AN UPDATE ON APPRAISAL: *STATE FARM LLOYDS V. JOHNSON AND BEYOND*

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With a few exceptions and asterisks, the law on appraisal seemed relatively settled. Appraisal was viewed as an efficient method to determine amount of loss in most property policies. It could not be used in every case and when causation, coverage, and liability were at issue, its use was improper. There was no flood of appraisal cases and the clause as interpreted by the Texas courts seemed to be working fine. And then the Supreme Court of Texas decided to tinker with the appraisal clause. The result was *State Farm Lloyds v. Johnson* which seemed to do the opposite of clarifying appraisal. 290 SW3d 886 (Tex. 2009).

A. PRE JOHNSON ERA

Texas courts for over one hundred (100) years had been rather consistent in interpreting appraisal clauses, although how an appraisal was used is another story. Appraisal is to be used to provide a simple, speedy, inexpensive, and fair method of determining the amount of loss only. *Fire Ass'n v. Ballard*, 112 S.W.2d 532, 534 (Tex. Civ. App. – Waco 1938, no writ). Appraisal is *not* arbitration. *In Re Allstate Ins. Co.*, 85 S.W.3d 193, 195 (Tex. 2002). If appraisal is properly invoked, carried out, and awarded, the *amount of loss* is binding on the insurer and insured. *Scottish Union National Ins. Co. v. Clancy*, 71 Tex. 5, 8 S.W. 630, 631 (1888). Appraisal may be waived. *Ins. Service Co. v. Brodie*, 337 S.W.2d 414, 415 (Tex. Civ. App. – Fort Worth 1960, writ ref'd n.r.e.). Appraisers and umpires are without authority or power in an appraisal to determine "questions of causation, coverage, or liability ... ." *Wells v. American States Preferred Ins. Co.*, 919 S.W.2d 679, 684 (Tex. App. – Dallas 1996, writ denied).

The parties to appraisal are required to choose competent and disinterested

appraisers. *General Star Indem. Co. v. Spring Creek Village Apt. Phase V, Inc.*, 152 S.W.3d 733, 737 (Tex. App. – Houston [14th Dist.] 2004, no pet.). An appraiser who has a financial interest in an appraisal award is not impartial. *Id.* An appraiser or umpire does not represent any party's interests or views and is to act in a quasi judicial capacity. *Pennsylvania Fire Ins. Co. v. W.T. Waggoner Estate*, 39 S.W.2d 593, 594-595 (Tex. Comm'n App. 1931, no writ). The use of an umpire and/or his signing of an award is unnecessary absent an actual disagreement about the amount of loss between the appraisers. *Fisch v. Transcontinental Ins. Co.*, 356 S.W.2d 186, 189-190 (Tex Civ.App. – Houston 1962, writ ref'd n.r.e.).

Every reasonable presumption will be indulged in favor of an appraisal award. *Hennessey v. Vanguard Ins. Co.*, 895 S.W.2d 794, 798 (Tex. App. – Amarillo 1995, writ denied). Nevertheless, an appraisal award may be disregarded in three (3) instances: 1) when the award was made without authority; 2) when the award was the result of fraud, accident or mistake; and 3) when the award was not made in substantial compliance with the terms of the contract. *Providence Lloyds v. Crystal City Indep. School Dist.*, 877 S.W.2d 872, 875 (Tex. App. – San Antonio 1994, no writ); *Hennessey*, 895 S.W.2d at 798.

The status of appraisal law appeared predictable and settled until the Texas Supreme Court's decision in *Johnson*.

B. THE HISTORY OF JOHNSON PRIOR TO THE TEXAS SUPREME COURT

In April 2003, Becky Ann Johnson's ("Johnson") house was damaged by hail. *Johnson v. State Farm Lloyds*, 204 S.W.3d 897, 898 (Tex. App. – Dallas 2006, pet. granted). State Farm Lloyds ("State Farm") inspected Johnson's property, specifically the roof, and concluded only the ridgeline of

Johnson's roof was damaged by hail, estimating the loss at $499.50 which was less than Johnson's deductible. *Id.*

Johnson requested a second inspection, but State Farm's conclusion remained the same. *Id.* Johnson did not accept State Farm's determination and contended the entire roof needed to be replaced, submitting an estimate for $6,400. *Id.* Johnson hired a lawyer who demanded appraisal. *Id.*

The appraisal clause in Johnson's policy provides:

> **SECTION I-CONDITIONS**
> ***
> **4. 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 that appraiser. Other expenses of the appraisal and the compensation of the umpire shall be paid equally by you and us.

Id. at 900.

