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## INSURABILITY OF PUNITIVE DAMAGES IN TEXAS

By David Plaut, Hanna & Plaut, L.L.P.

Texas decisions between 1972 and 1987 allowed for recovery of punitive damages under standard liability policies. Since that time, there has been a rather dramatic shift in the attitude of Texas courts. Recent Texas cases indicate that punitive damages are not insurable. Importantly, a recent decision of the Fifth Circuit -- *St. Paul v. Convalescent Services* -- found that punitive damages were not insurable and so the insurer had no *Stowers* liability.

### A. Texas Decisions on the Insurability of Punitive Damages

There have been seven Texas appellate decisions on the insurability of punitive damages. Two of these decisions concerned liability insurance coverage, and five concerned uninsured motorist coverage. In addition, there has been one Fifth Circuit decision and one Texas federal district case addressing the insurability of punitive damages. The older appellate cases hold that punitive damages are insurable while more recent decisions preclude coverage for punitive damages.

#### 1. *Wallgren* Holds Punitive Damages Are Insurable

Apparently, the first decision of a Texas court on the insurability of punitive damages is *Dairyland County Mutual Insurance Co. v. Wallgren*, 477 S.W.2d 341 (Tex.Civ.App.–Fort Worth 1972, writ ref'd n.r.e.). The issue in *Wallgren* was whether automobile insurance covered punitive damages assessed against an insured. *Id.* at 342. The court concluded that the insuring language of the policy was broad enough to extend the coverage to the punitive damage award. The public policy argument of the insurance company was rejected by the court's conclusion that the public policy of Texas was defined by the language of the insurance contract inasmuch as the terms and conditions of the policy contract were prescribed and approved by the State Board and because the policy was written in order to comply with the requirements of the Texas Motor Vehicle Safety Responsibility Act. *Id.* at 342-43.

2. *Tyler Relies on Wallgren and Holds Punitive Damages Are Insurable*

The Houston Court of Appeals addressed the insurability of punitive damages in *Home Indem. Co. v. Tyler*, 522 S.W.2d 594 (Tex.Civ.App.– Houston [14th Dist.] 1975, writ ref'd n.r.e.). *Tyler* involved the standard uninsured motorist provisions of a Texas automobile policy. The insureds under the policy were injured in a motor vehicle collision involving an automobile operated by an uninsured motorist. They sued the uninsured motorist and the insurance company. The jury awarded each of the insureds punitive damages against the uninsured motorist. The trial court had entered judgment in favor of the insureds and against the insurance company and the uninsured motorist, jointly and severally, for the amounts awarded by the jury as punitive damages as well as the amounts awarded as compensatory damages. On appeal, the insurance company argued that coverage did not extend to the punitive damage awards, maintaining that coverage under the insurance policy for those awards would contravene public policy. Relying almost entirely on the holding in *Dairyland v. Wallgren*, the appellate court affirmed the trial court's judgment. The appellate court also noted that the uninsured motorist laws are remedial in nature and should be interpreted liberally.

3. Fifth Circuit in *Ridgway* Holds Punitive Damages Are Insurable

In *Ridgway v. Gulf Life Insurance Co.*, 578 F.2d 1026 (5th Cir.1978), the Fifth Circuit was required to make an *Erie* guess about the insurability of punitive damages in Texas. The Fifth Circuit held there was coverage for the punitive damage award and that public policy was not violated. The insurer maintained that the insurance contract, which the court found extended coverage to the punitive damage award, violated the public policy of the State of Texas. The court rejected that contention, citing *Wallgren*. 578 F.2d at 1030 (after noting that some states have not allowed coverage for punitive damages, the Fifth Circuit concluded Texas “apparently does not share this policy, and that ends the inquiry”).

A recent federal district decision, *Hartford Casualty Insurance Co. v Powell*, 19 F.Supp.2d 678 (N.D. Tex. 1998), recently noted a dramatic shift in the attitude of Texas courts since the decisions of *Wallgren* and *Tyler*. *Powell* emphasized that *Ridgway* is clearly wrong “when considered in context with the present Texas legal environment.” 19 F.Supp.2d at 696. The district court also predicted that the Texas Supreme Court would reject the holdings of *Wallgren* and *Tyler* and find that “public policy” in Texas precludes the insurability of punitive damages.

