

## THE APPRAISAL PROCESS

### Presented By:

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### I. Introduction – Definition of Appraisal

The information presented in this course discussing the appraisal process, will focus on the process as it is applied in Texas. The Texas Department of Insurance provides a brief overview of the appraisal process on their website, found at <http://www.tdi.texas.gov/pubs/consumer/cb025.html> .

**Disputes.** *If you disagree with the adjuster's final estimate, tell the company why. The company may have overlooked something and may make adjustments. If you still disagree, you can use the appraisal process or hire a public insurance adjuster.*

**Appraisal.** *The appraisal process is only available in disputes regarding the amount of your claim. It can't be used for settling disputes about whether the damage is covered by the policy.*

*The appraisal process begins with you and the company each hiring an appraiser. The two appraisers then choose a third appraiser as the umpire. Your appraiser and the company's appraiser make their own estimates of your loss. If they are different, the umpire makes the final decision, which is binding on both you and the company. You are responsible for the expenses of the appraiser you hire and for half of the umpire's expenses.*

At the Insurance and Risk Management Institute (IRMI) website, the following definition is found:

*“Appraisal Clause” is a property insurance provision allowing either the insurer or the insured to demand a binding appraisal of damaged property in the event of a dispute as to its value and establishing the required appraisal procedure. A few jurisdictions*

*now allow either party to reject the demand for appraisal, as evidenced in state amendatory endorsements for commercial property policies, homeowner's policies, or both. Allowing the insurer to reject an insured's demand for appraisal is disadvantageous for insureds.*

<https://www.irmi.com/online/insurance-glossary/terms/a/appraisal-clause.aspx>

Very simply put, "Appraisal" is the method that many insurance companies offer as an attempt to resolve differences between what the insurance company has proposed as the value of a loss and what the insured believes is the value of a loss. Appraisal allows a difference of opinion in the value of a loss to be decided in a manner other than mediation, arbitration, or the courts.

Examples of an appraisal clause found in the insurance policy on projects in which I am currently involved:

**A. Appraisal.** If **you** and **we** fail to agree on the actual cash value, amount of loss, or cost of repair or replacement, either can make a written demand for appraisal. Each will then select a competent, independent appraiser and notify the other of the appraiser's identity within 20 days of receipt of the written demand. The two appraisers will choose an umpire. If they cannot agree upon an umpire within 15 days, **you** or **we** may request that the choice be made by a judge of a district court of a judicial district where the loss occurred. The two appraisers will then set the amount of loss, stating separately the actual cash value and loss to each item.

If the appraisers fail to agree, they will submit their differences to the umpire. An itemized decision agreed to by any two of these three and filed with **us** will set the amount of the loss. Such award shall be binding on **you** and **us**.

Each party will pay its own appraiser and bear the other expenses of the appraisal and umpire equally.

**B. "Appraisal.** If you and we fail to agree on the amount of loss, either one can demand that the amount of the loss be set by appraisal. If either makes a written demand for appraisal, each shall select a competent, disinterested appraiser. Each shall notify the other of the appraiser's identity within 20 days of receipt of the written demand. The two appraisers shall then select a competent, impartial umpire. If the two appraisers are unable to agree upon an umpire within 15 days, you or we can ask a judge of a court of record in the state where the residence premises is located to select an umpire. The appraisers shall then set the amount of the loss. If the appraisers submit a written report of an agreement to us, the amount agreed upon

shall be the amount of the loss. If the appraisers fail to agree within a reasonable time, they shall submit their differences to the umpire. Written agreement signed by any two of these three shall set the amount of the loss. Each appraiser shall be paid by the party selecting the appraiser. Other expenses of the appraisal and the compensation of the umpire shall be paid equally by you and us."

As you can see from the above examples, the language of an appraisal clause is simple, straightforward, and most importantly, binding on the two parties.

## **II. The purpose for implementing the Appraisal Clause**

- A. To Resolve Disputes.
- B. An Alternative to Litigation.