State Farm responded that the dispute was about coverage; therefore, appraisal was not proper or appropriate. *Id.* Johnson filed a declaratory judgment to compel appraisal. *Id.* at 898-899. Both parties moved for summary judgment. *Id.* The trial court granted State Farm's summary judgment motion and Johnson appealed. *Id.* at 899.

The Dallas Court of Appeals reversed, finding Johnson was entitled to appraisal. *Id.* at 899. The Dallas Court of Appeals framed the issue this way:

> This case involves the determination of whether the meaning of the term "amount of loss" in an appraisal clause of a homeowner's insurance policy includes the *extent* of loss and whether the insured can compel the insurer to appraisal when there is a dispute about the extent of loss.

Id. at 898. Emphasis added.

Johnson argued that the amount of loss includes a dispute over the extent of the damage. *Id.* at 900. In contrast, State Farm argued that no appraisal can be compelled unless the parties agree on causation, coverage, and liability. *Id.* In particular, State Farm took the position that because it only acknowledged coverage on the ridgeline and the remainder of the roof was damaged by an excluded cause – wear and tear - the issue was coverage, not the amount of loss. *Id.* at 901. Therefore, State Farm argued the amount of loss does not include the *extent of loss*, because it would necessarily include determining coverage, causation, and/or liability.

In evaluating both parties arguments, the Dallas Court of Appeals cited *Wells*, which it had decided ten (10) years earlier, and wrote that it stood for the proposition that appraisers and umpires do not determine coverage. *Id.* at 902. Instead, the Court of Appeals wrote that under *Wells*, appraisers are to determine the "amount of damage" resulting to the property submitted for their consideration. *Id.* citing *Wells*, 919 S.W.2d at 685.

According to the Dallas Court, the parties in *Wells* agreed "on the extent of the loss and cost of repairs, but disagreed on whether there was a covered loss at all." *Johnson*, 204 S.W.2d at 902. And the appraisers in *Wells*, according to the *Johnson* Court, used appraisal to determine if the loss was caused by a covered peril. *Id.* The Court distinguished *Wells* from *Johnson* by asserting that the parties in *Johnson* agreed there was a covered loss, but

disagreed on the extent of the loss and cost of repairs. *Id.*

The Dallas Court of Appeals also cited *Lundstrom v. United Services Automobile Ass'n*, 192 S.W.3d 78 (Tex. App. – Houston [14th Dist.] 2006, pet. denied) as being similar to the issues in *Johnson* by noting the appraisers in *Lundstrom* had to determine which damages were caused by one water leak, which was covered by the policy, versus damages occurring at another time, which were not covered. *Johnson*, 204 S.W.2d at 920. Based on the Dallas Court of Appeals reading of *Lundstrom*, both cases stood for the "narrow proposition that appraisers exceed their authority when they make legal determinations of what is or is not a covered loss based on their determination of what caused the loss or some portion of it." *Id.* at 902-903. Thus, appraisers "making decisions about the extent of damage" is not precluded by *Wells* or *Lundstrom*. *Id.* The rule then is 'if the parties agree there is coverage, but disagree on the extent of damage, the dispute concerns the 'amount of loss' and that issue can be determined in accordance with the appraisal clause." *Id.* at 903.

In very simple terms *Johnson* holds that the amount of loss *includes* the extent of loss. Therefore, applying the rationale of *Johnson*, if there is damage to an automobile caused by hail on a very small part of the car and other parts are allegedly suffering from rust, a noncovered peril, appraisal would be appropriate to decide the extent of the covered loss. Sound confusing? It is.

A review of the standard appraisal clause substantiates that the term *extent of loss* is not found. Reading this term into appraisal clause only confuses the appraiser's task and obligations and makes it unclear for the insurer and insured to decide when appraisal is proper. Including extent into appraisal translates into how much is

damaged and *what caused it*, rather than how much does it cost to repair or replace.

Under the Dallas Court of Appeals' *Johnson* opinion, once the parties agree there is some coverage for a loss, but disagree how much of the loss is actually covered, the extent of loss can be decided by appraisers. Nevertheless, it would appear obvious that the task of the appraisers in such a situation is to decide *how much of a covered loss exists*; logically, this task would entail an appraiser making a decision on causation – whether the damage was caused by hail as opposed to rust – wear and tear – or both hail and rust – concurrent causation. Hence, the actual effect is appraisers in such cases would be permitted to make causation determinations leading to coverage and liability which is contrary to *Wells*.

The consequences of Dallas Court of Appeals' opinion in *Johnson* would be an appraisal award where the extent of damage was decided would be binding on the parties even where the causation (covered vs. noncovered) was also at issue. Logically then, decisions regarding causation, and ultimately coverage, could be decided by appraisal – trial by appraisal through the use of appraisers.

