

24th Annual Insurance Symposium: Appraisals: Protection from Contractual and Extra-Contractual Claims

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Overview

- Appraisal Process
- Effect of Appraisal on Contractual and Extra-Contractual Claims



Appraisal Principles

- Appraisal clauses uniformly included in most property insurance policies
- Used to resolve disputes regarding amount of loss for a covered claim
- Often carried out without attorneys
- More deferential review because process is fair & efficient tool



Appraisal Principles

- Usually mandatory when properly demanded
- Binding on parties when properly executed



Appraisal Principles

- Similar to arbitration because:
 - (1) binding; and
 - (2) deciding parties are impartial, independent, and free from bias
- But unlike arbitration, appraisal is
 - (1) informal; and
 - (2) limited in scope



Appraisal Principles

Scope of appraisal:

- Amount of loss only
- Causation is not generally proper issue for appraisal.
- But appraisers may have to decide which damages were caused by a specific occurrence.
- *State Farm Lloyds v. Johnson, 290 S.W.3d 886*



Typical Appraisal Clause

- If we and you disagree on the value of the property or the amount of loss, either may make written demand for an appraisal of the loss. In this event, each party will select a competent and impartial appraiser. The two appraisers will select an umpire. If they cannot agree, either may request that selection be made by a judge of a court having jurisdiction. The appraisers will state separately the value of the property and the amount of the loss. If they fail to agree, they will submit their differences to the umpire. A decision agreed by any two will be binding. Each party will:
 - (a) Pay its chosen appraiser; and
 - (b) Bear the other expenses of the appraisal and umpire equally.
- If there is an appraisal, we still retain our right to deny the claim.



Elements

- Written demand for appraisal
 - either party
 - abatement not required
- Selection of appraiser
- Appraisers select umpire, or court appoints
- Appraisers separately determine amount of loss
- Submit differences to umpire
- Decision agreed to by any 2 is binding



Waiver

- Timeliness— not usually specified in clause, but must be within “reasonable time”
- Proof of loss— acceptance or retention
- Failure to participate after invoking
- Denial of claim



Overturning Award

Three ways:

- (1) Appraisal made without authority
 - E.g., umpire signing award where appraisers did not disagree on amount; outside scope
- (2) Award was the result of fraud, accident, or mistake
 - E.g., insured lies about damage
- (3) Award not in substantial compliance with policy terms
 - E.g., lack of written demand, nonpayment of appraisers/umpire



Contractual and Extra-Contractual Claims

- Contractual– Breach of Contract
- Extra-contractual–
 - common law bad faith
 - statutory bad faith
 - prompt payment
 - Other Insurance Code violations
 - DTPA



Contractual Claims

Garcia v. State Farm Lloyds, 2016 WL 7234064 (Tex.Civ.App.—San Antonio)

FACTS:

- Insured made claim for storm damage
- State Farm investigated and determined damage did not exceed deductible (\$902 loss, \$1760 deductible)
- Insured sued for breach of contract, bad faith, prompt payment, and DTPA



(Garcia Facts cont'd)

- State Farm invoked appraisal; litigation was stayed pending appraisal
- Appraisers estimated loss at \$6k ACV and \$7k RCV
- State Farm tendered award within three business days of issuance



(Garcia Facts cont'd)

- Stay lifted, State Farm files MSJ
- Insured rejected tender and moved to set aside Award
- Trial court ruled for State Farm, insured appealed.



COURT'S ANALYSIS:

Contractual claim

- HELD: where award is **valid** and carrier timely tenders the **full** amount, breach of contract claim is **estopped**.
- Strong public policy to prevent an insured from taking advantage of the appraisal process and then suing
- Particularly where the allegedly breached contract provides for appraisal



(Garcia analysis, cont'd)

- Here, no disagreement that State Farm tendered timely and in full. Only way to beat estoppel was to overturn award.
- Remember--only three ways to overturn an award:
 - (1) Appraisal made without authority
 - (2) Mistake, fraud, accident
 - (3) Violation of policy terms



(Garcia analysis, cont'd)

Here, insured argued award was invalid because:

- (1) The award was without authority because it excluded items contained in carrier's previous estimate (in other words, that appraiser must have determined coverage as to these items);
- (2) Award was due to mistake; and
- (3) The insured rejected State Farm's tender.



(Garcia analysis, cont'd)

The court rejected each of these, holding:

1) Appraisers are not obligated to follow previous estimates. Omitting or adding line items to appraisal award does not establish that appraisers acted outside their authority absent some proof that they improperly determined liability, coverage, or causation. See *Gutierrez v. State Farm Lloyds*, 2016 WL 3387179 (S.D.Tex.) (additional line items previously denied).



