OF TEXAS

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I. INTRODUCTION

The Texas Legislature, in June 2003, re-codified various portions of the Texas Insurance Code. Included in this re-codification was Article 21.21, which now is found in Chapter 541 of the Insurance Code. In discussing the re-codification, the Legislature stated:

> House Bill 2922, a continuation of the legislature's ongoing statutory revision program, contains nonsubstantive changes adding five titles and two subtitles to the Insurance Code, repealing various source laws from which the new code content is derived, and making other conforming amendments. The new titles and subtitles relate to Texas Department of Insurance fund and revenue matters, the protection of consumer interests, life and health coverage, title insurance, and the regulation of professionals.

Although the Texas Legislature indicates that the changes are nonsubstantive, there are, nevertheless, some significant changes as Article 21.21 becomes Chapter 541. The purpose of this paper is to document the significant changes made in the re-codification process and then to discuss recent cases interpreting the provisions of either 541.001 *et seq.* or the prior Article 21.21.

II. GENERAL TYPES OF CHANGES

The new format for consumer protection in Chapter 541 involves a number of different types of changes that range from minor to potentially significant. There are changes involving specific word choices, additions of new sections and subsections and changes to date calculations. The general changes are discussed below.

A. Word Choices

Although there are numerous examples of changes to the text involving what word is used in a particular statute, the vast majority of those changes are stylistic and do not change the meaning of the statute. Examples include changing the tense of the words that discuss a rule or prohibition. For example, Article 21.21 §4(3) discusses:

> making, publishing, disseminating, or circulating, directly or indirectly, or aiding, abetting or encouraging the making, publishing, disseminating or circulating of any oral or written statement…

Section 541.053 is the new code section and contains a very similar prohibition using the following language:

> It is an unfair method of competition or an unfair or deceptive act or practice in the business of insurance to directly or indirectly make, publish, disseminate, or circulate or to aid, abet, or encourage the making, publication, dissemination, or circulation of a statement…

As can be seen in this example, the change is one more of style of language rather than any change, or intent to change, the meaning of the prohibition contained in each section of the statute. These minor language changes are contained throughout the re-codification and they do not appear to create any intended or unintended changes to the law as previously set out in Article 21.21.

It should also be noted that the references to "the Board" that are included throughout Article 21.21 have been removed and replaced, where appropriate, by references to "the Commissioner." This is due to the fact that the State Board of Insurance turned over its authority over rates, policy forms and related matters to the Commissioner of Insurance on December 16, 1993.

B. New Subsections and Sections

The re-codification of Article 21.21 has greatly increased the number of sections and subsections contained in the statute as the Legislature has attempted to subdivide long paragraphs that contained more than one idea and the creation of new sections in place of one long section to make it, hopefully easier to follow and understand.

One obvious revision is found in the prior Article 21.21 §12, dealing with the subject of immunity from prosecution, which was previously written as follows:

> If any person shall ask to be excused from attending and testifying or from producing any books, papers, records, correspondence or other documents at any hearing on the ground that the testimony or evidence required of him may tend to incriminate him or

> subject him to a penalty or a forfeiture, he shall notwithstanding be directed to give such testimony or produce such evidence, he must nonetheless comply with such direction, but he shall not thereafter be prosecuted or subjected to any penalty or forfeiture for or on account of any transaction, matter or thing concerning which he may testify or produce evidence pursuant thereto, and no testimony so given or evidence produced shall be received against him upon any criminal action, investigation or proceeding; provided, however, that no such individual so testifying shall be exempt from prosecution or punishment for any perjury committed by him while so testifying and the testimony or evidence so given or produced shall be admissible against him upon any criminal action, investigation or proceeding concerning such perjury, nor shall he be exempt from the refusal, revocation or suspension of any license, permission or authority conferred, or to be conferred, pursuant to the Insurance Code of this state. Any such individual may execute, acknowledge, and file in the office of the Board a statement expressly waiving such immunity or privilege in respect to any transaction, matter or thing specified in such statement and thereupon the testimony of such person or such evidence in relation to such transaction, matter or thing, may be received or produced before any judge or justice, court tribunal, grand jury or otherwise, and if so received or produced, such individual shall not be entitled to any immunity or privilege on account of any testimony he may so give or evidence so produced.