The Appraisal Clause found in insurance policies is very clear on why it is there. If the insured and the insurer do not agree on the value of the loss, the insured may make a written demand for appraisal.

The Appraisal Clause allows for a less expensive method to resolve property disputes by allowing the disputes to be settled out of court. Litigation is often lengthy and expensive and by using the appraisal approach, disputes are typically settled reasonably quickly and costs are relatively low.

There is another distinct advantage to implementing the Appraisal Clause. With an appraisal, it is likely that experts in the field of the disputed matter are retained as appraisers for the insured and the insurance company at the outset. These experts should be knowledgeable and experienced in the disputed matter. It is hoped that with their knowledge of the matter, they will find common ground for settling the dispute.

The Texas Department of Insurance website states fairly clearly that "The appraisal process is only available in disputes regarding the amount of your claim. It can't be used for settling disputes about whether the damage is covered by the policy."

This statement still leaves a big question as to whether the appraisal process is authorized to consider "causation". In many appraisal matters one of the most important issues in the claim gets tossed to them at the outset,

- "Did this damage occur as a result of the incident?"
- Or, "What damage are we actually looking at here?"

Should it be the appraiser's duty to determine causation? Like it or not, in many cases it becomes the problem that must be decided before you begin to consider what the loss may be.

For Example: An insured files a claim for hail damage to their roof. The insurance company adjuster inspects the roof and does not find hail damage but does find minor wind damage and adjust the claim for a few hundred dollars.

Someone advises the homeowner that if they retain a public adjuster and invoke appraisal, they will likely get their roof replace. The homeowner requests appraisal, the appraisers are appointed and meet at the insured's residence to make an inspection.

Is the appraiser for the insurance company there to make a determination of hail damage to the roof? Perhaps not by the letter of the appraisal clause as now there has to be an agreement between the appraisers as to whether or not the roof actually suffered hail damage.

The appraiser is not there to inspect the quality of the shingles to make sure the correct shingles have been included in the estimate, or to check the dimensions of the roof to make sure the correct square footage has been included in the estimate, or to discuss the waste factor for the shingles or whether the roof should be classified "steep" which would incur additional cost...no, the appraiser is being asked to decide whether or not damage has actually occurred.

When selecting an appraiser, and we will discuss this in more detail later in our discussion, keep in mind that to settle the matter the appraiser may need to have expertise in several areas, not just a good background in estimating the cost of repairs.

Of course there are many legal cases involving appraisal when one of the parties is not pleased with the outcome. The purpose of this presentation, however, is not to explore the legal options of not getting what you wanted out of the appraisal. That is an entirely different presentation.

### **III. Obtaining and Examining Documents**

The old adage, “you cannot have too much information”, is especially true when approaching an appraisal. One of the basic tenets of appraisal is that all information is to be shared between the parties, and I believe this serves a twofold purpose.

- The first is that you acquire all the information on which the other appraiser bases his analysis and cost estimate,
- The second is that you make the other appraiser aware of the challenge he is facing.

Since appraisal usually occurs before the damage in question has been repaired, the appraisers will likely get to view the damage first hand. But that is not always the case. When safety concerns or mitigation of the damage requires certain work to take place on an emergency basis, there may be work already completed to repair the damage.

This is not necessarily a bad thing, as the work that has been done will have a specific cost attached to it. Whatever monies have been spent by the insured, whether already reimbursed to the insured or not, should be easily documented. The costs for the work performed to date should have receipts, cancelled checks, or documentation available. This documentation will be one of the items requested by the appraiser.

When first approaching the assignment, the appraiser should begin by requesting all of documents from his client that have been accumulated thus far in the matter. While assessing the damage and preparing a cost are the primary duties of the appraiser, some background can be very helpful in understanding the primary areas of disagreement.

