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## Antitrust and Consumer Protection

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# ANTITRUST AND CONSUMER PROTECTION

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## I. INTRODUCTION

Consumer welfare is the common concern of the antitrust laws, the Texas Deceptive Trade Practices-Consumer Protection Act (DTPA), the Texas Insurance Code (TIC), and various other statutes prohibiting fraudulent conduct in dealing with consumers.<sup>1</sup> Antitrust laws, however, primarily address the misuse of market power to harm consumers, while anti-deception statutes focus on consumer harm brought about through

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1. See TEX. BUS. & COM. CODE ANN. § 17.41. Section 17.50 of the DTPA provides: “A consumer may maintain an action where any of the following constitute a producing cause of economic damages or damages for mental anguish:

- (1) the use or employment by any person of a false, misleading, or deceptive act or practice that is:
  - (A) specifically enumerated in a subdivision of Subsection (b) of Section 17.46 of this subchapter; and
  - (B) relied on by a consumer to the consumer’s detriment;
- (2) breach of an express or implied warranty;
- (3) any unconscionable action or course of action by any person; or
- (4) the use or employment by any person of an act or practice in violation of Chapter 541, Insurance Code.”

TEX. BUS. & COM. CODE ANN. § 17.50(a).

deception and a litany of other unlawful practices.<sup>2</sup> The antitrust laws and the anti-fraud statutory schemes therefore are best viewed as focusing on complementary aspects of consumer welfare.

This article covers significant developments under federal and Texas antitrust laws and consumer protection laws (including the DTPA and its various tie-ins like the Texas Insurance Code)<sup>3</sup> during the Survey period, December 1, 2017, through November 31, 2018.

## II. ANTITRUST

As in prior years, it was difficult to be an antitrust plaintiff during the Survey period. Many plaintiffs alleging antitrust claims during the Survey period found themselves unable to get past the motion to dismiss stage; only one survived summary judgment, and one set of plaintiffs had their victory taken away by the appellate courts notwithstanding winning a seven-week bench trial.

### A. PLEADING-STAGE DECISIONS

SureShot Golf Ventures and Topgolf are competitors in the golf entertainment center market.<sup>4</sup> SureShot had a multi-year contract for golf ball tracking technology with Protracer when Topgolf bought Protracer.<sup>5</sup> SureShot sued, expressing concern that Topgolf would not renew SureShot's license for the tracking technology when SureShot's current contract expired.<sup>6</sup> The U.S. District Court for the Southern District of Texas dismissed the claims with prejudice, holding that the claims were not ripe and that SureShot had failed to plead antitrust injury.<sup>7</sup> On appeal, the U.S. Court of Appeals for the Fifth Circuit agreed that the claims as pled were not ripe because SureShot was complaining about hypothetical harm in the future.<sup>8</sup> However, the Fifth Circuit held that the district court's decision to reach the question of antitrust injury and dismiss with prejudice was improper, so the Fifth Circuit modified the judgment to a dismissal without prejudice.<sup>9</sup>

In *Montoya v. San Angelo Community Medical Center*, the plaintiff-doctor alleged that patients in the hospital emergency room needing the care of a nephrologist were being referred only to a hospital-affiliated

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2. *Reiter v. Sonotone Corp.*, 442 U.S. 330, 343 (1979); *Roy B. Taylor Sales, Inc. v. Hollymatic Corp.*, 28 F.3d 1379, 1382 (5th Cir. 1994); TEX. BUS. & COM. CODE ANN. § 17.44(a).

3. *See, e.g.*, TEX. INS. CODE ANN. § 541.151 (“A person who sustains actual damages may bring an action against another person for those damages caused by the other person engaging in an act or practice . . . specifically enumerated in [the DTPA] as an unlawful deceptive trade practice[.]”).

4. *SureShot Golf Ventures, Inc. v. Topgolf Int'l, Inc.*, 754 F. App'x 235, 236–37 (5th Cir. 2018).

5. *Id.* at 237.

6. *Id.* at 237–38.

7. *Id.* at 238.

8. *Id.* at 240–41.

9. *Id.* at 241.

physician group with which he competed and that this practice was an unlawful restraint of trade in violation of the Texas Free Enterprise and Antitrust Act of 1983 (TFEAA).<sup>10</sup> The Austin Court of Appeals affirmed dismissal of the claim under Texas Rule of Civil Procedure 91(a) on the ground that the plaintiff had only alleged injury to his own economic interests and thus had failed to allege facts demonstrating antitrust injury.<sup>11</sup>

In *Mary Kay Inc. v. Reibel*, Gerald Reibel was sued by cosmetics manufacturer Mary Kay for allegedly selling expired Mary Kay products on eBay without authorization.<sup>12</sup> Reibel counterclaimed for attempted monopolization under federal law and unfair competition under state law, alleging that Mark Kay was improperly using litigation against small vendors.<sup>13</sup> Mary Kay moved to dismiss on the grounds that Reibel had failed to plead antitrust injury.<sup>14</sup> The U.S. District Court for the Northern District of Texas agreed, explaining that “the antitrust laws are not intended to prevent a manufacturer’s ‘monopoly over the distribution of its own products.’”<sup>15</sup> The district court granted the motion to dismiss because Reibel failed to allege antitrust injury in that he “failed to allege an injury of the type the antitrust laws were intended to prevent.”<sup>16</sup> The district court alternatively granted the motion to dismiss on the ground that Reibel failed to allege the necessary elements of his antitrust claims.<sup>17</sup> Mary Kay argued that (1) Reibel failed to define the product and geographic markets; (2) failed to identify any actions by Mary Kay that could be deemed predatory or exclusionary; (3) failed to plausibly allege that Mary Kay had a specific intent to monopolize; and (4) failed to plausibly allege that Mary Kay had a dangerous probability of achieving monopoly power.<sup>18</sup> The district court held that Reibel did not specifically respond to any of these arguments and that Reibel’s failure to adequately plead specific intent to monopolize or the dangerous probability of obtaining monopoly power were fatal to Reibel’s claims.<sup>19</sup>

In *Batra v. Covenant Health System*,<sup>20</sup> a doctor whose credentials to practice at Covenant Health Systems’s facilities were not renewed, resulting in a report to the National Practitioner Data Bank, brought suit complaining, among other things, that Covenant’s actions constituted an unreasonable restraint of trade under TFEAA.<sup>21</sup> Covenant moved to dis-

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10. *Montoya v. San Angelo Cmty. Medical Ctr.*, No. 03–16–00510–CV, 2018 WL 2437508, at \*1, \*3 (Tex. App.—Austin May 31, 2018, pet. denied).

11. *Id.* at \*5–7.

12. *Mary Kay Inc. v. Reibel*, No. 3:17–CV–2634–D, 2018 WL 2984865, at \*1 (N.D. Tex. Jun. 14, 2018) (mem. op.).

13. *Id.* at \*4.

14. *Id.* at \*2–3.

15. *Id.* at \*4 (quoting *Domed Stadium Hotel, Inc. v. Holiday Inns, Inc.*, 732 F.2d 480, 488 (5th Cir. 1984)).

16. *Id.*

17. *Id.*

18. *Id.* at \*5.

19. *Id.*

20. 562 S.W.3d 696 (Tex. App.—Amarillo 2018, pet. filed).