As one may observe in reviewing that section in the old Article 21.21, the sentences are long and are difficult to follow. This provision has been re-codified as § 541.007, which adds subsections and is easier to read. The new provision is as follows:

> (a) This section applies to a person who requests to be excused from attending and testifying at a hearing or from producing books, papers, records, correspondence, or other documents at the hearing on the ground that the testimony or evidence may
>
> (1) tend to incriminate the person; or
>
> (2) subject the person to a penalty or forfeiture.
>
> (b) A person who, notwithstanding a request described by subsection (a), is directed to provide the testimony or produce the documents shall comply with that direction. Except as provided by subsection (c), the person may not be prosecuted or subjected to a penalty or forfeiture for or on account of a transaction, matter, or thing about which the person testifies or produces documents, and the testimony or documents produced may not be received against the person in a criminal action, investigation, or proceeding.
>
> (c) A person who complies with a direction to testify or produce documents is not exempt from prosecution or punishment for perjury committed while testifying, and the testimony or evidence given or produced is admissible against the person in a criminal action, investigation, or proceeding concerning the perjury, and the person is not exempt from the denial, revocation, or suspension of any license, permission, or authority conferred or to be conferred under this code.
>
> (d) A person may waive the immunity or privilege granted by this section by executing, acknowledging, and filing with the department a statement expressly waiving immunity for privilege for a specified transaction, matter or thing. On filing the statement: (1) the testimony or documents produced by the person in relation to the transaction, matter, or thing may be received by or produced before a judge or justice or a court,

> grand jury, or other tribunal; and (2) the person is not entitled to immunity or privilege for the testimony or documents received or produced under subsection (1).

Another example is former Article 21.21 § 4(2), which involved misrepresentations and false advertising of policies. That provision reads:

> Making, issuing, circulating, or causing to be made, issued or circulated, any estimate, illustration, circular or statement misrepresenting the terms of any policy issued or to be issued or the benefits or advantages promised thereby or the dividends or share of the surplus to be received thereon, or making any false or misleading statements as to the dividends or share of surplus previously paid on similar policies, or making any misleading representation or misrepresentation as to the financial condition of any insurer, or as to the legal reserve system upon which any life insurer operates, or using any name or title of any policy or class of policies misrepresenting the true nature thereof. Or making any misrepresentation to any policyholder insured in any company for the purpose of inducing such policyholder to lapse, forfeit, or surrender his insurance.

This complex and difficult to follow rule has been replaced, in § 541.051, by the following:

> It is an unfair method of competition or an unfair or deceptive act or practice in the business of insurance to:
>
> (1) make, issue, or circulate or cause to be made, issued, or circulated an estimate, illustration, circular, or statement misrepresenting with respect to a policy issued or to be issued:
>
> (A) the terms of the policy;
>
> (B) the benefits or advantages promised by the policy; or
>
> (C) the dividends or share of surplus to be received on the policy;
>
> (2) make a false or misleading statement regarding the dividends or share of surplus previously paid on a similar policy;
>
> (3) make a misleading representation or misrepresentation regarding:
>
> (A) the financial condition of an insurer; or
>
> (B) the legal reserve system on which a life insurer operates;
>
> (4) use a name or title of a policy or class of policies that misrepresents the true nature of the policy or class of policies; or
>
> (5) make a misrepresentation to a policyholder insured by any insurer for the purpose of inducing or that tends to induce the policyholder to allow an existing policy to lapse or to forfeit or surrender the policy.

