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COVERAGE IN A TIME OF STORMS

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INTRODUCTION

Following storm events, disputes can arise over the cause and amount of covered loss. Most policies allow parties to invoke appraisal by an appraiser or panel to establish the value or amount of the loss. This paper addresses issues that can arise when the appraisers are seen not to meet proper criteria, or transparency is lacking.

IMPARTIALITY IN APPRAISAL: LESSONS LEARNED

I. Appraisal has changed

A. Recent case law and policy language have changed the ground rules for appraisal.

B. Where it was once considered acceptable, and, indeed, expected, for the parties to appoint appraisers to serve as their advocates in appraisal, many policies now require the parties to appoint "impartial" appraisers, using language akin to the neutrality requirement for umpires.

C. Several courts have disqualified appraisers who are not impartial, and at least one federal court has sanctioned a party and its counsel for appointing an appraiser lacking impartiality.

II. Evolution of Appraisal as an Alternate Dispute Resolution Mechanism

A. Designed to be a quick, inexpensive method to resolve differences over the amount of loss.

B. Based on contract language in the policy.

C. Courts initially treated appraisal as "akin" to arbitration, and as such interpreted appraisal in accordance with arbitration case law. *Intracoastal Ventures Corp. v. Safeco Ins. Co.*, 540 So. 2d 162, 1989 Fla. App. LEXIS 1365, 14 Fla. L. Weekly 673 (Fla. Dist. Ct. App. 4th Dist. 1989)

D. One court found the appraisal provision void for lack of mutuality of obligation because the insurer reserved the right to deny the claim.

E. The Florida Supreme Court overturned this decision, noting that appraisal was limited to "amount of loss" issues, and not coverage. *State Farm Fire & Cas. Co. v. Licea*, 685 So. 2d 1285, 1996 Fla. LEXIS 2149, 21 Fla. L. Weekly S 543 (Fla. 1996)

F. What constitutes "coverage" (and not appraisable) vs. "amount of loss issues became in itself the subject of substantial litigation.

G. The Florida Supreme Court attempted to resolve this issue by ruling that if any part of a loss was covered, then the cause of loss was an appraisable issue; and the converse was true, if no part of a claim was paid, then the matter was not appraisable. *Johnson v. Nationwide Mut. Ins. Co.*, 828 So. 2d 1021, 2002 Fla. LEXIS 1885, 27 Fla. L. Weekly S 779 (Fla. 2002).

H. This concept was watered down through various decisions and the use of line item award forms. *Kendall Lakes Townhomes Developers, Inc. v. Agric. Excess & Surplus Lines Ins. Co.*, 916 So. 2d 12, 2005 Fla. App. LEXIS 15692, 30 Fla. L. Weekly D 2349 (Fla. Dist. Ct. App. 3d Dist. 2005).

I. Procedurally, appraisal was often conducted like arbitration and challenges were subject to the Florida Arbitration Code.

J. The Florida Supreme Court rejected this notion and held that appraisal was to be conducted in an informal manner, essentially without formal rules. *Allstate Ins. Co. v. Suarez*, 833 So. 2d 762, 2002 Fla. LEXIS 2592, 27 Fla. L. Weekly S 1028 (Fla. 2002). *Citizens Prop. Ins. Corp. v. Mango Hill #6 Condo. Ass'n*, 117 So. 3d 1226, 2013 Fla. App. LEXIS 10974, 38 Fla. L. Weekly D 1507, 2013 WL 3455604 (Fla. Dist. Ct. App. 3d Dist. 2013).

III. Partiality of Appraisers and Umpires

A. Because of the courts' reliance on arbitration law as a foundation for appraisal, courts held that in appraisal it was expected that the parties' appraisers would serve as advocates for the parties. *Lee v. Marcus*, 396 So. 2d 208, 1981 Fla. App. LEXIS 18889 (Fla. Dist. Ct. App. 3d Dist. 1981).