21. *Id.* at 704.

miss under the Texas Citizens Participation Act.<sup>22</sup> The Amarillo Court of Appeals affirmed the trial court's order granting the motion, holding, with regard to the plaintiff's TFEAA claim, that the plaintiff failed to present clear and specific evidence of an adverse effect on competition as a whole.<sup>23</sup>

The Foreign Trade Antitrust Improvements Act (FTAIA)<sup>24</sup> limits the application of U.S. antitrust laws in cases involving foreign commerce, excluding coverage when only foreign injury is alleged unless the complained-of conduct “has a ‘direct, substantial, and reasonably foreseeable effect’ on United States imports, domestic commerce, or United States exporters.”<sup>25</sup> *Leaf Trading Cards, LLC v. The Upper Deck Company* involved a dispute between two manufacturers of hockey trading cards. Leaf Trading Cards (Leaf) accused The Upper Deck Company (Upper Deck) of using its “dominant market position” to foreclose competition in U.S. and Canadian markets for hockey trading cards.<sup>26</sup> Upper Deck argued that the FTAIA barred Leaf's allegations regarding the Canadian market.<sup>27</sup> Leaf's contention was that Upper Deck's actions in excluding Leaf from the bigger Canadian market, had the direct, substantial, and reasonably foreseeable effect of Leaf being unable to achieve efficiencies necessary to compete in the American market.<sup>28</sup> Previously, in *Coors Brewing Co. v. Miller Brewing Co.*,<sup>29</sup> the U.S. District Court for the District of Colorado held that a defendant's anticompetitive conduct in Canada could satisfy the FTAIA in an integrated market.<sup>30</sup> Applying *Coors* to the dispute before it, and accepting Leaf's allegations as true, the United States District Court for the Northern District of Texas held that the North American hockey trading card market, like the National Hockey League whose players were depicted on the cards, was sufficiently integrated to render the harm alleged by Leaf in the United States a foreseeable effect of Upper Deck's alleged actions in Canada sufficient to survive a motion to dismiss.<sup>31</sup>

Louisiana law governing court reporters provides that an employee or attorney of a litigant may not act as a court reporter.<sup>32</sup> It defines “employee” to include “a person who has a contractual relationship with a

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22. *Id.*

23. *Id.* at 711–12; *see also* Location Servs., LLC v. Digital Recognition Network, Inc., No. 4:18-CV-744-A, 2018 WL 5787317, at \*2–3 (N.D. Tex. Nov. 11, 2018) (mem. op.) (dismissing antitrust claims for failure to plead facts sufficient to demonstrate antitrust injury, power to exclude competition, or existence of a conspiracy).

24. Foreign Trade Antitrust Improvements Act, 15 U.S.C. § 6a (2012).

25. *Leaf Trading Cards, LLC v. The Upper Deck Co.*, No. 3:17-CV-03200-N, 2018 WL 2971135, at \*2 (N.D. Tex. Mar. 16, 2018) (mem. op.) (quoting 15 U.S.C. § 6a (2012)).

26. *Id.* at \*1.

27. *Id.* at \*3.

28. *Id.*

29. 889 F. Supp. 1394 (D. Colo. 1995) (mem. op.).

30. *Id.* at 1398.

31. *Leaf Trading Cards*, 2018 WL 2971135, at \*3.

32. *Veritext Corp. v. Bonin*, 901 F.3d 287, 290 (5th Cir. 2018).

party litigant to provide shorthand reporting.”<sup>33</sup> This law is enforced by the Louisiana Board of Examiners of Certified Shorthand Reporters (the Board).<sup>34</sup> Starting in 2012, the Board began enforcing this provision against court reporters who had volume-based discount agreements and related concessions with their frequent customers.<sup>35</sup>

A national court reporting service, Veritext, sued alleging, among other things, that the Board’s actions violated the antitrust laws because the Board was acting to prevent competition from national and regional court reporting firms in order to increase business opportunities for local, freelance court reporters.<sup>36</sup> The U.S. District Court for the Eastern District of Louisiana granted the Board’s motion to dismiss the antitrust claims, but the U.S. Court of Appeals for the Fifth Circuit reversed.<sup>37</sup>

Veritext pled that the Board was comprised of market participants who acted to deter and delay the entry of large court reporting firms into the market.<sup>38</sup> The court held that these allegations were sufficient to support a finding that the Board’s conduct restrains trade.<sup>39</sup> The Fifth Circuit rejected the Board’s contention that its actions were immune. While *Parker* immunity provides immunity from federal antitrust laws for conduct by a state, this immunity applies only where (1) the challenged restraint is “clearly articulated and affirmatively expressed as state policy” and (2) the policy is “actively supervised by the State.”<sup>40</sup> The Fifth Circuit held that the Board satisfied the first requirement, but not the second, which requires that the state at least review the substance of any anticompetitive decisions.<sup>41</sup>

The Fifth Circuit explained that Veritext’s pleading set forth sufficient facts to support a finding of the absence of active supervision because “nothing in the record indicate[d]”<sup>42</sup> that any elected or appointed state officials oversaw the Board’s actions.<sup>43</sup> The court rejected the Board’s argument that active supervision could be found in the legislature’s ability to amend the law or veto proposed rules under the Louisiana Administrative Procedures Act, holding that “the ‘mere potential for state supervision’” is insufficient to constitute active supervision.<sup>44</sup> The Fifth Circuit also rejected the Board’s arguments that (1) Veritext had not suf-

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33. *Id.*

34. *Id.*

35. *Id.*

36. *Id.*

37. *Id.* at 291.

38. *Id.* at 292.

39. *Id.*

40. *Id.* (quoting *N. Carolina State Bd. of Dental Exam’rs v. Fed. Trade Comm’n*, 135 S. Ct. 1101, 1110 (2015)).

41. *Id.*

42. The Fifth Circuit’s opinion correctly reflects that the court was reviewing an order granting a motion to dismiss for failure to state a claim but recites the standard of review for summary judgment, refers several times to “the record,” and concludes by stating that the district court erred in granting summary judgment. *Id.* at 291–93.

43. *Id.* at 292.

44. *Id.* at 292–93 (quoting *N. Carolina State Bd. of Dental Exam’rs*, 135 S. Ct. at 1116).

ficiently pled that Board members were active market participants and (2) the Board does not advance private interests simply by enforcing state law.<sup>45</sup> Louisiana law provides that six of the nine Board members be certified shorthand reporters, which the court found sufficient to qualify them as active market participants.<sup>46</sup> The court further held that “it strains credulity to regard the Board’s conduct as strictly public minded,” given that the record reflected that the Board had convened a meeting that included “‘How to increase rates?’” as an agenda item.<sup>47</sup> The Fifth Circuit concluded that Veritext had pled sufficient facts to support a finding of active supervision by the state.<sup>48</sup>

#### B. RELEVANT MARKET

American Express (Amex) requires the merchants with which it contracts to agree to an antisteering provision under which the merchants must agree not to “steer” customers from using American Express cards to using other credit cards.<sup>49</sup> In *Ohio v. American Express Co.*,<sup>50</sup> the United States and several states sued Amex, alleging that the antisteering provision violated section 1 of the Sherman Act. The U.S. District Court for the Eastern District of New York held a seven-week bench trial and ruled against Amex, holding (1) that the credit card market should be treated as a market for merchants and a separate market for cardholders and (2) that the antisteering provisions have an anticompetitive effect in the merchant market.<sup>51</sup> The U.S. Court of Appeals for the Second Circuit reversed, holding (1) that the credit card market was a single market and (2) that viewing the market as a whole, Amex’s antisteering provision was not anticompetitive.<sup>52</sup>

The United States Supreme Court granted certiorari and affirmed, holding in a 5–4 decision that the United States had failed to meet its burden to prove that the antisteering provisions were anticompetitive.<sup>53</sup> The Supreme Court first explained that the credit card market was a two-sided transaction platform in that credit card companies brought two parties together and offered different services to each side.<sup>54</sup> Specifically, the credit card companies offer credit to the cardholders and processing services and quick payment to the merchants.<sup>55</sup> The Court engaged in a lengthy discussion, supported by citation to numerous academic journal articles, of the ways in which two-sided transaction platforms are different from traditional markets and concluded that two-sided platforms re-

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45. *Id.* 293.

46. *Id.*

47. *Id.*

48. *Id.*

49. *Ohio v. American Express Co.*, 138 S. Ct. 2274, 2277 (2018).

50. *Id.*

51. *Id.* at 2283.

52. *Id.*

53. *Id.* at 2283, 2287.

54. *Id.* at 2280–81.