Although the changes set out above, and which are found in the entire re-codification, do not make substantive changes to the prior sections, they do make the rules easier to read and understand. In addition to these types of changes, the new chapter contains new sections to divide up prior sections that appeared to be too long and complicated. For example, Article 21.21 §6, pertaining to hearings, witnesses, appearances and production of documents has been divided up and placed in separate sections as Sections 541.102, 541.103, 541.104, 541.105 and 541.106. Similarly, former Article 21.21 § 7 has been separated into Sections 541.107, 541.108, 541.109 and 541.110. These changes are, again, an attempt to make the provisions easier to read and understand.

C. Date Calculation Changes

A series of changes were made to provisions containing a calculation of a date or a deadline. In Article 21.21 § 6, there is a description of the amount of time to which an insurer is entitled prior to a hearing on allegations of deceptive practices:

> … it shall issue and serve upon such person a statement of the charges in that respect and a notice of a hearing thereupon to be held at a time and place fixed in the notice, which shall

> not be less than five days after the date of the service thereafter.

The re-codified provision states:

> The Department may not hold the hearing before the sixth day after the day the notice is served.

There are several other similar examples of this stylistic change to date calculation:

Old Article 21.21 § 19:

> At least 30 days prior to the commencement of a class action suit for damages under Section 17 of this Article, this prospective plaintiff must notify the intended defendant of his complaint…

New Section 541.255:

> Not later than the 31st day before the date a class action for damages is commenced under this chapter…

Old Article 21.21 § 16(d):

> All actions under this article must be commenced within two years after the date on which the unfair method of competition or unfair or deceptive act or practice occurred…

New Section 541.162:

> A person must bring an action under this chapter before the second anniversary of the following…

Old Article 21.21 § 16 describes the 60 day notice provision before filing suit as follows:

> As a prerequisite to filing a suit seeking damages under this section against any person, the person seeking damages shall give written notice to the other person at least 60 days before filing suit.

The new provision, contained in Section 541.154, states:

> A person seeking damages in an action against another person under this subchapter must provide written notice to the other person not later than the 61st day before the date the action is filed.

Again, these changes appear to be stylistic in nature. Although the style is consistent throughout the new chapter 541, it is difficult to say whether the new language actually is easier to understand as the basis for calculation of the dates and deadlines in question.

III. POTENTIALLY SUBSTANTIVE CHANGES

The stated purpose behind the re-codification of Article 21.21 was not to make substantive changes. Nevertheless, anytime language changes in a statute it can cause unintended changes. They will be discussed in this section.

A. Life and health Counselor

In Section 541.002 the definitions include one for "person" which is defined to include a "life and health counselor." The former definition, in Article 21.21 § 2, did not include a health counselor. It is not clear what impact this will have, but it certainly appears that the new definition seeks to make clear that "person" includes someone counseling on health policies as well as life policies.

B. Unfair Methods of Competition

With regard to prohibited acts and practices under the statute, Article 21.21 § 3 stated that:

> No person **shall** engage in this state in any trade practice that is defined in this Act as, or determined pursuant to this Act to be, an unfair method of competition…(emphasis added).

On the other hand, the new provision, Section 541.003, provides:

> A person **may** not engage in this state in the trade practice that is defined in this chapter as or determined under this chapter to be an unfair method of competition or an unfair or deceptive act or practice in the business of insurance. (emphasis added).

The Legislature probably did not intend to change the prohibitions listed in this provision, but there is generally a difference in the law between "shall" and "may." The word "may" implies a certain level of discretion that the Legislature likely did not intend and that is an interesting change in the two statutes.

C. Hearings

Another minor substantive change is in Section 541.103 (former 21.21 § 6) which involves hearings after the Department of Insurance has opened an investigation against an insurance company which has allegedly violated some forbidden unfair practice. The former law required the insurer to show cause "why an order should not be made by the Board requiring such person to cease and desist from the acts, methods or practices so complained of…." This language made it appear that the hearing could include activities not identified in advance, but that were brought up at the hearing. The new rule makes it clear that the hearing is limited to identified complaints with the following language:

> A person against whom charges are made under Section 541.102 is entitled at the hearing on the charges to have an opportunity to be heard and show cause why the Department should not issue an order requiring the person to cease and desist from the unfair method of competition or unfair deceptive act or practice **described in the charges.** (emphasis added).

