THE ZELLE LONESTAR LOWDOWN

Dedicated to Texas First-Party Property Claims

The Zelle Lonestar Lowdown | Tuesday, September 12, 2023 | ISSUE 5

Welcome to The Zelle Lonestar Lowdown, our monthly newsletter bringing you news from the trenches on everything related to Texas first-party property insurance claims and litigation. If you are interested in more information on any of the topics below, please reach out to the author directly. As you all know, Zelle attorneys are always interested in talking about the issues arising in our industry.

INSIDE THIS ISSUE

Upcoming Events

You don't want to miss this!

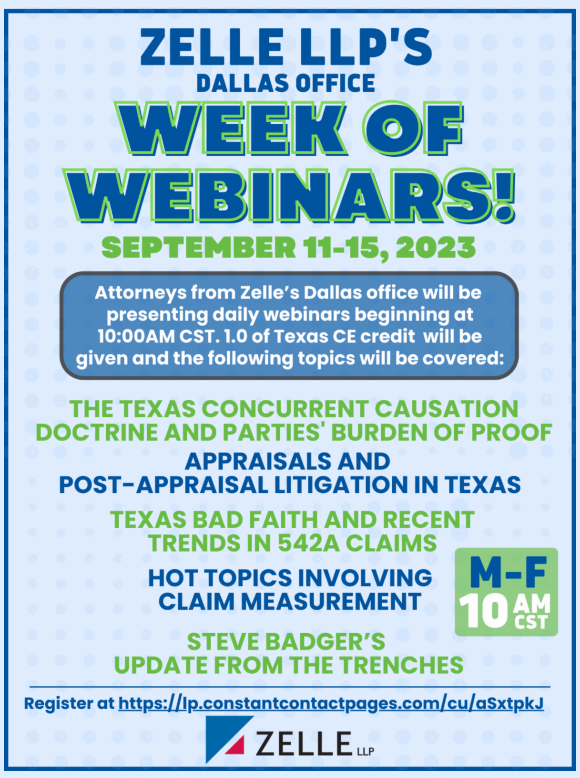
<u>September 11-15, 2023:</u> Happening Now!!

Zelle LLP's Dallas Office Week of Webinars!

There are three more courses in the Zelle LLP Dallas Office Week of Webinars. Featuring topics that are of critical importance to Texas adjusters and insurance professionals, all webinars will be offered free of charge and 1.0 of Texas CE credit will be given to all attendees for each class.

The following topics will be covered during the rest of the week:

- <u>WEDNESDAY 9/13:</u> Texas Bad Faith and Recent Trends in 542A Claims ***approved for 1.0 Ethics TX CE Credit**
- <u>THURSDAY 9/14:</u> Hot Topics Involving Claim Measurement
- <u>FRIDAY 9/15</u>: Steve Badger's Update from the Trenches



Registration Instructions: Each webinar requires separate registration.

There is no charge to attend. You will receive confirmation after your registration has been approved.

Register Here!

2024 *What The Hail?* Conference February 8-9, 2024!!

REGISTRATION IS NOW OPEN!!!

The 2024 *What The Hail?* Conference will be held on February 8-9, 2024 at the Irving Convention Center at Las Colinas in Irving, Texas. Here are the details:

Key Information

- **Cost:** $100 (inclusive of all classes/meals/events)
- **Dates:** Thursday, February 8 and Friday, February 9, 2024 - Two-day seminar format (all day Thursday/half-day Friday)
- **Location:** Irving Convention Center at Las Colinas
- **Continuing Education:** Approved for 12 hours of Texas CE credit (10 General and 2 Ethics)
- **Rooms:** The Westin Irving Convention Center. Book your rooms **here!**
- **Events:**
  - Welcome Reception Wednesday, February 7, 2024 for all attendees 6:00 pm - 9:00pm.
  - The legendary 80's Party will return on Thursday evening (February 8, 2024) at the Toyota Music Factory, with a full concert by *The Molly Ringwalds* band... and a few other special surprises.

A few sponsorship opportunities remain available! (contact abannon@zellelaw.com)

Register

September 18, 2023: Brandt Johnson will be presenting "What the Hail is Going On? Fraud in CAT Claims" on September 18, 2023 at the 2023 IASIU Annual Conference on Insurance Fraud in Dallas, TX.

September 22, 2023: Steven Badger will be presenting "Insurance and Public Policy Issues Arising From The 911 Terrorist Attack" at the Oklahoma Claims Association Annual Conference in Midwest City, Oklahoma

October 4, 2023: Steven Badger will be speaking at the PLAN Appraiser/Umpire Training Course in New Orleans, Louisiana.

October 6, 2023: Steven Badger will speaking on a panel discussion issues involving roofing and insurance at the Roofing Contactors of Texas Conference in Houston, Texas

News From the Trenches by Steve Badger

This is the place where Steve Badger gets to rant about all the issues we are dealing with in the first-party claims world. Some interesting new hot topics getting a lot of attention in the industry this month, all relating to the evolving insurance model due to climate change and abuses in the claims/appraisal/litigation process…

1. Effect of Climate Change on Insurance Availability

The Washington Post recently ran an article about climate change fueling an insurance crisis. Here is a link: **ClimateChangeArticle**. The article is spot on accurate as to what is happening -- the increased number of and severity of storm events is making it impossible for insurance companies to profitably insure risk in certain geographic locations (due to hurricanes in Florida and Louisiana, wildfires in California, etc.). As a result, we are seeing insurance companies entirely stop writing business in these states. Fortunately, we are not seeing that happen right now in Texas. Our laws have mostly worked in maintaining balance in the claims process (no AOBs, eliminating case runner public adjusters, hail litigation reform, etc.). But Texas insurance companies remain concerned. And as a result a lot of things are changing, including here in Texas. See the next five topics below.

