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SUPREME COURT OF TEXAS
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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

PETITIONER'S BRIEF ON THE MERITS

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STATEMENT OF THE CASE

Nature of the Case and Parties:	Homeowner Gail Menchaca sued her insurer, USAA Texas Lloyds Company, for contractual and extra-contractual claims arising from wind-related damages allegedly sustained to her home during Hurricane Ike. Menchaca also brought, but later dropped, tort and statutory claims against adjuster Darby Hambrick.
Trial Court:	Hon. Fred Edwards, 9th Judicial District Court, Montgomery County, Texas
Trial Court's Disposition:	A jury answered "No" when asked, "Did USAA Texas Lloyd's Company ("USAA") fail to comply with the terms of the insurance policy with respect to the claim for damages filed by Gail Menchaca resulting from Hurricane Ike?" App. 2; CR1:665. In the next question, the jury found that USAA failed to conduct a reasonable investigation. App. 2; CR1:666. The trial court disregarded the "no breach" answer and rendered judgment awarding Menchaca $164,371 ($11,350 in damages, $130,000 in attorney's fees through trial, $1,969.92 in prejudgment interest, $7,718.62 in penalty interest under Insurance Code section 542.060(a), $13,332.45 in court costs, and $15,000 in conditional appellate attorney's fees). App.1; CR1:716-19.
Court of Appeals:	Thirteenth Court of Appeals; opinion by Justice Garza, joined by Justices Rodriguez and Benavides. *USAA Tex. Lloyd's Co. v. Menchaca*, No. 13-13-00046-CV, 2014 WL 3804602 (Tex. App.—Corpus Christi July 31, 2014, pet. filed) (mem. op.); App. 3.
Court of Appeals' Disposition:	Modified the judgment to remove the award of penalty interest; affirmed the judgment as modified. App. 4.

STATEMENT OF JURISDICTION

This Court has jurisdiction under Government Code section 22.001(a)(6) because the court of appeals committed an error of law of such importance to the jurisprudence of the state that it requires correction. This Court has jurisdiction under Government Code section 22.001(a)(3) because the case involves the construction of Insurance Code chapter 541. This Court has jurisdiction under Government Code section 22.001(a)(2) because the court of appeals held differently from prior decisions of other courts of appeals and of this Court on a material question of law.

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?

3. Can a trial court "disregard" a jury question that is derived from the pleadings, that was tried to a jury, and that supports a take-nothing judgment in the defendant's favor?

REASONS TO GRANT REVIEW

An insurer has a contractual obligation to pay covered claims. But if an insurer has no legal obligation to pay a claim, and hence no contractual duty is owed, then the *extra*-contractual provisions of the Insurance Code cannot support recovery of *contractual* benefits. Until now. The court of appeals held that an insurer, which was not contractually obligated to its insured, nevertheless owed *contractual benefits* because a jury found that the insurer could have investigated harder before refusing to pay a claim. That is called liability without fault. And the holding ignores the inescapable fact that an insurer's investigation of a loss (which necessarily occurs *after* a loss) cannot also *cause* the loss.

This Court has squarely held that a failure to properly investigate a claim is not a basis in itself to require an insurer to pay policy benefits to its insured. *Provident Am. Ins. Co. v. Castañeda*, 988 S.W.2d 189, 198 (Tex. 1998). Here, the insured proved no injury independent of the contractual benefits she alleged she was owed under the policy. And what she was owed under the policy was $0, because the jury rejected her breach of contract claim. For either or both reasons, her claim is barred.

Believing that this case presented "unique circumstances," the court of appeals disregarded *Castañeda* and other cases from this Court, and summarily dismissed relevant precedent from intermediate appellate courts.

The questions presented in this case are *not* unique. They were directly presented—and answered—in *Castañeda*. Nor is the relevant precedent distinguishable. In similar cases, state and federal courts have held that an insured may not recover under circumstances like those involved here.

Hurricane Ike was the costliest storm in Texas history. *See Ike's Insured Losses Total Almost $12 Billion*, DALLAS MORNING NEWS, Jan. 29, 2010; App. 9. Insured losses from wind damage alone totaled almost $10 billion. *Id*. In litigation stemming from those and other storm-related losses, this Court must ensure that appellate courts scrupulously apply its precedent. The court of appeals failed to do so.

This Court should grant review.

STATEMENT OF FACTS

Two months after Hurricane Ike struck south Texas, Gail Menchaca called USAA to report a claim under her homeowners insurance policy. PX7; RR12:180-81. Menchaca expressed concern about possible damage to her roof, electrical box, fence, and air-conditioner. RR3:44.

Five days later, on Sunday, USAA sent adjuster Darby Hambrick to Menchaca's house. RR4:59; RR10:18. Hambrick found three missing or damaged shingles on the roof. RR10:19. He found no damage to the air conditioner, the fence, or the electrical system, although he noted that the electrical box was not attached to the house. RR10:21-23. Menchaca was also concerned about the water level in her toilets; Hambrick inspected them but found no problems. RR10:23-24.

Hambrick's repair estimate, completed three days after his inspection, included $455 to replace the missing shingles and $245 to attach the electrical box. DX4; RR17:79. The $700 estimate was less than Menchaca's $2020 policy deductible.[1] RR4:11. Because the insurance policy "cover[s] only that part of the loss over the deductible stated," DX1; RR17:9; RR17:11, USAA notified Menchaca that although her policy covered wind damage, the loss did not exceed the

[1] The home was insured for $202,000, and the policy had a 1% deductible. DX1; RR17:4-62.

deductible. DX3; RR17:77. As a result, she was not entitled to a contractual payment under the policy. DX3; RR17:77.

Five months later, Menchaca asked USAA to reinspect her roof. RR9:49. USAA adjuster David Glover, a 22-year employee, examined Menchaca's home and confirmed Hambrick's initial findings. RR4:78-79; RR9:5. Glover also found some unsealed shingles, which he attributed to an installation or manufacturing defect, not wind. RR4:79-80. Glover noted that the minimal damage to the roof did not warrant replacement under the policy. DX5; RR17:84.

Three weeks later, Menchaca sued USAA, alleging breach of contract, fraud, DTPA, and Insurance Code claims. CR1:9-23. She also sued claims adjuster Darby Hambrick for fraud, conspiracy to commit fraud, and Insurance Code violations.[2] CR1:15-19. Menchaca's notice letter, hand-delivered with her original petition, demanded $1,245,355.25 in economic damages, $50,000 for mental anguish, and $481,785.08 for expenses, including attorney's fees. CR1:24-25 (noting that demand "represents a tremendous savings to [USAA] given [its] potential exposure"); DX21; RR18:162.

Menchaca's claims were tried to a jury for eight days. One of Menchaca's experts testified that the entire roof needed to be replaced and that the storm caused

[2] Menchaca later nonsuited Hambrick in exchange for USAA's promise not to remove the case to federal court. CR1:99-101.

substantial interior damage, including cracks and separations. RR4:110, 115, 130. Another expert gave damage estimates that ranged from a low of $38,439.15 to a high of $76,348.67.[3] RR5:106, 116; DX23; RR18:176; DX39; RR22:55.

The trial court directed a verdict for USAA on the fraud claim and submitted the remaining contract and statutory claims to the jury. RR8:56. The first question, pertaining to contractual liability, asked whether USAA failed to comply with the terms of the insurance policy. The jury answered "No." App. 2; CR1:665. The second question, pertaining to extra-contractual liability, included a laundry list of statutory claims and asked whether USAA had engaged in deceptive acts or practices. App.2; CR1:666. Although it found no other violations, the jury determined that USAA "[r]efused to pay a claim without conducting a reasonable investigation with respect to a claim."[4] *Id.*; *see also* TEX. INS. CODE § 541.060(a)(7). The jury awarded Menchaca $11,350 in damages purportedly "caused by" the improper investigation. App. 2; CR1:667. The question defined damages as "the

[3] Menchaca notes that USAA stipulated to the reasonableness of Menchaca's electrician's $3,300 estimate for replacing the electrical box. RR3:5, PX16. But that does not mean that USAA agreed that the repair was necessary or that the alleged damage was caused by the windstorm. Rather, USAA disagreed that the electrical box needed to be replaced; it merely needed to be attached to the house, at a cost of $245. RR10:28; DX4.