For Example: The replacement of a flat roof on a single story retail establishment would appear to be a fairly straightforward project. Typically, scaffolding would not be required to access the roof as ladders and the standard roofing contractor’s equipment would be sufficient for both access and stocking of materials. A trash chute into a dumpster at the rear of the building would resolve the debris removal question and there would appear to be no additional concerns. And that was the approach when the insurance company adjuster prepared the original estimate for the repairs.

However, a significant portion of the work would occur along the front and ends of the retail building. This meant that the sidewalks would be directly below the work.

The contractor felt it would be necessary to provide scaffolding for a covered pedestrian walkway along those areas that had a potential for falling debris. And they were right.

My review of the photographs (no sight visit was required) indicated that not only would it be prudent to construct the covered pedestrian walkway, it was probably required by code or ordinance.

Therefore, my estimate for the repairs included the cost for the scaffolding and covered walkway, as did the insureds appraiser's estimate, and we negotiated the remaining minor items of disagreement.

Although my client, the insurance company, was required to increase the payment to the insured for the additional cost, there was no site visit required and the services of an umpire were not required. The appraisers reached a compromise settlement that was fair to both parties.

Each project will have its own particular set of documents that are pertinent to the matter. But generally, the following documents obtained from either the insured or the insurer will provide a good beginning point:

A. A Copy of the "Appraisal Clause" From the Insurance Policy.

This is very important as the information in the appraisal clause outlines the specific duties and time frames required in the particular policy.

B. Documentation of Expense Incurred to Date.

The cost or expense incurred to date will definitely impact the total amount paid by the insurance company to the insured. This cost should also be reviewed by the appraisers to insure that the costs were for the specified damages. A disagreement as to either the amount of the incurred cost, or the appropriateness of the work, should also be addressed by the appraisers if there is any disagreement.

C. Estimates of the Cost for Repairs Prepared by Either the Insurance Company and/or the Insured's Contractor.

This is usually the basis for the disagreement and the invoking of the appraisal clause. While it is the responsibility of the individual appraisers to prepare their own estimates and arrive at their own values, the information contained in the estimates prepared by others can provide valuable insight into the problems.

D. Photographs

It does not matter when photographs were taken, prior to the date of loss, on the date of loss, after the date of loss, or during the inspection. Photographs can often turn up unexpected information that can have a great bearing on the loss. Whatever photographs are available or are offered, the appraiser should take advantage of them by placing them in the file for review.

Other information and documentation that may be required or beneficial in determining the loss would include the following:

A. Copies and/or Review of Building Codes and/or Ordinances Affecting the Work.

Codes involving the insulation required on roofs, arc-fault breakers, fire walls, or any number of other regulations can greatly affect the cost of repairs. Some insurance policies specifically include or exclude code upgrades, while some policies have specified limits for code upgrades. The appraiser for the insurance company should request this specific information and provide it to the insured's appraiser.

B. Aerial Imagery

Aerial imagery is extremely helpful when the matter involves the roof of a residence or a building. Technology has progressed to the point that the measurements provided in the reports are very accurate and they are widely accepted in the roofing industry as a basis for quantities.

C. Weather Reports, Hail Reports, and/or Other Confirmation of Weather Events Occurring at the Date of Loss.

Your client may have obtained this information and will offer it with the documentation they originally provide. The services providing this information are also widely accepted in the industry as providing accurate documentation for weather events. While the weather event may be so obvious (tornado) that there is no question that it occurred, we confirm with third parties the date on which the weather event took place, and document that information in our report.

The documentation you obtain for a loss will be a large part of the basis for the estimate you will prepare. The documentation will often support your position and conclusions regarding what are included in the costs for repairs. Obtain as much documentation as you can, it doesn't take up much room in an electronic file.



#### **IV. Inspection**

The inspection of the property is the appraiser's opportunity to view first-hand the damage and to begin assessing the scope of work required to repair the damage. This is their chance to take their own photographs, make measurements, take samples if necessary, evaluate the quality of materials, and to begin formulating what they believe the costs may be for repairs.

