Settling a claim within policy limits

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In many health care liability claims, especially after the parties begin to discuss a settlement, it is not unusual for plaintiffs to make a demand on the defendant health care provider to settle the claim within policy limits. In Texas, this demand is known as a *Stowers* demand, after the Texas Supreme Court case *G. A. Stowers Furniture Co. v. American Indemnity Co.*, which recognized that a policyholder had a cause of action against his liability insurer for negligently refusing a settlement offer within policy limits (1). A *Stowers* demand is an important development in the case and requires action by the health care provider, his counsel, and his professional liability insurance carrier. This article describes the background of this doctrine, its application, and how to respond to such a demand.

A strategic purpose of a *Stowers* demand is to create tension between an insured and his insurance carrier in an effort to force a settlement or to obtain a settlement for a greater amount than the insurance carrier might otherwise be willing to pay. This situation often arises in obstetrical or similar claims in which the patient has significant neurological problems that have required and will require extensive medical care and that may also involve loss of earning capacity. Because the potential damages in such cases almost always exceed the limits of the health care provider's insurance coverage, plaintiffs almost invariably make a *Stowers* settlement demand (1). Similarly, plaintiffs often submit a *Stowers* demand when the injuries may not be as severe but the defendant has a low amount of insurance coverage.

The duties of an insurance carrier to its insured arise from the insurance contract. Generally, the insurance carrier owes the insured 2 duties: to defend and to indemnify. The duty to defend simply means that the insurance carrier must retain and compensate counsel to represent, defend, and protect the interests of the insured in litigation. The duty to indemnify means that the insurance carrier must pay an amount up to the limits of its insurance coverage (i.e., policy limits) in the event of an adverse judgment or settlement. The *Stowers* doctrine arises out of both of these duties. Simply put, the *Stowers* doctrine is an implied duty that requires the insurance carrier to exercise reasonable care in deciding whether to accept a settlement demand made within the limits of its coverage for an insured.

This *Stowers* duty arises when a settlement demand on the insured satisfies 3 prerequisites: 1) the claim against the insured is within the scope of coverage; 2) the demand is within policy limits and proposes to release the insured fully; and 3) the terms of the demand are such that an ordinarily prudent insurer would accept it (2, 3).

Whether the claim against the insured is within the scope of coverage is generally not an issue in health care liability claims. Insurance policies that cover health care providers generally cover all aspects of their professional activities. Further, while these policies invariably exclude from coverage liability for intentional and malicious conduct and for punitive damages, plaintiff's counsel will be sure to assert claims that are covered by the policy. There generally is no dispute between the insured health care provider and the insurer over the scope of coverage. Moreover, most plaintiff's counsel want to focus predominantly, if not exclusively, on covered claims so that they are assured of access to the insurance policy's limits of coverage.

The second requirement, that the demand be within policy limits, is also rather straightforward. The demand at issue generally will be made for a specific sum within policy limits. A specific sum need not be identified. A demand to settle for "policy limits" is adequate (4). This is based upon the fact that a professional liability insurance policy requires the carrier to indemnify the insured only up to the contracted limits of coverage. Accordingly, a demand above policy limits, even though reasonable under the circumstances, does not trigger the insurance carrier's *Stowers* duty to settle (4, 5).

Consequently, the primary issue for considering a *Stowers* question is whether or not the terms of the demand are such that an ordinarily prudent insurer would accept it, considering the likelihood and degree of the insured's potential exposure to an excess judgment. The duty on the liability insurance carrier is to accept a settlement demand within policy limits if an ordinarily prudent person managing his own business would have accepted that offer (6, 7). If the insurer fails to exercise reasonable care when responding to settlement demands within policy limits, the insured health care provider may recover from the insurance carrier the entire amount of the judgment rendered in excess of the policy limits (8–10). Thus, the insurance carrier may be liable to pay the full amount of the adverse judgment rendered against its insured, even if the amount is in excess of the insured's policy limits.

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A health care provider must take a number of steps to protect himself from the possibility of an excess judgment in response to a *Stowers* demand. Generally, the process begins with defense counsel's receipt of a written settlement demand from the claimant's attorney that offers to fully and completely settle the case within the insured's policy limits and that points out that the demand is made pursuant to the *Stowers* doctrine. The letter often has a deadline and states that if the offer is not accepted by the deadline, it will be revoked.

These deadlines can be problematic. First, if the deadline is unreasonably short or is given before the liability and damages facts have been sufficiently developed, the insurer may be relieved of its obligation to settle or may escape liability for failure to settle within policy limits (11). Plaintiff's counsel generally are aware of the parameters of the *Stowers* duty and will operate within those parameters to keep pressure on the insurance carrier. Thus, while the time frame to respond will generally be tight, typically it will not be unreasonable. Second, these demands require coordinated and timely action and response by the insured, counsel, and carrier to protect the insured's interest. Thus, action must be taken quickly to act within the deadline.