It would seem insurers would be in the best position to take advantage of *Johnson*, yet it was State Farm who sought review in the Texas Supreme Court contending where issues of causation, and ultimately coverage and liability, are being decided, then appraisal is not appropriate. Overall, State Farm contended in this situation that appraisal had no value as an efficient and inexpensive method to determine the amount of loss because it could not be binding. *State Farm Lloyds v. Johnson*, 290 S.W.3d at 887-888.

***STATE FARM LLOYDS V. JOHNSON* IN THE SUPREME COURT OF TEXAS**

The Texas Supreme Court accepted State Farm Lloyds' petition for review to decide whether the dispute presented fell within the scope of the appraisal clause. *Id.* at 888. Against most appellate odds (considering that acceptance of review usually translates into reversal), the Court affirmed the Dallas Court of Appeals. *Id.* at 887. Hinting that its affirmance was a pro-consumer decision, the Court wrote: "... we affirm the court of appeals' judgment *in favor of the insured*." *Id.* Emphasis added. There were no dissents. This decision, though, can hardly be termed a pro policyholder decision.

The Court at the outset noted it had infrequently written about appraisal. *Id.* at 888. From that logic, the Court then concluded appraisal must be working well, so why limit it. *Id.* at 888-889.

The Court framed the issue before it as follows: "whether the dispute ... fell within the scope of the appraisal clause." *Id.* at 888. In beginning its opinion, the Court held that trial courts have no discretion to ignore a valid appraisal provision *entirely*. *Id.*

The Court began its opinion by attempting to trace the history of appraisal clauses. *Id.* The Court concluded appraisal clauses are enforceable and used to determine *the amount of loss for a covered claim*, *Id.* But the Court pointed out it had not resolved a dispute about the scope of appraisal, more particularly the meaning of "amount of loss." *Id.* at 888-889. The Court did note an appraisal clause instructs the appraisers to decide the "amount of loss," but not decide policy construction or whether the claim should be paid. *Id.* at 889-890. Again reasoning that because of the "scarcity of suits" on appraisal, the focus is on damages as opposed to liability and

suggested appraisal provisions were working. *Id.* at 890. Despite these statements, the Court embarked on inconsistent reasoning which results in appraisal being used to decide at least implicitly coverage, causation and/or liability.

In evaluating State Farm's appeal, this state's highest civil court wrote that the Texas courts *have split on the question of whether appraisers can decide causation.* *Id.* at 890-891. In making this statement, the Court in a footnote cited one case allegedly supporting appraisers determining causation and four (4) cases that prohibit it. *Id.* at 890-891, n. 24. In making this conclusion, the Court did not discuss its implicit approval of *Wells* by denying review of the Dallas Court of Appeals' decision almost fourteen (14) years ago. *Wells* explicitly prohibited appraisers deciding causation. *Wells*, 919 S.W.2d at 684.

But the Court did decide that the facts in *Johnson on the record presented to it* did not prove the dispute was about causation. *Id.* at 891. The Court reasoned: because State Farm acknowledged some shingles were damaged by hail, a covered peril, the dispute surrounded how many shingles were damaged; "A dispute about how many shingles were damaged and needed replacing is surely a question for the appraisers." *Id.*

To support this conclusion, the Court asserted that the cost of replacing shingles "is a function of both *price* and *number* ... " *Id.* (emphasis in the original). Which shingles need replacing is a dispute for appraisal. *Id.* To the extent the parties disagree which shingles need replacing, that dispute would fall within the scope of appraisal. *Id.* See a problem?

According to the Court, nothing in the summary judgment record revealed that the shingles were damaged by anything but

hail. *Id.* Because there was no contrary evidence in the record about covered versus noncovered causes (according to the Court), the trial court could not deny appraisal as a matter of law simply because State Farm contended the dispute was about causation. *Id.* Additionally, the summary judgment record did not show the dispute was *solely* about how much of Johnson's roof was damaged. *Id.* Thus, because this was a summary judgment proceeding, the trial court erred when it decided the dispute was about causation. *Id.*

Nevertheless, Justice Brister wrote "Even if the parties' dispute involves causation, that does did not prove whether it is a question of liability or damages". *Id.* at 891. Reasoning further the Court determined that causation relates to both liability and damages because it is the connection between them." *Id.* at 891-892. To justify this contention, the Court referred to the *Texas Pattern Jury Charges* which placed causation in both liability and damage categories. *Id.* at 892. Abstractively, the Court wrote that causation could fall equally into both categories – liability and damages. *Id.*

To arrive at this conclusion, the Court cited *Wells* and *Lundstrom*. *Wells* where the appraisers determined damages based on two causes, one covered peril versus another noncovered peril, and *Lundstrom* where appraisers allegedly did the same thing. *Id.* at 892. The Court held that both decisions were correct because courts determine coverage and appraisers decide the amount of damage caused by each peril. *Id.* This principle also is applicable in evaluating a loss due to a covered event versus a preexisting condition. *Id.* According to the Court, to hold otherwise would mean that appraisers could never evaluate hail damage unless the roof was brand new, making an appraisal clause invalid, a construction which the Court must avoid. *Id.* at 892-893.