B. Generally, the policies required appointment of "competent" and "independent" appraisers. *State Farm Fire & Casualty Co. v. Middleton*, 648 So. 2d 1200, 1995 Fla. App. LEXIS 2, 20 Fla. L. Weekly D 99 (Fla. Dist. Ct. App. 3d Dist. 1995).

C. Public adjusters with contingent fee agreements were permitted to serve as appraisers, as were independent adjusters handling claims for insurance companies. *Rios v. Tri-State Ins. Co.*, 714 So. 2d 547, 1998 Fla. App. LEXIS 7507, 23 Fla. L. Weekly D 1523 (Fla. Dist. Ct. App. 3d Dist. 1998).

D. The parties sought to appoint as appraisers those who would most effectively advocate on their behalf, rather than those who necessarily were most qualified to determine the amount of loss.

E. Relationships with umpires were deemed essential.

F. The only restrictions seemed to be appointment of the parties themselves.

G. The courts held the line on umpires—those with financial ties to the parties were not considered to be impartial or neutral. *Weinger v. State Farm Fire & Casualty*,

620 So. 2d 1298, 1993 Fla. App. LEXIS 6656, 18 Fla. L. Weekly D 1487 (Fla. Dist. Ct. App. 4th Dist. 1993).

H. But how impartial are umpires when an appraisal industry has arisen, dependent on repeat business.

I. Recent Florida statutes seek to define "impartiality" of an umpire in a contrived, restricted manner, inconsistent with the English language. Fla. Stat. § 627.70151 (2016):

- An insurer that offers residential coverage as defined in s. 627.4025, or a policyholder that uses an appraisal clause in a property insurance contract to establish a process for estimating or evaluating the amount of loss through the use of an impartial umpire, may challenge an umpire's impartiality and disqualify the proposed umpire ***only*** if:

    - (1) A familial relationship within the third degree exists between the umpire and a party or a representative of a party;

    - (2) The umpire has previously represented a party in a professional capacity in the same claim or matter involving the same property;

    - (3) The umpire has represented another person in a professional capacity on the same or a substantially related matter that includes the claim, the same property or an adjacent property, and the other person's interests are materially adverse to the interests of a party; or

    - (4) The umpire has worked as an employer or employee of a party within the preceding 5 years.

J. Eventually, a court held the party's attorney could not serve as its appraiser. *Fla. Ins. Guar. Ass'n v. Branco*, 148 So. 3d 488, 2014 Fla. App. LEXIS 14602, 39 Fla. L. Weekly D 2020 (Fla. Dist. Ct. App. 5th Dist. 2014).

K. Policy language has changed: ***it now often requires the parties to appoint "impartial" appraisers, where previously they were required to appoint "independent" or "competent" appraisers.***

L. In general, case law has not kept pace, and the use of completely neutral appraisers—i.e., those with no existing business relationship to the party—is rare.

M. There are potential perils to the above approach.

IV. Case Authority

A. *Auto-Owners Ins. Co. v. Summit Park Townhome Ass'n*, 2018 U.S. App. LEXIS 7334, 2018 WL 1440627 (10th Cir. 2018) and *Auto-Owners Ins. Co. v. Summit Park Townhome Ass'n*, 2018 U.S. App. LEXIS 7335 (10th Cir. 2018).

1. $10 million appraisal award set aside and attorneys for the insured sanctioned over $300,000 where the court found the appraiser for the insured was not impartial.

2. Policy language in Colorado required impartial appraiser.

3. Case law in Colorado required impartial appraiser.

4. Court order required full disclosure.

5. Factual and legal basis of the *Summit Park* decision.

    a. Implications of *Summit Park*

    A party cannot avoid the consequences of the acts or omissions of a freely selected agent. Sanctions were based on violation of the district court's disclosure order.

    To the extent it is based on policy language requiring the appointment of an *impartial* appraiser it can be considered persuasive.

