Case No. 10-0238

IN THE SUPREME COURT OF TEXAS

In re UNIVERSAL UNDERWRITERS OF TEXAS INSURANCE COMPANY,
Petitioner,

Original Proceeding from the 141st Judicial District Court
Tarrant County, Texas, Cause No. 141-237069-09

BRIEF OF AMICI CURIAE, TEXAS APARTMENT ASSOCIATION, INC., TEXAS ASSOCIATION OF SCHOOL BOARDS LEGAL ASSISTANCE FUND, AND TEXAS ORGANIZATION OF RURAL & COMMUNITY HOSPITALS

Brendan K. McBride
State Bar No. 24008900
MCBRIDE LAW FIRM
Of Counsel to GRAVELY & PEARSON, LLP
425 Soledad, Suite 600
San Antonio, Texas 78205

Marc E. Gravely
State Bar No. 00787582
Matthew R. Pearson
State Bar No. 0078817
William J. Chriss
State Bar No. 04222100
Shannon E. Loyd
State Bar No. 24045706
GRAVELY & PEARSON, LLP
425 Soledad, Suite 600
San Antonio, Texas 78205

COUNSEL FOR AMICI CURIAE, TEXAS APARTMENT ASSOCIATION, INC., TEXAS ASSOCIATION OF SCHOOL BOARDS LEGAL ASSISTANCE FUND, AND TEXAS ORGANIZATION OF RURAL & COMMUNITY HOSPITALS

IDENTITY OF AMICI CURIAE AND COUNSEL

The Amici Curiae Submitting this Brief are:

Texas Apartment Association, Inc.
Texas Association of School Boards Legal Assistance Fund
Texas Organization of Rural & Community Hospitals

The Amici Curiae Submitting this Brief are Represented by:

Brendan K. McBride
State Bar No. 24008900
MCBRIDE LAW FIRM
Of Counsel to GRAVELY & PEARSON, LLP
425 Soledad, Suite 600
San Antonio, Texas 78205
(210) 227-1200 Telephone
(210) 681-6752 Facsimile

Marc E. Gravely
State Bar No. 00787582
Matthew R. Pearson
State Bar No. 0078817
William J. Chriss
State Bar No. 04222100
Shannon E. Loyd
State Bar No. 24045706
Gravely & Pearson, LLP
425 Soledad, Suite 600
San Antonio, Texas 78205
(210) 472-1111 Telephone
(210) 472-1110 Facsimile

TABLE OF CONTENTS

Page

Identity of Amici Curiae and Counsel i

Table of Contents iii

Table of Authorities iv

Interests Of Amici Curiae 1

Issue Presented 3

Argument 4

A. If Misconstrued, Appraisal Will Negate the Duties Placed on Insurers to Promptly Investigate and Pay Covered Claims In Good Faith. 5

B. Consistent With Common Law and Statutory Policy, the Court Should Clarify When An Insurer Waives the Right to Invoke Appraisal. 15

1. Waiver by delay. 15

2. Waiver by denial. 18

Conclusion 20

Certificate of Service 23

TABLE OF AUTHORITIES

Page

CASES

Am. Fire Ins. Co. v. Stuart, 38 S.W.395 (Tex. Civ. App. 1996, no writ)........................15

Arnold v. Nat'l County Mut. Fire Ins. Co., 725 S.W.2d 165 (Tex. 1987).........................6

Boston Ins. Co. v. Kirby, 281 S.W. 275 (Tex. Civ. App. – Eastland 1926, no writ)..16, 17

Breshears v. State Farm Lloyds, 155 S.W.3d 340 (Tex. App. – Corpus Christi 2004, pet. denied)..passim

Brownlow v. United Services Auto. Assoc., No. 13-03-00758-CV, 2005 Tex. App. LEXIS 1987 (Tex. App. – Corpus Christi 2005, pet. denied) 8, 9

Gulf Ins. Co. v. Carroll, 333 S.W.2d 227 (Tex. Civ. App. – Waco 1959, no writ)..16, 17

Hartford Lloyd's Ins. Co. v. Yarbrough, No. G-05-056, 2006 U.S. Dist. LEXIS 36832 (S.D. Tex. May 24, 2006)...20

In re Acadia Ins. Co., 279 S.W.3d 777 (Tex. App. – Amarillo 2007, orig. proceeding)...19

In re Allstate County Mut. Ins. Co., 85 S.W.3d 193 (Tex. 2002).................................7, 8

In re Liberty Mut. Ins. Co., No. 14-09-00086-CV, 2009 Tex.App.LEXIS 1234 (Tex. App. – Houston [14th Dist.] 2009, orig. proceeding)................................6

In re Sec. Nat'l Ins. Co., No. 14-10-00009-CV, 2010 Tex. App. LEXIS 2911 (Tex. App. – Houston [14th Dist.] 2010, orig. proceeding)..............................19

In re Slavonic Mut. Fire Ins. Ass'n, 308 S.W.3d 556 (Tex. App. – Houston [14th Dist.] 2010, orig. proceeding)..16, 17, 18