The Court further stated that appraisers "must always consider causation, at least as an initial matter. An appraisal is for damages caused by a specific occurrence, not every repair a home might need." *Id.* at 893. Therefore, appraisal necessarily must include some causation because the appraisers have to decide damages where coverage is claimed versus damages to other property caused by something else. *Id.*

Attempting to provide some comfort, the Court held that State Farm does not have to pay for wear and tear or other excluded perils. *Id.* If the appraisers go beyond damage questions, then the award may be avoided, but the mere existence of a causation question is not enough. *Id.*

The Court further opined that even if appraisal does involve liability questions, it should not be prohibited initially. *Id.* at 894. In making this statement, the Court provided four (4) reasons. *Id.* First, appraisals that have yet to occur involve conditions precedent and allowing litigation preappraisal would encourage more litigation, thereby defeating the purpose of appraisal. *Id.* Second, appraisals that have yet to occur can be structured to avoid liability questions; even if the insurer denies coverage, there is no harm in an appraiser setting the amount of loss. *Id.* Third, the lack of precedent on scope of appraisal suggests that appraisal generally resolves such disputes. *Id.* at 894-895. Fourth, a flawed appraisal can be disregarded. *Id.* at 895. Based on this reasoning, the Court held that appraisal should occur prelitigation and not involve the legal process, such as lawyers, judges, discovery, motions, and hearings. *Id.* at 894-895. Appraisals should proceed without "preemptive intervention by the Courts." *Id.* at 895.

Yet, *Johnson* does a disservice to insurers and insureds. Instead of limiting the reasoning in *Johnson* to the facts in the

summary judgment record, the Texas Supreme Court went far beyond the facts to permit futile exercises which needlessly complicate and increase the cost of a claim and ultimately litigation.

State Farm petitioned for rehearing which was denied. In its *Motion for Rehearing*, State Farm tried to draw the Court's attention that its decision confused more than helped, created needless and wasted efforts, increased the costs to all parties to an appraisal, complicated litigation about a claim, pointed out that an appraisable issue plus an unappraisable issue does not equal an appraisable issue, and the Court's reasoning was rewriting the policy. *See Petitioner's Motion for Rehearing.* Based on prior decisions and practical application, State Farm's arguments are persuasive and have a great deal of merit.

C. THE CONFUSING AFTERMATH

Johnson left open a few circumstances where appraisal may be defeated preappraisal – that is permitting court intervention preappraisal.

One issue is waiver of the clause. This may take two forms. The first is by waiver by denying the claim. *In re Acadia Ins. Co.*, the insured suffered hail damage to its roofs. 279 SW3d 377, 778-779 (Tex. App. – Amarillo 2007, orig. proceeding). Acadia denied the claim seven (7) months after the loss. *Id.* The insured filed suit nine (9) months after the denial. *Id* at 779. Nearly two (2) years after the loss and eight months after the insured filed suit, Acadia demanded appraisal. *Id.* The trial court denied the insurer's request and Acadia sought mandamus relief. *Id.* The Court of Appeals denied Acadia's request for relief finding waiver due to denial of the claim. *Id.* at 778-781. *But see In re State Farm Lloyds, Inc.*, 170 S.W.3d 629 (Tex. App – El Paso 2005, orig. proceeding) (holding that an insurer's breach of other policy

conditions does not waive its rights to appraisal).

A second area of waiver may be the timelines in seeking appraisal. *In Sanchez v. Property and Casualty Ins. Co.*, Judge Altas from the Southern District of Texas was confronted with a request for appraisal that occurred nearly eleven (11) months after the insurer was aware that a dispute existed over the amount of damages. 2010 WL 413687 *1-2 (S.D. Tex 2010). This delay, according Judge Atlas, constituted waiver of the appraisal clause – "Hartford waived an appraisal by failing to invoke the right for almost an entire year . . ." *Id.* at *8.

Following *Sanchez* is a wave of *Hurricane Ike* litigation in South Texas, particularly in Houston, now culminating in yet another soon to be appraisal decision rendered by the Texas Supreme Court.