[4] The jury rejected Menchaca's claim that USAA acted knowingly in that regard. App.2; CR1:670.

difference, if any, between the amount USAA should have paid Gail Menchaca for her Hurricane Ike damages and the amount that was actually paid." App. 2; CR1:667. The jury also awarded Menchaca $130,000 in attorney's fees through trial. App.2; CR1:672.

Contending the jury's answer to the breach question precluded Menchaca's recovery of policy benefits and that Menchaca's failure to prove an injury independent of policy benefits barred her recovery, USAA moved for judgment as a matter of law. CR1:675-80. At the post-trial hearing on that motion, the trial court disregarded the jury's failure to find a breach of the insurance contract, contending that the court's question—which tracked the Pattern Jury Charge[5]—was improper:

> It says, "Breach of contract," but it doesn't say what kind of breach. It doesn't even explain breach of contract. It doesn't even give a definition for breach of contract. There's all kinds of other things that should have been put in there about what's material breach, definition of material breach. The question fails altogether. It shouldn't have been submitted in the first place. . . . I think I can easily ignore question number one as being incomprehensible to a layman and that it has no effect. . . . I'm going to ignore question number one entirely because I think it was poorly worded. It did not have adequate definitions with it to aid the jurors. I think its response is meaningless.

[5] *Compare* App. 2; CR1:665 ("Did USAA Texas Lloyd's Company ("USAA") fail to comply with the terms of the insurance policy with respect to the claim for damages filed by Gail Menchaca resulting from Hurricane Ike?"), *with* Comm. on Pattern Jury Charges, State Bar of Tex., *Texas Pattern Jury Charges: Business Consumer Insurance Employment* PJC 101.2 (2012) ("Did Don Davis fail to comply with the agreement?").

Menchaca, 2014 WL 3804602, at *4 n.12; CR1:783. The trial court also disregarded the jury's refusal to award appellate attorney's fees. CR1:718-19.

The trial court rendered judgment for Menchaca for $164,371, including $11,350 in damages, $130,000 in attorney's fees through trial, $1,969.92 in prejudgment interest, $7,718.62 in penalty interest under the Insurance Code, $13,332.45 in court costs, and $15,000 in conditional appellate attorney's fees. App. 1; CR1:717-18.

After modifying the judgment to eliminate the award of penalty interest, the court of appeals affirmed. *Menchaca*, 2014 WL 3804602, at *9. Although the jury rejected her breach of contract action, the court of appeals held that Menchaca's extra-contractual claims were not barred. It concluded that the trial court was justified in disregarding the contract finding. Finally, it decided that Menchaca could recover policy benefits on her extra-contractual claim even though she proved no independent injury caused by USAA's investigation: "[u]nder the unique circumstances presented in this case, USAA did not breach the policy but policy benefits are indeed the correct measure of damages caused by USAA's violation of the insurance code." *Id.*

SUMMARY OF THE ARGUMENT

From its inception, this lawsuit has centered on Menchaca's claim that USAA breached the insurance policy by not paying her any policy benefits. *See, e.g.*, CR1:11-12 (petition alleging that "USAA wrongfully denied Plaintiff's claim," "refused to pay the full proceeds of the Policy," and "breach[ed] the insurance contract"). But after the jury rejected her contract claim, Menchaca pinned her right to policy benefits only on a purported failure to investigate. The salient question is whether this Court's declaration–that the "failure to properly investigate a claim is not a basis for obtaining policy benefits"–remains true, *Provident Am. Ins. Co. v. Castañeda*, 988 S.W.2d 189, 198 (Tex. 1998), or whether, as the court of appeals concluded, "policy benefits are indeed the correct measure of damages" for an insurer's failure to properly investigate a claim, *Menchaca*, 2014 WL 3804602, at *9.

Menchaca thinks *Castañeda* is beside the point because her USAA policy covers wind damage. That distinguishes *Castañeda* which, she emphasizes, involved an insurer's outright denial of coverage. But *Castañeda* still precludes recovery here. The *Castañeda* Court's analysis was predicated on an *assumption* of coverage, making the insurer's denial immaterial to the holding. Accordingly, whether an insurer refuses to pay a claim because of a policy exclusion, or because the assessed damages fall below the deductible, *Castañeda*'s holding is equally

germane—a failure to conduct a reasonable investigation is not a legal basis for recovering policy benefits. Thus, *Castañeda* directly refutes Menchaca's argument that the jury's award of $11,350 for Hurricane Ike damage is recoverable based on the jury's failure-to-conduct-a-reasonable-investigation finding.

Menchaca also argues that the Court need not dwell on the legal proposition that "failure to properly investigate a claim is not a basis for obtaining policy benefits," because during the charge conference USAA allegedly forfeited its right to enlist that precedent. But this case does not turn on charge waiver, as this Court's precedent, the charge, and the charge objections demonstrate.

The trial court chose to ignore the jury's rejection of Menchaca's contract claim, characterizing the answer to Question No. 1 as "meaningless." *Menchaca*, 2014 WL 3804602, at *4 n.12. The court of appeals endorsed that approach. *Id*. at *7. This Court should, instead, affirm the jury's verdict and render the take-nothing judgment it compels.

The arguments Menchaca advances, and those the court of appeals adopted, are incompatible with this Court's decrees. The court of appeals' opinion should not stand.

ARGUMENT

I. Because Menchaca failed to prove that USAA breached the contract, and because there was no proof of damages beyond contract damages, USAA is entitled to rendition of judgment.

"[I]n most circumstances, an insured may not prevail on a bad faith claim without first showing that the insurer breached the contract." *Liberty Nat'l Fire Ins. Co. v. Akin*, 927 S.W.2d 627, 629 (Tex. 1996). There may be one exception: this Court has recognized the theoretical possibility that "in denying the claim, the insurer may commit some act, so extreme, that would cause injury independent of the policy claim." *Republic Ins. Co. v. Stoker*, 903 S.W.2d 338, 341 (Tex. 1995). Menchaca has never contended—and the lower courts did not address or find—that this hypothetical exception applies in this case. Because Menchaca failed to prove either a breach or an independent injury, her claim fails. *See Castañeda*, 988 S.W.2d at 198.

A. A failure to properly investigate a claim is not a basis for obtaining policy benefits, and Menchaca proved no injury independent of the policy claim.

This Court has already decided this precise issue. *See Castañeda*, 988 S.W.2d at 198. In that case, Denise Castañeda's father purchased a Provident American health insurance policy covering his family. *Id*. at 191. After Castañeda became ill, requiring surgery to remove her spleen and gallbladder, she submitted claims to Provident American, which denied them. *Id*. at 192. Provident American relied on policy exclusions for (1) illnesses that manifested within thirty days of the policy's

effective date, and (2) gallbladder disorders during the first six months of the policy period. *Id*.

Castañeda sued Provident American for violations of the Insurance Code and the DTPA, but not for breach of contract. *Id*. at 192, 201. A jury rejected Provident's coverage defense[6] and found for Castañeda on the statutory claims, awarding her $50,000 for loss of benefits and harm to her credit reputation. *Id*. at 192. The jury charge defined "loss of benefits" as "the amount of benefits due under the policy." *Provident Am. Ins. Co. v. Castañeda*, 914 S.W.2d 273, 281 (Tex. App.—El Paso 1996). The trial court rendered judgment in Castañeda's favor, and the court of appeals affirmed. *Id*. at 284.

This Court reversed, specifically rejecting Castañeda's argument that she was entitled to recover damages equivalent to policy benefits for her insurer's failure to adequately investigate a claim:

> With regard to the damages that might be recoverable if an insurer failed to adequately investigate a claim, we indicated in *Stoker* that ***failure to properly investigate a claim is not a basis for obtaining policy benefits***. We did recognize, though, that there might be liability for damage to the insured other than policy benefits or damages flowing from the denial of the claim if the insured mishandled a claim. We said: "We do not exclude, however, the possibility that in denying the claim,

[6] The jury failed to find that Castañeda's illness manifested within the thirty-day exclusionary period. *See Castañeda*, 988 S.W.2d at 196 n. 31 (noting jury's "no" answer to "Do you find from a preponderance of the evidence the HEMOLYTIC SPHEROCYTOSIS of Plaintiff, DENISE CASTAÑEDA, first manifested prior to July 17, 1991?").