55. *Id.* at 2280.

quire a different analysis for antitrust purposes.<sup>56</sup> Specifically, two-sided platforms “cannot raise prices on one side without risking a feedback loop of declining demand . . . [a]nd the fact that two-sided platforms charge one side a price that is below or above cost reflects differences in the two sides’ demand elasticity, not market power or anticompetitive pricing.”<sup>57</sup> Likewise, a price increase on one side of the platform is not evidence of anticompetitive effects if it has not “increased the overall cost of the platform’s services.”<sup>58</sup> The Court concluded that a two-sided transaction market should be analyzed as a single market for antitrust purposes.<sup>59</sup>

Turning to the evidence, the Supreme Court held that the plaintiffs had not carried their burden to show anticompetitive effects in the relevant market.<sup>60</sup> The plaintiffs had proven only that Amex’s agreements increased merchant fees and had not shown anticompetitive effects in the market as a whole—such as an increased cost of credit-card transactions, reduced number of credit-card transactions, or other harm to competition in the credit-card market.<sup>61</sup>

Justice Stephen Breyer, writing for the dissent, described the anticompetitive effects on the merchant side of the transaction found by the district court after the bench trial.<sup>62</sup> The dissent then challenged the majority’s decision to combine the two sides of the credit card transaction into a single market, stating that there was no support for doing so in either antitrust caselaw or in the academic articles the majority relied upon.<sup>63</sup> The dissent also accused the majority of incorrectly discounting the evidence the plaintiffs offered reflecting an increase in the price Amex charged merchants.<sup>64</sup>

*Viva Cinemas Theaters and Entertainment, LLC v. AMC Entertainment Holdings, Inc.*<sup>65</sup> arose from complaints about agreements between a movie theater and motion picture studios, known as movie clearances. The United States District Court for the Southern District of Texas held that absent evidence of horizontal agreements between movie producers, claims arising from movie clearances must be analyzed under the rule of reason, which requires analysis of anti-competitive effects in a relevant product and geographic market.<sup>66</sup> AMC moved for summary judgment, arguing that Viva lacked sufficient evidence to define the relevant market.<sup>67</sup> The court held that while an expert’s opinion regarding a geo-

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56. *Id.* at 2280–81, 2285–87.

57. *Id.* at 2285–86.

58. *Id.* at 2286.

59. *Id.* at 2286–87.

60. *Id.* at 2287.

61. *Id.* at 2287–90.

62. *Id.* at 2293–94 (Breyer, J., dissenting).

63. *Id.* at 2297–2301.

64. *Id.* at 2296, 2301–02.

65. No. 4:15-CV-1015, 2018 WL 4895841 (S.D. Tex. Aug. 21, 2018).

66. *Id.* at \*1.

67. *Id.*



graphic market cannot be based solely on the plaintiff's data, a geographic market opinion is not legally insufficient simply because the expert's opinion is based on practical indicia, such as the defendant competitor's data reflecting its understanding of its competitors, rather than an independent economic analysis focusing on consumers.<sup>68</sup> The district court held that evidence that the availability of first run films with Spanish dubbing or subtitles had fallen to "almost zero" in the relevant market was sufficient evidence of harm to competition to survive summary judgment.<sup>69</sup>

### C. HARM TO COMPETITION

*Howard v. Lowe's Home Centers, LLC*<sup>70</sup> arose from an allegedly defective refrigerator the plaintiff purchased from Lowe's. The plaintiff alleged that the defective appliance caused personal injuries and a host of damage to personal property.<sup>71</sup> She brought suit alleging, among other things, that Lowe's had violated the Sherman Act by entering into an agreement with Whirlpool described by the plaintiff as an "agreement with the manufacturer to ignore the replacement requirements of all warranty cases" and as a "secret Agreement."<sup>72</sup> The U.S. District Court for the Western District of Texas gathered from the plaintiff's deposition testimony that she was referring to the Master Standard Buying Agreement between Lowe's and Whirlpool that governs the parties' responsibilities for harm to goods in shipment, invoicing, and warranties.<sup>73</sup> Lowe's moved for summary judgment on the plaintiff's Sherman Act claim, which the court granted because the plaintiff offered no evidence that the Master Standard Buying Agreement or any other agreement between Lowe's and Whirlpool was anticompetitive.<sup>74</sup>

## III. CONSUMER PROTECTION

Consumer protection developments in 2018 highlight the ever-growing importance of choosing the right claims against the right parties. As is often the case, 2018's most significant developments arose under of the TIC. The Texas Supreme Court made it clear that extra-contractual, bad-faith denial claims and damages *theoretically* exist, but only to the dubious extent that the courts are willing to entertain them. Meanwhile, and as predicted in last year's article, federal courts across Texas are confronting a new species of statutory-induced diversity that plaintiffs are combating to mixed degrees of success. On the federal statutory front, the U.S. Court of Appeals for the Fifth Circuit has now clarified that banks

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68. *Id.* at \*2 (citing *Brown Shoe Co. v. United States*, 370 U.S. 295, 325 (1962)).

69. *Id.*

70. 306 F. Supp. 3d 951 (W.D. Tex. 2018).

71. *Id.* at 954.

72. *Id.* at 954, 960.

73. *Id.* at 960.

74. *Id.*

are not liable for loan-servicing companies' unscrupulous practices, at least not under principal/agent theories of vicarious liability.

These developments all share a common theme in that they reveal the tension between old and new, between modern statutory schemes and traditional common-law concepts.

#### A. STATE CONSUMER PROTECTION

##### 1. *Menchaca and the Independent Injury Rule*

The Texas Supreme Court issued a long-overdue opinion in 2018 clarifying a critical overlap between insurance policy contractual claims and deceptive-practice claims under the TIC and at common law.<sup>75</sup> In *Menchaca*, a majority of the supreme court issued a well-reasoned, thoroughly researched, and overall helpful exposition on the blurred distinction between a claim for breach of an insurance policy (as a contract action) and a purely statutory claim for deceptive insurance practices.<sup>76</sup> Despite this helpful holding, the *Menchaca* court—or a plurality of it—arguably misapplied the majority's legal synthesis.

*Menchaca* involved USAA's denial of coverage after a Galveston homeowner filed a claim for damages caused by 2008's Hurricane Ike. Two adjusters determined that some of the storm's damages were covered under the applicable policy, but they concluded that the repair costs would fall below the homeowner's deductible. Hence, USAA denied coverage.<sup>77</sup>

The homeowner sued USAA for breach of contract and for first-party insurance violations for bad-faith denial of coverage (or, more precisely, for failure to adequately investigate before denying coverage). "As damages for both claims, [the homeowner] sought only insurance benefits under the policy, plus court costs and attorney's fees."<sup>78</sup> At trial, a jury found that USAA did not breach the insurance policy by denying coverage. But the jury also found that USAA did commit a statutory violation by "refus[ing] 'to pay a claim without conducting a reasonable investigation with respect to' that claim."<sup>79</sup> The jury awarded the homeowner roughly \$11,000 in damages. USAA sought judgement notwithstanding verdict, contending the damage award conflicted with the first answer as a matter of law.<sup>80</sup> The homeowner countered that the damage award properly rested on the jury's finding of a statutory violation.<sup>81</sup>

On appeal, the Corpus Christi-Edinburg Court of Appeals affirmed, essentially holding that the TIC "imposes a duty on an insurer, above and

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75. USAA Texas Lloyds Co. v. *Menchaca*, 545 S.W.3d 479, 497 (Tex. 2018).

76. *See id.*

77. *Id.* at 485 n.1 ("The policy's declaration page provides that the policy covers 'only that part of the loss over the deductible stated,' and then lists the deductible amounts for 'wind and hail' and for 'all other perils.'").

78. *Id.* at 485.

79. *Id.* at 485–86.

80. *Id.* at 486.