First came *In re Slavonic Mutual Fire Ins. Assoc.*, 308 S.W.3d 556 (Tex App. – Houston [14th Dist.] 2010, orig. proceeding) involving hurricane damage to a residential home. *Id.* at 558. The Requences were insured with Slavonic Mutual Fire Insurance Association ("Slavonic") under a homeowners' policy. *Id.* Following Hurricane Ike, the Requenas reported a loss on September 14, 2008 and the loss was assigned to an outside adjuster who inspected the loss on September 23, 2008. *Id.* at 560. The insureds were sent a check for their loss which included $1,530.70 for roof repairs. *Id.*

On October 17, 2008, the Requenas notified Slavonic that the entire roof needed repair, as the homeowners' association would not permit a partial repair. *Id.* Slavonic agreed to a reinspection and on December 17, 2008, sixty (60) days later, sent out another adjuster. *Id.* However, the roof had already been replaced with the insureds supplying the new adjuster with a contract for the new roof totaling $7,560.00 plus $550.00 for air conditioning duct work

not previously included. *Id.* Following the receipt of the adjuster's report on January 14, 2009, Slavonic sent the Requenas a check for $350.00 on January 16, 2009. *Id.*

On April, 2009, The Requenas filed suit and included a notice letter. *Id.* On May 14, 2009, Slavonic demanded appraisal. *Id.* After receiving no response from the insureds, Slavonic filed a plea in abatement and motion to compel appraisal. *Id.* Following a hearing and briefing, the trial court denied Slavonic's Motion on November 12, 2009, finding waiver. *Id.* at 561.

The policy at issue included an "anti-waiver" clause which stated: "no provision, stipulation, or forfeiture of this policy shall be waived by any requirement, act, or proceedings of this company relating to investigation, appraisal, or adjustment of any loss." *Id.* The Court of Appeals cited a 1897 Texas Supreme Court case which gave credence to the "anti waiver" clause. *Id.* at 561-562 citing *American Central Ins. Co. v. Buss*, 90 Tex. 380, 38 SW 1119 (1897).

The Court of Appeals rejected three (3) prior long standing precedents, finding waiver of the appraisal provision for an unreasonable delay in demanding appraisal. In rejecting these three (3) precedents, the Court of Appeals noted that these opinions do not rely on Texas Supreme Court authority. *Id.* at 563. The 14th Court also declined to follow *Sanchez*, holding it distinguishable because appraisal was demanded after seeking abatement for a deficient presuit notice and following an unsuccessful mediation. *Id.* at 562.

The 14th Court of Appeals determined waiver had not occurred. *Id.* at 563. The point of reference for waiver is when the demand for appraisal was made. *Id.* at 563-564. This point of reference for Slavonic was when it received the Requenas' demand letter on May 8, 2009 concurrently served with the lawsuit. *Id.* at

562-563. Implicitly, the Court found the 118 days between the $350.00 check sent to the insureds and the date suit and the demand letter were served on May 8, 2009 were not controlling, assumably because there can be no objective measure to determine a disagreement. The insurer could equally assume that the insureds were not disagreeing with what was paid, as the insurer had no notice of a disagreement.

Furthermore, the appellate court determined abatement was proper given the Texas Supreme Court's direction in *Johnson* that appraisal is to take place presuit. *Id.* at 564-565.

Following *Slavonic*, some three (3) weeks later, the 14th Court decided *In Re Security National Ins. Co.*, 2010 WL 1609247 (Tex. App. – Houston [14th Dist.] 2010, orig. proceeding), another Hurricane Ike case. In *Security National*, the issue of waiver had an interesting twist – the insured Waloon Investment ("Waloon") requested appraisal but later abandoned its request but only after the insurer named its appraiser. *Id.* at *2. One week later, the insured notified the insurer that it was no longer pursuing appraisal. *Id.*

About two (2) weeks later, March 10, 2010, a contractor for the insured sued the insured for nonpayment of work done related to the loss. *Id.* *Security* filed an interpleader and declaratory relief action about four (4) days later (March 13, 2009), depositing the amounts already paid the insured into the registry of the court. *Id.* On May 20, 2009 Security's lawsuit and the contractor's lawsuit were consolidated. *Id.* On June 4, 2009, Waloon filed a counterclaim against Security. *Id.* On July 2, 2009, the parties mediated. *Id.* at *3. On July 13, 2009, Security asserted its right to appraisal. *Id.* On August 6, 2009, Security again reasserted its intent to pursue appraisal. *Id.* On August 7, 2009 Waloon responded declining appraisal. *Id.* at *4.