> the insurer may ... cause injury independent of the policy claim." The concurring Justices in *Stoker* agreed that ***the manner in which a claim is investigated must be the proximate cause of damages before there could be a recovery***. Castañeda and the dissent fault Provident American's investigation of the claim and claims-handling procedures on a number of counts, but ***none of the actions or inactions of Provident American was the producing cause of any damage separate and apart from those that would have resulted from a wrongful denial of the claim,*** as we discuss in Part IV.B below.

Castañeda, 988 S.W.2d at 198 (Tex. 1998) (emphasis added) (citations omitted).

Thus, Castañeda could not recover the policy benefits the jury awarded. *Id*. at 199. The loss of credit reputation stemmed from the denial of benefits, so those damages were not recoverable either. *Id*. Accordingly, there was no evidentiary support for the extra-contractual claims or damages. *Id*. at 201. And because "Castañeda did not plead and did not obtain a determination from the trial court that Provident American was liable for breach of the insurance contract, . . . there is no basis on which Castañeda may recover based on this record." *Id*. The Court rendered judgment that Castañeda take nothing. *Id*.

B. A failure to investigate can never cause damages equating to policy benefits.

Castañeda's holding makes sense. The Insurance Code allows an insured to recover only those actual damages "caused by" the particular statutory violation. TEX. INS. CODE § 541.151. A failure to properly investigate can *never* cause damages equating to benefits owed under the insurance contract. Those are necessarily *contract* damages arising, if at all, from the event triggering the

contractual claim—here, Hurricane Ike—and any related contractual breach. *Castañeda*, 988 S.W.2d at 198. That is why *Castañeda* cited to *Stoker*'s concurrence, which noted that "there [was] no evidence that the manner in which [the insurers] investigated the claim was a proximate cause of damages to [the insured,]" because "[t]he investigation of the claim clearly did not cause the damages to the Stokers' vehicle; the Stokers would have incurred those same damages even if their claim had been investigated properly." *Stoker*, 903 S.W.2d at 342 (Spector, J., concurring). It also explains *Castañeda*'s (and *Stoker*'s) holding that "the failure to properly investigate a claim is not a basis for obtaining policy benefits." *Castañeda*, 988 S.W.2d at 198.[7]

Castañeda decides this case. Like Castañeda, Menchaca did not obtain a finding that USAA breached the contract. App. 2; CR1:665. And there is no evidence to support damages, because none of USAA's actions or inactions was the

[7] *See also Mai v. Farmers Tex. Cnty. Mut. Ins. Co.*, No. 14-07-00958-CV, 20090 WL 1311848, at *6 (Tex. App.—Houston [14th Dist.] May 7, 2009, pet. denied) (holding that trial court properly directed verdict on failure-to-investigate claims because insureds offered "no evidence of any damages resulting from such investigative failure," and that their "position, that expected policy benefits can equate to bad faith damages, has been firmly rejected by the Texas Supreme Court") (citing *Castañeda* and *Stoker*); *see also, e.g.*, *Tracy v. Chubb Lloyds Ins. Co. of Tex.*, Nos. 4:12-CV-042-A, 4:12-CV-174-A, 2012 WL 2477706, at *5 (N.D. Tex. June 28, 2012) (recognizing that Insurance Code claims require showing that conduct caused injury beyond that which would always occur when an insured is not properly paid its demand).

producing cause of any harm separate from what would have resulted from a wrongful denial of the claim. The only damages sought or awarded were policy benefits; Menchaca explicitly disclaimed mental anguish and consequential damages. RR6:7-10; CR1:21. Much like the charge in *Castañeda*, 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."[8] App.2; CR1:667; *see also Castañeda*, 914 S.W.2d at 281 (noting that charge defined "loss of benefits" as "the amount of benefits due under the policy"). But there is no evidence that USAA's conduct caused "Hurricane Ike damages." App.2; CR1:667. And Menchaca has never alleged, nor did she prove, that her damages resulted from "some act, so extreme" by USAA that it caused "injury independent of the policy." *Stoker*, 903 S.W.2d at 341.

[8] The court of appeals stated that USAA failed to object to Question 3's instruction that the jury answer the damages question if it either found either a breach or a statutory violation. *USAA Tex. Lloyd's Co. v. Menchaca*, No. 13-13-00046-CV, 2014 WL 3804602, at *7 (Tex. App.—Corpus Christi July 31, 2014, pet. filed) (mem. op.). But USAA *did* object to the question, arguing that "the Texas courts have held that extra contractual damages need to be independent from policy damages." RR10:37. USAA also tendered its own separate damages questions on the contractual and extra-contractual claims, which the trial court refused. CR1:114-137; RR10:38. As more fully discussed in section II, *infra*, the court's suggestion that USAA waived error is wrong. *Menchaca*, 2014 WL 3804602, at *7 n.17.

C. Menchaca's attempts to distinguish *Castañeda* are unavailing.

Menchaca urges that *Castañeda* is not binding because that case involved a denial of coverage. But the *Castañeda* jury rejected the insurer's coverage defense, and this Court assumed without deciding that the claims were covered. *Castañeda*, 988 S.W.2d at 196 (discussing jury's failure to find that illness manifested within excluded time period, and analyzing the issue by assuming that "the jury's negative answer to this issue amounted to a finding of contractual coverage"), 197 ("We assume, but need not decide for purposes of our analysis, that the removal of Castañeda's gallbladder did not fall within policy exclusions."). The Court's analysis proceeded on that assumption. Indeed, had the Court accepted the insurer's contention that the claims were not covered, the Court's analysis of the bad faith claims would have been unnecessary. The Court could have simply applied *Stoker* and rendered judgment for the insurer. *See Stoker*, 903 S.W.2d at 341 ("As a general rule there can be no claim for bad faith when an insurer has promptly denied a claim *that is in fact not covered*."). There would have been no need for the Court to delve into whether policy benefits could be recovered under a failure-to-investigate finding, because the absence of coverage would have vitiated Castañeda's right to policy benefits under any circumstances. Instead, the Court reached the issue and rejected Castañeda's claims. Because that decision was predicated on an assumption

of coverage, there is no basis for distinguishing *Castañeda* from the facts presented here.

Menchaca also argues that "the absence of contract findings was not deemed fatal to the Castañedas' [sic] extra-contractual claims." Resp. at 16-17. Instead, she contends, "the *Castañeda* court disallowed recovery because the evidence did not support the jury's findings on the inadequate-investigation claim …." *Id*. at 17.

But the absence of contract findings *was* fatal to Castañeda's claims for *policy benefits*: that claim failed because she "did not plead and ***did not obtain a determination from the trial court that Provident American was liable for breach of the insurance contract.***" *Castañeda*, 988 S.W.2d at 201 (emphasis added). Accordingly, "there [was] no basis on which Castañeda may recover based on this record." *Id*.

The reason the evidence in *Castañeda* did not support the jury's findings on the inadequate-investigation claim is that the only damages proven were benefits owed under the policy. Because the investigation could not have caused those damages, Castañeda could not recover them. *Id*. at 199. In the same way, USAA's investigation, which occurred after the storm, obviously could not have caused Menchaca's alleged Hurricane Ike damage. Menchaca's arguments ignore *Castañeda*'s direct holding.

D. *Castañeda*, not *Vail*, controls here.

The court of appeals cited *Castañeda* only in passing. *Menchaca*, 2014 WL 3804602, at *8, *9. Instead, the court (and Menchaca[9]) relied on *Vail v. Texas Farm Bureau Mutual Insurance Co.*, 754 S.W.2d 129 (Tex. 1988), to conclude that, while USAA cannot be charged with breaching the policy, USAA still owed Menchaca policy benefits. In *Vail*, a divided Court[10] stated that an insurer that violated the Insurance Code or the DTPA could be liable for policy benefits under those statutes: "an insurer's unfair refusal to pay the insured's claim causes damages as a matter of law in at least the amount of the policy benefits *wrongfully withheld*." *Vail*, 754 S.W.2d at 136 (observing that statutory remedies were cumulative of common law claims) (emphasis added). For several reasons, *Vail* is either inapposite (benefits cannot be "wrongfully withheld" if they are not owed) or no longer controlling (because inconsistent with this Court's later holding in *Castañeda*).