81. *Id.*

beyond the duties established by the insurance policy itself, to conduct a reasonable investigation prior to denying a claim.”<sup>82</sup> Thus, the intermediate court concluded, “[i]t follows that USAA could have fully complied with the contract even if it failed to reasonably investigate [the homeowner’s] claim.”<sup>83</sup> The appellate arguments pitted two landmark Texas Supreme Court decisions against each other. On the one hand, the supreme court had held that “an insurance company’s ‘failure to properly investigate a claim is not a basis for obtaining policy benefits.’”<sup>84</sup> On the other hand, the supreme court had also held that “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.’”<sup>85</sup>

Confronted with an opportunity to clarify the contradictory holdings, the supreme court granted review and delved deep into the historical and policy background underlying the distinction between a statutory breach and a contractual breach, including the damage model available in each.<sup>86</sup> The *Menchaca* court explained that a statutory violation (which sounds in tort) and a policy breach (which sounds only in contract) are two wholly-distinct causes of action based on different underlying duties to the insured.<sup>87</sup> Though distinct, such claims “are often ‘largely interwoven,’ and the same evidence is often ‘admissible on both claims.’”<sup>88</sup>

In *Menchaca*, which presented an improbable jury verdict, the question therefore was whether policy benefits may constitute “actual damages” under the TIC. The *Menchaca* court noted that the answer, generally speaking, is no—“but the issue is complicated and involves several related questions.”<sup>89</sup> The *Menchaca* court then distilled decades of Texas law on the issue into a laudably well-researched and pensive list of applicable rules, as follows:

- (1) **General Rule:** “[A]n insured cannot recover policy benefits for an insurer’s statutory violation if the insured does not have a right to those benefits under the policy. This rule derives from the fact that the Insurance Code only allows an insured to recover actual damages ‘caused by’ the insurer’s statutory violation.”<sup>90</sup>
- (2) **Entitled-to-Benefits Rule:** “[A]n insured who establishes a right to receive benefits under an insurance policy can recover those benefits as ‘actual damages’ under the statute if the insurer’s statutory

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82. *USAA Texas Lloyd’s Co. v. Menchaca*, 13-13-00046-CV, 2014 WL 3804602, at \*5 (Tex. App.—Corpus Christi July 31, 2014) (discussing TEX. INS. CODE ANN. § 541.060(a)(7)), *rev’d*, 14-0721, 2017 WL 1311752 (Tex. Apr. 7, 2017), opinion withdrawn and superseded, 545 S.W.3d 479 (Tex. 2018) and *rev’d*, 545 S.W.3d 479 (Tex. 2018).

83. *Id.*

84. *Menchaca*, 545 S.W.3d at 487 (quoting *Provident Am. Ins. Co. v. Castañeda*, 988 S.W.2d 189, 198 (Tex. 1998)).

85. *Id.* (quoting *Vail v. Tex. Farm Bureau Mutual Ins. Co.*, 754 S.W.2d 129, 136 (Tex. 1988)).

86. *Id.* at 486–503.

87. *Id.* at 489.

88. *Id.* (quoting *Liberty Nat’l Fire Ins. Co. v. Akin*, 927 S.W.2d 627, 630 (Tex. 1996)).

89. *Id.* at 489.

90. *Id.* at 490.

violation causes the loss of the benefits. . . . Because the Insurance Code provides that the statutory remedies are cumulative of other remedies, we concluded that the insureds could elect to recover the benefits under the statute even though they also could have asserted a breach-of-contract claim.”<sup>91</sup>

- (3) **Benefits-Lost Rule:** “[A]n insured can recover benefits as actual damages under the Insurance Code even if the insured has no right to those benefits under the policy, *if the insurer’s conduct caused the insured to lose that contractual right.*”<sup>92</sup> The supreme court offered several examples, including situations where an agent’s misrepresentations induced the insured to purchase a policy, only to later learn that the claim type is not actually covered.<sup>93</sup> Another example would be a situation in which the insurer pays out other claims during the course of litigation until the policy limit is reached and obviates the otherwise triggered policy.<sup>94</sup> The *Menchaca* majority<sup>95</sup> explained that, “[p]ut simply, an insurer that commits a statutory violation that eliminates or reduces its contractual obligations cannot then avail itself of the general rule.”<sup>96</sup>
- (4) **Independent-Injury Rule:** The *Menchaca* court reiterated the familiar notion that “there can be no claim for bad faith when an insurer has promptly denied a claim that is in fact not covered.”<sup>97</sup> However, the *Menchaca* court noted that the Texas Supreme Court had not foreclosed recovery where an insurer with no policy obligations nonetheless commits a statutory violation that entitles the plaintiff to recover.<sup>98</sup> The *Menchaca* court warned that such cases “would be rare, and we in fact have yet to encounter one.”<sup>99</sup>
- (5) **No-Recovery Rule:** “An insured cannot recover any damages based on an insurer’s statutory violation unless the insured establishes a right to receive benefits under the policy or an injury independent of a right to benefits.”<sup>100</sup> This rule “is simply the natural corollary to the first four rules.”<sup>101</sup>

The *Menchaca* court thus offered an invaluable roadmap for first-party insurance litigants.

Of the five principles above set forth by *Menchaca*, the “benefits-lost rule” is particularly noteworthy. The *Menchaca* facts actually bore some

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91. *Id.* at 495 (noting that this result harmonizes *Vail v. Texas Farm Bureau Mutual Ins. Co.*, 754 S.W.2d 129, 130 (Tex. 1988)).

92. *Id.* at 497 (emphasis by court).

93. *Id.* at 497–98.

94. *Id.* at 498 (discussing *Kennedy v. Sale*, 689 S.W.2d 890, 891–92 (Tex. 1985); *JAW The Pointe, L.L.C. v. Lexington Ins. Co.*, 460 S.W.3d 597, 599–602 (Tex. 2015)).

95. *Id.* A majority participated in the five-rule portion of the *Menchaca* holding. A plurality participated in the application that resulted in the remand.

96. *Id.* at 499.

97. *Id.* (quoting *Republic Ins. Co. v. Stoker*, 903 S.W.2d 338, 341 (Tex. 1995)).

98. *Id.*

99. *Id.* at 500.

100. *Id.*

101. *Id.*

resemblance to those in the case the majority cited to as an example of where the benefits-lost rule could have applied.<sup>102</sup> The *Menchaca* majority explained that *JAW Pointe* was a bad-faith insurance claim case where the supreme court indicated, in dicta, that an insured's statutory violations—payments to other insureds during litigation that resulted in exhaustion of the plaintiff's policy limits—might support recovery of contractual benefits. According to the *Menchaca* court, *JAW Pointe*'s insured/plaintiff would have statutorily recovered policy benefits based on the carrier's depriving it of contractual rights through payments to other insureds during litigation with the plaintiff (exhausting the policy limits).<sup>103</sup> During litigation the insurance carrier continued remitting payments to other policyholders until it hit the \$25 million limit, at which point the carrier moved for summary judgment on those grounds. The plaintiff effectively ignored the summary judgment motion and instead took its statutory recovery of benefits up on appeal, where it ultimately lost based on an unrelated issue involving a policy exclusion. Though the relevant portion of the *JAW Pointe* holding was either dicta or implied (because of its unique posture on the unchallenged policy-limits argument), the *Menchaca* court highlighted the *JAW Pointe* facts as an example of where statutory recovery might be decoupled from contractual liability.<sup>104</sup>

What the *Menchaca* plurality did next as it applied those rules to its facts is puzzling. The *Menchaca* court acknowledged that it must find a way, *any* way, to harmonize allegedly conflicting jury answers, "if reasonably possible," to avoid a remand.<sup>105</sup> Thus, based on the appellate record and applicable standards for reviewing a jury charge, all the *Menchaca* court needed to do was find some way to square the jury's verdict with one of the enumerated exceptions.

