ZELLE LLP LONESTAR LOWDOWN

Dedicated to Texas First-Party Property Claims

The Zelle Lonestar Lowdown | Monday, Novmber 2, 2026 | ISSUE 41

Welcome to The Zelle Lonestar Lowdown, our monthly newsletter bringing you relevant and up-to-date news concerning Texas first-party property insurance law.

In 2025, we focused on Collaboration. We had people reach out with article ideas, their own articles, and ideas for industry events. In 2026, we will continue that effort. We continue to invite our readers to let us know what they are worried about, legal topics that pique their interest, and new advances in the industry – all with a Texas twang.

As always, if you are interested in more information on any of the topics below, please reach out to the author directly. Zelle attorneys are always interested in talking about the issues arising in our industry. If there are any topics or issues you would like to see in the Lonestar Lowdown moving forward, please reach out to our editors: Shannon O'Malley, Todd Tippett, and Steve Badger.



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Upcoming Events

You don't want to miss this!

November 3 – Steven Badger will present "Update From The Trenches" at the Wisconsin Fire Loss Association meeting in Fond du Lac, WI.

November 4-6 – Steven Badger, Jennifer Gibbs, and Bennett Moss will present at the PLRB Large Loss Conference in Nashville, TN.

November 10 – Michael Upshaw will present "From Land Acquisition and Entitlements to Site Development and Pad Ready Construction, Data Centers: What Nobody is Talking About," with John Peiserich (J.S. Held) at the 2026 Onshore Energy Conference (OEC) in London, UK.

November 12 – **Zelle** will sponsor the 2026 STEM is for Everyone Charity Dinner in London, UK.

November 25 – Jason Reeves will co-present during the British Institute of International and Comparative Law (BIICL)'s online course on *Climate Change Litigation.* (4- 6 pm UK Time)

December 2 – **Brandt Johnson** will present at the Allied Trust - 2026 Litigation Summit in Houston, TX. Co-presenters include Howard Altschule (Forensic Weather Consultants).

January 12 – Steven Badger will present at the P.L.A.N. Appraiser & Umpire Certification Conference in Naples, FL.

January 18 – Steven Badger will present at the Jack Hanks Public Adjuster Training in Dallas, TX.

January 24 – 28 – Steven Badger, George Reede, Brandt Johnson, and Jessica Port will present at the 2027 NACA Annual Convention in Reno, Nevada.

January 31 - February 2 – Steven Badger and Jennifer Gibbs will present at the 2027 Windstorm Insurance Network conference in Aurora, CO.

February 16 – Steven Badger will present at the International Roofing Expo (IRE) in Las Vegas, NV.



1. **The Rainmaker** (1997) – Based on a John Grisham novel. A young, underfunded attorney takes on an insurance company that wrongfully denied a life-saving medical claim.

2. **Momento** (2000) - A man with short-term amnesia tracks his wife's killer while flashing back to his former career as an insurance investigator.

3. **Sleuth** (1972) - A wealthy mystery novelist sets up a fake jewel robbery with his wife's friend as part of a twisted insurance scam and psychological game.

4. **Double Indemnity** (1944) - An insurance salesman and a femme fatale plot to murder her husband and collect on a policy with a double-indemnity clause, only to be hunted down by a sharp claims adjuster.

5. **The Apartment** (1960) - A humble clerk at a massive New York insurance firm climbs the corporate ladder while helping the corporate leaders with their extracurricular activities.

6. **The Thomas Crown Affair** (1968 / 1999) - A wealthy mastermind pulls off a high-stakes art heist, matching wits with a relentless insurance investigator determined to recover the loot.

7. **The Killers** (1946) - After a former boxer accepts his murder with resignation, while a life insurance investigator digs into the dead man's past and

News from the Trenches

by Steven Badger

Can insurance proceeds be used to pay public adjuster fees?

We all know it goes on. There's no denying it.

The common scenario….

The insured, its public adjuster, and its contractor tell the insurance company that the roof costs $1,000,000 to replace. They provide either an estimate or a contract stating a $1,000,000 roof replacement price in order to recover the withheld depreciation/replacement cost value (RCV).

But here's what they don't tell the insurance company….