In re State Farm Lloyds, Inc., 170 S.W.3d 629 (Tex. App. - El Paso 2005, orig. proceeding) 8

Int'l Srvc. Ins. Co. v. Brodie, 337 S.W.2d 414 (Tex. Civ. App. – Fort Worth 1960, writ ref'd n.r.e.)..16, 17

Laas v. State Farm Mut. Auto. Ins. Co., No. 14-98-00488-CV, 2000 Tex. App. LEXIS 5332 (Tex. App. – Houston [14th Dist.] 2000, pet. denied)......16, 17, 18

Northern Assur. Co. v. Samuels, 33 S.W. 239 (Tex. Civ. App. – San Antonio1895, no writ)...15

Republic Underwriters Ins. Co. v. Mex-Tex, Inc., 106 S.W.3d 174 (Tex. App. – Amarillo 2003) *rev'd* 150 S.W.3d 423 (Tex. 2004) 12

Sanchez v. Prop. & Cas., Ins. Co. of Hartford, No. H-09-1736, 2010 U.S. Dist. LEXIS 6295 (S.D. Tex. Jan. 27, 2010) 16, 17

Scottish Union & Nat'l Ins. Co. v. Clancy, 71 Tex. 5, 8 S.W. 630 (Tex. 1888) 8, 17, 19

Sec. Ins. Co. v. Kelly, 196 S.W.2d 874 (Tex. Civ. App. – Amarillo 1917, writ ref'd) 15

Springfield Fire & Marin Ins. Co. v. Cannon, 46 S.W. 375 (Tex. Civ. App. 1898, no writ) 15

State Farm Lloyds v. Johnson, 290 S.W.3d 886 (Tex. 2009) 4, 8, 20

Viles v. Sec. Nat'l Ins. Co., 788 S.W.2d 566 (Tex. 1990) 5, 6

Waterhill Cos. v. Great Am. Assur. Co., No. H-05-4080, 2006 U.S. Dist. LEXIS 15302 (S.D. Tex. Mar. 16, 2006) 8, 9

Wells v. Am. States Pref'd Ins. Co., 919 S.W.2d 679 (Tex. App. – Dallas 1996, writ denied) 20

STATUTES

TEX. CIV. PRAC. & REM. CODE §38.001, *et. seq.* 7

TEX. INS. CODE §541.060 7

TEX. INS. CODE §541.152 7

TEX. INS. CODE §542.003(b) 7

TEX. INS. CODE §542.003(b)(5) 13

TEX. INS. CODE §542.051, *et. seq.* 1, 7

TEX. INS. CODE §542.054 7

TEX. INS. CODE §542.060. 7

INTERESTS OF AMICI CURIAE

This brief is submitted jointly on behalf of three amici curiae, whose common interest is that they represent the interests of various owners of real property in Texas who pay substantial premiums for property insurance, and who depend upon clear legal duties being imposed on their insurers to promptly investigate and pay for covered losses in good faith. The purpose of this brief is to apprise the Court of some of the crucial policy and practical implications of encouraging insurers to create unnecessary delay in paying covered claims and by allowing insurers to shift the duty and cost of investigating covered losses to the insured through the appraisal process.

Because the outcome of this case substantially affects the rights of all Texas property owners to timely obtain full insurance benefits for covered losses, these amici join together in this brief urging the Court to adopt a rule that does not reward unnecessary delay in investigating and paying covered insurance claims, that does not reward underpaying or delaying payment of covered claims, and that protects the public policies embodies in the Texas Legislature's passage of Chapter 542 of the TEXAS INSURANCE CODE, including the Prompt Payment of Claims Act (TEX. INS. CODE §542.051, *et. seq.*).

Texas Apartment Association, Inc. ("TAA") is a non-profit trade association that has been serving the rental housing industry in Texas for more than 40 years. In that capacity, TAA represents an association comprised of landlords, managers and allied service representatives of the rental housing industry. TAA has 25 affiliated local chapters and more than 10,500 members. Through its members, TAA represents more

than 1.75 million residential dwelling units that provide housing for more than 4 million individuals across the State of Texas, and who pay for and depend on available property insurance benefits in the event of damage and loss to their property. TAA members hold property with a market value in excess of $150 billion and pay more than $3 billion in annual property taxes.

Texas Association of School Boards Legal Assistance Fund ("TASB LAF") has nearly 800 public school districts in Texas and advocates the positions of local school districts in litigation with potential statewide impact. The TASB LAF is governed by three organizations: TASB, the Texas Association of School Administrators ("TASA"), and the Texas Council of School Attorneys ("CSA"). TASB is a non-profit unincorporated association of public school districts in the State of Texas. Approximately 1,030 public school districts in the state, through their elected boards of trustees, are members of TASB. The members of TASB are responsible for the governance of the public schools of Texas. TASA represents the state's school superintendents and other central office administrators who are responsible for carrying out the education policies adopted by their local boards of trustees. CSA is comprised of attorneys who represent more than ninety percent of the public school districts in Texas.