First, in *Vail,* the insured proved that his insurer breached the contract *and* was liable, in addition, for extra-contractual torts. *Id*. at 136 (holding that evidence supported breach of contract claim, and plaintiff's damages were, "at minimum, the amount of policy proceeds *wrongfully* withheld") (emphasis added). Under *Vail*, a

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[9] *See* Resp. at 18-19; Menchaca Brief of Appellee/Cross-Appellant, at 26 ("*Vail* is dispositive of USAA's complaint.").

[10] Justice Spears wrote the Court's opinion; Justice Gonzalez dissented; and Chief Justice Phillips dissented on motion for rehearing.

breach is a necessary predicate to extra-contractual liability. *See id*. ("It was not until [the insurer] wrongfully denied the claim that the [insured's] loss was transformed into a legal *damage*."); *cf. United Nat'l Ins. Co. v. AMJ Invs., LLC*, 447 S.W.3d 1, 11-12 (Tex. App.—Houston [14th Dist.] 2014, pet. dism'd by agr.) (deciding *Vail*, rather than *Castañeda*, controlled because the insured obtained a finding that the insurer breached the contract). There was no such finding here; just the opposite.

Second, *Vail* did not establish a blanket rule for all bad faith claims. This Court has cautioned that *Vail*'s holding should not be extrapolated to a claim involving a failure to properly investigate, which "do[es] not necessarily relate to the insurer's breach of its contractual duties to pay covered claims, and may give rise to different damage." *Twin City Fire Ins. Co. v. Davis*, 904 S.W.2d 663, 666 n.3 (Tex. 1995). And in at least three cases, this Court has refused to allow recovery of contract damages as a remedy for an allegedly improper investigation. *See Progressive Cnty Mut. Ins. Co. v. Boyd*, 177 S.W.3d 919, 922 (Tex. 2005) (per curiam) (holding that even if trial court incorrectly granted summary judgment on failure-to-investigate claim, error was harmless because plaintiff "d[id] not allege that he suffered any damages unrelated to and independent of the policy claim"); *Castañeda*, 988 S.W.2d at 198; *Stoker*, 903 S.W.2d at 341.

Third, if *Vail* applies to a failure-to-investigate claim even when there is no finding of breach, it cannot be squared with *Castañeda*, which was decided a decade later and is directly on point. Menchaca suggests that this Court reinvigorated *Vail* four years after deciding *Castañeda*, when it stated that "'*Vail* remains the law as to claims for alleged unfair claims settlement practices brought by insureds against their insurers.'" *Rocor Int'l, Inc. v. Nat'l Union Fire Ins. Co.*, 77 S.W.3d 253, 259 (Tex. 2002) (quoting *Allstate Ins. Co. v. Watson*, 876 S.W.2d 145, 149 (Tex. 1993)); *see also* Resp. at 19. But that statement merely quoted the Court's 1993 *Allstate* decision, which held that *Vail* correctly described the insurer-insured relationship under the Insurance Code.

In fact, this Court has not cited *Vail* for the relevant proposition since 1995—three years before *Castañeda*. *See Twin City*, 904 S.W.2d at 666. Even then, the Court held only that *Vail* was inapposite to the question presented in that case: whether policy benefits wrongfully withheld supported an award of punitive damages under the Workers' Compensation Act. *Id*. (noting that "[w]e did not even discuss in *Vail* the argument Twin City makes here"). The decision hardly represents an endorsement of *Vail*; *Twin City* criticized the court of appeals for "rephras[ing] and broaden[ing] the rule we announced in *Vail*" and explicitly stated that *Vail* should not be extrapolated to failure-to-investigate claims, which "do not necessarily relate to the insurer's breach of its contractual duties to pay covered claims, and may

give rise to different damages." *Id*. at n.3. The *Twin City* dissent characterized the Court's approach as a "retreat[] from [*Vail*'s] holding." *Id*. at 667 (Spector, J., dissenting).

Since then, and shortly before *Castañeda*, the Court issued a per curiam opinion that did not cite *Vail* but nonetheless held that policy benefits were "contract, as well as tort damages." *Waite Hill Servs., Inc. v. World Class Metal Works, Inc.*, 959 S.W.2d 182, 184-85 (Tex. 1998) (per curiam) (requiring party who prevailed on contract and extra-contractual claims to elect a remedy).[11] At the close of 1998, however, *Castañeda* firmly rejected the notion that, in the absence of a breach of contract finding, policy benefits are recoverable based on an insured's failure to reasonably investigate a claim. *See Castañeda*, 988 S.W.2d at 198; *see also Charla G. Aldous PC v. Lugo*, No. 3:13-CV-3310-L, 2014 WL 5879216, at *5 (N.D. Tex. Nov. 12, 2014) (granting motion to dismiss Insurance Code claims, including one alleging failure to reasonably investigate, because plaintiff had not alleged an injury independent of the contractual claims for benefits; **"subsequent to issuing its decision in *Vail*, the Texas Supreme Court left no doubt that an independent injury was required to recover under the Texas Insurance Code"**) (citing *Castañeda*) (emphasis added).

[11] *Waite Hill* was decided on January 16, 1998; *Castañeda* was decided on December 31 of the same year.

With the exception of the appellate court in this case, courts of appeals have overwhelmingly interpreted *Castañeda* to permit recovery of extra-contractual damages only when an insured proves damages independent of those resulting from a wrongful denial of policy benefits. *See, e.g., Laird v. CMI Lloyds*, 261 S.W.3d 322, 328 (Tex. App.—Texarkana 2008, pet. dism'd w.o.j.) ("An insured is not entitled to recover extra-contractual damages unless the complained-of actions or omissions cause injury independent of the injury resulting from a wrongful denial of policy benefits."); *USAA v. Gordon*, 103 S.W.3d 436, 442 (Tex. App.—San Antonio 2002, no pet.) (same). The United States Court of Appeals for the Fifth Circuit has embraced a similar reading of the Texas rule: "there can be no recovery for extra-contractual damages for mishandling claims unless the complained of actions or omissions caused injury independent of those that would have resulted from the wrongful denial of policy benefits." *Great Am. Ins. Co. v. AFS/IBEX Fin. Servs. Inc.*, 612 F.3d 800, 808 n.1 (5th Cir. 2010); *Parkans Int'l, LLC v. Zurich Ins. Co.*, 299 F.3d 514, 519 (5th Cir. 2002) (same). Numerous federal district courts apply the same requirement.[12]

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[12] *See, e.g.*, *Hulcher Servs., Inc. v. Great Am. Ins. Co.*, No. 4:14-CV-231, 2015 WL 3921903, at *11 (E.D. Tex. June 25, 2015) (granting summary judgment for insurer on Insurance Code claims because insured had not presented evidence of damages independent of underlying contract claim; "there are no damages alleged other than the wrongful denial of policy benefits"); *Admiral Ins. Co. v. Petron Energy, Inc.*, 1 F. Supp. 3d 501, 503 (N.D. Tex. 2014) ("[Bad faith] claims also require a showing of independent injury—*i.e.*, an insured can only recover for § 541.060 violations if

Conversely, the Fourteenth Court has interpreted *Castañeda* to apply only if an insured fails to prove a contractual breach. *See AMJ Investments*, 447 S.W.3d at 11. The *AMJ Investments* court held that policy benefits were recoverable under the Insurance Code because "[u]nlike the insured in *Castañeda*, the insured in this case pleaded and proved that its claim was covered and its insurer breached the contract." *Id*. at *12 (relying on *Vail*). The decision provoked some critical commentary,[13] and the insurer petitioned this Court for review. The case settled after the Court

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the insurer's complained of actions caused injury independent of a wrongful denial of policy benefits."); *Tracy v. Chubb Lloyds Ins. Co.,* Nos. 4-12–042-A, 4:12-CV-174-A, 2012 WL 2477706, at *5 (N.D. Tex. June 28, 2012) ("Texas law does not, as a general rule, consider a Texas Insurance Code or common-law good faith and fair dealing claim to be viable unless the insured has suffered damages beyond the damages claimed for, or resulting from, breach of the insurance policy contract."); *Powell Elec. Sys., Inc. v. Nat'l Union Fire Ins. Co.*, Civil Action No. H-10-993, 2011 WL 3813278, at *9 (S.D. Tex. Aug. 29, 2011) (granting summary judgment for insurer because insured "failed to allege damage independent of the damages arising from the underlying breach of the insurance contract").