There is an undisclosed agreement, usually unwritten, between the insured, its contractor, and its public adjuster that the public adjuster fee will be paid out of the $1,000,000 total claim payment. As part of the agreement, the contractor agrees to do the work for the net remaining amount after paying the public adjuster.

We all know it goes on. There's no denying it.

And sometimes the contractor and public adjuster aren't very smart and actually put the agreement into the contract between the insured and the contractor, such as this contract language from a recent Florida matter:

"For all work covered by Company's flood insurance policy, the total Contract Price shall reflect the portion of proceeds [Moorings] receives from its insurance carrier less an amount equal to [Moorings]'s public adjuster's fee (the "Discount"). The Discount shall not exceed 8% of Diamond's total Contract Price for such Work."

So let's do a little math….

Assuming the contract price to do the work is $1,000,000, after subtracting the "Discount" necessary to pay the $80,000 public adjuster fee, the contractor has agreed to do the work for $920,000.

With the contractor having effectively agreed to do the work for $920,000 (the "amount actually incurred" to repair the damaged property), how much does the insurance company owe on the claim? Of course, only $920,000. Because public adjuster fees aren't covered by the policy.

Anyone contest my math? Of course not. You can't.

Hence, the final question….

uncovers a web of double-crosses and a botched robbery.

8. **Cedar Rapids** (2011) – Small-town insurance agents attend a nationwide insurance industry conference and show the entire industry how to misbehave.

9. **The Truman Show** (1998) - An insurance salesman/adjuster discovers his entire life is actually a TV show.

10. **Lloyd's of London** (1936) – Two young men learn that sailors/pirates are planning to swindle an insurance company, so they travel to London to warn the owners of "Lloyd's Coffee-House." Their news results in a job with the company that eventually becomes "Lloyd's of London."

Feel free to contact **Todd M. Tippett** at 214-749-4261 or ttippett@zellelaw.com if you would like to discuss these Tips in more detail.

Did the insured, its public adjuster, and its contractor all commit insurance fraud by telling the insurance company that the roof cost $1,000,000, knowing that the contractor was discounting the price to $920,000 in order to pay the public adjuster fee?

In my opinion, indeed they absolutely did.

I've said it before, and I will say it again….

Insurance companies should always inquire into how the public adjuster fee is being paid. This can be done by simply asking the question, requesting relevant documents, or through an examination under oath. Insurance companies have the right to ensure that their RCV payments are not being used to pay public adjuster fees and are only being used to complete repairs as represented in the RCV holdback request.

Here is a link to the Florida court decision mentioned above.



AI Update

Quantum Computing and AI: Why the Next Computing Shift Matters

by Jennifer Gibbs

Artificial intelligence gets most of the headlines, but a second technology is moving quickly in the background. Quantum computing and AI are often lumped together as "futuristic tech," but they are very different things. AI is software that learns from data to automate or support decisions. Quantum computing is hardware built on the principles of quantum physics and designed for calculations that would take traditional computers millennia. The more interesting question is what happens when the two start working together.

Quantum Computing 101

Classical computers process information as bits, and each bit is either a 0 or a 1. Quantum computers use "qubits," which can represent many possible states at once. In theory, that lets a quantum machine work through huge numbers of potential solutions in parallel. A related property called entanglement links qubits together so they can carry out computations jointly.

The technology is real, but it is still early. Today's quantum devices are limited and prone to errors. They have outperformed classical systems only on narrow benchmark tasks. The machines are also delicate. They typically run inside refrigerators kept just above absolute zero, because heat causes errors in the qubits. For that reason, most users are expected to reach quantum computers remotely through the cloud rather than own one.

A Two-Way Relationship

The link between quantum computing and AI runs in both directions.

Quantum could supercharge AI. Training AI models takes enormous computing power, and even the most advanced chips can struggle to keep up. The research suggests that the parallel processing power of quantum computers may eventually meet that demand. Quantum hardware could let AI models consider far more options at once, search possible solutions faster, and tune themselves more quickly. Researchers are also looking at quantum computing as a way to clean the data used to train AI more effectively, which would lead to more accurate models. Quantum methods may also help with AI's energy problem. One Cornell proposal suggests a quantum-based optimization framework could cut the data center burden of AI workloads by up to 12.5%.