*Menchaca*'s plurality probably could have done so by applying the benefits-lost rule—i.e., interpreting the jury's finding to be that, while USAA did not breach the policy/contract because the deductible was not reached, a statutorily prohibited failure to fully investigate caused the damages to fall short of that deductible. The application might have been a bit awkward, but it would have fit the facts better than the chosen outcome. First, application of the benefits-lost rule would have negated any alleged conflict in the verdict. It also would have also afforded a much smoother disposition of the case than a tortured remand on an issue that the *Menchaca* court expressly noted was not properly preserved for appeal but that it considered anyway "[i]n the interest of justice."<sup>106</sup>

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102. *See id.* at 498–99 (discussing *JAW The Pointe, L.L.C. v. Lexington Ins. Co.*, 460 S.W.3d 597, 609 (Tex. 2015)).

103. *Id.* ("We accepted this argument[.]").

104. *Id.* ("Put simply, an insurer that commits a statutory violation that eliminates or reduces its contractual obligations cannot then avail itself of the general rule [whereby contractual liability is a prerequisite to recovery under statutory claims].").

105. *Id.* at 509.

106. *Id.* at 520.

Again, disposition under the benefits-lost rule would have been less-than-ideal, but still better than the procedural contortion that actually did follow.<sup>107</sup> *Menchaca*'s relevant facts actually coincided somewhat with the facts the court pointed out in *JAW Pointe*. According to the *Menchaca* court's own analysis, *JAW Pointe*'s plaintiffs lacked a contractual claim (even if hypothetically, as dicta) due to the insured's statutorily wrongful triggering of the policy's *ceiling*; the *Menchaca* plaintiff likewise lacked a contractual claim due to USAA's statutorily wrongful triggering of the policy's *floor*. The parallels are compelling.

Perhaps quibbling over this arguably incorrect result, at least for purposes of this article, amounts to nothing more than hair-splitting in the face of an otherwise helpful holding that added some clarity to a murky area of Texas insurance law. Indeed, one intermediate court of appeals later cited *Menchaca* and declared that, in Texas, "[t]he independent injury rule is alive and well."<sup>108</sup> But is that really the takeaway from *Menchaca*?

On the one hand, it is probably not. On its face, *Menchaca* enumerated exceptions to the rule. Clearly, the Texas Supreme Court acknowledged that statutory recovery may lie even in the absence of a contractual breach—at least in the abstract or by dusting off its own earlier dicta.

On the other hand, maybe it is. While the supreme court recognized a perhaps narrow exception to the rule, it nevertheless failed to apply it despite having decent facts to do so. For practitioners, perhaps this is the more telling aspect of *Menchaca*. An exception only exists to the extent that Texas courts are willing to apply it.

## 2. Federal Courts Grapple With New Diversity Statute Practice

As the authors' 2017 article predicted, 2018 saw the defense bar take advantage of a new Texas law that makes more lawsuits under the TIC potentially removable to federal court.<sup>109</sup> This new provision, TIC Section 542A.006, became effective in September 2017. The authors' 2017 article noted that the law "affords insurance carriers that are sued for allegedly deceptive insurance practices . . . an option to assume agents' (including adjusters) liability as their own."<sup>110</sup> Dismissing adjusters and other insurance agents from the case often creates complete diversity. This is good for defendants, of course, because federal procedure permits an early-stage dispositive motion practice that is either riskier or unavail-

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107. The *Menchaca* court ultimately deviated from the TIC and the independent injury rule and veered into the realm of appellate procedure, including fundamental error and appellate preservation. It ultimately decided to remand in favor of USAA despite USAA's failure to preserve those same grounds.

108. *Turner v. Peerless Indem. Ins. Co.*, No. 07-17-00279-CV, 2018 WL 2709489, at \*4 (Tex. App.—Amarillo June 5, 2018, no pet.).

109. Leslie Sara Hyman & Matthew J. McGown, *Consumer Protection*, 4 SMU ANN. TEX. SURV. 127, 129–30 (2018) (discussing TEX. INS. CODE ANN. § 542A.006).

110. *Id.* at 129.

able in state courts.<sup>111</sup>

Although the legislative changes appear to have been somewhat effective in creating diversity in some 2018 cases,<sup>112</sup> plaintiffs have used long-

111. Compare FED. R. CIV. P. 12(b)(6) (granting defendants a relatively consequence-free option to seek dismissal for failure to state a claim), with TEX. R. CIV. P. 91a.7 (“[T]he court must award the prevailing party on the motion all costs and reasonable and necessary attorney fees incurred with respect to the challenged cause of action in the trial court.”). Once again in 2018, research conducted for this article revealed no shortage of instances where Texas federal courts were not shy about early dismissals of consumer protection fraud lawsuits. See *Thornton v. Ditech Fin. LLC*, No. 2:18-CV-156, 2018 WL 4408979, at \*3 (S.D. Tex. Sept. 17, 2018); *Carroll v. State Farm Mut. Auto. Ins. Co.*, No. 4:18-CV-458-A, 2018 WL 4100939, at \*3 (N.D. Tex. Aug. 28, 2018) (mem. op.); *Ford v. Fitness Int’l, LLC*, No. 3:17-CV-1460-L-BT, 2018 WL 4376415, at \*5 (N.D. Tex. Aug. 15, 2018), *report and recommendation adopted*, No. 3:17-CV-1460-L, 2018 WL 4362606 (N.D. Tex. Sept. 13, 2018); *Murillo v. Allstate Vehicle*, No. 7:18-CV-208, 2018 WL 3862108, at \*3 (S.D. Tex. Aug. 13, 2018) (“For the foregoing reasons Defendant’s motion for partial dismissal for Plaintiffs’ misrepresentation claims under the TIC and the DTPA is warranted.”); *Guey Ming Yeh v. Safeco Ins. Co. of Indiana*, No. 4:18-CV-00026, 2018 WL 1858151, at \*5 (E.D. Tex. Apr. 18, 2018) (mem. op.); *Caruth v. Chubb Lloyd’s Ins. Co. of Texas*, No. 3:17-CV-2748-G, 2018 WL 1729136, at \*4–5 (N.D. Tex. Apr. 9, 2018) (mem. op.) (“But because [t]he DTPA claim is derivative of the Texas Insurance Code Claims,’ and the court has already concluded that the Caruths have not adequately pleaded a cause of action under the Texas Insurance Code, any claim against Morgan under the DTPA must fail.”); *Bradford v. Nationwide Ins. Co. of Am.*, No. 1:17-CV-1067-RP, 2018 WL 2452971, at \*2 (W.D. Tex. May 31, 2018) (granting leave to amend); *Univ. Baptist Church Fort Worth v. Lexington Ins. Co.*, No. 4:17-CV-962-A, 2018 WL 2372645, at \*5 (N.D. Tex. May 23, 2018) (mem. op.); *Dickey v. State Farm Bank, F.S.B.*, No. CV H-18-770, 2018 WL 2454159, at \*5 (S.D. Tex. May 10, 2018), *report and recommendation adopted*, No. 4:18-CV-770, 2018 WL 2441647 (S.D. Tex. May 30, 2018) (mem. op.); *Massachusetts Mut. Life Ins. Co. v. Loew*, No. A-17-CV-119-LY, 2018 WL 2085212, at \*4 (W.D. Tex. Mar. 27, 2018) (“Loew has failed to adequately plead violations of the Texas Insurance Code and TDTPA by Otis and Gomez.”), *report and recommendation adopted*, No. A-17-CV-119-LY, 2018 WL 3603101 (W.D. Tex. May 16, 2018); *Click v. State Farm Lloyds*, 1:17-CV-00108-BL, 2018 WL 1322167, at \*3 (N.D. Tex. Mar. 13, 2018) (mem. op.); *TEU Servs., Inc. v. Inventronics USA, Inc.*, No. SA-16-CV-01023-RCL, 2018 WL 3338217, at \*7–8 (W.D. Tex. Feb. 5, 2018) (mem. op.); *Univ. Baptist Church v. Lexington Ins. Co.*, No. 4:17-CV-962-A, 2018 WL 580633, at \*4 (N.D. Tex. Jan. 25, 2018) (mem. op.); *Ada Noles Props., LLC v. CitiMortgage, Inc.*, No. 3:17-CV-1241-K (BF), 2018 WL 889451, at \*2 (N.D. Tex. Jan. 8, 2018), *report and recommendation adopted*, No. 3:17-CV-1241-K, 2018 WL 837697 (N.D. Tex. Feb. 13, 2018). This is not to say that state court dispositive motion practice is unheard of under Texas Rule of Civil Procedure 91a. See, e.g., *Marshall v. Enter. Bank*, 10-16-00379-CV, 2018 WL 4224078, at \*4 (Tex. App.—Waco Sept. 5, 2018, pet. filed) (mem. op.) (“Accordingly, based on the foregoing, we cannot say that appellants were consumers within the ambit of the DTPA.”).