Security responded by filing a motion to compel appraisal on September 21, 2009. *Id.* The trial court denied the motion on November 12, 2009. *Id.* Security petitioned for mandamus relief. *Id.*

Following *Slavonic*, the 14th Court granted relief. *Id.* at *1. The Court found the objective point of disagreement or impasse was January 22, 2009 when the insured requested appraisal. *Id.* at *5. Still, the Court found Security timely invoked appraisal. *Id.* at * 5-6. Because Waloon submitted three (3) separate additional requests for payments with the final submission being on June 9, 2009 – the request for appraisal was timely. *Id.* Finally, any breach of the policy by Security did not waive appraisal. *Id* at *6. *See also In the Continental Casualty Co.*, 2010 WL 3703664 (Tex. App. – Houston [14th Dist.] 2010, orig. proceeding).

The latest case on waiver is *In Re Universal Underwriters of Texas Ins. Co.*, No. 10-0238. In *Universal,* the insured, Grubbs Infinity ("Grubbs") sustained a hail loss. *Real Party In Interest's Brief on the Merits*, pp 1-2. Universal inspected the property and issued a payment on May 20, 2007. *Id.* at Tab B, p. 1. A later reinspection occurred on September 12, 2008 and a additional payment was issued. *Id.* at Tab B, pp. 1-2. Universal subsequently sent the insured a letter, reserving its rights and telling its insured that it had two years and one day to bring suit under the policy. *Id.* at Tab 6.

On April 13, 2009, Grubbs filed suit. *Id.* at Tab A. On May 15, 2009, Universal answered asserting a general denial and invoking the appraisal clause. *Id.* at Tab D. Some six months passed with the parties engaging in discovery. *Id.* at p. 3. Universal then set its motion and asked for it to be heard. *Id.* After hearing, the trial court denied the motion. *Id.* Mandamus relief was sought in the Second District Court of

Appeals (Forth Worth) which denied relief. *Id.* at p.1.

Universal sought mandamus relief in Texas Supreme court which has set oral arguments for later this year. Needless to say, this case has generated much interest with amicus briefs coming from various insurance companies through trade groups. *See Brief of Amice Curiae Insurance Council of Texas and Properly Casualty Insurers Association of America.* One trade group urges that a prejudice standard should be imposed for an insured to successfully interpose a waiver of appraisal demand. *Id.* at pp. 25-26.

D. SOME OBSERVATIONS

First, it is ironic, but certainly laudable, that an insurer would be the party complaining about appraisals with the Texas Supreme Court at least implicitly contending that its decision was pro insured. Given the enormous resources of insurers, they are certainly in the best position to reap the benefits of *Johnson* and of course they now have. In theory, appraisal is now a prelitigation process without lawyers, judges, lawsuits, process, discovery, and juries. *Johnson*, 290 S.W.2d at 894. Insurers have access to numerous experts who they use over and over again and insurers are sophisticated in the appraisal process. The insured without representation is at an obvious disadvantage. The reasoning in *Johnson* would seem to bind the insured to damages and issues of causation as it relates to the loss, thereby permitting trial by appraisal.

Undoing the appraisal puts a tremendous burden on the unsophisticated insured who may become aware of the binding results of an appraisal too late. As State Farm stated – it forces the losing party to "unring the bell." Because appraisal will be viewed as presumptively a legitimate process, the Courts will be swayed to enforce the award no matter how the results

are obtained or unjust – just like a binding mediated or arbitration agreement.

The decision is not pro-consumer. An insured will bear the costs of appraisals for its own appraiser and often likely one-half the cost of an umpire. It may require the insured to take on an additional burden of proving the appraisers exceeded their authority or that liability has been decided. This may require depositions, the hiring of other experts, and of course, attorney's fees. The Court has complicated a rather simple process which has been used properly if we are to conclude, as the court does, that the scarcity of cases means appraisal works. Appraisal after *Johnson* would seem to be acceptable for almost every property claim.

Much like health care liability cases which require the use of expert reports before the case may proceed and the multiplicity of appellate litigation about the sufficiency of these expert reports, the Supreme Court has created a whole new area of satellite litigation. The Court has greatly expanded mandamus litigation to intercede in the trial court process to address unnecessary discovery and proceedings, evaluate arbitration requests, examine the granting of new trials and avoidance of wasted judicial resources, etc. *See In Re Columbia Medical Center*, 290 S.W.3d 204, 215-216 (Tex. 2009) (O'Neill, J. dissenting). The *Johnson* opinion seems contrary to the Supreme Court's willingness to uncomplicate trials and keep litigation costs down. The standard to undo an appraisal is hardly simple or easy to satisfy. The Court did no one any favors with this decision.