AI is already helping quantum. AI is being used today to stabilize and control quantum systems. It adjusts settings automatically, spots glitches early, and helps the hardware run for longer stretches. AI is also being applied to the field's biggest obstacles, including the design of quantum algorithms and error correction. The results can be dramatic. TIME reported that AI was "instrumental" in new research from

Google and the startup Oratomic. Experts told TIME that research could "significantly" shorten the time needed to build a quantum computer capable of threatening encryption.

Early Results Worth Watching

Some practical gains are already showing up. Researchers at the University of Toronto and Insilico Medicine combined quantum computing, generative AI, and classical methods to design molecules that target KRAS, a cancer-driving protein long considered "undruggable." One co-investigator said approaches like this could shorten the preclinical phase of drug discovery "by years." Beyond medicine, possible applications include materials science, weather modeling, finance, and logistics. Many of these remain speculative, but early proofs of concept have been promising.

The Security Question

For financial institutions and their advisers, the most immediate issue may be cybersecurity. Shor's algorithm, developed in the 1990s, could eventually let a powerful quantum computer break asymmetric (public key) encryption. The CSA notes that this type of encryption protects about 90% of our data. Security experts are especially concerned about "harvest now, decrypt later" attacks. In these attacks, bad actors collect encrypted data today so they can decrypt it once quantum tools are ready. The good news is that "quantum hard" encryption codes designed to resist quantum attacks are already available. Computer scientists are also building post-quantum cryptography to protect data over the long term.

Keeping Perspective

Timelines are still uncertain, although IBM has stated that 2026 will be the first year a quantum computer outperforms all classical-only methods on a problem. In August 2026, IBM and its collaborators announced three demonstrations that they say show this "quantum advantage," with IBM's quantum processors outperforming all known classical algorithms on specific tasks. In one experiment, the team says it mathematically proved that no classical computer can efficiently reproduce the patterns its quantum computer generated. Outside experts called the work meaningful progress, but cautioned that the tasks were niche problems tailored to IBM's hardware, that the results are hard to verify independently, and that commercial usefulness is still years away.

Either way, the two technologies are best seen as partners, not rivals. Most predict that classical computing is likely to stay dominant, with quantum hardware used selectively to speed up specific tasks.

The practical lesson is to stay prepared without falling for the hype. Most enterprises will not be running quantum-AI systems tomorrow. But the choices organizations make now about AI governance, cryptographic agility, and data controls will shape how ready they are when the technology matures.

Hail No! Focus on the Pleadings!

by Michael Upshaw

Texoma Cowboy Church, Inc. v. Church Mutual Insurance Company, S.I., No. 7:26-CV-00062-O, 2026 WL 3166210, at *1 (N.D. Tex. Oct. 22, 2026)

In Texas, even the most simple disputes over the cause and extent of damage can end up in a lawsuit alleging standard breach of contract, Texas Insurance Code violations, and breach of the duty of good faith and fair dealing. Those are easy hurdles to jump in a federal court complaint. But when the policyholder alleges fraud, negligent misrepresentation based on the same supporting facts as fraud, and conspiracy, federal courts pay special attention. We call this a “throw everything at the wall and see what sticks” type of pleading.

In *Texoma Cowboy Church, Inc. v. Church Mutual Insurance Co., S.I.*, 2026 WL 3166210 (N.D. Tex. Oct. 22, 2026), Chief Judge Reed O’Connor threw out half of the claims, and he made a useful point for carriers along the way.

The Storm

On April 5, 2025, a hail and windstorm hit Texoma Cowboy Church’s property on U.S. Highway 281 outside Wichita Falls, which was insured by Church Mutual. The church hired a public adjuster and Church Mutual hired an engineering firm. The engineer found that the hail did hit the roof, leaving dents and separating panels. Church Mutual then had a third-party contractor prepare a bid. In December 2025 it issued a replacement-cost estimate and payment after application of the policy deductible and depreciation. But the church didn’t think the payment was enough and filed suit.

The Lawsuit

The church’s state court petition pleaded eight causes of action: breach of contract (both the ordinary kind and the anticipatory kind), bad faith, DTPA violations, Prompt Payment Act violations, unfair insurance practices, negligent misrepresentation, fraud, and conspiracy.