[13] *See, e.g.*, App. 10; James W. Holbrook III, *AMJ Investments May Not Alter Texas Claims Landscape*, LAW360, Sept. 24, 2014 (observing that "*AMJ Investments* is undoubtedly at odds with the litany of post-*Castañeda* cases that applied the independent injury requirement in Section 541 cases"). That commentator noted that the appellate court "did not mention (let alone square its holding) with the many cases in which the Fifth Circuit, federal district courts, and other Texas courts of appeals applied *Castañeda*'s independent injury requirement to matters in which the insured—like the insured in AMJ Investments—proved its insurer wrongfully withheld policy benefits." *Id*. He also questioned whether "the opinion breathed new life into *Vail*, which—prior to *AMJ Investments*—had, in practical effect been overruled *sub silentio* by *Castañeda* and its progeny on the independent injury issue." *Id.*

requested a response to the petition. *See* 14-0965; *United Nat'l Ins. Co. v. AMJ Investments, LLC*, in the Supreme Court of Texas, Case Events, http://www.search.txcourts.gov/Case.aspx?cn=14-0965&coa=cossup (last visited Jul. 21, 2015).

Even if the precise extent of *Castañeda*'s reach is debatable, this case falls squarely within its holding. The court of appeals' contrary conclusion was incorrect.

E. The court of appeals' attempts to distinguish relevant precedent are fruitless.

The court of appeals also focused on *Stoker*, which—like *Castañeda*—it found distinguishable. *Menchaca*, 2014 WL 3804602, at *9. The court recognized the "'general rule' that breach of the policy must be established before policy benefits may be recovered," but held that this case presented an exception. *Id*. The court observed that *Stoker* involved a claim that was not covered. But here, the court wrote, "it was not 'established' that the policy provided no coverage for Menchaca's claim." *Id*. The court also disregarded the numerous authorities USAA cited, because "[m]ost of them involve situations where the policy at issue was explicitly found not to cover the category of damages claimed by the plaintiff." *Id*. at *8.

The court of appeals' decision rests on the dubious distinction between a finding of no coverage, on the one hand, and no breach on the other. But the court never explains why that distinction should matter. In either case, the insurer is not obligated to pay policy benefits. *See, e.g., In re Allstate Cnty. Mut. Ins. Co.*, 447

S.W.3d 497, 501 (Tex. App.—Houston [1st Dist.] 2014, orig. proceeding) ("An insurer generally cannot be liable for failing to settle or investigate a claim that it has no contractual duty to pay."). Under this Court's precedent and the insurance contract, there is no basis for differentiating the two.

In *Castañeda*, for example, this Court assumed there was coverage but still rejected the insured's recovery of policy benefits under a failure-to-investigate theory, because the improper investigation did not cause those damages. *Castañeda*, 988 S.W.2d at 201. Thus, the insured's failure to "obtain a determination from the trial court that [the insurer] was liable for breach of the insurance contract" barred her recovery of policy benefits. *Id*.

In *Stoker*, the Court held that "there can be no claim for bad faith when an insurer has promptly denied a claim that is in fact not covered." *Stoker*, 903 S.W.2d at 341. The statement was phrased in terms of "no coverage," because the claim in that case was not covered. But the authorities *Stoker* cited made clear that the same rule applies to a claim for policy benefits when there has been *no breach* of the insurance policy:

- a Fifth Circuit decision noting that Mississippi law did not support a bad faith recovery for the insured without first establishing "liability under the policy";[14]

[14] *O'Malley v. U.S. Fidelity & Guar. Co.*, 776 F.2d 494, 500 (5th Cir.1985).

- an Alabama Supreme Court case holding that a plaintiff seeking to recover on a bad faith claim must prove a breach of contract by the defendant;[15]

- a Kentucky Supreme Court decision that a bad faith claim requires proof that the insurer was obligated to pay under the policy;[16]

- a Rhode Island Supreme Court holding that there can be no bad faith claim unless the insured establishes the insurer breached its duty under the contract;[17] and

- a leading treatise stating that extra-contractual recovery was prohibited "where the insured is not entitled to benefits under the contract of insurance which establishes the duties sought to be sued upon."[18]

Id. (collecting authorities). And there is ample additional authority—aside from this Court's own precedent[19]—to support that interpretation. *See, e.g., Capstone Bldg. Corp. v. Am. Motorists Ins. Co.*, 67 A.3d 961, 998 (Conn. 2013) (joining "the majority of jurisdictions to consider the matter" and holding that "in the absence of a breach of an express duty under the insurance policy, there is no independent cause of action for deficiencies in the insurer's investigation"). It is clear that *Stoker*'s

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[15] *Gilbert v. Congress Life Ins. Co.*, 646 So.2d 592, 593 (Ala.1994).

[16] *Wittmer v. Jones*, 864 S.W.2d 885, 890 (Ky.1993).

[17] *Bartlett v. John Hancock Mut. Life Ins. Co.,* 538 A.2d 997, 1000 (R.I.1988).

[18] 15A RHODES, COUCH ON INSURANCE LAW 2d § 58:1 at 249 (Rev. ed. 1983).

[19] *E.g.*, *Liberty Nat'l Fire Ins. Co. v. Akin*, 927 S.W.2d 627, 629 (Tex. 1996).

exception for "some act, so extreme" that it caused "injury independent of the policy" has not been satisfied here. *Stoker*, 903 S.W.2d at 341.

Additionally, Menchaca's insurance contract states that a loss that fails to exceed the deductible is not a covered loss. The agreement "*cover[s]* only that part of the loss over the deductible stated." DX1; RR17:9; RR17:11 (stating that insurance contract consists of the Declarations page, the policy, and applicable endorsements) (emphasis added). USAA determined that Menchaca's claim was below the deductible, and Menchaca failed to prove that this decision breached the policy. So even though wind damage was generally covered under the policy, Menchaca did not have a "covered" claim.

The court of appeals also distinguished *USAA v. Gordon*, 103 S.W.3d 436, 442 (Tex. App.—San Antonio 2002, no pet.), which it incorrectly described as a Texas Supreme Court case. *Menchaca*, 2014 WL 3804602, at *8. In *Gordon*, a jury found for the plaintiffs on their contractual and extra-contractual claims and awarded the identical amounts under both theories of recovery. The San Antonio Court of Appeals held that "[a]n insured is not entitled to recover extra-contractual damages unless the complained of actions or omissions cause injury independent of the injury resulting from a wrongful denial of policy benefits." *Gordon*, 103 S.W.3d at 442. The court rendered judgment that the insured take nothing on his extra-contractual claims. *Id*. at 444.

The court of appeals in this case found *Gordon* distinguishable because the *Gordon* jury determined that USAA breached the insurance policy and awarded damages for that breach. Accordingly, the court stated that "an award of extra-contractual damages—where the only damages in evidence 'stemm[ed] from the denial of the claim'—would have constituted an impermissible double recovery." *Menchaca*, 2014 WL 3804602, at *8. "Such circumstances are not present in this case," the court reasoned. *Id*.

But the court of appeals' analysis is wrong. The *Gordon* court did not render judgment against the plaintiff on the extra-contractual claims to avoid a double recovery. Even though the *Gordon* jury awarded identical amounts for the contractual and extra-contractual claims, the plaintiffs *elected* to recover only on the extra-contractual claim. *Gordon*, 103 S.W.3d at 438. So double recovery was not an issue, and is not mentioned anywhere in the opinion. The *Gordon* court rendered judgment against the plaintiffs on the extra-contractual claims because policy benefits were not recoverable as damages for that claim. If extra-contractual damages were legally permissible, the *Gordon* plaintiffs' election of remedies would have been proper. Only after reversing the extra-contractual award did the *Gordon* court affirm the trial court's *conditional* contractual damages award. *Id*. at 437. The court of appeals' reasoning to the contrary is not supportable.