An examination of existing case law at the time *Johnson* was decided calls into question the reasoning of *Johnson*. For example and not by way of limitation: appraisal may be invoked in the lawsuit itself. *Allstate*, 85 S.W.3d at 196; a request for appraisal must be made within a reasonable time. *American Fire Ins. Co. v.*

Stuart, 38 S.W.395 (Tex. Civ. App. – 1996, no writ) (58 day delay); *Boston Ins. Co. v. Kirby*, 281 S.W. 275 (Tex. Civ. App. – Eastland 1926, no writ) (59 day delay); and a trial court may determine the timing of appraisal and abatement is not mandatory. *In re Terra Nova*, 992 S.W.2d 741, 742 (Tex. App. – Texarkana 1999, orig. proceeding) (also holding trial court has discretion to decide if appraisal is to take place at all when contractual and bad faith claims are brought together). And prior to the Texas Supreme Court's decision in *Johnson*, but after *Wells*, it was settled law that the appraisal clause must be strictly construed. *Richardson v. Allstate Texas Lloyds*, 2007 WL 1990387 (Tex. App. – Dallas 2007, no pet); *Laird v. CMI Lloyds*, 261 S.W.3d 322, 326 (Tex. App. – Texarkana 2008, rev. dism'd w.o.j.); *Germania Farm Mut. Ins. Co. v. Williams*, 2002 WL 32341841 (Tex. App. – Eastland 2002, no pet); *General Star Indem. Co. v. Spring Creek Village Apartments Phase V, Inc.*, 152 S.W.3d 733 (Tex. App. – Houston [14th Dist.] 2004, no pet); and *Hartford Lloyds Ins. Co. v. Yarborough*, 2006 WL 1469705 (S.D. Tex. 2006).

The *Johnson* opinion noted at least three (3) cases that held causation cannot be determined by appraisers with Wells being the most frequently relied upon. *Wells* has been widely cited and applied with little or no confusion. 919 S.W.2d 679 (Tex. App. – Dallas 1996, writ denied). To recap, in *Wells*, the appraisers were called upon to determine the damages due to a foundation movement of a home. *Id.* at 682. The appraisers and umpire arrived at a figure of $22,875.94. *Id.* However, the insurer's appraiser and umpire determined that the damage related to the plumbing leak was zero. *Id.* The trial court granted summary judgment in favor of the insurer, denying the Plaintiffs' claim. *Id.* The Plaintiffs appealed and the Dallas Court of Appeals

determined that appraisal was limited to determining the "amount of money involved in the controversy." *Id.* at 685. An appraisal is not to be used to determine liability, causation, or coverage. *Id.* at 683-684. *Wells* makes it clear that appraisal is improperly used and has no binding effect if causation, coverage, or liability is decided by the appraisers and/or umpire.

The Supreme Court, in contrast to *Wells*, cites *Lundstrom* for the proposition of appraisers determining coverage. *Johnson*, 290 S.W.3d at 892. But in *Lundstrom*, the insureds did not participate in appraisal and USAA made its appraisal demand for the interior of the home caused by the initial wetting. *Lundstrom*, 192 S.W.3d at 82. The appraisal award was for $4226.19 which amounted to $1,666.19 after applying the deductible. *Id.* The insured cashed the appraisal award check. *Id.* Furthermore, USAA's appraisal demand was limited to the interior of the home from the initial wetting and *not* ongoing leaking or mold which had resulted which was a coverage issue and had been previously denied. *Id.* at 87. The scope of appraisal was specifically stated and not objected to. *Id.* USAA also noted in their appraisal demand that all that was at issue was property damage not "policy conditions or coverage." *Id.* The *Lundstrom* court found there were no coverage issues before the appraiser/umpire and there was no partition in the appraisal award according to causes. *Id.* at 89.

Instead of limiting its decision to the particular facts of the case or even ruling that appraisal could take place as to the roof without regard to cause, the Supreme Court in *Johnson* embarked on a lengthy discussion that the amount of damages necessarily includes causation, thereby broadly expanding the function of appraisal. But liability in an insurance claim necessarily includes coverage; if there is no coverage it is well settled law that no

payment is due (absent some unique circumstances).

The Texas Supreme Court in *Johnson* apparently holds that it is proper for appraisers (umpires) to factor in cause in evaluating damage. This may be done implicitly by considering what is hail damage versus what is wear and tear. Thus, based on the reasoning of *Johnson*, the appraisers must necessarily decide what is the amount of damage due to hail versus wear and tear. And according to this same reasoning, the amount determined in appraisal will be binding on both Johnson and State Farm. What then is left for trial?

Since State Farm is asserting coverage/causation precludes payment for anything more than the rigid line shingles as opposed to the entire Johnson roof, if there is an appraisal award for $10,000 as a result of the Johnson's appraiser and umpire agreeing, can State Farm litigate coverage or challenge the basis for the appraisal award, regardless of whether the award is silent on causation? Can State Farm unring the bell?