B. *Church Mutual Insurance Company v. Coutu*, No. 17-cv-00209-RM-NYW, 2017 WL 4029589 (D. Col. Sept. 13, 2017):

A church submitted a claim for roof repair costs following a windstorm and associated hail. The insurer paid on the claim and continued adjusting activities. The church hired a public adjuster (Coutu) who convinced the church to initiate appraisal proceedings. The appraisal demand named Bensusan of Atlantis Claims as the "impartial" appraiser while the insurer named its own appraiser. The appraisers then selected Mr. Kezer as the umpire. A substantial appraisal award was thereafter entered in favor of the church. At a meeting between Bensusan, the church and Coutu to divide up the proceeds, the church learned for the first time that Bensusan's compensation was a percentage of the award. The church then filed a bad faith claim against the insurer, which counterclaimed seeking to vacate the appraisal award due, amongst other reasons, to Bensusan's undisclosed financial interest in the outcome. In addition, the insurer claimed that Bensusan and Coutu actively concealed their financial and business relationships. In unscrambling this, the court made several observations which bear on the matters at hand.

First, the court had to determine the status of Coutu and Bensusan –one a public adjuster and the other purportedly an appraiser. The court found that a public adjuster is hired by the insured in assisting with the claim and would thus be considered an agent of the insured. An appraiser, on the

other hand, is supposed to be "impartial," and thus may not be, in actuality, an agent of the insured. (This would not, however, insulate either from tort liability for their own wrongs).

Second, the court had to consider the nature and scope of any duty of disclosure as this would impact the existence of tort liability arising from any alleged failure to disclose. The court found a duty to disclose and a sufficiently-alleged breach of that duty. " Taking the (insurer's) factual contentions as true, the appointments of Messrs. Bensusan and Kezer as 'impartial' under the Policy were statements that purported to tell the whole truth but did not, thereby creating a duty to disclose the necessary information regarding (their) financial interests in the transaction to prevent these statements from being misleading." Id., *8. In part, the court's determination is buoyed by a Colorado Division of Insurance bulletin, defining impartial to mean an appraiser has no financial interest in the outcome and does not have a pecuniary interest in the amounts determined by the appraisal process.

Regarding the public adjuster, Coutu, the court similarly found a duty of disclosure, albeit for other reasons. The court found that good faith and fair dealing required the public adjuster to also make full disclosure of his financial interest in the outcome.

C. *Owner's Insurance Co. v. Dakota Station II Condominium Assoc*., No. 16CA0733, 2017 WL 3184568 (Col. Ct. App. July 27, 2017):

Wind and hail damaged the Dakota condominium and a claim was made with the insurer. The parties went to appraisal, each naming an appraiser who in turn selected an umpire. The umpire ultimately adopted four damage estimates from the insurer's appraiser (Burns) and two from Dakota's (Haber). Burns refused to sign the final award. The insurer then paid Dakota. Dakota then filed suit claiming delay in resolving the claim. During discovery, the insurer obtained information suggesting that Haber was not impartial moving to vacate the award.

The trial court ruled in favor of Dakota and the insurer appealed. The key issue on appeal is what is meant by the phrase "impartial appraiser" as used in the insurance policy. The court first observed that "the policy does not hold an appraiser as not favoring one side more than another in the sense that a judge or arbitrator….would be required to be impartial." Id. at *4. Quoting an Iowa Supreme Court case with approval, the court found that "so long as the selected appraiser acts fairly, without bias, and in good faith, he or she meets the policy requirement of an impartial appraiser." *Id*.

First, the court found entirely proper a pre-appointment meeting between Haber, the insured and the insured's public adjuster.

Second, a communication between Haber and the insured's public adjuster during the appraisal process was also found to be appropriate.

Last, the court found that a 5% cap on the appraiser's fee did not show bias, but protected the insured.

On February 20, 2018, the Colorado Supreme Court agreed to hear the insurers' appeal.

D. *North Glenn Homeowners Ass'n v. State Farm Fire and Casualty Co.*, No. 16-0912, 2017 WL 2875869 (Iowa Ct. App. July 6, 2017):

North Glenn submitted a claim for hail damage to State Farm which was paid. A second claim was then made due to a later storm, but State Farm rejected it, opining the damage was caused by the earlier storm. North Glenn requested appraisal and after certain court maneuverings, the appraisal proceeded.

