NO. 14-0721

IN THE SUPREME COURT OF TEXAS

USAA Texas Lloyds Company,

Petitioner,

v.

Gail Menchaca,

Respondent.

On Petition for Review from the
Thirteenth Court of Appeals at Corpus Christi–Edinburg, Texas
Cause No. 13-13-00046-CV

AMICUS CURIAE BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA IN SUPPORT OF PETITIONER

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STATEMENT OF INTEREST

The Chamber of Commerce of the United States of America is the world's largest federation of businesses and associations, representing 300,000 direct members and indirectly representing the interests of more than three million U.S. businesses and professional organizations of every size and in every relevant economic sector and geographical region of the country. An important function of the Chamber is to represent its members' interests by filing amicus curiae briefs in cases involving issues of national concern to American businesses.

The Chamber has no direct financial interest in the outcome of this litigation. No counsel for a party wrote this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than the amicus curiae, its members, or its counsel made a monetary contribution intended to fund its preparation or submission.

ISSUES PRESENTED

1. When a jury rejects an insured's claim that her insurer breached its contract, is the insured precluded from recovering policy benefits for an extra-contractual claim?

2. When a jury rejects an insured's claim that her insurer breached its policy, can the insured nevertheless recover policy benefits if the same jury finds fault with the insurer's investigation?

TO THE HONORABLE SUPREME COURT OF TEXAS:

INTRODUCTION

Amicus Curiae The Chamber of Commerce of the United States of America submits this brief to urge the Court to reaffirm the well-settled principle of insurance law that there can be no recovery of damages equivalent to or greater than policy benefits without a breach, no matter whether an insured's extra-contractual claim sounds in common law or statute. The Court should not sanction the lower court's sudden departure from established precedent, when doing so would disrupt not only the insurance industry but all businesses that can be subject to statutory violations. Accordingly, the Court should grant Petitioner USAA's petition for review, reverse the court of appeals' judgment, and render judgment that the plaintiff take nothing consistent with the jury's finding below that there was no breach of the insurance contract.

STATEMENT OF THE CASE

The Chamber adopts the Statement of the Case in USAA's Brief on the Merits.

STATEMENT OF FACTS

The Chamber adopts and incorporates by reference the facts as relevant to this brief that are found in USAA's Statement of Facts in its Brief on the Merits.

SUMMARY OF THE ARGUMENT

There is well-established precedent from this Court that if a contract does not legally obligate a party to provide a contract benefit (and hence the contract has not been breached if the benefit has not been provided), a party may not recover the contract benefits or damages equivalent to the contract benefit. This is true in general business contracts as well as specialized insurance contracts.

Yet the court of appeals diverged from this well-established precedent by holding that the plaintiff was entitled to obtain 'policy benefits' even though the plaintiff failed to prove at trial that her insurer had breached the contract. The court of appeals erroneously held that if an insurer violates an extra-contractual insurance statute, the insurer owes 'policy benefits' even in the absence of a breach of the underlying policy contract. Though the court of appeals recognized the general, well-adhered-to rule that recovery must be predicated on a breach, it justified its exceptional decision by characterizing this suit as one of "unique circumstances." There is nothing unique here. Insurers, and indeed many

businesses in this state, conduct their business through contracts with its consumers. Those policies are—in the absence of extreme wrongdoing causing a harm unrelated to the contract—the beginning and end of the parties' legal relationships. That is a basic tenet of contract law. The court of appeals' anomalous holding upends this fundamental principle and warrants reversal.

ARGUMENT

This "bad faith" lawsuit centers on an insured's attempts to convert her insurer's denial of an insurance claim for $455 in storm damage to her home into a recovery of $1.2 million in damages, nearly *six times* the home's insured value. The core issue is whether, under Texas law, a plaintiff may recover policy benefits for an insurance company's alleged "bad faith" in rejecting a claim when the insurer did not, in fact, breach the insurance contract. The Chamber urges this Court to reaffirm its precedent and make clear that contractual benefits are not available for extra-contractual claims, when there has been no breach of the contract or policy.

I. This Court Has Made Clear That Policy Benefits Are Not Recoverable Damages When There Has Been No Breach Of The Contract.

This Court has decided several key cases dealing with an insured's attempt to recover policy benefits, which the parties have extensively briefed. *See Vail v. Tex. Farm Bureau Mut. Ins. Co.*, 754 S.W.2d 129, 136 (Tex. 1988); *Twin City Fire Ins. Co. v. Davis*, 904 S.W.2d 663, 666 n.3 (Tex. 1995); *Repub. Ins. Co. v. Stoker*,

903 S.W.2d 338, 341 (Tex. 1995); *Provident Am. Ins. Co. v. Castañeda*, 988 S.W.2d 189, 198 (Tex. 1998). Beyond just the interplay of these key cases with the facts of this suit, there are broader legal issues that affect the entire insurance industry, and indeed any business that regularly engages in consumer contracts. Unfortunately, the court of appeals' decision misinterpreted the legal principles from these cases and has injected uncertainty into an industry predicated on being able to assess and anticipate *contractually-allocated* risk. Menchaca's and the court of appeals' treatment of contract and insurance law is untenable and warrants reversal by this Court.