4. *Safway* Holds Punitive Damages Are Insurable

Another appellate decision, *American Home Assurance Co. v. Safway Steel Prods. Co.*, 743 S.W.2d 693 (Tex.App.–Austin 1987, writ denied), found that punitive damages are insurable. The issue in *Safway* was whether a liability insurance policy would protect a corporation that was the insured under the policy from a

punitive damage award in a tort action. The court took note of the competing views, citing and quoting at length from *Northwestern Nat'l Cas. Co. v. McNulty*, 307 F.2d 432 (5th Cir. 1962) (punitive damages not insurable under Florida and Virginia law) and *Lazenby v. Universal Under. Ins. Co.*, 214 Tenn. 639, 383 S.W.2d 1 (1964) (punitive damages insurable under Tennessee law), but found that punitive damages were insurable.

The *Safway* court doubted that the denial of insurance coverage for punitive damages actually deters the culpable actor and explained that “[i]n Texas, juries are not allowed to consider the defendant’s wealth, resources, or other insurance coverage when assessing compensatory or punitive damages.” 743 S.W.2d at 704. This observation no longer correctly reflects Texas law. The Texas Supreme Court has held that the financial status of the defendant is relevant the jury’s determination of punitive damages.

#### 5. *Lichte* Holds Punitive Damages Are Not Insurable

A 1990 decision of the El Paso Court of Appeals addressed the issue of whether uninsured motorist coverage would provide payment to an insured for punitive damages recovered by the insured against the uninsured motorist. *Government Employees Insurance Co. v. Lichte*, 792 S.W.2d 546 (Tex.App.–El Paso 1990), writ denied per curiam, 825 S.W.2d 431 (Tex. 1991). Without directly addressing the public policy issue, *Lichte* held that coverage did not exist. The court emphasized that “[t]he purpose of allowing the recovery of punitive damages is to punish the wrongdoer.” *Id.* at 549. Because the wrongdoer was the uninsured motorist and not the insured, the *Lichte* court did not believe it was bound to follow the cases holding that an insured’s liability insurance policy provides coverage when a judgment is obtained against the insured awarding exemplary damages. *Id.*

#### 6. *Vanderlinden* follows *Lichte* and Holds Punitive Damages Are Not Insurable

In *Vanderlinden v. United Servs. Auto. Ass’n Property & Cas. Ins. Co.*, 885 S.W.2d 239 (Tex.App.–Texarkana 1994, writ denied), the Texarkana Court of Appeals dealt with the issue of whether a request for recovery of punitive damages should be stricken from the plaintiff’s pleading in her suit against her own insurance company for recovery of benefits under uninsured motorist coverage extended to her by her insurer. The court commenced its analysis observing that “[p]unitive damages are typically not to compensate a damaged plaintiff for his injuries; rather, they are to discourage the defendant from continuing his heinous activities and to likewise discourage others from similarly misbehaving.” *Id.* at 240. *Vanderlinden* acknowledged the conflict between *Tyler* and *Lichte*, but followed *Lichte*, holding that punitive damages are not insurable. The court explained that “[m]ost of the states that have expressly considered this question have held that in this context an insurance company should not be liable

for punitive damages because to allow such a recovery would be antithetic to the acknowledged purpose to be served by rendition of such damages.” *Id.* at 242.

#### 7. *Shaffer* Holds Punitive Damages Are Not Insurable

Coverage for punitive damages was also rejected in *State Farm Mut. Auto. Ins. Co. v. Shaffer*, 888 S.W.2d 146 (Tex.App.–Houston [1st Dist.] 1994, writ denied). The *Shaffer* court held that, under usual rules of construction of insurance contracts, the language of the insurance policy would extend coverage to punitive damages. The court looked to the legislative intent of the Texas statute that defined the purpose of uninsured motorist coverage, which the court concluded was to protect conscientious motorists from financial loss caused by negligent financially irresponsible motorists. *Shaffer* also looked to the objective of the Texas Motor Vehicle Safety- Responsibility Act, which has as its objective the protection of persons from potential losses arising out of the operation of a vehicle. After examining both statutory enactments, the court noted that “it appears that the legislative intent . . . is only to provide compensatory damages to an injured party under an uninsured motorist policy.” *Id.* at 149. *Shaffer* emphasized that “neither deterrence of wrongful conduct nor punishment of [the insured], the wrongdoer, is achieved by imposing exemplary damages upon [the] insurance carrier . . . .” *Id.*