Texas Organization of Rural & Community Hospitals ("TORCH") is an organization of rural and community hospitals, corporations, and interested individuals working together to address the special needs and issues of rural and community hospitals, staff, and patients they serve. The organization's mission is to be the voice and principal advocate for rural and community hospitals in Texas, and to provide leadership

in addressing the special needs and issues of these hospitals. As with other property owners, owners and operators of rural and community hospitals pay for and depend on the availability of insurance coverage in order to continue to deliver service to patients in the event of damage or loss to hospital property.

ISSUE PRESENTED

Amici Curiae, TAA, TASB LAF and TORCH, respectfully submit this brief to address the following issue:

Consistent with and in furtherance of the public and statutory policy of encouraging insurers to promptly investigate, adjust and pay covered losses in good faith, should the burden be clearly placed on the insurer to unequivocally invoke and initiate the appraisal process without any undue delay after the insurer is aware that the insured does not agree with the amount of the loss as determined during the insurer's investigation and adjusting of the claim?

ARGUMENT

In *State Farm Lloyds v. Johnson*, 290 S.W.3d 886, 887 (Tex. 2009), the Court noted that appraisals had occurred for nearly a century with little need for this Court's input. But in the last two years there has been a sudden explosion of litigation of issues surrounding insurance appraisals. The reasons for this are two-fold: (1) as detailed below, a line of cases has emerged from lower courts absolving insurers from any liability for breach of contract, attorneys' fees, bad faith or statutory penalties for violation of the Prompt Payment of Claims Act ("PPCA") if the insurer invokes the appraisal process even if the insurer loses in appraisal and it is determined that the insurer underpaid the loss; and, (2) the expansion of the scope of appraisal by this Court's opinion in *Johnson* to include some types of causation disputes has encouraged many insurers who denied all or part of a claim to invoke appraisal more frequently.

Insurers are now taking the position that they are insulated from any liability for breach of contract, delay or bad faith if they later invoke the appraisal process and promptly pay any adverse appraisal award - even if they lose the appraisal and it is determined that the insurer underpaid the covered loss when they investigated the claim. As a result, there has been a remarkable rise in litigation surrounding appraisal as insurers who ignored an obvious disagreement about the amount of the loss, or initially denied a claim, now seek to avoid liability for breaching their insuring agreements or delaying full payment by invoking appraisal only after their policyholders have had to initiate a suit to collect the full amount of benefits under their policies.

If not carefully construed and applied, the contractual appraisal process threatens to undermine the policy of placing the duty on the insurer and not the insured to investigate and pay covered losses in good faith. It will enable insurers to contractually negate the common law and statutory tools enacted to encourage insurers to satisfy these duties. As explained below, consistent with the existing common law and statutory policies that place the duty on the insurer to promptly investigate claims and pay covered losses in good faith, the Court should clarify that an insurer waives appraisal by denying coverage for the claim, and otherwise must promptly invoke the appraisal process with reasonable diligence after it is apparent that the parties disagree about the amount of loss, or else it is waived. The Court should also clarify that the payment of an appraisal award resolving a dispute over the amount of the loss does not preclude an action against the insurer for breach of contract, bad faith or for violation of the PPCA.

A. If Misconstrued, Appraisal Will Negate the Duties Placed on Insurers to Promptly Investigate and Pay Covered Claims In Good Faith.

The duty to promptly investigate and pay covered claims in good faith, both as a matter of both public policy and statute, are squarely upon the insurer – as they should be. It is long settled in Texas that because of the "special relationship between an insured and an insurer" the law imposes upon the insurer a "duty to investigate thoroughly and in good faith." *Viles v. Sec. Nat'l Ins. Co.*, 788 S.W.2d 566, 568 (Tex. 1990). Likewise, Texas law provides that an insurer has a duty to deal fairly and in good faith with its insured in processing and paying claims. *Arnold v. Nat'l County Mut. Fire Ins. Co.*, 725 S.W.2d 165, 167 (Tex. 1987).

"This duty of good faith and fair dealing arises out of the special trust relationship between the insured and the insurer." *Aranda v. Ins. Co. of N. Am.*, 748 S.W.2d 210, 212 (Tex. 1988). Because this duty arises out of a relationship recognized at common law, it gives rise to a common law action in tort that is separate and apart from any cause of action for breach of the underlying contract. *In re Liberty Mut. Ins. Co.*, No. 14-09-00086-CV, 2009 Tex.App.LEXIS 1234, *9 (Tex. App. – Houston [14th Dist.] 2009, orig. proceeding)(mem. op.)(citing *Viles*, 788 S.W.2d at 567).

These duties are not only imposed on an insurer through the common law as a matter of public policy, but are codified by the Texas Legislature. Chapters 541 and 542 of the Texas Insurance Code imposes numerous, specific duties on the insurer to promptly investigate and pay covered claims, including duties to:

- Conduct a reasonable investigation of the claim;
- Effectuate a prompt, fair and equitable settlement of a claim with respect to which the insurer's liability has become reasonably clear;
- Adopt and implement reasonable standards for the prompt investigation of claims;
- Attempt in good faith to effect a prompt, fair and equitable settlement of a claim; and,
- Abstain from compelling a policyholder to institute a suit to recover amounts due under the policy.