Other factors that will be noted on the inspection may include:

- Access to the project;
- Proximity of power and water;
- Noise considerations or hours of work;
- Traffic considerations;
- Safety of personnel or the public.

There is no particular training for an "appraiser", as their training is typically their background and experience in the construction industry, the insurance adjusting industry, or the particular field of work for the damage being inspected.

Therefore, on a roof hail claim, an appraiser may have a background in roofing, having owned or worked for a roofing company for much of their career; they may have a background as an insurance adjuster having worked for a number of insurance or adjusting companies in their career; they may have a background in general construction having estimated and bid projects and employing roofing companies; or they may have a background as a public adjuster having represented insureds for losses of many kinds, including roofs.

Note that none of these individuals are distinguished as being knowledgeable or an expert in determining if the roof was damaged by hail. That would be "causation" and that determination should have been made prior to the inspection. For that matter, the causation and whether the resulting damage is covered under the insured's policy are areas that a determination should have been made prior to invoking the appraisal clause.

However, we play the cards we are dealt, and it helps if you are somewhat experienced in inspecting roofs for hail damage. When discussing an assignment with an insurance company adjuster, it is wise to know exactly what the disagreement involves so if you are not comfortable with that area of building or construction, you may politely decline the assignment. You will have save yourself embarrassment and the insurance company a lot of money.



## V. Preparing an estimate

Depending on your background and experience, preparing an estimate can either be the easiest part of an appraisal assignment, or the most difficult. An estimator is part CPA/bookkeeper, part research analyst, part architect/draftsman, part mechanical, electrical, structural engineer, and part clairvoyant.

I would be the first to recommend an expert in each of these fields be retained for their expertise in that particular discipline. But the reality is that in many, many instances, the appraiser is expected to pull together costs for several disciplines and prepare an estimate of what it will take to repair the damages. Obviously, there will be times when the appraiser will go to a professional, be it an architect, engineer, construction professional, subcontractor or supplier for help with certain costs. But often the appraiser will rely on his own knowledge and experience, as well as a reputable estimating program or two, and prepare an estimated cost for repairs to the best of his ability.

There are a number of estimating programs available to the general contractor and specialized programs for all of the subcontractor trades. The estimating program that has found the greatest favor among those working in the insurance industry is the Xactimate cost estimating program. We are actually fortunate that both the insurance industry and many of the contractors who regularly perform work for insurance companies have settled on one estimating program.

What I have discovered is that if a contractor inspects a loss and prepares an Xactimate estimate that is in agreement with the insurance companies scope of work for the loss, there is usually agreement on the cost.

The Rimkus “disclaimer” on each of our estimates is along the following format.

*This is a repair estimate. It is not an authorization to repair, nor is it a promise of payment of a claim or payment for work already done. This report was prepared for the exclusive use of **(Our Client Name)** and is not intended for any other purpose. Our report is based on the information available to us at this time. Should additional information become available, we reserve the right to determine the impact, if any, of the new information on our opinions and conclusions, and to revise our opinions and conclusions if necessary and warranted.*

*The totals of our estimated costs are found in the “Summary” portion of the estimate and are as follows:*

**Replacement Cost Value (RCV):** \$  
**Depreciation:** \$  
**Actual Cash Value (ACV):** \$

*This estimate was prepared using the Xactimate Version 27.5 Estimating Program. The Xactimate program is widely recognized and accepted in the insurance and construction industry for providing accurate cost estimates involving a wide variety of property damage. The Xactimate program provides pricing lists for over 470 geographical regions worldwide. The pricing data is researched and reported by Xactimate's in-house Pricing Data Services Team. The structural price list contains approximately 10,000 line items containing time-and-material data including labor costs, labor productivity rates, labor-and-burden overhead, material costs, and equipment costs. Rimkus Consulting Group utilizes the Xactimate program as the primary method of preparing estimates to repair damages to real property. Rimkus also utilizes data obtained from other estimating programs and industry sources, where applicable. The inclusions of data obtained from sources other than the Xactimate program are noted in the estimate.*