Finally, the court of appeals stated that "USAA has not directed us to any cases, nor can we find any, involving a situation such as this one where: (1) the insurer complied with the policy, but (2) nonetheless violated the insurance code, and (3) the insurer *would have been* contractually obligated to pay policy benefits had the insurer complied with the insurance code." *Menchaca*, 2014 WL 3804602, at *9. But the "situation" the court described is not presented in this case. There was no determination that USAA would have been *contractually obligated* to pay policy benefits had it conducted a more thorough investigation. As this Court has recognized, a failure to investigate can never cause damages in the form of policy benefits—those are caused by a contractual breach. *Castañeda*, 988 S.W.2d at 201.

So the jury's damage award cannot be viewed as a finding of contractual liability, and USAA directed the court to a case so holding: *Castañeda*. The *Castañeda* jury charge defined the damages as "the amount of benefits due under the policy." *Castañeda*, 914 S.W.2d at 281. This Court held that, absent a separate breach-of-contract finding, a failure to investigate could not support recovery of that amount. *Castañeda*, 988 S.W.2d at 201. The same is true here.

F. This Court should reject Menchaca's argument that USAA is liable for policy benefits even though she could not prove that it breached the policy.

Menchaca has asserted that Question 2 (the Insurance Code question), which asked whether USAA refused to pay her claim without conducting a reasonable

investigation, implicitly includes a breach finding: "[t]he evidence and the jury's answer to Question No. 2(D) ***conclusively establish USAA's failure to comply with its insurance policy***." CR1:689 (emphasis added). In the court of appeals she argued that Question 3—the damages question—established not just damages, but contract liability: "it is in response to Question 3 that the jury affirmatively found the Hurricane Ike damages covered by the policy." Brief of Appellee/Cross-Appellant at 22. In this Court, she contends that "[t]ogether, the jury's liability and damage findings support the judgment against USAA." Resp. at 10.

The plain language of the charge defeats these arguments. Those arguments contradict the charge's plain language and this Court's precedent. Question 2(D) asked only whether USAA refused to pay a claim without conducting a reasonable investigation. Question 3 asked the jury to determine the damages caused by any failure to comply with the contract or any unfair or deceptive act. CR1:667. The only question about breach was Question 1, to which the jury answered, "No." CR1:665 ("Did USAA . . . fail to comply with the terms of the insurance policy with respect to the claim for damages filed by Gail Menchaca resulting from Hurricane Ike?"); *see also Mo. Pac. Ry. Co. v. Whittenburg & Alston*, 424 S.W.2d 427, 430 (Tex. 1968) (rejecting argument that jury's answer to damage questions also established liability); *cf. Beltran v. Brookshire Grocery Co.*, 358

S.W.3d 263, 269-70 (Tex. App.—Dallas 2011, pet. denied) (holding that jury's failure to find negligence liability controlled over its finding apportioning fault).

The arguments cannot square with *Castañeda*. If a jury question about failing to investigate also inquires about contractual breach, or if a damage finding of policy benefits is the equivalent of a finding that the insurer ignored its obligations under the policy, then *Castañeda* could not have been decided the way it was. *Castañeda* rejected the insured's recovery of damages equivalent to policy benefits for her insurer's failure to adequately investigate a claim. If, as Menchaca argues, the failure-to-investigate or damages findings included an implicit breach determination, Castañeda would have been entitled to judgment on that basis. If the jury's award of policy benefits were proper for a failure to properly investigate, judgment for Castañeda also would have been appropriate. But this Court rendered a take-nothing judgment despite the jury findings on those issues, because Castañeda "did not plead and did not obtain a determination from the trial court that Provident American was liable for breach of the insurance contract." *Castañeda*, 988 S.W.2d at 201 (noting that "there is no basis on which Castañeda may recover based on this record").

Deemed findings would be inappropriate. Menchaca asks the Court to deem findings in favor of the judgment. Resp. at 13. She has argued that "[e]ven if the jury's findings in response to Question Number 3 were not a finding of covered

losses, the issue of coverage must be deemed in support of the trial court's judgment." Brief of Appellee/Cross-Appellant at 23. But that rule applies only when an incomplete theory is submitted without complaint, which is not the case here, where breach was submitted—and soundly rejected. *See, e.g.*, *Gulf States Utils. Co. v. Low*, 79 S.W.3d 561, 565 (Tex. 2002) (rejecting deemed finding that defendant acted knowingly under DTPA). Second, if such findings were appropriate, this Court would have deemed them in *Castañeda*. If the Court did not do so there, when breach was not submitted to the jury, it certainly should not do so here, when the jury explicitly rejected that cause of action.

G. Absent a breach finding, Menchaca is not entitled to policy benefits.

Relying on *Vail*, Menchaca argues that she is entitled to benefit-of-the-bargain damages for her Insurance Code claim. Resp. at 18-19. It is true that the statute allows a prevailing plaintiff to recover the amount of "actual damages" caused by the statutory violation. TEX. INS. CODE § 541.152(a)(1). But benefit of the bargain is a contract measure of damages that is appropriate for "an accompanying breach of contract claim," not for the tort of bad faith. *Transp. Ins. Co. v. Moriel*, 879 S.W.2d 10, 17 (Tex. 1994). Those cases stating that contract damages can qualify as "actual damages" under the Insurance Code[20] involve situations in which an

[20] *See, e.g.*, *Waite Hill Servs., Inc. v. World Class Metal Works, Inc.*, 959 S.W.2d 182, 184-85 (Tex. 1998) (per curiam); *Twin City Fire Ins. Co. v. Davis*, 904 S.W.2d

insurer faces contract liability *in addition to* Insurance Code liability.[21] *See, e.g.*, *Twin City*, 904 S.W.2d at 665-67 (explaining *Vail*'s holding that policy benefits wrongfully withheld qualified as "actual damages" under Insurance Code's cumulative remedy provision).

H. The differences Menchaca identifies are only semantic.

Menchaca observes that the jury's refusal to find a breach is not equivalent to a finding that USAA complied with the contract. That is true, but immaterial. Menchaca was required to prove, as a prerequisite to recovering policy benefits, that USAA was contractually obligated to pay policy benefits. To prove a contractual obligation to pay, Menchaca needed an affirmative finding that USAA breached its

663, 665-67 (Tex. 1995); *Vail v. Tex. Farm Bureau Mut. Ins. Co.*, 754 S.W.2d 129, 136 (Tex. 1988).

[21] Menchaca asserts that Insurance Code section 541.151 would "become a toothless, useless remedy" if an insurer could escape liability any time a plaintiff could not prove that the relevant conduct also breached the insurance policy. But *Castañeda* recognized that even though the failure to prove breach vitiates the insured's right to recovery of policy benefits for an improper investigation, an insured could still seek damages flowing from "some act, so extreme, . . . that it caused injury independent of the policy." *Castañeda*, 988 S.W.2d at 199 (quoting *Stoker*, 903 S.W.2d at 341). Additionally, the attorney general may seek injunctive relief and civil penalties against insurers that violate the statutory requirements. TEX. INS. CODE §§ 541.201, 541.204.

contract by refusing to pay. Her arguments to the contrary ignore this Court's (and other courts')[22] direct precedent:

- "The threshold of bad faith is reached when a breach of contract is accompanied by an independent tort." *Moriel*, 879 S.W.2d at 17.

- "In most circumstances, an insured may not prevail on a bad faith claim without first showing that the insurer breached the contract." *Akin*, 927 S.W.2d at 629.

Menchaca perceives a "critical distinction" between refusing to pay a claim that is not covered, and refusing to pay a "covered" claim because it falls below the deductible. Resp. at 1. The court of appeals agreed, noting that "[t]he disagreement here does not involve the extent of coverage afforded under the policy; rather, it is about the precise amount of damages inflicted by the storm on the covered property." *Menchaca*, 2014 WL 3804602, at *6. Neither Menchaca nor the court of appeals

[22] *See also, e.g., Watson v. Allstate Texas Lloyd's*, 224 F. App'x 335, 343 (5th Cir. 2007) (holding that plaintiff could not recover on extra-contractual claims "without making the predicate showing the [the insurer] breached the insurance contract"); *Lundstrom v. United Servs. Auto. Ass'n-CIC*, 192 S.W.3d 78, 96 (Tex. App.—Houston [14th Dist.] 2006, pet. denied) ("[T]here can be no claim for bad faith when an insurer has denied a claim that is, in fact, not covered and has not otherwise breached the contract."); *Toonen v. United Servs. Auto Ass'n*, 935 S.W.2d 937, 941 (Tex. App.—San Antonio 1996, no writ) (affirming summary judgment against insured on breach of contract claim and holding that "[a]s a general rule, an insured does not have a bad faith claim in the absence of a breach of contract by the insurer").

explains why that distinction would permit recovery of policy benefits for bad faith when the insurer's rejection of benefits violates no policy provision.