Ordinarily, allegations of claim mishandling do not entitle an insured to recover policy benefits. *See Castañeda*, 988 S.W.2d at 198 (relying on *Stoker* and rejecting insured's attempt to recover "damages equivalent to policy benefits" for claims-handling violations under predecessor statute to Chapter 541). Stated another way, there can be no recovery under Chapter 541 unless the insured suffers an injury "*independent* of the policy claim." *Stoker*, 903 S.W.2d at 341 (emphasis added). And it is only when the insurer, in denying the claim, commits some act, "so extreme," that the insured may suffer some injury independent of the policy claim. *See id.* Thus, this Court has indicated that it is a rare—and heretofore merely theoretical—instance that this exception to the settled rule would apply.

In sum, there can be no recovery for extra-contractual claims in this case, whether they sound in common law or statute, without proof of an injury independent of the policy claim.

Though Menchaca relies heavily on *Vail*, the Court in that case found that an insurer's "*unfair refusal* to pay the insured's claim" allows recovery of policy benefits as damages. *See* 754 S.W.2d at 136 (emphasis added). Not only is that inapposite to the inadequate-investigation claim alleged here, but the Court later warned against construing *Vail* to authorize policy benefits as damages for *other* allegations of bad-faith:

> This extrapolation—from a case involving an unfair refusal to pay policy benefits, to all bad faith cases—is unwarranted, even in the context of a DTPA or Insurance Code claim. The reason is that some acts of bad faith, *such as a failure to properly investigate a claim* or an unjustifiably delay in processing a claim, do not necessarily relate to the insurer's breach of its contractual duties to pay covered claims, and may give rise to different damages.

Twin City Fire Ins., 904 S.W.2d at 666 n.3 (emphasis added).

Unlike where an insurer wrongfully refuses to pay a covered claim, there is no causal link between an insurer's allegedly deficient investigation and the loss of policy benefits to the insured, which are controlled by the policy. *Compare Castañeda*, 988 S.W.2d at 198 (insurer's failure to adopt reasonable standards for investigating claims was not the "producing cause of any damage separate and apart from those that would have resulted from a wrongful denial of the claim"),

with Vail, 754 S.W.2d at 136 (an insurer's unfair refusal to pay the insured's claim causes damages in at least the amount of the policy benefits wrongfully withheld).

Here, Menchaca's attempt to recover policy benefits is not premised on any breach of the policy—which the jury refused to find—but rather on an extra-contractual claim alleging an inadequate investigation. But any deficiency in the investigation could not have "caused" Menchaca any loss of policy benefits, which was the *only measure of damages* submitted in the charge.[1] *Accord Stoker*, 903 S.W.2d at 342 (Spector, J., concurring) ("The investigation of the claim clearly did not cause the damages to the [insured who] would have incurred those same damages even if their claim had been investigated properly."). Menchaca never sought or obtained a finding on any separate investigation-related damages. At bottom, Menchaca is impermissibly attempting to recover extra-contractual economic damages based on duties created by the contract (*i.e.*, the insurance policy), in direct contravention of the economic loss rule. *See Sw. Bell Tel. Co. v. DeLanney*, 809 S.W.2d 493, 494-95 (Tex. 1991); *see also Jim Walter Homes, Inc. v. Reed*, 711 S.W.2d 617, 618 (Tex. 1986) ("When the injury is only the economic loss to the subject of a contract itself the action sounds in contract alone.").

[1] The charge here defined damages 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."

Menchaca's position that expected policy benefits can equate to bad-faith damages "has been firmly rejected by the Texas Supreme Court" with respect to allegations that the insurer failed to properly investigate a claim. *Mai v. Farmers Tex. Cnty. Mut. Ins. Co.*, No. 14-07-00958-CV, 2009 WL 1311848, at *6 (Tex. App.—Houston [14th Dist.] May 7, 2009, pet. denied) (citing *Castañeda*, 988 S.W.2d at 198; *Stoker*, 903 S.W.2d at 341). Simply put, *Vail* cannot plausibly be read to permit a recovery of policy benefits for a statutory violation in the absence of a breach of contract. Indeed, as USAA points out in its brief, this Court has repeatedly rejected policy benefits as a recoverable measure of damages for mishandled-investigation claims. *See Progressive Cnty Mut. Ins. Co. v. Boyd*, 177 S.W.3d 919, 922 (Tex. 2005); *Castañeda*, 988 S.W.2d at 198; *Stoker*, 903 S.W.2d at 341.