*This estimate does not restrict the contractor, or others, from using whatever means and methods are deemed necessary for the successful prosecution of the work in a safe and cost efficient manner.*

Other estimating programs are also available and often used when preparing cost estimates. We often use the RSMeans Online cost estimating program. I used the RSMeans cost books 40 years ago when estimating projects. They have been providing cost estimating guidelines since the 1940's and have proprietary programs that are used by the Corps of Engineers and other branches of the U.S. Government.

We often insert pricing from the RSMeans program into an Xactimate estimate when there is not a suitable line item available in Xactimate. In those cases we note the line items source and provide a reference number.

Pricing is also available from contacting subcontractors and suppliers to find special or unique items that need to be accounted for in the estimate. Again, when inserting these costs in an Xactimate estimate, a notation is always given for the source of the pricing.

We also include a narrative with each estimate to explain the basis of the estimate. A typical disclaimer may read similar to the following:

*This estimate is based on the field inspection performed by Mr. Michael Lamp, LEED A+P, Principal Consultant, with Rimkus Consulting Group, on May 8, 2014.*

*We have referred to Mr. Lamp's "Report of Findings", dated May 21, 2014, for information that would assist in the preparation of this estimate.*

*It is stated in the Rimkus' report that "The Jones residence was a two-story, wood-framed, residential structure, which was supported by a concrete slab-at-ground foundation system. The roof surface was covered with fiber cement shingles and the exterior claddings were brick veneer."*

*This estimate includes the combing of air conditioner fins for two (2) A/C units.*

*This estimate includes the replacement of copper valley flashing which receive cosmetic damage but was not noted as having received functional damage.*

*This estimate includes the furnishing and installing of one (1) square (100 sf) of fiber cement composite roofing shingles to allow for damaged shingles that may occur when installing the valley flashing.*

*This estimate includes the replacement of one (1) window screen which is noted to have been torn.*

*Although the exact age of the residence is not known, we have allowed depreciation based on 20 years due to the appearance and condition of the existing roof.*

## V. Analyzing Factors That Affect the Cost

It is not possible to prepare an estimate for a project until you have a scope-of-work. A scope-of-work defines the limits of the project, or the repairs, and identifies the items that are to be included or excluded from the estimate. In new construction, a scope-of-work is most often a set of plans and a book of specifications. Even with the most detailed plans and comprehensive specifications, questions still arise on construction project as to what is supposed to be included and what is an “extra”.

Is it any wonder that agreeing to a scope-of-work between the two appraisers is often the most difficult part of reaching an agreement?

For example, if a washing machine overflowed and water went over the floors in a residence, some areas of damage are obvious. If there were wood floors and the water penetrated and warped the flooring, replacement of the flooring would be included in the estimate. Inspection of the flooring would tell you if it was solid wood or pre-engineered, and if there was doubt as to the wood species, it could be sent to a laboratory for identification.

However, if the water extended into the kitchen and impacted the bottoms of the cabinets, there could be a disagreement whether the entire cabinet required replacement, or just the toe kick. Obviously replacing the toe kick would be much less expensive than the entire cabinet, but close inspection would be required to determine the extent of the damage. End panels of the cabinets may be damaged and require replacement, as well as drywall behind the cabinets if the water penetrated that far.

The original inspection by the insurance adjuster may not have included items that required destructive investigation or that only manifested after time. Therefore, an insured’s contractor who provided a higher estimate than the adjuster may have a more accurate scope-of-work.

The factors which help to define the scope of work and will therefore affect the cost, include the following:

- A. Measurements: Measuring and sketching the property are required to know the quantities of materials required. For many, if not all, roofing assignments, getting a report from a company that provides an aerial report will give you the information required for most roof claims.