A jury may reject an insured's claim for breach of the contract because there is no coverage. A jury may also reject an insured's claim for breach of contract because, although the type of loss is covered under the policy, the loss is below the deductible. In neither case is the insurer contractually obligated to pay policy benefits. Additionally, because the contract does not cover damages that fall below the deductible, a dispute about whether damages exceed that marker *is* a coverage dispute. Menchaca's wordplay on the meaning of "coverage" thus fails when the law's consequences meet undisputed facts.

Menchaca argues that *Deese v. State Farm Mutual Automobile Insurance Co.*, 838 P.2d 1265 (Ariz. 1992), supports the distinction she urges. In *Deese*, the Arizona Supreme Court held that breach of the insurance policy was not a necessary prerequisite to a tort claim for bad faith. *Deese*, 838 P.2d at 505. This Court cited *Deese* in a footnote in *Stoker*:

> Our attention has been particularly called to *Deese v. State Farm,* 838 P.2d 1265, 838 P.2d 1265 (1992). The insurance company in *Deese* did not deny coverage. The dispute was whether portions of the medical bills were not reasonable and therefore not compensable. *Id.* 838 P.2d at 1266–67.

Stoker, 903 S.W.2d at 341 n.1. One should not read too much into that statement. Three years later, this Court assumed that coverage existed but still rejected a claim

for policy benefits premised on an Insurance Code failure-to-investigate claim. *See Castañeda*, 988 S.W.2d at 198.

Nor can this Court's other precedent be read so narrowly. In *Progressive County Mutual Insurance Co. v. Boyd*, 177 S.W.3d 919, 922 (Tex. 2005), for example, Boyd sued his insurer for breach of contract and for extra-contractual claims, including a failure to fairly investigate his accident. This Court held that Boyd's unsuccessful breach-of-contract claim barred his extra-contractual claims. It spoke broadly about the relationship between the insurance policy and damages tied to bad faith. The Court's language is not limited to cases in which a claim is denied because there was no coverage—the opinion explored "an insurer's denial of a claim *it was not obligated to pay*." *Id*. (emphasis added). That is consistent with the way other courts have interpreted the rule. *See, e.g.*, *In re Allstate Cnty. Mut. Ins. Co.*, 447 S.W.3d at 501 ("An insurer generally cannot be liable for failing to settle or investigate a claim that it has no contractual duty to pay.").

This is what the jury found here:

QUESTION NO. 1:

1. Did USAA Texas Lloyd's Company ("USAA") fail to comply with the terms of the insurance policy with respect to the claim for damages filed by Gail Menchaca resulting from Hurricane Ike?

   Answer "Yes" or "No".

   Answer: No

The only question is whether the law still holds that the "failure to properly investigate a claim is not a basis for obtaining policy benefits." *Castañeda*, 988 S.W.2d at 198.

I. Conclusion: USAA is entitled to rendition of judgment.

Because the extra-contractual claims and damages fail as a matter of law and were not supported by legally sufficient evidence, the judgment (including the attorney's fee award) cannot stand. *See id*. at 201.[23]

II. USAA has preserved the issues it presents to this Court.

Menchaca believes USAA did not preserve a complaint that her failure to prove a breach bars recovery of policy benefits. She argues that USAA waived error

[23] *See also* TEX. INS. CODE § 541.152 (authorizing attorney's fee recovery only for a prevailing plaintiff); *State Farm Life Ins. Co. v. Beaston*, 907 S.W.2d 430, 437-38 (Tex. 1995) (holding that attorney's fee award under Insurance Code requires that party (1) prevail on a cause of action for which fees are recoverable, and (2) recover damages).

by not objecting to a failure to predicate the Insurance Code question on an affirmative answer to the contract question; waived error by not requesting an instruction directing the jury not to answer the Insurance Code question if it answered "no" to the contract question; waived error by not objecting to the predication instructing the jury to award damages if it found an Insurance Code violation but not a breach of contract; and waived error by not requesting an instruction directing the jury not to answer the damages question if it answered "no" to the contract question. Resp. at 1-2.

But none of those predicates (or lack thereof) matters here. *See, e.g.*, *Castañeda*, 988 S.W.2d at 198 (rendering judgment in insurer's favor despite jury's answer awarding policy benefits for Insurance Code claims). USAA's petition presents a purely legal issue that USAA preserved in its post-trial motions. Additionally, to the extent charge-error preservation was necessary, USAA achieved it.

A. USAA moved for judgment that Menchaca could not recover as a matter of law.

USAA's issues do not implicate the intricacies of charge submission. As a matter of law, Menchaca cannot recover damages equating to policy benefits because the jury rejected her assertion that USAA breached the policy. USAA preserved this legal issue in its motion for entry of a take-nothing judgment and motion to alter or amend the judgment. CR1:675-79, 723-28. In both motions,

USAA asserted the same arguments it asserted in the court of appeals and presents to this Court. *See id*. at 675 (arguing that extra-contractual claims failed as a matter of law), 678 (complaining that there was no evidence that failure to investigate caused injury independent of that resulting from denial of policy benefits), 723-28 (same).

Those legal questions do not hinge on the jury's role as fact-finder. In *Holland v. Wal-Mart Stores, Inc*., 1 S.W.3d 91 (Tex. 1999) (per curiam), Wal-Mart contended that, as a matter of law, Holland could not recover attorney's fees for a particular statutory claim. *Id*. at 92. The court of appeals determined the argument was waived because Wal-Mart did not object to a jury question that included attorney's fees as an element of damages for that claim. *Id*. at 94.[24] This Court disagreed, holding that no objection was necessary and Wal-Mart's post-verdict motion preserved the complaint:

> The availability of attorney's fees under a particular statute is a question of law for the court. Consequently, the jury's finding about the *amount* of reasonable attorney's fees is immaterial to the ultimate legal issue of whether such fees are recoverable under [the statute] as a matter of law. By asserting nonrecoverability in its motion for j.n.o.v., Wal-Mart gave the trial court ample opportunity to rule on the availability of attorney's fees before an erroneous judgment was rendered.

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[24] *See also Wal-Mart Stores, Inc. v. Holland*, 956 S.W.2d 590, 600 (Tex. App.—Tyler 1997) ("We note that Wal-Mart waived error in the submission of the attorney's fees question by failing to object to it as an improper element of damages under 8307c."), *rev'd*, *Holland v. Wal-Mart Stores, Inc*., 1 S.W.3d 91 (Tex. 1999) (per curiam).

> This is not a case in which the trial court had to resolve a legal issue before the jury could properly perform its fact-finding role. In such instances, a party must lodge an objection in time for the trial court to make an appropriate ruling without having to order a new trial. A jury can determine the amount of attorney's fees whether or not they can be recovered under the theory of law submitted to the jury.

Id. (citations omitted); *see also id*. at 95 (noting that "[b]ecause the availability of attorney's fees is solely a question of law for the court, error did not occur until the trial court rendered judgment awarding such fees" and post-verdict motion "specifically challenged the availability of attorney's fees . . . before the error resulted"). The Court then determined that fees were not recoverable, and it reversed and rendered a take-nothing judgment on that claim. *Id*. at 95-96.

Similarly, the Court held that a party's post-verdict motion preserved a complaint that a statute authorized only equitable relief—even though the party had not objected to the submission of jury questions on compensatory and punitive damages. *Wal-Mart Stores, Inc. v. McKenzie*, 997 S.W.2d 278, 278-79 (Tex. 1999) (per curiam). *See also Felton v. Lovett*, 388 S.W.3d 656, 660 n.9 (Tex. 2012) (concluding that post-verdict motion preserved error on a "purely legal issue which does not affect the jury's role as fact-finder"); *Hoffmann-La Roche Inc. v. Zeltwanger*, 144 S.W.3d 438, 450 (Tex. 2004) ("Because the issue [whether plaintiff could recover under jury finding of intentional infliction of emotional distress based on same conduct supporting statutory sexual-harassment claim] presented a pure

legal question which did not affect the jury's role as fact finder, the post-verdict motion was sufficient to preserve error.").