TEX. INS. CODE §§ 541.060 & 542.003(b). In addition, under the Prompt Payment of Claims Act ("PPCA"), the legislature has enacted clear timelines for the acknowledgment, investigation, adjusting and payment of claims, making clear its intent to place the duty upon the insurer to promptly investigate claims and pay covered losses. *See* TEX. INS. CODE §542.051, *et. seq.* Thus, an insurer's failure to meet the clear timelines for the acknowledgement, adjusting and payment of claims provides an

additional civil penalty of 18% per year on any claim for which the insurer is liable. *See* TEX. INS. CODE §542.060. The legislature has made the policy behind this statute clear, as well, indicating that it is to be "liberally construed to promote the prompt payment of insurance claims." TEX. INS. CODE §542.054.

The legislature has also made it clear that an insurer who breaches these duties is also liable for the insured's attorneys' fees to obtain its coverage benefits. These are provided for both under the insurance code (TEX. INS. CODE §541.152), and as a remedy for breach of contract (TEX. CIV. PRAC. & REM. CODE §38.001, *et. seq.*).

This Court has explained that the purpose of an appraisal is to determine whether a breach of the insuring agreement has occurred. *In re Allstate County Mut. Ins. Co.*, 85 S.W.3d 193, 196 (Tex. 2002)(noting the parties agreed the appraisal process was "the method by which to determine whether a breach has occurred.). Indeed, the Court held that to deny appraisal would be to deny Allstate the right to "defend the breach of contract claim" and that the outcome of the appraisal process goes "to the heart of the plaintiff's breach of contract claim." *Id.*

The Court reasoned that if the appraisal determined that the property's full value is what the insurance company offered, there would be no breach of contract. *Id.* It is likewise axiomatic that if the appraisal determines that the property's full value is more than what the insurance company offered, a court can, as a matter of law, determine that the insurer breached the contract by not fully investigating or paying the full amount of covered loss. The court in *In re State Farm Lloyds, Inc.*, 170 S.W.3d 629 (Tex. App. - El Paso 2005, orig. proceeding), addressing appraisal under a property policy, likewise

explained that the function of appraisal is to determine whether there was a breach of contract when the insurer adjusted the claim and offered less than the value of the insured loss. *Id.* at 632.

Thus, by its very nature, an appraisal operates as an alternative dispute resolution process for the purpose of resolving one discreet type of factual dispute – a dispute about the amount of the loss. That factual dispute is, in turn, the predicate for the insurer's obligation under the contract to pay the amount of the covered loss, as well as its statutory and common law obligations to investigate and promptly pay covered losses in good faith – all of which are to be determined by the courts and not in appraisal. *See e.g. Allstate*, 85 S.W.3d at 196; *Scottish Union & Nat'l Ins. Co. v. Clancy*, 71 Tex. 5, 8 S.W. 630, 631 (Tex. 1888); *see also Johnson*, 290 S.W.3d at 889.

Despite the obvious purpose of appraisal as noted in *Allstate*, several lower courts, and at least one federal court, have misconstrued appraisal as though it were a part of the claims investigation and adjusting process, rather than a method of resolving a dispute after the insurer has already adjusted and offered to pay the claim. *See e.g. Brownlow v. United Services Auto. Assoc.*, No. 13-03-00758-CV, 2005 Tex. App. LEXIS 1987 (Tex. App. – Corpus Christi 2005, pet. denied)(mem. op.); *Breshears v. State Farm Lloyds*, 155 S.W.3d 340, 344 (Tex. App. – Corpus Christi 2004, pet. denied); *Waterhill Cos. v. Great Am. Assur. Co.*, No. H-05-4080, 2006 U.S. Dist. LEXIS 15302 (S.D. Tex. Mar. 16, 2006)(citing *Breshears*).

In each of these cases, the appraisal process determined that the insurer had underpaid the claim. In other words, the dispute about the amount of the loss was

resolved *against the insurer* in each case. Yet each court concluded that even if the appraisal award determines that the insurer failed to fully pay the covered loss, its prompt payment of the appraisal award precluded any further claims against the insurer for breach of contract, bad faith, or violation of the PPCA. *See e.g. Waterhill*, 2006 U.S. Dist. LEXIS 15302 at *7. Indeed, despite acknowledging that the "purpose of an appraisal clause is to provide a binding, extra-judicial 'remedy for any disagreement regarding the amount of the loss,'" several courts have dismissed claims against an insurer that had undisputedly underpaid a covered loss on the theory that by promptly paying the appraisal award that resolved the dispute, the insurer never breached the contract, and cannot therefore be liable for delaying payment under the PPCA or for bad faith. *Breshears*, 155 S.W.3d at 344; *Brownlow*, 2005 Tex.App.LEXIS 1987 at *9.