#### 8. Houston Court of Appeals Revisits *Tyler* and Holds Punitive Damages Are Not Insurable

In *Milligan v. State Farm Mutual Automobile Insurance Co.*, 940 S.W.2d 228 (Tex.App.–Houston [14th Dist.] 1997, writ denied), the Houston Court of Appeals took a second look at its earlier decision in *Tyler*, which held that punitive damages were insurable. In *Milligan*, the court pointed out that *Tyler* relied on *Dairyland v. Wallgren* in finding that punitive damages were insurable. *Milligan* recognizes that subsequent appellate decisions -- including *Shaffer*, *Vanderlinden*, and *Lichte* -- are contrary to *Tyler*.

Emphasizing the evolving nature of Texas law on the subject, the *Milligan* court rejected its earlier holding in *Tyler*, finding that “[i]n view of the Texas Supreme Court’s clear guidelines concerning the imposition of exemplary damages and the policy reasons therefor, we no longer accept the position taken in *Tyler*.” *Milligan* agreed with *Shaffer* and thus held that the uninsured motorist clause in the auto policy did not cover exemplary damages as a matter of law.

*Id.* at 232.

#### B. Other Jurisdictions that Preclude the Insurability of Punitive Damages

The following states have recognized that it is against public policy to insure against punitive damages:

- Arizona (*State Farm Mut. Auto. Ins. Co. v. Wilson*, 162 Ariz. 251, 782 P.2d 727 (1989));
- California (*J.B. Aguerre, Inc. v. American Guarantee & Liab. Ins. Co.*, 59 Cal. App.4th 6, 68 Cal. Rptr.2d 837 (1997));
- Colorado (*Lira v. Shelter Ins. Co.*, 913 P.2d 514 (Colo.1996));
- Connecticut (*Bodner v. United Servs. Auto. Ass'n*, 222 Conn. 480, 610 A.2d 1212 (1992));
- Florida (*U.S. Concrete Pipe Co. v. Bould*, 437 So.2d 1061, 1065 (Fla.1983));
- Illinois (*Warren v. Lemay*, 144 Ill.App.3d 107, 98 Ill.Dec. 279, 494 N.E.2d 206, 212 (1986));
- Indiana (*Commercial Union Ins. Co. v. Ramada Hotel Operating Co.*, 852 F.2d 298, 306 n. 9 (7th Cir.1988));
- Kansas (*Hartford Accident & Indem. Co. v. American Red Ball Transit Co.*, 262 Kan. 570, 938 P.2d 1281, cert. denied, 118 S.Ct. 372, 139 L.Ed.2d 290 (1997));
- Minnesota (*Lake Cable Partners v. Interstate Power Co.*, 563 N.W.2d 81 (Minn.Ct.App.1997));
- Missouri (*Crull v. Gleb*, 382 S.W.2d 17 (Mo.Ct.App.1964));
- Nevada (*Lombardi v. Maryland Cas. Co.*, 894 F.Supp. 369 (D.Nev.1995));
- New Jersey (*Johnson & Johnson v. Aetna Cas. & Sur. Co.*, 285 N.J.Super. 575, 667 A.2d 1087 (App.Div.1995));
- New York (*Zurich Ins. Co. v. Shearson Lehman Hutton, Inc.*, 84 N.Y.2d 309, 618 N.Y.S.2d 609, 642 N.E.2d 1065 (1994));
- North Dakota (*Employers Reinsurance Corp. v. Landmark*, 547 N.W.2d 527 (N.D.1996));
- Ohio (*Ruffin v. Sawchyn*, 75 Ohio App.3d 511, 599 N.E.2d 852 (1991));
- Oklahoma (*Jordan v. Cates*, 935 P.2d 289 (Okla.1997));
- Pennsylvania (*Butterfield v. Giuntoli*, 448 Pa.Super. 1, 670 A.2d 646 (1995));
- Rhode Island (*Douglas v. Bank of New England/Old Colony N.A.*, 566 A.2d 939 (R.I.1989)); and
- South Dakota (*City of Fort Pierre v. United Fire & Cas. Co.*, 463 N.W.2d 845 (S.D.1990)).

