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Eroding Limits: Causing Trouble for *Tilley* Counsel?

by JOE K. LONGLEY

The term "*Tilley* counsel" is used to describe a lawyer appointed by an insurance company to represent the insured under a liability insurance policy. It comes from the 1973 Texas Supreme Court case *Employers Casualty Co. v. Tilley*.

Through use of the "eroding" limits policy, the property and casualty industry has put *Tilley* counsel in direct competition for the dollars available to pay claims brought against insured clients. Stated differently, money available for claims release is spent on claims handling. This can become problematic for counsel's compliance with the fiduciary duties arising from an attorney-client relationship. Noncompliance can, in turn, put an attorney's financial assets at risk.

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Two seemingly unrelated events occurred in 1973 that now have evolved into a dangerous dynamic to *Tilley* counsel and an insurance company providing a defense.

The *Tilley* decision came on the heels of the amendments to what was Article 21.21 of the Texas Insurance Code. These amendments, for the first time, provided private remedies to "persons" damaged by another who engaged in prohibited unfair or deceptive practices "in the business of insurance." (Since 2005, these remedies are in §§541.151 and 541.152 of the Insurance Code.)

Tilley established that evidence provided by a lawyer to the carrier paying the bills could not be used by the company to deny coverage to its insured. The high court adopted a form of estoppel arising from the "unqualified duty of loyalty" owed by counsel to the client.

Over the years, the use of the "eroding" limits policy coupled with statutory bad-faith remedies created new hazards in the business of insurance for *Tilley* counsel and an insurance carrier that pays their fees. In 2012, it is clear that statutory bad faith in the business of insurance applies not only to insurance companies, but also to employees, independent contractors, adjusters, third-party administrators, agents, clerks and lawyers who engage in prohibited conduct.

It is not difficult to anticipate an insurance bad-faith case against an insurer and *Tilley* counsel where the limits have eroded to the point of making settlement and release impossible.

For example, in 1998's *State Farm v. Traver*, the Texas Supreme Court held "that an insurer is not vicariously liable for the malpractice of an independent attorney it selects to defend an insured. . . ."

In his dissent, Justice Raul A. Gonzalez (joined by Justice Greg Abbott) raised the issue of direct liability where ". . . an insurer, as the party that retains counsel for the insured and pays the lawyer's bills, has both the opportunity and the motive to exert improper influence over that attorney." Gonzalez noted that ". . . an insurance company may be directly liable for its own conduct if it causes harm in the course of defending the insured, whether the theory is based on statute or applicable common law."

Left unexamined in Gonzalez's statement was whether *Tilley* counsel could likewise have direct liability for his or her own conduct in the business of insurance where the client suffers financial harm resulting from noncompliance with disclosures relating to coverage, including the effects of "eroding" limits on the client's financial health.

Tilley counsel is called upon to protect the assets of the insured client through exercising the unqualified duty of loyalty, which includes the evaluation of the claims being made against the client and prompt disclosure of any actual or potential conflicts of interest. "Eroding" limits places a great burden upon *Tilley* counsel to fulfill this duty by protecting the client from all threats to the insurance asset, including the amounts available for settlement being depleted by continued payments to the attorney to defend the claim.

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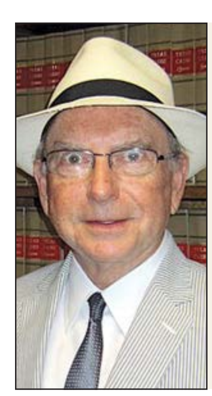
This peril becomes more pronounced where a *Stowers* demand is made by plaintiffs counsel that is dangerously close to the limits of insurance that *Tilley* counsel can reasonably estimate will be available for settlement and release.

These circumstances actually may present the insured with having another source of funds available to pay the claim. In other words, there now lurks a sort of "super S*towers*" doctrine in the form of statutory bad faith. This phenomenon occurs when the client has not been kept fully informed of the consequences of not accepting a settlement demand within the policy limits, coupled with the erosion of the limits below that demand, leaving the client's personal assets completely at risk.

Under such circumstances, unlimited coverage may be the result from *Tilley* counsel's conduct, rather than diminished coverage caused by the "erosion" of policy limits under the terms of the contract. TL



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