Church Mutual moved to dismiss four of them: fraud, negligent misrepresentation, gross negligence, and conspiracy. The court granted the motion on all four, with prejudice.

An Estimate Isn't Fraud

The church argued that because the estimate left out costs it believed should have been included, Church Mutual had knowingly defrauded it. The court rejected that. Under the Texas Supreme Court's decision in *Transportation Insurance Co. v. Faircloth*, 898 S.W.2d 269 "an expression of opinion about monetary value is not a representation of fact which gives rise to an action for fraud." An estimate built on an adjuster's and a contractor's professional judgment is an opinion about value. Someone can disagree with it and sue over it as a breach of contract, but disagreeing with it doesn't make it fraud.

Name Names

The fraud allegations were also too vague. The petition said the misconduct was committed by "Defendant individually and/or through its agent(s)." The court held that this phrasing doesn't satisfy Rule 9(b), which requires a fraud plaintiff to plead who said what, when, where, and how.

The church tried to keep its negligent misrepresentation claim alive by arguing that it rested on different facts and therefore didn't need the same level of detail. The court disagreed. Both claims came from the same allegations, so both had to meet Rule 9(b), and both failed.

It's a Contract Case

The court also applied Texas's independent injury / economic loss rule. When the harm is that the plaintiff didn't receive money owed under a contract, the claim belongs in contract, not tort. The church's injury was an underpaid claim, so its tort theories couldn't proceed.

A Property Insurance Dispute Isn't an "Extreme Risk"

Gross negligence under Texas law requires an "extreme degree of risk." Courts have read that to mean risks like death, serious physical injury, or financial ruin. A disputed insurance payment doesn't meet that standard. The petition also didn't allege facts showing Church Mutual was actually aware of any such risk, which is the second element. That claim was dismissed too.

Tin Foil Hats

The conspiracy count alleged that Church Mutual was "a member of a combination of two or more persons" who reached a "meeting of the minds" to mislead the church. The petition never said who the other members were or what they did. The court called this a recitation of the elements and dismissed it. The claim also failed for a second reason: a conspiracy claim depends on an underlying tort, and the fraud claim was already gone.

Not a Complete Win

As expected, the breach of contract, bad faith, DTPA, Chapter 541, and Chapter 542 claims are still in the case. The dispute will come down to the usual question: whether certain damages were caused by the storm or preexisted. Prompt-payment interest is still a live risk if any additional amount turns out to be owed.

Takeaways

- **Pay attention to the pleadings (or ensure your attorneys do) and file the partial motion to dismiss.** Fraud, conspiracy, and gross negligence claims show up from time to time, and Rule 12(b)(6) is an effective way to remove them early.
- **Cite *Faircloth* in every "the estimate was fraud" case.** This opinion is a clean, recent federal application of it.
- **Document the basis for the estimate.** The court treated this estimate as an opinion partly because it rested on outside professional judgment from an engineer and a third-party contractor. A file showing that basis puts the carrier in a better position.

Late Notice of an Old Storm Means No Coverage

by Tom Papa

Policyholders sometimes try to fix a timing problem by moving the date of loss. In *Gann v. Depositors Insurance Co.*, No. 25-11291, 2026 WL 2983701 (5th Cir. Oct. 5, 2026) (per curiam), the Fifth Circuit held that a hail claim reported more than four years after the storm was late as a matter of law.

Background

Depositors insured the policyholder's commercial building in Irving under a 2018–2019 policy and a 2022–2023 policy. Both required "prompt notice of the loss or damage."

In September 2022, the policyholder reported interior water damage under the 2022 policy, with an August 9, 2022 date of loss. Depositors inspected, found hail damage to part of the roof, and paid. In October 2023, the policyholder produced a consultant's report that, for the first time, dated the loss to a June 5, 2018 hailstorm and called for replacing the entire roof. Depositors declined to pay more. The 2018 date fell outside the 2022 policy, and hailstorms in March and April 2023 had likely caused additional damage.

Spotlight

Insurance Law Section of the State Bar of Texas

The Insurance Law Section of the State Bar of Texas is seeking sponsors for 2027. Its 2,300+ members include policyholder lawyers, defense lawyers and in-house counsel, so sponsors are seen across both sides of insurance practice.