(Garcia analysis, cont'd)

2) Mistake in the appraisal context means that the award **operates in a way that the appraisers did not intend**. Here, no mistake.

2) **Insured's rejection of carrier's tender does not invalidate the award.** If award is valid, and carrier tenders timely and in full, breach of contract is estopped.



Contractual Claims: Summary

- A carrier can protect its estoppel defense by ensuring that appraisal is properly invoked, carried out, and paid. Mind time requirements. Pay promptly and in full.
- Appraisal only protects carrier from breach of contract claim for underpayment/nonpayment on the disputed claim—NOT for breach of another contractual provision.



Contractual Claims: Additional Considerations

- *Gutierrez v. State Farm Lloyds*, 2016 WL 3387179 (S.D.Tex.)
- Policy included recoverable depreciation if repairs made within 180 days of date of loss.
- State Farm initially paid storm damage claim along with recoverable depreciation.



(Gutierrez cont'd)

- Insured filed suit two years later and invoked appraisal.
- State Farm promptly paid award **minus depreciation** (more than 180 days from DOL)
- Insured argued for breach of contract because after time for dispute and appraisal process had passed, it was well past the 180 day limit and would be deprived of the depreciation payment.



(Gutierrez cont'd)

- **HELD:** Withholding of depreciation in strict adherence to policy terms is **NOT** breach of contract. Claim estopped.

- *Accord Powell v. State Farm Lloyds*, 2016 WL 3654762 (S.D.Tex)

- *See also Cantu v. State Farm Lloyds*, 2016 WL 5372542 at *7 (S.D.Tex)(date of loss is date of **actual damage**, not date that carrier pays appraisal award).



Extra-Contractual Claims

If the breach of contract claim is estopped, what happens to the related extra-contractual claims?

General answer: These claims die with the underlying contractual claim.

But the *Graber* case holds that this is not the case for prompt pay penalty interest.



Prompt Pay Claims: *Graber* case

- *Graber v. State Farm Lloyds*, 2015 WL 3755030 (N.D.Tex.)

FACTS:

- Insured made hail damage claim. State Farm inspected, made an estimate, and paid the claim.
- Insured requested additional estimate. State Farm agreed and ended up finding new damage and paying again.



(Graber cont'd)

- Several months later, insured sent carrier a DTPA demand letter. State Farm did third inspection but found no additional damage.
- Insured filed suit and invoked appraisal.
- State Farm paid appraisal award in full within 4 days.
- The court found the insured's breach of contract claim was estopped, *but that the prompt payment penalty was recoverable.*



(Graber cont'd)

- The court concluded that the carrier was liable for prompt payment penalties for items *included in State Farm's initial estimate for which it admitted liability*
- This was true even though the parties had disputed the amounts recoverable for these items. The court found that the prompt payment clock starts ticking **when liability is admitted.**



So *Graber* is bad news for insurers. But the *Garcia* court had a different take:

- Remember- the breach of contract claim was estopped.
- The carrier next argued that the insured's claims for common law bad faith, DTPA and statutory bad faith, and prompt payment penalties should all die with the underlying breach of contract claim.



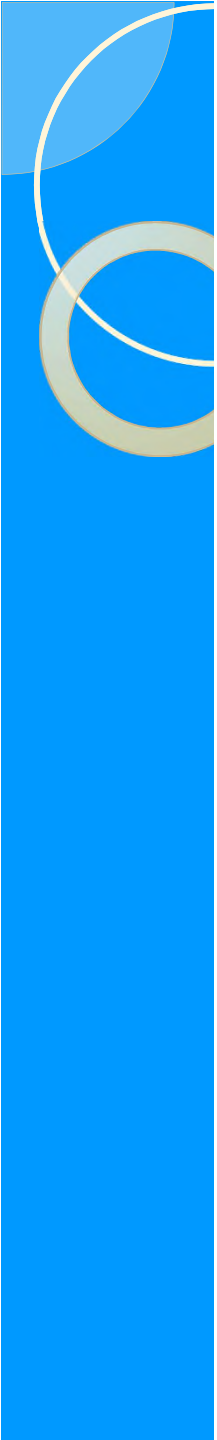
(Garcia cont'd)

Prompt Pay claim:

- The insured argued that, at best, appraisal only tolls the accrual of statutory interest damages from the date of wrongful denial to the date appraisal was invoked.