112. See, e.g., *Yan Qing Jiang v. Travelers Home & Marine Ins. Co.*, 1:18-CV-758-RP, 2018 WL 6201954, at \*2 (W.D. Tex. Nov. 28, 2018) (“In its response to Jiang’s motion to remand, Travelers provides written notice to Jiang that it elects to accept responsibility for her claims against Pustka. The [c]ourt must therefore dismiss all of Jiang’s claims against Pustka relating to Jiang’s insurance claim. Because all of Jiang’s claims against Pustka relate to her insurance claim, the [c]ourt must dismiss all of Jiang’s claims against Pustka with prejudice.”); *Electro Grafex, Corp. v. Acadia Ins. Co.*, No. SA-18-CA-589-XR, 2018 WL 3865416, at \*4 (W.D. Tex. Aug. 14, 2018) (“Given that any claim that [p]laintiff makes against Odermatt will be dismissed under § 542A.006(c), the [c]ourt finds that Acadia has met its burden to show that there is no reasonable basis to predict that [p]laintiff might be able to recover against [d]efendant Odermatt.”). But see *Vasquez v. State Farm Lloyds*, No. SA-17-CV-01080-DAE, 2018 WL 1899808, at \*3 (W.D. Tex. Mar. 15, 2018), *report and recommendation adopted*, No. 5:17-CV-1080-DAE, 2018 WL 1905112 (W.D. Tex. Apr. 2, 2018) (“State Farm conceded at the hearing that this amendment, which took effect the day after this lawsuit was filed, does not apply to this case. Further, that the Texas Legislature passed this amendment is evidence that it construed the pre-amendment version of the

standing diversity-defeating principles to combat the new provision, which has led to some pitched developments and even some apparent disagreement amongst Texas federal courts. The following is a chronological discussion of the case law under TIC Section 542A.006.

In *Massey*, the United States District Court for the Southern District of Texas held that removal was improper based on the traditional notion that “an action nonremovable when commenced may become removable thereafter only by the voluntary act of the plaintiff.”<sup>113</sup> The *Massey* case landed in federal court on a motion to remand exactly as one would expect under the new TIC provision. The plaintiffs’ Houston-area home sustained damage during Hurricane Harvey.<sup>114</sup> The homeowners sued Allstate in state court after the carrier denied coverage.<sup>115</sup> The homeowners also named four Texas-resident insurance adjusters, whose liability Allstate elected to assume under the new provisions of TIC Section 542A.006. The district court dismissed the individual adjusters and left only Allstate as a defending party.<sup>116</sup> Allstate removed to federal court, at which point the homeowners filed a motion to remand asserting that diversity may not ordinarily be created based on acts taken exclusively by the defendant.<sup>117</sup> As the district court explained, this so-called “voluntary-involuntary rule” provides that “an action nonremovable when commenced may become removable thereafter only by the voluntary act of the plaintiff.”<sup>118</sup> One well-known exception to the rule permits removal where a plaintiff fraudulently joined the diversity-defeating defendant.<sup>119</sup> The U.S. Court of Appeals for the Fifth Circuit added another exception in *Crockett*, where it held that removal may be proper following the state court’s dismissal of *improperly* joined (not just *fraudulently* joined) parties.<sup>120</sup>

Invoking *Crockett* and citing a purportedly analogous 2006 case from the U.S. District Court for the Southern District of Texas,<sup>121</sup> Allstate urged the trial court to essentially carve out another exception to the vol-

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Texas Insurance Code (the version that applies in this case) to permit liability to be imposed on adjusters.”).

113. *Massey v. Allstate Vehicle & Prop. Ins. Co.*, CV H-18-1144, 2018 WL 3017431, at \*2 (S.D. Tex. June 18, 2018 no pet.) (mem. op.) (Judge Gray Miller, adopting recommendation by Magistrate Judge Nancy Johnson) (quoting *Crockett v. R.J. Reynolds Tobacco Co.*, 436 F.3d 529, 532 (5th Cir. 2006); *Weems v. Louis Dreyfus Corp.*, 380 F.2d 545, 547 (5th Cir. 1967)).

114. *Id.* at \*1.

115. *Id.*

116. *Id.*

117. *Id.*

118. *Id.* at \*2 (quoting *Crockett*, 436 F.3d at 532; *Weems*, 380 F.2d at 547); see also 28 U.S.C. § 1446(b) (2011) (addressing diversity jurisdiction and removal).

119. See *Weems*, 380 F.2d at 547.

120. *Crockett*, 436 F.3d at 533 (holding that the voluntary-involuntary rule “is designed to prevent plaintiffs from blocking removal by joining nondiverse and/or in-state defendants who should not be parties. That salutary purpose is also served by recognizing an exception to the voluntary-involuntary rule where defendants are improperly, though not fraudulently, joined[.]”).

121. See *Zea v. Avis Rent a Car Sys., Inc.*, 435 F. Supp. 2d 603, 606–07 (S.D. Tex. 2006).



untary-involuntary rule applicable to defendants' acceptance of agents' liability under TIC Section 542A.006.<sup>122</sup> Allstate premised its argument on what the trial court framed as a merits-based test for application of the voluntary-involuntary rule, one where a case is nonetheless removable following dismissal so long as the dismissal was not based on the merits.<sup>123</sup> The district court rejected Allstate's argument and held that the merits-versus-non-merits distinction is irrelevant.<sup>124</sup> Instead, the *Massey* court reasoned, the Fifth Circuit has only handed down just the one exception applicable under just the one test—did “the plaintiff fraudulently or improperly joined the non-diverse defendant”?<sup>125</sup> Noting that Allstate at no pointed contended that the adjusters' joinder was proper, the *Massey* court concluded the issue by holding that “Allstate could not remove the case based on the state court's dismissal of the adjusters as that dismissal was involuntary to the Masseys.”<sup>126</sup>

The *Massey* court's reasoning and interpretation of the applicable Fifth Circuit case law were sound, so for a period afterward it seemed safe to assume that removal based on TIC Section 542A.006 was improper in the Fifth Circuit.

But then, about two months later, the United States District Court for the Western District of Texas issued its holding in *Electro Grafix*, where removal was deemed proper because a TIC Section 542A.006 election carries the removal proponent's burden to show that the plaintiff has “no reasonable basis to predict that [p]laintiff might be able to recover against [the dismissed adjuster].”<sup>127</sup> The *Electro Grafix* court noted that, upon a defendant's written notice that it has elected to accept agents' liability, the TIC gives courts no choice but to dismiss those defendants with prejudice.<sup>128</sup> Thus, reasoned Judge Xavier Rodriguez in the *Electro Grafix* decision, a removing defendant has met its burden to establish (under the improper joinder test) that “there is no reasonable basis to predict that [p]laintiff might be able to recover against” the dismissed agent.<sup>129</sup> The *Electro Grafix* court did not cite to, allude to, or otherwise address the somewhat contrary holding in *Massey*.

Then, two months after *Electro Grafix*, Allstate employed the lessons learned from the *Massey* holding and took a different and—this time—successful, new approach against remand by arguing to Judge Rodriguez of the U.S. District Court for the Western District of Texas that an agent being a named defendant is itself an improper joinder following a TIC

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122. *Massey*, 2018 WL 3017431, at \*2.

123. *Id.*

124. *Id.* at \*3.