The result is that insurers, with the aid of the courts, are using the appraisal process to contractually absolve themselves of their common law and statutory duties to promptly investigate and pay covered losses in good faith. The threat to these policies from the misapplication and misuse of appraisal is four-fold and provides a rather obvious explanation for why insurers have suddenly latched on to appraisal in recent years after a century of near silence on this issue.

Insurers can shift the duty and expense of investigating claims onto the insured. The first way in which appraisal is undermining these established duties is that it incentivizes the insurer to shift the duty and expense of investigating and valuing the claim onto the insured. If an insurer does not completely investigate and pay for a covered loss, it can rely on the appraisal clause to avoid any responsibility in the civil

justice system. The insured would have to perform its own investigation, at its own expense, to navigate through the appraisal process in order to get the coverage it was owed. Under the mistaken reasoning of *Breshears* and its progeny, the insurer would not pay anything more than it would have paid had it properly adjusted and agreed to pay the claim promptly.

Absent any potential liability for attorneys fees (for breach of contract), PPCA delay penalties or any potential liability for bad faith, the insurer has a direct and immediate financial incentive to shift the burden and expense to the insured to investigate its own claim by under-investigating or undervaluing the claim and resolving any ensuing disputes through appraisal only after the insured has paid experts to perform its own investigation. Importantly, by doing so, the insurer would not pay any more than it would have otherwise paid had it fully investigated and paid the claim. This is compounded if the insurer can add to the delay and expense by ignoring a clear disagreement about the amount of the loss and force the insured to retain legal counsel or file suit to resolve the dispute.

Insurers can delay payment of claims by delay in invoking the appraisal process. Misconstrued to absolve an insurer of contractual and bad faith liability, appraisal also provides an insurer an incentive to undervalue the loss. At best, an insured who has suffered a catastrophic loss and cannot afford any delay or expense in proving up its covered loss may have to accept substantially less than it is owed under its policy. At worst, the insured proves up the actual value of the loss at its own expense and the insurer simply invokes the appraisal clause and pays an appraisal award equal to what it

would have had to pay had it properly evaluated the amount of the loss in the first place. In the meantime, the insurer has been able to retain all or part of the amount owed for the covered loss until such time as the appraisal process is complete, both placing pressure on the insured to accept less than it is owed and collecting interest on policy benefits that rightfully belong to the policyholder.

Insurers can use appraisal to coerce the insured into agreeing to less than the amount owed. This problem is further compounded by allowing the insurer to ignore an existing disagreement and forcing the insured to hire counsel or initiate suit before the insurer invokes appraisal, as this Court is asked to do in this case. By doing so, the insurer can take advantage of the delay and the additional expense the insured will have to incur, in order to get the insured to agree to accept a lesser amount than it is owed. Since *Breshears* and its progeny cut off the insured's ability to be compensated for its additional expenses, attorneys' fees, delay penalties and bad faith claims when the insurer invokes appraisal, the insurer's delay in invoking appraisal places more pressure on the insured, who will have to incur substantial expenses that it cannot recover. This undermines, and indeed negates, the insurer's existing common law and statutory duties to both investigate and pay covered losses in good faith because, while the expense and risk compounds for the insured, the insurer will never owe more than it would have anyway.

This is particularly problematic because many property insurance policies include language (typically in the form of a "Texas Changes" endorsement) that specifies that the insurer has no obligation to ever pay the loss unless the insured either agrees to accept

whatever amount the insurer is offering, or the insured invokes and pays for the appraisal of its own covered loss. These endorsements are common in both residential and commercial property policies, and typically read as follows:

> We will pay for covered loss or damage within 5 business days of after:
>
> (a) We have reached agreement with you on the amount of the loss; or
>
> (b) An appraisal award has been made.

See e.g. Republic Underwriters Ins. Co. v. Mex-Tex, Inc., 106 S.W.3d 174, 177 (Tex. App. – Amarillo 2003) *rev'd* 150 S.W.3d 423 (Tex. 2004).

Despite the common law and statutory duty to promptly pay for covered losses, this provision provides an incentive to insurers to under-investigate or under-pay covered losses in order to force the insured to either waive its right to full policy benefits by agreeing to the insurer's valuation of the loss, or else invoke the appraisal clause, thereby incurring additional expenses for experts and attorneys to prove its loss. It also indefinitely extends the insurer's obligation to pay *any* policy benefits until after the appraisal is completed. In any subsequent lawsuit, the insurer need simply take the position that it did not breach the contract by failing to pay the covered loss because it had no duty to do so if the insured disagreed with the loss.

Relator in this case would have the Court further hold that the insurer can simply ignore such a disagreement and invoke it even after the insured has been forced to file suit to get the coverage benefits it is owed. Under *Breshears* and its progeny, the insurer

could then obtain a dismissal of any claims for breach of contract, bad faith or violation of the PPCA despite putting the insured through the additional delay and expense.