The policyholder sued for breach of contract, violations of Chapters 541 and 542 of the Insurance Code, and breach of the duty of good faith and fair dealing. The Northern District of Texas granted summary judgment for Depositors. It held that even if the policyholder had made a claim under the 2018 policy, its notice was late as a matter of law and Depositors was prejudiced. The court later denied the policyholder's Rule 59(e) motion.

The Fifth Circuit's Analysis

The panel started with the Texas rule that notice is a condition precedent to coverage. *Blanton v. Vesta Lloyds Ins. Co.*, 185 S.W.3d 607, 611 (Tex. App.—Dallas 2006, no pet.).

On timeliness, it wasn't close. The policyholder first reported a claim more than four years after the June 2018 storm, and didn't point to that storm as the cause until more than five years after it. The court relied on *Ridglea Estate Condominium Ass'n v. Lexington Insurance Co.*, 415 F.3d 474, 479 (5th Cir. 2005), where a six-year delay on a hail claim was unreasonable as a matter of law, and on *Alaniz v. Sirius International Insurance Corp.*, 626 F. App'x 73, 77 n.2 (5th Cir. 2015), which found shorter delays unreasonable.

The policyholder argued that it acted promptly once it saw water inside the building. The problem, as both courts noted, is that it never explained why the roof damage couldn't have been found sooner. Without an explanation, "an inexcused delay or delay because of a flimsy excuse entitles the insurance company to judgment as a matter of law." *Nat'l Union Fire Ins. Co. v. Bourn*, 441 S.W.2d 592, 595 (Tex. Civ. App.—Fort Worth 1969, writ ref'd n.r.e.).

Depositors also had to show prejudice, and it did. Five years of delay kept it from investigating "while the matter is fresh." *Stonewall Ins. Co. v. Modern Exploration, Inc.*, 757 S.W.2d 432, 435 (Tex. App.—Dallas 1988, no writ).

The extra-contractual claims failed with the contract claim. The policyholder had no evidence of an injury independent of the policy benefits, which defeated the Chapter 541 and bad-faith claims. *Senechal v. Allstate Vehicle & Prop. Ins. Co.*, 127 F.4th 976, 979 (5th Cir. 2025). And without liability under the 2018 policy, there was no Chapter 542 claim. *Weiser-Brown Operating Co. v. St. Paul Surplus Lines Ins. Co.*, 801 F.3d 512, 518 (5th Cir. 2015). The Rule 59(e) ruling was affirmed because the motion repeated arguments the district court had already considered.

The panel added one more point in a footnote. It said the district court was "likely" right that no claim was ever made under the 2018 policy at all. The court didn't need to decide the issue, but it is a good reminder that the policy period in play is set by what the policyholder actually reported and pleaded.

The Lowdown

This decision is consistent with *Ridglea* and with the *H5R* decision we covered in February. For adjusters, the lesson is practical. When a policyholder's expert comes back with a much older date of loss, note when you first learned of it, ask why the damage wasn't reported sooner, and document what has happened to the property since, like the 2023 storms here. That record is what carried Depositors through summary judgment.

Sponsorship supports the Section's continuing legal education, law student scholarships and networking events throughout the year. New sponsors who sign up in 2026 for 2027 will receive the rest of 2026 at no additional cost.

For the 2027 Sponsorship Prospectus, contact Shannon O'Malley. Also, the Insurance Law Section wants to hear from you! If you are a lawyer member, please respond here. If you are a partner/vendor with the Section, please respond here.

Castillo v. State Farm Lloyds: Court's Finding of a Bona Fide Dispute Defeats Bad-Faith and Treble Damages Claims

by Austin Taylor

Recently, the United States District Court for the Northern District of Texas granted summary judgment dismissing a policyholder's claims for breach of the duty of good faith and fair dealing, as well as most of her statutory bad-faith claims arising under Chapter 541 of the Texas Insurance Code and the Texas Deceptive Trade Practices-Consumer Protection Act ("DTPA"). *Levya Castillo v. State Farm Lloyds*, No. 3:25-CV-2636-D, 2026 WL 3075509 (N.D. Tex. Oct. 14, 2026) (Fitzwater, J.). The court also dismissed her claims for treble and exemplary damages (including the statutory bad-faith claims that survived summary judgment), holding that the insurer's reliance on two reasonable inspections created a bona fide dispute over coverage. *Id.* Although the court allowed the policyholder's breach of contract claim and a handful of statutory extracontractual claims to proceed, the decision highlights that a disagreement over the cause or extent of hail damage, without more, is not bad faith and that conclusory allegations of "knowing" conduct will not carry treble or exemplary damages past summary judgment.