The Texas Supreme Court for whatever reason has taken a rather simple process and needlessly complicated it. Simply because the appraisal clause exists in an insurance policy does not mean that if it is not used then it makes its inclusion meaningless or that the appraisal clause in a property policy is a one size fits all method for determining damages.

Appraisal was not meant to be used in every first party property case. It was designed to be employed in circumstances such as grandmother's antique diamond ring being stolen, an event covered by the policy. There is *no controversy* as to what extent the ring is covered. Appraisal properly framed is that the insured says the ring is worth $5,000 while the insurer argues the value is $1,000. Appraisal would certainly be proper and an efficient means of resolving the issue

of damages, the value of grandmother's stolen antique diamond ring.

In contrast though, where there are multiple causes of a loss, some covered and others not, an appraisal which includes appraisers (umpires) undertaking causation, implicitly or expressly, whether stated in the award or not, when evaluating the amount of loss confuses the parties, the court, what is to be tried, and the binding effect of the award. Thus, the Supreme Court's discussion in *Johnson* is frankly not helpful and does not make appraisal attractive.

What the Texas Supreme Court in *Johnson* is apparently saying is that once a party requests appraisal, it must take place. Additionally, courts should not get involved with the propriety of appraisal before it takes place; rather, any problems with appraisal such as appraisers exceeding their authority, determining liability, etc. can and should be dealt with post appraisal. Determining damages necessarily includes causation. Given the rule that a court will indulge every reasonable presumption to sustain an appraisal award, the burden to undo it or have it set aside is on the party challenging the award. *Lundstrom*, 192 S.W.3d at 87. Obviously, if you are on the wrong end of appraisal, you have an uphill battle.

The Court, only in the last few sentences of its *Johnson* opinion, suggests that when appraisal may be too expensive or coverage so unlikely that in these circumstances appraisal might be avoided; preemptive action by the courts might then be proper. *Johnson*, 290 S.W.3d at 895. But what if an insured cannot afford to hire and pay an appraiser? Must he default in favor of the decision of the insurer's appraiser and the umpire? And if the appraisal involved a commercial building where multiple perils were involved, some covered and others not, must the insured or for that matter the insurer pay hundreds of

thousands of dollars towards an appraisal that is rendered a nullity?

The language in the Supreme Court's opinion in *Johnson* that the amount of loss is always going to be an issue in a property case pre-suit and the Court's undoubted propensity for arbitration would seem to lead to the conclusion that the Court views appraisal as some sort of alternative dispute resolution like procedure which can lessen or even avoid litigation between insurer and insured and appraisal must be working due to the "scarcity" of decisions on the subject. *See In Re Allstate*, 85 S.W.3d at 199 (Baker, J. dissenting). These perceptions are not only questionable, but seemingly counterproductive to both insureds and insurers. *Id.* It is also disadvantageous to insureds. *Id.* at 195 (noting the contentions of insureds that appraisal is costly and insureds are unlikely to challenge insurer's valuations). Given the Court's rationale and reasoning, we may have now arrived at trial by appraisal, or at the least trial to undo appraisal.

So, if the appraisal award in *Johnson* turns out to be $5,000, will State Farm be able to show that the award factored in covered and noncovered perils? Or now by definition, is the award which factors in causation, but does not mention cause, unchallengeable or a proper exercise of authority of appraisers and the umpire? And if the award is properly challenged and negated, is appraisal helpful at all? Agreeing on a number does not imply or concede liability or does it?

Finally, the Court also does not address how appraisers and/or umpires are to be screened and evaluated for competence and/or impartiality. In other words, can appraisers tell the difference between hail damage and ordinary wear and tear? Does *Robinson* ever apply to the appraisal process or is there some other standard or test? *See E.I. du Pont de Nemours v. Robinson,* 923

S.W.2d 549 (Tex. 1995). How does a party challenge an appraiser if court intervention pre-appraisal is to be avoided? Allowing appraisers and umpires to decide causation implicitly or expressly is permitting trial by appraisal without any gatekeeping rules.

E. CONCLUSION

Appraisal is intended to be an efficient and inexpensive method to determine damages. But when issues of causation, including concurrent causation, and coverage, are at issue, the efficiency, expense, and usefulness of appraisal must be called into question. Nevertheless, the Texas Supreme Court in *Johnson* has clearly indicated appraisal should take place without court intervention and let the results be sorted out later. Given the presumption in favor of the results of appraisal, it causes the "loser" of appraisal to have to undo the results. With the Texas Supreme Court's holding, we have arrived at trial by appraisal. It goes with the old saying "shoot first and ask questions later."