Insurers can force their policyholders to retain counsel or initiate suit to collect insurance benefits. One of specific statutory duties imposed on an insurer in the claims handling process is a duty not to compel the insured to initiate suit to recover amounts due under the policy. *See* TEX. INS. CODE §542.003(b)(5). The common law and Insurance Code ordinarily provide penalties for an insurer for failing to pay amounts it knows are owed – bad faith liability, liability for attorneys' fees, PPCA delay penalties, and interest. However, since the appraisal process is being treated by many courts as merely an additional part of the claims adjusting process, an insurer has a financial incentive to underpay a claim and force the insured to try to navigate through the appraisal process or initiate litigation at the insured's expense in order to get amounts owed for the covered loss.

This gives an incentive to insurers to do what occurred in this case – ignore a known disagreement over the amount of the loss and delay invoking appraisal until after its policyholder retains counsel and/or initiates suit to obtain the amounts due under the policy. Appraisal, while not as complex as litigation in the courts, is still a relatively complex and expensive alternative dispute resolution process that in many, if not most, instances will require the insured to retain counsel who understands the process, the applicable deadlines, and when and how to exercise the insured's rights. This is especially true of a catastrophic loss or a significant loss to a large commercial property, such as an apartment complex, hospital or school building.

Thus, an insurer has an incentive to provoke disputes over the amount of the loss for the specific purpose of increasing the insured's expenses to obtain its policy benefits. When the appraisal award fixes the amount of the loss, the insurer simply pays the covered loss, and then argues that it bears no responsibility for having breached the contract when it investigated and adjusted the claim and a matter of law.

In sum, as it is being construed and applied by numerous Texas courts, the appraisal process is undermining and negating critical public and statutory policies that squarely place the duty on an insurer to promptly investigate and pay covered claims in good faith, and cuts off the civil and statutory remedies for breach of those duties. This problem is substantially exacerbated if the Court further allows an insurer to invoke appraisal after a period of unexplained delay, when the insurer knows that the insured disagrees with the amount of the loss, because it provides an incentive to insurers to under-investigate and underpay claims in order to impose additional delay and expenses on its policyholders.

In order to give effect to the public policy underlying these duties, this Court should clarify that paying the appraisal award does not preclude an action against the insurer for breaching the contract, for bad faith or violation of the PPCA if the award establishes that the insurer underpaid the covered loss, and impose a clear duty on the insurer to invoke the appraisal clause reasonably promptly after learning of a disagreement about the amount of the loss in order to facilitate the prompt investigation and payment of claims.

B. Consistent With Common Law and Statutory Policy, the Court Should Clarify When An Insurer Waives the Right to Invoke Appraisal.

The two most common ways in which an insurer waives its right to resolve a dispute by appraisal are by denying the claim, or by delaying before invoking appraisal after the insurer knows the parties disagree about the amount of the loss.[1] The Court should clarify that, in the context of the insurer's special relationship to its policyholders and its clear legal duties to promptly investigate and pay covered losses in good faith, waiver should be found as a matter of law where either the insurer denies the claim – thereby making it clear that it does not intend to pay anything for the loss – or where there is an unexplained delay between the time the insurer is aware that the insured disagrees with the insurer's valuation of the loss and the time the insurer invokes appraisal.

1. Waiver by delay.

Though the results have varied as to when the parties had a disagreement, courts that have dealt with the issue of when an insurer waives its right to submit the dispute to appraisal have generally agreed that the proper rule is that the insurer should invoke

[1] Denying the claim and delay in invoking appraisal are not the *only* bases for finding waiver of appraisal, however. An insurer also waives appraisal by accepting a proof of loss. *Springfield Fire & Marin Ins. Co. v. Cannon*, 46 S.W. 375 (Tex. Civ. App. 1898, no writ); *Am. Fire Ins. Co. v. Stuart*, 38 S.W. 395 (Tex. Civ. App. 1996, no writ). Waiver can also occur where the insurer demands appraisal but refuses to participate (*Northern Assur. Co. v. Samuels*, 33 S.W. 239 (Tex. Civ. App. – San Antonio 1895, no writ)), where an invalid appraisal has already occurred (*Sec. Ins. Co. v. Kelly*, 196 S.W. 874, 878 (Tex. Civ. App. – Amarillo 1917, writ ref'd) and – just as with any right – by express waiver or facts constituting promissory or equitable estoppel.

appraisal reasonably promptly after it is aware that the insured disagrees with the amount of the loss.[2]

Thus, the Court need only affirm the rule that is already being applied by most courts that have addressed this issue. Waiver should be measured from the time that the right to invoke appraisal arose – i.e. the time at which the insured expresses its disagreement. *Sanchez*, 2010 U.S. Dist. LEXIS 6295 at *24 (phone call from insurer expressly stating disagreement with amount of loss fixed date for purposes of waiver) (*citing Laas*, 2000 Tex. App. LEXIS 5332); *see also Slavonic*, 308 S.W.3d at 562 ("the date of disagreement, or impasse, is the point of reference to determine whether a demand for an appraisal is made within a reasonable time").

This rule is consistent with and supportive of the existing duties under both the common law and the Texas Insurance Code that an insurer must reasonably promptly investigate and pay for covered losses in good faith as explained above. As a matter of public policy these duties are imposed upon the insurer based on its special relationship to the insured**.** Consistent with that policy of encouraging the prompt investigation and resolution of claims, the insure**r** should be charged with reasonable diligence in asserting appraisal.