Factual Background

Laura Levya Castillo's home was insured by State Farm. The policy covered hail and windstorm damage but excluded coverage for wear and tear. *Id.* at *1. In April 2023, Castillo submitted a claim for an April 2, 2023, hailstorm. *Id.* State Farm inspected the property and found hail damage to two turbine vents, one turtle vent, and portions of the gutters and

downspouts. *Id.* State Farm noted wear-and-tear damage to the roof shingles but expressly found no hail damage to them. *Id.* Castillo made no repairs to the property between 2019 and May 2024. *Id.*

On July 8, 2024, Castillo reported a new claim for hail damage from a May 27, 2024, storm. *Id.* State Farm inspected on July 15, 2024, observed hail impacts to the turbine vents but no hail damage to the shingles, and issued a coverage determination that same day explaining that the covered loss did not exceed the $2,512 deductible. *Id.* at *1, *10. After Castillo retained a public adjuster, State Farm conducted a second inspection on September 16, 2024, and advised that its conclusions were unchanged. *Id.* at *1. Castillo sued in August 2025, asserting claims for breach of contract, violations of Chapter 541 of the Texas Insurance Code, the Texas Prompt Payment of Claims Act ("TPPCA"), and the DTPA, and breach of the duty of good faith and fair dealing. *Id.* State Farm removed the case and moved for summary judgment on all claims. *Id.*

The Court's Analysis

The court concluded that a bona fide coverage dispute precluded Castillo's claim for breach of the common-law duty of good faith and fair dealing

The court began its analysis with Castillo's common-law bad-faith claim. *Id.* at *8. Under Texas law, an insurer breaches the duty of good faith and fair dealing when it denies or delays payment after liability has become reasonably clear, with the reasonableness of the insurer's conduct judged by the facts available to it at the time of the denial. *Id.* (citing *Universe Life Ins. Co. v. Giles*, 950 S.W.2d 48, 49 (Tex. 1997); *State Farm Fire & Cas. Co. v. Simmons*, 963 S.W.2d 42, 44 (Tex. 1998)). An insurer cannot avoid liability by failing to investigate, but its duty to investigate is not unlimited, and if, after a reasonable investigation, the insurer has evidence showing that the insured's claim may be invalid, a bad-faith action is not viable. *Id.* (citing *Tucker v. State Farm Fire & Cas. Co.*, 981 F. Supp. 461, 465 (S.D. Tex. 1997)).

Applying those principles, the court found that State Farm had a reasonable basis for its claim determination as a matter of law. State Farm acknowledged the claim, inspected the property, evaluated the reported damage, prepared an estimate, and timely communicated its determination. *Id.* After a public adjuster became involved, State Farm reviewed the additional information submitted and re-inspected. *Id.* After litigation commenced, State Farm's retained experts inspected the property and agreed with the two claim-stage inspections. *Id.*

Castillo argued that her extracontractual claims rested on more than a coverage disagreement, pointing out that State Farm documented no hail damage to the shingles in 2023 and then again found no covered shingle damage after the 2024 storm, contrary to her expert's findings. *Id.* at *9. The court was not persuaded, explaining that this argument demonstrated a dispute over coverage rather than evidence of bad faith. *Id.* Relying on its own prior decision in *Hall Arts Center Office, LLC v. Hanover Insurance Co.*, 327 F. Supp. 3d 979, 998 (N.D. Tex. 2018), the court held that a reasonable jury could only conclude that State Farm's reliance on two reasonably conducted inspections gave it a reasonable basis to deny payment. *Id.*

Notably, the court reached this conclusion while also holding that Castillo's expert testimony was sufficient to create a fact issue on her breach of contract claim. *Id.* at *3–6. In other words, a genuine dispute over whether hail damaged the roof did not translate into a fact issue on whether State Farm acted in bad faith by declining to pay Castillo's claim.