IV. RECENT CASES ON ARTICLE 21.21/ CHAPTER 541

There are not a lot of recent cases of much interest on the chapter entitled "Deceptive, Unfair, and Prohibited Practices," but we will discuss those that appear to have significance.

A. *Texas Mutual v. Ray Ferguson*

Because communications made during the course of judicial proceedings are privileged, allegedly defamatory statements made by the Texas Workers' Compensation Insurance Fund about the insured employer during the litigation process cannot be the basis of an unfair practice or act under former Article 21.21. *Texas Mutual Insurance Co. v. Ray Ferguson Interests, Inc.*, 2006 Tex.App. LEXIS 2001 (Tex.App.—Houston [1st Dist.] 2006, pet. denied). That also means that the claimant could not recover attorneys' fees under Article 21.21 for such communications. *Id.* at 25-26.

B. *Farmers Group v. Lubin*

In *Farmers Group, Inc. v. Lubin*, 222 S.W.3d 417 (Tex. 2007), the Texas Attorney General attempted to bring a class action under Chapter 541 of the Insurance Code against certain insurance companies on behalf of insurance buyers. The trial court certified the class, but the intervenor policyholders appealed, arguing that the Attorney General did not two of the certification requirements to act as a class representative. The court of appeals agreed with the policyholders and reversed the certification. The Texas Supreme Court reversed that ruling, noting that the Insurance Code, in Chapter 541, specifically allows the Attorney General to bring class action suits. *Id.* Therefore, the court ruled that the standard class action requirements had to be applied generally to the claims asserted by the Attorney General and not to the Attorney General himself. *Id.* at 426.

C. *Rocor International v. National Union*

On May 23, 2002, the Texas Supreme Court in *Rocor International, Inc. v. National Union Fire Ins. Co. of Pittsburgh, Pa.*, 77 S.W.3d 253 (Tex. 2002) for the first time recognized statutory liability from an insurer to its insured for failing to settle a third-party claim. This liability was predicated upon violation of the Unfair Claims Settlement Practices Act. In that decision, a majority held that in order to establish liability for the insurer's failure to reasonably attempt settlement of a claim against the insured, the insured must show that:

> (1) the policy covers the claim; (2) the insured's liability is reasonably clear; (3) the claimant has made a proper settlement demand within policy limits; and (4) the demand's terms are such that an ordinarily prudent insurer would accept it.

In many of the issues, the requirements for a valid or proper settlement demand are the same. In addressing whether or not the same rules that govern *Stowers* demands were going to govern liability under the Unfair Claims Settlement Practices Act, the Supreme Court stated that:

> We see no reason why an insurer's duty to its insured under article 21.21 should not be similarly circumscribed. Accordingly, we hold that an insurer's statutory duty to reasonably attempt settlement of a third-party claim against its insured is not triggered until the claimant has presented the insurer with a proper settlement demand within policy limits that an ordinarily prudent insurer would have accepted. *See id.* A proper settlement demand generally must propose to release the insured fully in exchange for a stated sum, although it may substitute the "policy

limits" for that amount. *See id.* 848-49. At a minimum, the settlement demand must clearly state a sum certain and propose to fully release the insured. *See id.* at 849.

V. CONCLUSION

As the foregoing analysis indicates, the re-codification of Article 21.21 into the new Chapter 541 involved few substantive changes, but the new sections and subsections have definitely assisted in making the statutes easier to read and interpret. Only time and future cases will tell us whether or not any of the potentially substantive changes will actually spawn any significant cases.

In the meantime, the significance of the *Rocor* decision is still being felt as the rulings made therein will continue to impact future cases.

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