125. *Id.*

126. *Id.*

127. *Electro Grafix, Corp. v. Acadia Ins. Co.*, No. SA-18-CA-589-XR, 2018 WL 3865416, at \*4 (W.D. Tex. Aug. 14, 2018).

128. *Id.*

129. *Id.*

Section 542A.006 election.<sup>130</sup> Unlike its concession in *Massey* that the joinder was proper,<sup>131</sup> in *Flores*, Allstate maintained from the very beginning and throughout the removal/remand proceedings that the joinder of an adjuster was improper the moment the plaintiff received Allstate's election notice.<sup>132</sup> Allstate's new approach convinced Judge Rodriguez, who relied on the *Electro Grafix* holding to reiterate that:

even when a plaintiff asserts viable claims against an insurance agent, an election of liability by the insurer for the agent's acts or omissions is sufficient to show improper joinder on the basis that there is no reasonable basis to predict that the plaintiff might be able to recover against the agent.<sup>133</sup>

Judge Rodriguez went even further and held that the thirty-day removal clock may begin to run at the time of the state court's dismissal based on TIC Section 542A.006, which the court held "is tantamount to a finding of improper joinder."<sup>134</sup>

Judge Rodriguez's holdings in *Electro Grafix* and *Flores* appear superficially reconcilable with Judge Miller's holding in *Massey*, but arguably a district split is brewing amongst Texas federal courts. Although *Massey* did not present the Southern District with an opportunity to weigh whether joinder of an agent is inherently improper upon an insurer's notice of assuming agents' liability, the tone and tenor of Judge Miller's holding reveals skepticism in the Southern District about TIC Section 542A.006's ability to circumvent the voluntary-involuntary rule. Judge Rodriguez, on the other hand, appears inclined to find diversity jurisdiction even when removal occurs under the lenient deadlines of 28 U.S.C. § 1446, which indicates that the Western District is more likely to find that it has diversity jurisdiction despite TIC Section 542A.006.

In January 2019, the United States District Court for the Eastern District of Texas, in *Stephens*, took a stance more akin to *Massey* than *Electro Grafix/Flores* and held that TIC Section 542A.006 election establishes improper joinder *only if* the insurer serves notice of its election prior to the commencement of the state court action.<sup>135</sup> The *Stephens* court concluded that "[t]he timing of an insurer's election is critical to a court's improper joinder inquiry" after a detailed analysis of the U.S. Court of Appeals for the Fifth Circuit rule mandating that courts focus on the facts and posture

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130. *Flores v. Allstate Vehicle & Prop. Ins. Co.*, No. SA-18-CV-742-XR, 2018 WL 5695553, at \*3 (W.D. Tex. Oct. 31, 2018).

131. Allstate actually had no choice in *Massey* but to concede that joinder was initially proper on the face of the pleadings because otherwise its removal would have been untimely. *Massey*, 2018 WL 3017431 at \*3-4 (noting that, although a case generally is removable within 30 days of service of the pleadings, removal is also proper within 30 days of service of an amended pleading or other paper—like a court order—if the later paper is what permits a defendant to ascertain diversity jurisdiction) (discussing 28 U.S.C. § 1446(b)(1)).

132. *Flores*, 2018 WL 5695553, at \*5.

133. *Id.*

134. *Id.*

135. *Stephens v. Safeco Ins. Co. of Ind.*, No. 4:18-CV-00595, 2019 WL 109395, at \*6 (E.D. Tex. Jan. 4, 2019) (mem. op.) (Judge Amos Mazzant).

at the time of the joinder, not the foreseeable futility of the joinder following the post-lawsuit election of liability under TIC Section 542A.006.<sup>136</sup> Specifically, the *Stephens* court rejected the defendant's emphasis on the "possibility of recovery" because it confused the odds of recovery with the propriety of the joinder itself.<sup>137</sup> The *Stephens* court generally agreed with *Massey*'s remand because the election occurred after the case commenced.<sup>138</sup> The *Stephens* court also agreed with *Electro Grafix*'s remand result because the defendant there had served its TIC election notice prior to the case's commencement.<sup>139</sup> The *Stephens* court stopped just short of outright rejecting *Flores*.<sup>140</sup>

Obviously, TIC Section 542A.006's enactment has stirred much debate and left many questions unanswered as its interplay with the voluntary-involuntary rule works its way to the Fifth Circuit. Practitioners should take heed of *Stephens*, which is the most recent holding and the latest word on the issue. *Stephens* advises that counsel should act swiftly in making their election under the new statute. While requiring pre-suit election perhaps seems a bit draconian, the *Stephens* court observed a valid point regarding the Fifth Circuit's improper-joinder rule requiring emphasis on a procedural snapshot in time rather than the wisdom of naming the party. Whether the Fifth Circuit agrees is anybody's guess, but for now, the safe play is the earliest possible assumption of agents' liability.

#### B. FEDERAL CONSUMER PROTECTION: REAL ESTATE SETTLEMENT PROCEDURES ACT

The U.S. Court of Appeals for the Fifth Circuit issued a holding in 2018 that the Real Estate Settlement Procedures Act (RESPA), a federal statutory scheme aimed at protecting consumers from predatory mortgage-collection practices, does not permit allegedly defrauded mortgagors to bring claims against the banks, as opposed to the loan servicing company, under a principal-agent theory of liability.<sup>141</sup>

The *Christiana Trust* plaintiff brought claims against the company that serviced her loan (Ocwen) through Bank of America (BOA) and also against the bank itself, alleging that BOA stood vicariously liable for the

136. *Id.* at \*5–7 (discussing, *inter alia*, *Smallwood v. Ill. Cent. R.R. Co.*, 385 F.3d 568 (5th Cir. 2004)).

137. *Id.* at \*4.

138. *Id.* at \*6.

139. *Id.* at \*7.

140. *Id.* at \*6. ("Flores' reliance on *Electro Grafix*, however, is misplaced because the diverse defendant-insurer in *Electro Grafix* made the election before the plaintiff-insured commenced action in state court. The timing of an insurer's election is critical to a court's improper joinder inquiry. That is, whether an insurer's election to accept full liability of an adjuster is tantamount to a finding of improper joinder turns on if it was made prior to or after the state court action was commenced.").

141. *Christiana Trust v. Riddle*, 911 F.3d 799, 805 (5th Cir. 2018); *see also* 12 U.S.C. §§ 2601–2617.

unlawful practices of its agent, Ocwen.<sup>142</sup> The U.S. District Judge for the Northern District of Texas dismissed the claims against BOA because (in addition to pleading deficiencies), “[b]y its plain terms, the regulation at issue here imposes duties only on servicers.”<sup>143</sup> The Fifth Circuit affirmed based on a reconciliatory reading of the Consumer Financial Protection Bureau (CFPB) rules and applicable underlying statute.<sup>144</sup> The appellate panel reasoned that Congress drafted RESPA such that its various prohibitions expressly apply only to a “servicer,” which is defined as “‘the person responsible’ for” servicing of a loan (including the person who makes or holds a loan if such person also services the loan).<sup>145</sup> The prescriptive language in RESPA provides that “a *servicer* of a federally related mortgage shall not . . . fail to comply with any other obligation found by the [CFPB].”<sup>146</sup> Noting that the CFPB mirrored congressional language in the rule—i.e., “a servicer shall”<sup>147</sup>—the *Christiana Trust* court held that “the regulation at issue here imposes duties only on servicers.”<sup>148</sup> The statute also provides that “[w]hoever fails to comply with any provision of this section shall be liable to the borrower for each such failure.”<sup>149</sup> The Fifth Circuit concluded that “because only ‘servicers’ can ‘fail to comply’ . . . only servicers can be ‘liable to the borrower’ for those failures.”<sup>150</sup> According to the Fifth Circuit, “[t]he text squarely settles the issue.”<sup>151</sup>

The Fifth Circuit noted at the outset that it appeared to be the first federal appellate court, and the first court within the Fifth Circuit, to address the vicarious-liability issue.<sup>152</sup> Most other district courts to address the issue reached the same conclusion as the Fifth Circuit.<sup>153</sup> The *Christiana Trust* panel expressly rejected the approach taken by the District Court of New Hampshire in *Rouleau*, which in 2015 held that a RESPA claim is “‘a species of tort liability’” and that therefore Congress drafted RESPA “against a legal background of ordinary tort-related vicarious liability rules.”<sup>154</sup> The Fifth Circuit explained its disagreement with *Rouleau*

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142. *Christiana Trust*, 911 F.3d at 802. Specifically, RESPA—pursuant to rulemaking by the CFPB—requires lender-side entities to provide homeowners with the various options available to prevent foreclosure. See 12 C.F.R. § 1024.41(c)(1); see also 12 U.S.C. § 2605(k)(1)(E) (conferring rulemaking authority).