- B. Materials: Examine closely the types of materials that have been damaged. Samples of some materials may be available and those can be sent to a lab which will provide information and sources for the materials.

The quality of cabinetry, crown moldings, base moldings, doors and frames, hardware, and other finishes need to be documented if possible, and an agreement between the appraisers as to the level of quality. Most estimating programs will have categories of Economy, Standard, High, Premium, or other similar descriptions for quality.

## **VI. Considerations Outside the Scope of the Work**

Even when a scope-of-work has been somewhat agreed to, the quantities of work are similar, and the unit costs are within an acceptable range, what factors often arise that seemingly have nothing to do with the repair costs and keep the appraisers from reaching agreement? Often times they are factors which have more to do with personality, pride, and/or greed than with the actual damages.

It is important for an appraiser to maintain decorum and professionalism in all dealings with the other appraiser and especially an umpire. Some appraisers will attempt to impress you with the number of years they have been in the business, how many appraisals they have done, how successful they have been, and every topic except the matter you are looking at now.

Pressure is a powerful tool, and many appraisers will attempt to use pressure to achieve their goal of agreement with their point of view. However, careful analysis, logic, and persuasive argument will hopefully have a greater effect, if not on the other appraiser, then on the umpire.

As with any inspection, you must be careful what you say and how you say it. You must discuss the matter with the other appraiser, and try to have a meeting of the minds on some issues. But remember, this is the first meeting and the first inspection. You may need to do more research and review documents before committing to any final determinations.

If there have obviously been errors in the original estimates which you can see will significantly affect the cost, acknowledge that you see some areas that will have to be addressed. Knowing what the final total will be is not possible at this point, so agreement to some figure would not be appropriate. Making a list of the items that need to be reviewed by both parties would be a reasonable approach.

Keep in mind that there are a number of factors that may affect the final outcome and some of them may not occur to you until you have fully digested all of the information.

## VII. Conclusion

The initial inspection of the property and the claimed damage is usually the first time the appraisers will meet. It will be the first opportunity that the appraisers have to really “size each other up”. They will get a chance to see what type of expert they will be working with when trying to negotiate a settlement.

It is my view that working toward a “fair” settlement for the insured is what the whole process is about. But if the attitude of your fellow appraiser is “how much can we get out of this project”, then you may have a difficult road in front of you.

Something to keep in mind, although it may not hold true in every appraisal, is what the interest the parties have in the outcome. My opinions are my own, but I do believe that what I have observed in the course of several appraisals and various other projects holds somewhat true across the board.

We are dealing with the real world here, and when an insured retains a public adjuster, who then retains an appraiser, we now have to consider that the insured must now reach a settlement with the insurance company that not only pays for the cost that will be incurred to repair the damages, but also enough extra to pay the commission for the public adjuster as well as the expense for the appraiser and umpire.

As an appraiser and an expert that has been retained by insurance companies and law firms to represent defendants, my observation is that insurance companies do not deliberately low-ball estimates for their insureds. On the contrary, my experience has been that insurance companies have been overly generous in most cases, and retain my services as a last resort, or wish to confirm cost on projects where they have little expertise.

If an insured’s claim has been denied because the insurance company’s adjuster did not observe some type of damage and therefore a loss, then the insured may take the position that “something is better than nothing”, and “something” is fairly universally what public adjusters offer the insured.

Therefore, as an appraiser retained by an insurance company I must at least be aware that there is a profit motive involved in this equation somewhere. That does not allow me to approach my duty in any manner other than to apply my experience and expertise to the matter at hand and prepare a complete and fair estimate for whatever loss I observe.



There will eventually be negotiating involved and I will need to prepare the most clear, logical and persuasive argument I am capable and present to the other appraiser, and most likely to the umpire. Hopefully, my views and opinions will be reasonable and persuasive to the other parties, and the matter will conclude to the satisfaction of everyone.