Most of Castillo's remaining statutory bad-faith claims also failed as a matter of law

The court's finding of a bona fide dispute was also fatal to most of Castillo's statutory bad-faith claims. The court determined that because Castillo failed to present evidence that would enable a reasonable jury to find in her favor on her claim for breach of the duty of good faith and fair dealing, her claims under Section 541.060(a)(2)(A) (failure to attempt a fair settlement once liability is reasonably clear) and Section 541.060(a)(7) (refusal to pay without a reasonable investigation) also failed. *Id.* at *9 (citing *Kim v. Nationwide Mut. Ins. Co.*, 614 F. Supp. 3d 475, 497 (N.D. Tex. 2022)).

The court also dismissed Castillo's misrepresentation claim under Section 541.060(a)(1). *Id.* at *10. The court noted that every alleged misrepresentation cited by Castillo in her pleadings—the amount of damage, the cost to repair, the cause of loss, and the amount of coverage—rested on the same theory as her common-law bad-faith claim, i.e., that State Farm had no reasonable basis to deny policy benefits. *Id.* The court further noted that an actionable misrepresentation must concern the details of the policy, not the facts giving rise to the claim, and Castillo identified no misstatement about the policy itself. *Id.*

Castillo's Section 541.060(a)(3) claim for failure to provide a reasonable explanation fared no better. State Farm's coverage letter explained that the loss did not exceed the deductible and enclosed its estimate, and Castillo offered only conclusory allegations in response. *Id.* Finally, the court dismissed Castillo's DTPA claims under Section 17.46(b) and Sections 17.50(a)(2) and (a)(3) because they arose from the same factual allegations as her common-law bad-faith claim and therefore failed for the same reasons. *Id.* at *11.

Treble and exemplary damages dismissed for lack of evidence of knowing conduct

Perhaps the most significant part of the ruling is the court's dismissal of Castillo's claims for treble and exemplary damages. Both the Insurance Code and the DTPA permit the award of up to three times actual damages if the insurer acted "knowingly," which means an actual awareness of the falsity, unfairness, or deceptiveness of the act or practice. *Id.* at *12 (citing Tex. Ins. Code §§ 541.002(1), 541.152(b); Tex. Bus. & Com. Code §§ 17.45(9), 17.50(b)(1)).

State Farm argued that Castillo had no evidence that it acted with actual awareness of any false or deceptive conduct, and the court agreed. *Id.* Castillo's petition alleged that State Farm made its misrepresentations "knowingly or recklessly" and

that all of its acts were committed knowingly and intentionally, but the court explained that the supposed misrepresentations were, in substance, coverage disputes, and that Castillo pointed to no evidence supporting her allegations of knowing conduct. *Id.* Her response brief did not address these damages claims at all. *Id.* Because Castillo did not come forward with specific evidence, the court granted summary judgment on both the treble and exemplary damages claims. *Id.*

Importantly, the court's ruling applied across the board to all of Castillo's bad-faith claims. Even though some of Castillo's statutory claims survived (discussed below), she could no longer seek treble or exemplary damages on those claims. However, it is important to note that the court's ruling turned in part on the absence of any responsive briefing or evidence on the issue; thus, a plaintiff who develops and presents evidence of actual awareness may present a closer question.

What survived

The decision was not a complete win for State Farm. The court denied summary judgment on Castillo's breach of contract claim, holding that Castillo's expert created a fact issue sufficient to survive summary judgment. Because the contract claim survived, so did Castillo's TPPCA claim for delayed payment under Sections 542.058 and 542.060. The court also allowed the Section 541.060(a)(4) claim (failure to affirm or deny coverage within a reasonable time) and the derivative DTPA claim under Section 17.50(a)(4) to proceed. *Id.* at *10–11. State Farm had not directly addressed those statutory bad-faith claims in its summary judgment briefing, and the court explained that a reasonable basis for denying a claim does not automatically resolve whether the insurer was prompt in making its determination. *Id.* (citing *Gerstman v. Crestbrook Ins. Co.*, No. 3:24-CV-0635-D, 2025 WL 1644533, at *10 (N.D. Tex. June 9, 2025)).