Likewise, whether Menchaca can recover policy benefits under her failure-to-investigate claim when she lost on her contract claim presents a purely legal issue that USAA fully preserved in its post-trial motions. As in *Holland*, "[a] jury can determine the amount of [damages] whether or not they can be recovered under the theory of law submitted to the jury." *Holland*, 1 S.W.3d at 94. And that jury finding does not preclude a court's determination that recovery of those damages is barred as a matter of law under the theory submitted to the jury. *See id*.

B. To the extent necessary, USAA timely and correctly objected to the jury charge.

Menchaca's contention that USAA waived all of its legal arguments misconstrues USAA's primary stance. USAA's objection to the charge was not that the Insurance Code question must be conditioned on a "yes" answer to the contract question. Instead, USAA twice urged the trial court to submit separate damage questions related to the contract and Insurance Code questions because, as this Court has made clear,[25] bad-faith damages must be independent of damages that are recoverable for breach of the policy—policy benefits. USAA thus preserved error

[25] *Castañeda*, 988 S.W.2d at 198 (holding that inadequate investigation was not a basis for obtaining policy benefits but recognizing theoretical possibility of recovering for conduct that causes "injury independent of the policy claim").

by (1) objecting on the record to the damages questions, and (2) filing requests for certain jury instructions and questions.

Objection to the damages question. First, USAA timely objected to the damages question.

> With respect to Question No. 3, we object to the combining of contractual damages from Question 1 and statutory damages from Question 2 for the reason that the Texas courts have held that extra contractual damages need to be independent from policy damages.
>
> And it's going to be unclear potentially if we get "yes" answers to 1 and 2 what the damages are based on. So we object to 3 as submitted by the plaintiffs.

RR10:36-37. The trial court overruled this objection. RR10:38.

An objection preserves a complaint that a submitted jury instruction or question is defective or erroneous. TEX. R. CIV. P. 274; *Spencer v. Eagle Star Ins. Co. of Am.*, 876 S.W.2d 154, 157 (Tex. 1994). A request is not required. *Spencer*, 876 S.W.2d at 157. An objection must: (1) point out distinctly what is objectionable, and (2) provide the grounds for the objection. TEX. R. CIV. P. 274. The primary test for charge-error preservation is "whether the party made the trial court aware of the complaint, timely and plainly, and obtained a ruling." *Wackenhut Corp. v. Gutierrez*, 453 S.W.3d 917, 919-20 (Tex. 2015) (quoting *State Dep't of Highways & Pub. Transp. v. Payne*, 838 S.W.2d 235, 240, 241 (Tex. 1992)).

USAA's objection preserved error in the damages question, including the predication instruction. It was timely, separate from USAA's requests, made on the

record, and ruled on by the trial court. TEX. R. CIV. P. 272, 273. It complied with Rule 274 and *Payne* because it apprised the court (1) that it should have submitted separate damages questions for the contract claim and the Insurance Code claims, and (2) *why* the damages question should not have been based on a "yes" answer to either or both Questions 1 and 2. TEX. R. CIV. P. 274; *Payne*, 828 S.W.2d at 240, 241.

Requesting questions and instructions. Although not required to challenge a defect in the charge, TEX. R. CIV. P. 274, USAA also submitted proposed questions regarding Menchaca's breach and Insurance Code claims. CR1:595-99. USAA requested separate damage questions for each claim. *Id*. At the charge conference, USAA sought and obtained a ruling on its requests. RR10:38. The trial court refused each of them. *Id*.

These requests further demonstrate that USAA "made the trial court aware" of its complaint that there should be separate damage questions for Menchaca's contract and Insurance Code claims. *Payne*, 838 S.W.2d at 241. Accordingly, to the extent USAA was required to preserve error in the charge in order to present its issues to this Court, USAA did.

This Court observed twenty-three years ago that labyrinthine charge-error preservation requirements "hardly subserve[] the fair and just presentation of the case." *Id*. at 240. The only relevant inquiry is whether the party made the trial court

aware of the complaint, timely and plainly, and obtained a ruling. *Id*. at 241; *see also Ulico Cas. Co. v. Allied Pilots Ass'n*, 262 S.W.3d 773, 777 (Tex. 2008) (holding that error was preserved when party's "position was made clear to the trial court and the trial court ruled against it"). Construing issues to involve charge error when they do not, and requiring charge objections more intricate than necessary to apprise the trial court of the issue, defeat, rather than serve, the principles underlying this Court's efforts to simplify charge procedure. *See Payne*, 838 S.W.2d at 240. USAA's issues are properly before this Court.

III. The trial court improperly disregarded the jury's failure to find a contractual breach.

Although this Court's precedent requires rendition of judgment for USAA even if no breach of contract claim had been submitted, *see Castañeda*, 988 S.W.2d at 201, the trial court erred in disregarding the jury's negative answer to the contract-breach submission.

Menchaca realized that a breach finding was a prerequisite to liability for policy benefits. *See id*. at 201 (holding that "there [was] no basis on which Castañeda may recover [policy benefits] based on this record," as she "did not obtain a determination from the trial court that Provident American was liable for breach of the insurance contract"). That is why Menchaca insisted on the question. As the trial court advised her after the jury returned its verdict, "You're the one that wanted

question no. 1. . . . You're stuck with it. You asked for it, and you got it. . . . y'all insisted." RR11:7-8.

By the time of the hearing on the motion to enter judgment, the trial court had changed its tune. Concluding that the question was "poorly worded" and lacked adequate definitions, the trial court decided it was free to "ignore" Question No. 1, which inquired whether USAA failed to comply with the policy. *See Menchaca*, 2014 WL 3804602, at *4 n.12; CR1:782-84. The trial court determined that the jury's response was "meaningless." CR1:784.

The trial court's remarks are telling. The question asked, "Did USAA Texas Lloyd's Company ("USAA") fail to comply with the terms of the insurance policy with respect to the claim for damages filed by Gail Menchaca resulting from Hurricane Ike?" App. 2; CR1:665. The court said, "look at the question again. It says, 'Breach of contract,' but it doesn't say what kind of breach. It doesn't even explain breach of contract. It doesn't even give a definition for breach of contract." CR1:783. But the question did not say "breach of contract"; it asked whether USAA failed to comply with the contract.

The question tracked the Pattern Jury Charge and complied with Rule 277's mandate for broad-form questions when feasible. *See* TEX. R. CIV. P. 277; Comm. on Pattern Jury Charges, Texas Pattern Jury Charges—Contracts 101.2 (State Bar of Texas 2012). A trial court may disregard a jury finding only if it is unsupported by

evidence or if the issue is immaterial. *Spencer*, 876 S.W.2d at 157. A question is immaterial when it should not have been submitted, or when it was properly submitted but has been rendered immaterial by other findings. *Id*. Even a defective question may not be disregarded as immaterial. *Id*. And a trial court's judgment must conform to the pleadings, the nature of the case proved, and the verdict. TEX. R. CIV. P. 301.

Breach of contract was pleaded, tried, argued, submitted, and answered by the jury. How can the question be immaterial when it supports a take-nothing judgment in USAA's favor? It is certainly material to USAA, and its submission is the culmination of a lawsuit that Menchaca initiated for an alleged contractual breach.

The trial court characterized its judgment as a "small victory for the plaintiff." *Menchaca*, 2014 WL 3804602, at *4 n.12. "Small victories" like these, when extrapolated to the thousands of storm-related claims pending in Texas courts, will have a monumentally devastating impact. This Court must ensure that any victory, however "small," is supported by the law. This one was not.

CONCLUSION AND PRAYER

"The threshold of bad faith is reached when a breach of contract is accompanied by an independent tort." *Moriel*, 879 S.W.2d at 17. This case never met that threshold. USAA requests that the Court grant this petition for review,

reverse the court of appeals' judgment, and render judgment that Menchaca take nothing. USAA also requests all other relief to which it is entitled.

Respectfully submitted,

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