The health care provider needs to demand that the insurance carrier settle the claim within policy limits. A first step is to discuss the situation with the assigned counsel. If the deadline is too short or the facts not determined, the defense counsel can often negotiate an extension on the deadline or an agreement to mediate the case after reasonable investigation has occurred, thereby removing the need for immediate action and response. If, instead, discovery has been sufficient to respond to the settlement demand, the health care provider should obtain personal counsel. If he does not already have personal counsel or does not know someone who could act meaningfully in that capacity, he should seek input from defense counsel as to potential personal attorneys. Defense counsel will likely have been through this process before and will know well-qualified attorneys who know what to do and will appropriately protect the insured's interest in that situation. Further, when personal counsel is retained, the insured should make the personal counsel aware of any deadline so that personal counsel can coordinate with defense counsel and make the appropriate demand on the insurance carrier well enough in advance of that deadline for that demand to have the desired effect.

The use of outside counsel is beneficial for 2 reasons. First, the assigned defense lawyer has some conflict of interest between the insurance carrier and the insured. While the defense counsel is obligated to act in the best interests of the insured and will do so, his fees and expenses are paid by the insurance carrier, and he often receives other business from that carrier. A demand on the insurance carrier by the insured's personal counsel is not subject to this scrutiny and is clearly made solely to protect the interests of no one other than the insured health care provider. Additionally, input from a separate, independent attorney demanding that the case be settled puts additional pressure on the insurance carrier to settle the claim within limits. *Stowers* placed a duty on the insurance carrier to act as a reasonable and ordinarily prudent person would in managing his own affairs. Demands from a second attorney to settle based on his review of the case would be particularly damaging evidence in a subsequent bad faith claim against the insurance carrier for failing to settle within policy limits. That, in essence, puts more pressure on the carrier to settle and helps to eliminate the insured's risk of an excess judgment. Thus, use of personal counsel is the preferred practice.

For personal counsel's input to be most effective and credible, personal counsel should review the pertinent medical records, depositions, and expert reports before making this demand on the insurance carrier. Further, the demand on the insurance carrier should point out that personal counsel has reviewed these materials, should reference the problematic facts and issues, and should clearly show that reason dictates that a demand within policy limits is reasonable and should be accepted to protect the health care provider's interests.

While this maneuvering, or "dance," does not guarantee that a health care provider will not be exposed to a judgment in excess of policy limits, it does provide him with a position from which to negotiate with opposing counsel. If the case goes to trial and an excess judgment is rendered against the insured, he can negotiate with the plaintiff to obtain satisfaction for this excess judgment from the insurance carrier as part of the insured's claim for negligence against the carrier (12, 13).

Hopefully, taking these steps to respond to a *Stowers* demand will result in settling the claim within policy limits, protecting the provider from excess liability, and avoiding future litigation.

1. *G. A. Stowers Furniture Co. v. Am. Indem. Co.*, 15 S.W.2d 544 (Tex. Comm. App. 1929, holding approved).
2. *State Farm Lloyds Ins. Co. v. Maldonado*, 963 S.W.2d 38 (Tex. 1998).
3. *Birmingham Fire Ins. Co. of Pennsylvania v. Am. Nat. Fire Ins. Co.*, 947 S.W.2d 592 (Tex. App.—Dallas 1997, writ denied).
4. *American Physicians Ins. Exchange v. Garcia*, 876 S.W.2d 842, 848–849 (Tex. 1994).
5. *Hanson v. Republic Ins. Co.*, 5 S.W.3d 324 (Tex. App.—Houston [1st Dist.] 1999, writ denied).
6. *Texas Farmers Ins. Co. v. Soriano*, 881 S.W.2d 312 (Tex. 1994).
7. *Ranger County Mutual Ins. Co. v. Guin*, 723 S.W.2d 656, 659 (Tex. 1987).
8. *Hernandez v. Great Am. Ins. Co. of New York*, 464 S.W.2d 91 (Tex. 1971).
9. *Ecotech Intern., Inc. v. Griggs & Harrison*, 928 S.W. 2d 664 (Tex. App.—San Antonio 1995, writ denied).
10. *Becker v. Allstate Ins. Co.*, 678 S.W.2d 561 (Tex. App.—Houston [14th Dist.] 1984, writ ref nre).
11. *Allstate Ins. Co. v. Kelly*, 680 S.W.2d 595 (Tex. App.—Tyler 1984, writ ref nre).
12. *Whatley v. City of Dallas*, 758 S.W.2d 301, 307 (Tex. App.—Dallas 1988, writ denied).
13. *Becker v. Allstate Ins. Co.*, 678 S.W.2d 561 (Tex. App.—Houston [14th Dist.] 1984, writ ref nre).