### C. Jurisdictions Holding Punitive Damages are Insurable

Some states have no clear policy on the insurability of punitive damages. For example, Maine disallows coverage for punitive damages in the uninsured motorist context, but no case addresses liability insurance. *Braley v. Berkshire Mut. Ins. Co.*, 440 A.2d 359 (Me.1982). There do not appear to be any applicable cases for Hawaii, Massachusetts, Nebraska, New Hampshire, South Carolina, Utah, or Washington.

The remaining states that have discussed the matter simply conclude that public policy does not preclude coverage:

- Delaware (*Whalen v. On-Deck, Inc.*, 514 A.2d 1072 (Del.1986) (no evidence of public policy against such insurance));

- Georgia (*Lunceford v. Peachtree Cas. Ins. Co.*, 230 Ga.App. 4, 495 S.E.2d 88, 91-92 (1997) (insurance coverage of punitive damages allowed in liability context, but not in uninsured motorist context));
- Iowa (*Skyline Harvestore Sys., Inc. v. Centennial Ins. Co.*, 331 N.W.2d 106 (Iowa 1983));
- Michigan (*Meijer, Inc. v. General Star Indem. Co.*, 826 F.Supp. 241 (W.D.Mich.1993), *aff'd*, 61 F.3d 903, 1995 WL 433592 (6th Cir.1995) (noting that no Michigan case has squarely addressed whether an insured should be permitted to recover punitive damages from an insurer but finding that it appears that Michigan law permits recovery));
- Mississippi (*Anthony v. Frith*, 394 So.2d 867 (Miss.1981));
- Montana (*Fitzgerald v. Western Fire Ins. Co.*, 209 Mont. 213, 679 P.2d 790 (Mont.1984));
- New Mexico (*Baker v. Armstrong*, 106 N.M. 395, 744 P.2d 170 (N.M.1987));
- North Carolina (*New South Ins. Co. v. Kidd*, 114 N.C.App. 749, 443 S.E.2d 85 (1994));
- Oregon (*A-1 Sandblasting & Steamcleaning Co. v. Baiden*, 293 Or. 17, 643 P.2d 1260 (Or.1982) (distinguishing between “intentional act” and “intentionally inflicted injury”));
- West Virginia (*Perry v. Melton*, 171 W.Va. 397, 299 S.E.2d 8 (W.Va.1982) (punitive damages are awarded to punish and deter, but also benefit the injured party));
- Wisconsin (*Brown v. Maxey*, 124 Wis.2d 426, 369 N.W.2d 677 (Wis.1985));
- Wyoming (*Sinclair Oil Corp. v. Columbia Cas. Co.*, 682 P.2d 975 (Wyo.1984).

Many of these cases note the overriding public policies of freedom of contract and enforcing the terms of a contract against the insurer.

The cases holding that public policy allows punitive damages to be covered by insurance do so in a limited number of settings. *See, e.g.*,

- Alabama (*Montgomery Health Care Facility, Inc. v. Ballard*, 565 So.2d 221 (Ala.1990) (Alabama public policy allows liability insurance to cover punitive damages in the wrongful death context));
- Arkansas (*Southern Farm Bureau Cas. Ins. Co. v. Daniel*, 246 Ark.849, 440 S.W.2d 582 (1969) (vicarious liability));
- Idaho (*Abbie Uriguen Oldsmobile Buick, Inc. v. United States Fire Ins. Co.*, 95 Idaho 501, 511 P.2d 783, 789 (1973) (adopting the *Lazenby* approach));
- Kentucky (*Continental Ins. Cos. v. Hancock*, 507 S.W.2d 146 (Ky.1973) (vicarious liability));
- Louisiana (*Sharp v. Daigre*, 555 So.2d 1361 (La.1990) (uninsured motorist context));
- Maryland (*First Nat'l Bank of St. Mary's v. Fidelity & Deposit Co.*, 283 Md. 228, 389 A.2d 359 (1978) (vicarious liability));
- Tennessee (*Lazenby v. Universal Underwriters Ins. Co.*, 214 Tenn. 639, 383 S.W.2d 1 (1964));

- Vermont (*State of Vermont v. Glens Falls Ins. Co.*, 137 Vt.313, 404 A.2d 101 (1979)); and
- Virginia (*United Servs. Auto. Ass'n v. Webb*, 235 Va. 655, 369 S.E.2d 196 (1988) (noting *McNulty* overruled by statute)).