---

[2] *See e.g. In re Slavonic Mut. Fire Ins. Ass'n*, 308 S.W.3d 556 (Tex. App. – Houston [14th Dist.] 2010, orig. proceeding); *Laas v. State Farm Mut. Auto. Ins. Co.*, No. 14-98-00488-CV, 2000 Tex. App. LEXIS 5332 (Tex. App. – Houston [14th Dist.] 2000, pet. denied); *Int'l Srvc. Ins. Co. v. Brodie*, 337 S.W.2d 414, 416 (Tex. Civ. App. – Fort Worth 1960, writ ref'd n.r.e.); *Boston Ins. Co. v. Kirby*, 281 S.W. 275, 276 (Tex. Civ. App. – Eastland 1926, no writ); *Gulf Ins. Co. v. Carroll*, 333 S.W.2d 227, 231-232 (Tex. Civ. App. – Waco 1959, no writ); *Sanchez v. Prop. & Cas., Ins. Co. of Hartford*, No. H-09-1736, 2010 U.S. Dist. LEXIS 6295 (S.D. Tex. Jan. 27, 2010).

It is also consistent with the Court's pronouncement in *Scottish Union*, that waiver should be found where the insurer's conduct would be taken by the insured as a "denial of liability, or a refusal to pay the loss." *Id.*, 71 Tex. at 10, 8 S.W. at 632. From the insured's perspective, when the insurer is aware that the insured disagrees with the insurer's valuation of the loss, but the insurer simply stops any further action to resolve or pay the claim and takes no prompt action to invoke appraisal, such is "reasonably calculated" to induce the insured to believe that the insurer does not intend to pay the claim. *See id.*

Any extended or unexplained delay should constitute waiver of the insurer's right to have the dispute resolved by appraisal as a matter of law. *Brodie*, 337 S.W.2d at 416 (39 days); *Kirby*, 281 S.W. at 276 (58 days); *Carroll*, 333 S.W.2d at 231-232 (4 months); *Sanchez*, 2010 U.S. Dist. LEXIS 6295 at *24 (10 months)**.** By contrast, short periods of time - where the delay is but a matter of a few days between the date of disagreement and invocation of appraisal – should not constitute waiver as a matter of law. *See e. g. Slavonic*, 308 S.W.3d at 563 (6 days not waiver); *Laas*, 2000 Tex. App. LEXIS 5332 at *15 (9 days not waiver).

Even a short delay in the processing and payment of a covered loss can have disastrous consequences for an insured. For example, if an apartment complex that depends on rental income to meet its operating expenses and debts were to suffer a catastrophic loss from a covered event (such as a hurricane or fire), rendering all or a substantial part of the complex uninhabitable, a delay of as little as a few weeks in paying

for the loss could result in the owner of complex becoming insolvent. It may also result in hundreds of tenants being left homeless.

Likewise, any unnecessary delay in paying a covered loss to a hospital in a rural community could not only cause tremendous financial stress for the hospital, but may very well interrupt the ability of the citizens of that community to have access to medical treatment. Similarly, a significant covered loss to a school could render the property unusable and unnecessary delay in processing and paying claims could adversely impact the school's ability to provide educational services to its students. It could also cause the school to undertake massive additional expenditures of public funds to provide alternative arrangements when a covered claim is delayed or underpaid.

In short, the prompt payment of insurance claims is of paramount importance to property owners. Any unexplained delay by an insurer should be resolved against the insurer consistent with the purpose of property insurance and public policies established both in the common law and by the Texas Legislature.

Some limited fact issues may exist. Depending on the particular facts of a claim, there could be some circumstances in which a delay of more than a few days could give rise to a fact question for a jury to resolve. However, only in the event of a short delay of a few days, as in *Slavonic* and *Laas* (6 and 9 days, respectively), should the question be resolved in the insurer's favor as a matter of law.

2. Waiver by denial.

In addition, the Court should reiterate that alternatively, an insurer waives appraisal as an alternative dispute resolution when it denies coverage and simply refuses

to pay anything for the claim. This rule has also been consistently recognized as an alternative basis for finding waiver as a matter of law. *In re Acadia Ins. Co.*, 279 S.W.3d 777, 780 (Tex. App. – Amarillo 2007, orig. proceeding) ("It is clear that denying coverage under an insurance policy does, in fact, waive the right of the insurer to request an appraisal."); *see also In re Sec. Nat'l Ins. Co.*, No. 14-10-00009-CV, 2010 Tex. App. LEXIS 2911, *16 (Tex. App. – Houston [14th Dist.] 2010, orig. proceeding) ("Denying coverage under an insurance policy waives the right of the insurer to request an appraisal.").

In *Acadia*, the insurer denied liability on the basis that the property damage predated the covered cause of loss. *Id.*, 279 S.W.3d at 778-79. When the insured sued, the insurer invoked the policy's appraisal clause. The trial court denied a motion to compel appraisal. The court denied a writ of mandamus and held that the trial court had not abused its discretion because the insurer "intentionally and unequivocally relinquished the right [to an appraisal] so that it could challenge coverage and, thus, waived that right." *Id.* at 780.