Conclusion

Castillo reinforces that the bona fide dispute rule remains a powerful defense to extracontractual liability in Texas first-party property cases. Competing expert opinions may be enough to send a coverage dispute to a jury, but they do not, on their own, create a fact issue on bad faith where the insurer reasonably investigated and relied on its inspections. Further, the survival of the Section 541.060(a)(4) claim highlights that insurers moving for summary judgment should address each statutory theory specifically, rather than relying on the bona fide dispute rule to dispose of claims that turn on timeliness rather than the reasonableness of the denial.

BEYOND THE BLUEBONNETS

California's New Smoke Damage Recovery Act: Shifting the Burden

by Elizabeth (Betsy) Doyle (Oakland office)

Two bills recently signed into law by Governor Newsom, enacted as the "Smoke Damage Recovery Act," may represent an inflection point in the relationship between California and insurance carriers amid escalating wildfire losses and declining insurance availability.

Background

In California's spate of recent wildfires, thousands of residential properties that survived the blaze have nevertheless been affected by smoke, soot, char, ash, and contaminants. Thousands of smoke damage insurance claims have been filed as a result. The lack of clear standards for the testing and remediation of smoke damage has prompted complaints from numerous homeowners that their insurance claims have been improperly denied, along with their requests for post-remediation testing to ensure their homes were restored to pre-loss conditions of air quality.

The enactment of the Smoke Damage Recovery Act was fast-tracked, in large part, by the June 2026 Lineage Logistics fire in Los Angeles. The Legislature declared that the Lineage fire "exposes the gaps in insurance coverage that exist in the absence of a mandatory evacuation order, even when conditions may render a home uninhabitable, and the need to modernize insurance protections for vulnerable communities facing smoke, odor, and environmental contamination as a result of complex, urban, industrial disasters. Without a mandatory evacuation order and the insurance coverages triggered thereby, residents may have no choice but to remain in their homes despite unsafe and unhealthy conditions and impacted businesses may suffer financial losses." Cal. Health & Safety Code § 25544 (a)(9)

The New Code Sections

Assembly Bill 1795, to be codified under Insurance Code Section 2060.1 and Section 2060.2, goes into effect on January 1, 2027 and will apply to claims arising from wildfires with respect to residential properties within any zip code deemed to have been in a wildfire impact zone. If smoke, ash, soot, char, or combustion byproducts are present in a surviving residential property in the impact zone after the wildfire, Section 2060.1 establishes a rebuttable presumption that smoke damage is the result of that wildfire. Insurers may rebut the presumption and prove otherwise, but they will bear the costs of doing so and must do so under tight deadlines.

A.B. 1795 also enacts Insurance Code Section 14048, which will require, as of July 1, 2029, that adjusters must be certified in order to handle smoke damage claims. The California Department of Insurance will be responsible for the development of training and certification of adjusters. Assigning an uncertified adjuster to handle a smoke damage claim will be deemed an unfair claims practice under the Insurance Code.

Assembly Bill 1642, to be codified under Insurance Code Section 2061.1 (a) classifies smoke damage as an air-quality threat and provides that additional living expense policy benefits cannot be terminated until a dwelling “has been restored to pre-loss condition and cleared for human occupancy, in accordance with the regulations or guidance described in Section 25402.3 of the Health and Safety Code … subject to the applicable policy limit.”

Takeaways

If an insurer senses that smoke damage did not arise from a wildfire in the impact zone, the new statutes place the burden on insurers to investigate and perform tests to prove it. The insurer must do this within 30 days of the notice of claim (unless site access is restricted). Regardless of the findings, any undisputed costs to restore must be paid within 30 days of the testing. Additionally, an insurer may not terminate coverage for additional living expenses (up to policy limits) until testing proves that the air quality of a residence is safe for human occupancy.

Formalizing standards for smoke damage as an air contaminant is an important development in the evolving arena of California insurers, wildfires, and state regulations. The new bills place increased burden and costs on insurers and their strategies for absorbing those remain to be seen. Stakeholders will want to monitor those developments as well as legal activity that will clarify the regulations, especially as they relate to the coming certification process for adjusters. The law goes into effect for residential claims arising after January 1, 2027, but designated new programs for training and certification for smoke damage adjusters are not required until July 1, 2029.

Of course, we will keep an eye on this as it develops as well.



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Zelle LLP | 901 Main Street Suite 4000 | Dallas, TX 75202 US

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