HELD: Full and timely payment of appraisal award precludes the insured from recovering prompt payment penalties as a matter of law.

The court explicitly rejected *Graber*.

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- As it turns out, *Graber* is an outlier—the weight of Texas authority is in line with the rule used in *Garcia*.
 - Two federal district courts have explicitly declined to follow *Graber*. *Mainali Corp. v. Covinton Spec. Ins. Co.*, 2017 WL 840977 (N.D.Tex); *Stewart v. Geovera Spec. Ins. Co.*, 2015 WL 12778800 (S.D.Tex.).
 - The Fifth Circuit recently adopted the *Garcia* rule. *Quibodeaux v. Nautilus Ins. Co.*, 655 Fed. Appx. 984, 988 (5th Cir. 2016).



Prompt pay claims: Summary

- The weight of caselaw is in favor of estopping prompt pay claims where a carrier tenders promptly and in full. Same advice applies to preserve this defense: mind all policy requirements, act promptly and in good faith.
- Until it is overturned outright, *Graber* is still available to be cited by insureds. But it does not have the weight of Texas legal authority behind it.



(Garcia cont'd)

Common Law Bad Faith claim:

- Under Texas law, a bad faith claim generally requires breach of contract accompanied by an independent tort.
- Therefore, a bad faith claim generally dies with the underlying breach of contract claim.
- But the Texas Supreme Court has left the door open:



(Garcia cont'd)

- Even where the insurer did not breach the contract, it might still have acted in bad faith **“if its conduct was extreme and produced damages unrelated to and independent of the policy claim.”**
- HELD: In *Garcia*, this standard was not met. It is unclear what conduct is sufficiently extreme to satisfy—but the door is open nonetheless.



(Garcia cont'd)

- Statutory bad faith and DTPA:

HELD: These claims arose from the same underlying theory as the common law bad faith claim, and therefore die along with it.

- This is the general rule.



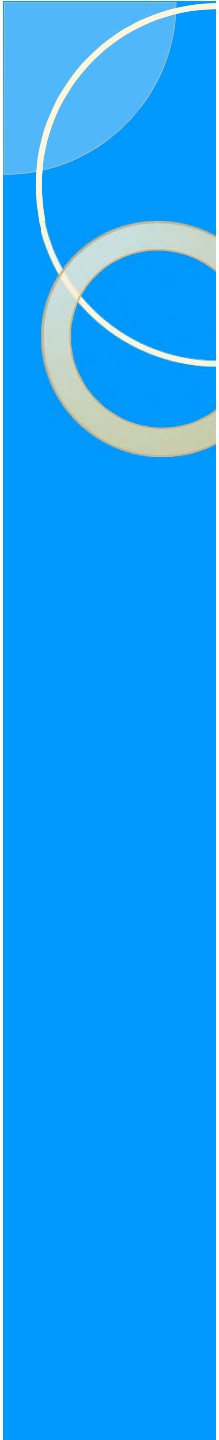
Extra-Contractual Claims: Summary

- Common law bad faith, DTPA, and statutory bad faith claims fail where the underlying breach of contract claim fails **UNLESS** the insured can show **independent injury**.
- Note: this does not protect against a claim for failure to timely investigate.
Montoya v. State Farm Lloyds, 2016 WL 7734650 (S.D.Tex.).

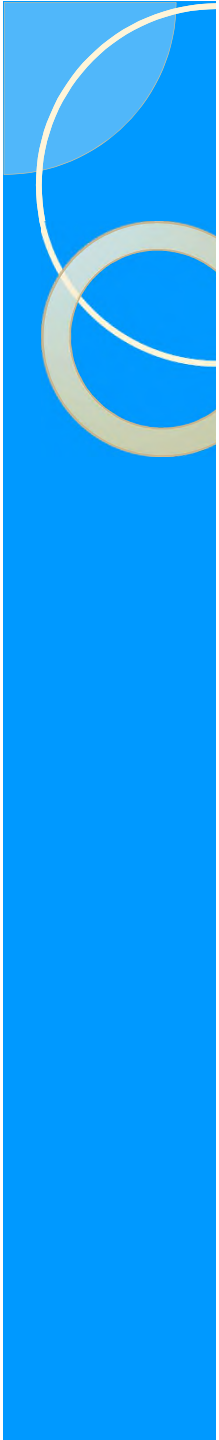


Extra-Contractual Claims: Summary (cont'd)

- A carrier is likely also protected from liability for prompt payment penalty interest.
- But until it is explicitly overturned, *Graber* is available to be cited to by insureds.



Questions?



THE END

Thank you!