143. *Christiana Trust*, 911 F.3d at 804; see also FED. R. CIV. P. 12(b)(6).

144. *Christiana Trust*, 911 F.3d at 804.

145. *Id.* (quoting 12 U.S.C. § 2605(i)(2)).

146. *Id.* (quoting 12 U.S.C. § 2605(k)(1)(E)) (emphasis and omission added by court).

147. *Id.* (quoting 12 C.F.R. § 1024.41(c)(1)).

148. *Id.* (internal citations omitted).

149. *Id.* (quoting 12 U.S.C. § 2605(f)).

150. *Id.* (quoting 12 U.S.C. §§ 2605(k)(1)(E), 2605(f)).

151. *Id.*

152. *Id.*

153. *Id.* at 805 (discussing *Hawk v. Carrington Mortg. Services, LLC*, 3:14-CV-1044, 2016 WL 4433665, at \*2 (M.D. Pa. Aug. 17, 2016) (mem. op.); *Green v. Cent. Mortg. Co.*, 148 F. Supp. 3d 852, 876–77 (N.D. Cal. 2015); *Bennett v. Nationstar Mortg., LLC*, CA 15-00165-KD-C, 2015 WL 5294321, at \*10 (S.D. Ala. Sept. 8, 2015); *McAndrew v. Deutsche Bank Nat'l Trust Co.*, 977 F. Supp. 2d 440, 445 (M.D. Pa. 2013)).

154. *Id.* (discussing *Rouleau v. US Bank, NA*, No. 14-CV-568-JL, 2015 WL 1757104, \*7 (D.N.H. Apr. 17, 2015) (mem. op.)).

as follows:

We decline to adopt *Rouleau*'s reasoning because it falls short even on its own terms. Congress did express an intent contrary to the incorporation of traditional vicarious liability rules. 12 U.S.C. § 2605(f) defines the parameters of § 2605 liability: “[w]hoever fails to comply with any provision of this section” is liable. This legislatively prescribed definition—which makes parties responsible solely for their own failures to comply—fundamentally conflicts with traditional vicariously liability, which imputes liability “based on the tortious acts of *another*.” Restatement (Third) of Torts § 13 (2000) (emphasis added). Congress could have imposed § 2605 liability on “whoever fails to comply or whoever has hired an agent who fails to comply.” It could have imposed liability on “whoever would be liable under traditional principles of tort law.” It could have said nothing at all, perhaps leaving the common law as a gap filler. It could have imposed the statutory duty to ensure compliance with the CFPB’s regulations not only on loan servicers, but also on lenders. But Congress did none of those things.<sup>155</sup>

The *Christiana Trust* panel probably reached the correct result, but it did so through somewhat anemic reasoning. While lawmakers and the CFPB arguably intended the applicable provisions to apply only to servicers (not lender banks), drafters did not write such intent into the statute/rule “plainly and unambiguously.”<sup>156</sup> The *Christiana Trust* court itself cited general notions that the drafters’ use of one word (e.g., a servicer) instead of others (e.g., a person) speaks volumes about legislative intent.<sup>157</sup> This argument both supports and cuts against the Fifth Circuit’s reasoning. If Congress intended RESPA liability to apply only to “servicer[s],” why did it neglect to draft that same language into the portion of the statute that answered the “ultimate question of [RESPA] liability”? Instead of providing that consumers have a cause of action against “servicers” (which would be consistent with the drafting of the substantive liability statutes), the statute instead provides that consumers may recover from “whoever” violates RESPA. Again, the Fifth Circuit probably reached the right decision, but its analysis on the statutory construction contains holes, and the statute, perhaps, is less “plain and unambiguous” than the Fifth Circuit suggested.

*Christiana Trust* is also problematic from a broader perspective—namely, it might have muddied the water regarding the interplay between statutory claims and common-law background principles. The notion that lawmakers’ used the term “whoever” to mean only those who actually violate the section is questionable because it suggests that common-law principles do not apply to statutory torts unless lawmakers specifically

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155. *Id.* at 805–06.

156. *But see id.* at 806.

157. *Id.* at 805 (“‘When Congress includes particular language in one section of a statute but omits it in another,’ we ‘presume[ ] that Congress intended a difference in meaning.’”) (quoting *Digital Realty Trust, Inc. v. Somers*, 138 S. Ct. 767, 777 (2018); *Loughrin v. United States*, 573 U.S. 351, 357 (2014)).

incorporate those principles.<sup>158</sup> While the Fifth Circuit correctly stated that common-law principles may be read into RESPA if Congress had said “nothing at all,” it also indicated that preservation of the common law would require affirmative statutory language.<sup>159</sup> The Fifth Circuit arguably inverted the United States Supreme Court’s standard, which instructs courts to read common law principles into a statute unless specifically instructed by Congress *not* to.<sup>160</sup> Indeed, “[t]he difference matters.”<sup>161</sup>

#### IV. CONCLUSION

Antitrust and consumer protection developments in 2018 teach us that this legal sector continues to favor defendants. In the antitrust context, only a diligent few plaintiffs survive even early-stage dismissal on the pleadings. In the consumer protection realm, courts appear as willing as ever to whittle away common-law principles traditionally available to plaintiffs.

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158. *See id.* at 806.

159. *See id.* (“Congress could have imposed § 2605 liability on ‘whoever fails to comply or whoever has hired an agent who fails to comply.’ It could have imposed liability on ‘whoever would be liable under traditional principles of tort law.’ It could have said nothing at all[.]”). There is a good argument to be made that—in light of the flawed statutory construction explained—Congress did, in fact, say “nothing at all” on the issue when it drafted RESPA.

160. *See, e.g., Meyer v. Holley*, 537 U.S. 280, 290–91 (2003) (“We believe that courts ordinarily should determine that matter in accordance with traditional principles of vicarious liability—unless, of course, Congress, better able than courts to weigh the relevant policy considerations, has instructed the courts differently.”). In addition to the Fair Housing Act discussed in *Meyer*, other statutory schemes have been construed in light of common law principles. *See United States v. Texas*, 507 U.S. 529, 534–35 (1993) (holding that debt-collection statute did not abrogate common-law availability of prejudgment interest because “[i]n order to abrogate a common-law principle, the statute must ‘speak directly’ to the question addressed by the common law”). One ready example is statutory real estate fraud, which borrows from centuries of common law. *See, e.g., TEX. BUS. & COM. CODE ANN. § 27.01(b)* (“A person who makes a false representation or false promise commits the fraud described in Subsection (a) of this section and is liable to the person defrauded for actual damages.”). *But see III Forks Real Estate, L.P. v. Cohen*, 228 S.W.3d 810, 814 (Tex. App.—Dallas 2007, no pet.) (“A principal is liable for the fraudulent acts and misrepresentations of its authorized agent, even though the principal had no knowledge of the fraud and did not consent to it, whether or not the principal derives a benefit from it.”); *Scott v. Sebree*, 986 S.W.2d 364, 368 (Tex. App.—Austin 1999, pet. denied) (“[W]e think ‘actual damages’ in the statutory-fraud context should receive the same treatment as ‘actual damages’ in the common-law fraud context.”).

161. *See Christiana Trust*, 911 F.3d at 805.