The importance of this issue cannot be overstated, not just to the insurance industry but to businesses across this state, for reasons discussed in more detail in Section II. The Fifth Circuit recently certified a question on this very issue and noted in its opinion that, while it had previously held *Castañeda* to be the controlling precedent, subsequent lower courts' opinions, including the court of appeals in this case, have confused the issue. *See In re Deepwater Horizon*, 807 F.3d 689, 698-99 (5th Cir. 2015). In doing so, the Fifth Circuit noted that the

differing positions "illuminate the magnitude and wide ramifications for insurance law that this issue presents." *Id.* at 698 (internal quotation and alteration omitted).

It is beyond dispute that if an insurer breaches the policy, it is liable for damages, and it may be liable for statutory penalties in certain instances. It is also beyond dispute that if an insurer causes an injury to an insured separate and apart from policy benefits, then it can be liable for those resulting damages. But there is no justification for allowing an insured to recover policy benefits when the insurer has not breached the contract. *Castañeda* squarely resolves this issue. The court of appeals failed to apply this binding precedent, and this error has ramifications not just for USAA, and not just for all insurers in this state, but also for all businesses that regularly do business by contract. An error of this magnitude requires reversal.

II. Allowing Policy Benefits In The Absence Of A Breach Is Against Texas' Policy In Favor Of Freedom Of Contract And Upends Not Only Longstanding Legal Precepts For The Insurance Industry But Also For All Other Businesses That Regularly Enter Contracts.

Notwithstanding the fact that this Court's precedents support the merits of USAA's legal arguments, this issue is important to the insurance industry and also of concern more broadly to the businesses in other industries. If left to stand, the court of appeals' erroneous holding will be invoked by enterprising plaintiffs' lawyers to attempt to hold *any* Texas business that enters into a contract to liability for contract benefits for statutory violations *even in the absence of a breach of the*

contract. This would be true whether the statutory violation was alleged under the Insurance Code or whether it was alleged under the Deceptive Trade Practices Act, under Title 4 of the Finance Code concerning consumer loans, or under the Property Code provisions governing landlord-tenant matters, to name just a few examples.

All of these circumstances are governed, largely, by contractual relationships between parties. The parties' rights and obligations are bargained for and spelled out in the contract, usually in some detail. The parties can structure their conduct accordingly, knowing the consequences if one or the other fails to perform the contractually imposed duties. This accords with "Texas' strong public policy in favor of preserving the freedom of contract." *Fairfield Ins. Co. v. Stephens Martin Paving, L.P.*, 246 S.W.3d 653, 664 (Tex. 2008); *see also Wood Motor Co. v. Nebel*, 238 S.W.2d 181, 185 (Tex. 1951). "Freedom of contract allows parties to…allocate risk as they see fit." *Gym-N-I Playgrounds, Inc. v. Snider*, 220 S.W.3d 905, 912 (Tex. 2007).

But to allow one party to obtain contract benefits—despite the other party performing under the contract, or otherwise not committing a breach—could open businesses up to massive, widespread, and *uncertain* liability. It is an impermissible end-run that imposes contractual liability on a party that has not breached its obligations under the contract. Uncertainty is anathema to businesses,

especially insurance companies whose entire business model is based on predicting risk and loss, and this Court should not condone one court's attempt to unsettle well-established insurance and contract law in this state.

CONCLUSION AND PRAYER

This case does not present "unique circumstances," nor should it serve as an exception to the established—and eminently sensible—rule that a party cannot recover contractual benefits when there has been no breach of the contract. Businesses across this state enter contracts every day, and those contracts in turn serve as templates for the contracting parties' relationships. The four corners of the contract provide the consequences in the event of a breach, but if there is no breach, then there can be no obligation to pay contract benefits.

For these reasons, Amicus The Chamber of Commerce of the United States of America supports Petitioner USAA Texas Lloyds Company's request that this Court grant the petition for review and reverse the court of appeals' judgment, and, in doing so, reaffirm the *Castañeda* rule that there can be no recovery of policy benefits absent a breach of the insurance policy.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that a copy of the Amicus Brief of The Chamber of Commerce of the United States was electronically filed with the Clerk of the Court using the eFile.TxCourts.gov filing system which will send notification to the attorneys of record in this case.

/s/ *Dale Wainwright*
Dale Wainwright

CERTIFICATE OF COMPLIANCE

Based on a word count run in Microsoft Word, this brief contains 2,272 words, excluding the portions of the brief exempt from the word count under Texas Rule of Appellate Procedure 9.4(i)(1).

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