A final award was rendered resulting in further court proceedings during which State Farm claimed North Glenn's appraiser was biased.

Quoting from an earlier decision, the court rejected State Farm's claim, stating "the intent of the appraisal procedure is not to provide appraisers who possess the total impartiality that is required in a court of law. The appraisers do not violate their commitment by acting as advocates for their respective selecting parties. However, appraisers should be in a position to act fairly and be free from suspicion or unknown interest." *Id*, *6.

E. *Heritage Property and Cas. Ins. Co. v. Romanach*, No. 3D16-995, 2017 WL 2960729 (Fla. 3d DCA July 12, 2017):

A water leak damaged the interior of the insureds' home and a claim was made to Heritage. A dispute arose and Heritage invoked appraisal under a clause requiring the umpire be competent and impartial. The appraisers selected Guerrero to be the umpire who issued a substantial award to the insureds, and the insurer's appraiser objected.

Heritage filed a declaratory action seeking a new appraisal, contending that the insured's appraiser and the umpire "colluded." In support, Heritage claimed it had discovery evidence that there were professional and familial relationships between the insureds' appraiser, the umpire and the owner of a water mitigation company hired by the insureds. Had these matters been disclosed, Heritage claimed its appraiser would never have agreed to the selection of Guerrero.

On motion, the trial court dismissed the case with prejudice and Heritage appealed. The appellate court reversed, finding that Heritage had stated a valid claim. Of particular interest, the court declined to opine – expressly-

on what relief Heritage might obtain; a new appraisal or a tort claim against the umpire…or perhaps something else.

F. *In re Philadelphia Indemnity Ins. Co.*, Case No. 13-17-00506 Court of Appeals, 13th District of TX:

The trial court's granting of a motion to set aside an appraisal award based upon its finding that the appraiser appoint by the insurer was not impartial was upheld as, at the time of the appraisal, he was a defendant in an unrelated lawsuit in which the insured's counsel was the Plaintiff's attorney.

G. *General Star Indem. Co. v. Spring Creek Village Apartments Phase V, Inc.*, 2004152 S.W.3d 733, 737-738 (Tex. App.—Houston [14th] 2004)

The fact that the appraiser had a financial interest (contingency fee contract) in the outcome of appraisal created a fact issue regarding whether he was impartial.

H. *Gardner v. State Farm Lloyds*, 76 S.W.3d 140 (Tex. App.—Houston [1st. Dist.] 2002)

The fact that the appraiser appointed by State Farm was an employee of Haag Engineering which had a significant business relationship with State Farm was no evidence that the appraiser was not "independent." He had no individual interest in the claim, was not an employee of State Farm and there was no evidence that State Farm exerted control over him.

I. *Holt. v. State Farm Lloyds*, 1999 WL 261923 (N.D. Texas 1999)

A fact issue existed regarding whether the State Farm appointed, Tim Marshall of Haag, was "independent" as one quarter of his income came from appraisal work for State Farm.

J. *Amtrust Ins. Co. of Kanses, Inc. v. Starship League City, L.P.*, 2013 WL 1222329 (E.D. Texas—Sherman Division, 2013)

The court denied Plaintiffs' Motion to Set Aside Appraisal Award, instead finding that a fact issue existed on whether the appraiser appointed by the insured was impartial, as he was an advocate for the insured. Prior to the appraisal he had recommended experts to the insured and gave advice to the insured on when to ask for an appraisal and how to proceed with the appraisal process.

K. *Franco v. Slavonic Mut. Fire Ins. Assn.*, 154 S.W.3d 777, 786-787 (Tex.App.—Houston [14th] 2004).

Appraiser was not found to be biased even though he previously inspected the property because his conclusions regarding the cause of the damage were his own and there was no evidence anyone exercised control over him.

L. Practical Implications & Pointers

1. How does a party choose an appraiser?

2. What kind of disclosures must be made?

3. How does a party challenge another's appraiser?

4. What is the appraiser's obligation?

5. What is the umpire's obligation?

6. What is counsel's obligation?

7. How does a State's statute figure in the analysis?