When an insurer simply denies a claim, or fails to provide the insured with any valuation of the loss, not only is there no disagreement about the "amount of the loss" (a precondition for the appraisal provision to apply in the first place), but the insurer that offers nothing for a claim or part of claim for damages is clearly signaling to the insured that resolution under the appraisal clause "is not desired, or would be of no effect if performed." *Scottish Union*, 71 Tex. at 10, 8 S.W. at 632. As the court explained in

Wells v. Am. States Pref'd Ins. Co., 919 S.W.2d 679, 685-86 (Tex. App. – Dallas 1996, writ denied):

> Hence, we must conclude that the appraisal clause at issue pertains to a dispute over the amount of money involved in the controversy. Indeed, we read the phrases "actual cash value," "amount of loss," and "cost of repair or replacement" as triggering the demand for appraisal. It cannot be doubted that these are "dollar" controversies. Thus, nowhere do we read a "causation dispute" or a "liability dispute" as the means or manner by which the demand for appraisal can be made operative.

Id., 919 S.W.2d at 685; *see also Johnson*, 290 S.W.3d at 892 ("The Dallas Court of Appeals set aside the appraisal, holding appraisers could decide the amount of damage but not what caused it. Appraisers can decide the cost of repairs in this context, but if they can also decide causation there would be no liability questions left for the courts.") (*citing Wells*)*; Hartford Lloyd's Ins. Co. v. Yarbrough*, No. G-05-056, 2006 U.S. Dist. LEXIS 36832, *9 (S.D. Tex. May 24, 2006)("Since an appraiser is not allowed to resolve disputes over causation or coverage, the appraisal was made without proper authority and is therefore, not binding.").

Thus, where only one side is proposing a cost of repairs, there is no dispute about the "amount of the loss" to be resolved in appraisal.

CONCLUSION

Amici Curiae, Texas Apartment Association, Inc., Texas Association of School Boards Legal Assistance Fund, and Texas Organization of Rural & Community Hospitals, respectfully request that in deciding this issue, the Court give careful consideration to the purposes underlying property insurance, and the importance of clearly placing the duty on the insurer to promptly investigate and pay covered claims in

good faith. The Court should resolve this issue in a manner that honors the well-established public and statutory policy of assuring that those who pay for insurance to help them in times of crisis are not denied all or part of their benefits should the law give a financial incentive to insurers to delay the investigation and payment of covered losses.

To that end, this Court should clarify that the prompt payment of an appraisal award does not absolve the insurer of potential liability for breach of contract, bad faith or for liability under the Prompt Payment of Claims Act, and that a denial of coverage or any unexplained delay by an insurer in invoking appraisal after it has reasonable notice of the insured's disagreement about the amount of the loss should constitute waiver of appraisal as a matter of law.

Respectfully submitted,

____

Brendan K. McBride
State Bar No. 24008900
MCBRIDE LAW FIRM
Of Counsel to GRAVELY & PEARSON, LLP
425 Soledad, Suite 600
San Antonio, Texas 78205
(210) 227-1200 Telephone
(210) 681-6752 Facsimile

Marc E. Gravely
State Bar No. 00787582
Matthew R. Pearson
State Bar No. 0078817
William J. Chriss
State Bar No. 04222100
Shannon E. Loyd
State Bar No. 24045706
GRAVELY & PEARSON, LLP
425 Soledad, Suite 600
San Antonio, Texas 78205
(210) 472-1111 Telephone
(210) 472-1110 Facsimile

ATTORNEYS FOR AMICI CURIAE, TEXAS APARTMENT ASSOCIATION, INC., TEXAS ASSOCIATION OF SCHOOL BOARDS LEGAL ASSISTANCE FUND, and TEXAS ORGANIZATION OF RURAL & COMMUNITY HOSPITALS

CERTIFICATE OF SERVICE

This is to certify that a true and correct copy of the above and foregoing Amici Curiae brief has been forwarded to all counsel of record via certified mail, return receipt requested, on this the 30th day of November, 2010.

George L Lankford
Rebecca Raper
Fanning Harper Martinson Brandt & Kutchin, P.C.
4849 Greenville Ave., Suite 1300
Dallas, Texas 75206
Counsel for Relator

Scott M. Keller
Law Offices of Scott M. Keller
1700 Commerce St., Ste. 1310
Dallas Texas 75201
Counsel for Real Party In Interest

Robert N. Grisham, II
Law Offices of Robert N. Grisham, II
8750 N. Central Expressway, Ste. 1010
Dallas, Texas 75231
Counsel for Real Party In Interest

Wade C. Crosnoe
Thompson, Coe, Cousins & Irons, LLP
701 Brazos Street, Suite 1500
Austin, Texas 78701
Counsel for Amici Curiae, Insurance Council of Texas and Property Casualty Insurers Association of America

____
Brendan K. McBride