2. Policy Form Rewrites

Insurance companies loathe changing policy terms. They want predictability. And consistency in form language provides that predictability. But sometimes they have no choice to modify policies. Over the past year, we have seen a significant increase in insurance companies coming to us for assistance in changing their policy forms. In fact, in the past two months we have done three complete policy rewrites for different companies. This is in addition to helping dozens of our clients with changes to endorsements and other policy forms dealing with ACV definitions, cosmetic damage issues, notice of claim deadlines, appraisal clause modifications, and much more. Forms that remained constant for decades are now being

changed. Why? The combination of climate change and claim/appraisal/litigation abuse are leaving the industry with no other choice.

3. “Indemnity Only” Insurance

Under the traditional model, insurance companies initially issue an actual cash value payment followed by a replacement cost value payment after the work is completed. The initial ACV payment has always been a monetary payment sent by the insurance company without regard to whether any work was actually performed. This results in large amounts of cash floating around after any insured event, especially a major CAT. And that predictably leads to the influx of third-parties hell bent on getting their hands on a portion of that cash in an effort to “win the storm”. Some of these third-parties are professionals, such as reputable public adjusters who truly want to assist the insured. But others are not. Their objective is to somehow inject themselves into the claims process to bleed a little of that money into their own pockets. And when this happens the insured suffers, as there is not enough money remaining to complete the required work. To combat this, some insurers are considering a radical change to the historical insurance process -- no more ACV payments. These insurers are considering going to a pure “indemnity only” model. When work is done and the repairs are made, the insured advises of the cost and the insurance company sends in a reimbursement check. No cash is ever floating around. Insurance companies have no *obligation* to make an ACV payment, but have the *option* to issue a discretionary advance payment if it is shown that the insured needs money to fund construction work. Watch for more on this significant issue in the months ahead.

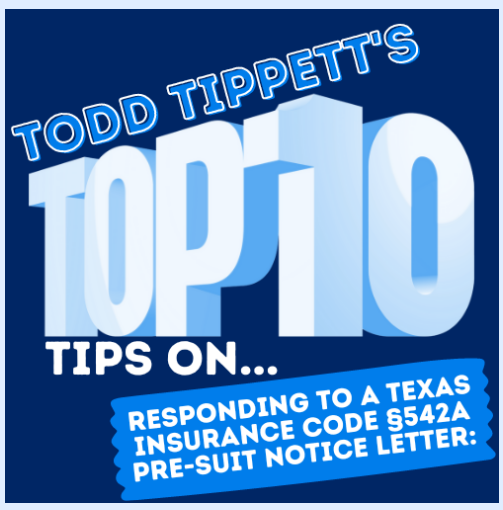
4. Preferred Contractor Programs

I have been saying it for years to every contractor group I speak to -- you are killing your golden goose and the insurance industry is going to respond to your abuses with managed repair and preferred contractor programs. And it is absolutely happening. No, not all managed repair programs in the past have been perfect. But the industry is getting smarter. I am seeing more preferred contractor programs that are fair to all parties in ensuring that damaged property is repaired quickly, correctly, and for a reasonable price. An outcome that is successfully serving the best interests of the contractor, the insurance company, and the insured. And as a result of this success we are being asked to help insurers in drafting policy forms using these programs.

5. Invoking The Right To Repair

Insurance companies always have had a provision in their policies giving them the right to actually step in and have damaged property repaired. But insurance companies seldom invoked this right. They would rather pay to fix damage than take on the responsibility of fixing it themselves. Well, not any more. Some of our clients are realizing they can engage a reputable contractor who will do the job quickly, correctly, and for a fair price. With this approach, all of the usual arguments with the insured’s contractor go away. No more fighting about various Xactimate line items, including GCOP, supervision, harnesses, toilets, etc., and then dealing with the inevitable contractor-driven appraisal demand. The work gets done (and done right). The claim is finally resolved.

Obviously, all of these topics are reactions to both the increase in claims due to climate change and, just as importantly, the abuses insurers are dealing with in the claims/appraisal/litigation process. Change is coming.



Todd Tippett's

Top 10 Tips on...

Responding to a Texas Insurance Code §542A Pre-Suit Notice Letter:

1.Always respond within 60 days of the date of the letter.

2. Ensure the letter clearly states a “specific amount alleged to be owed” under the policy.

3. Ensure that the insured was provided with a copy of the letter.

Eastern District Upholds Heightened Pleading Standard to Insured’s Prompt Payment Claim

by Megan Zeller

While Federal courts have routinely applied heightened pleading standards to fraud complaints under Federal Rules of Civil Procedure 9(b),**[1]** in recent years we have witnessed some federal courts expand this heightened standard to § 541 violations of the Insurance Code for misrepresentation allegations when they are “substantively identical to fraud.” *See, e.g.*, *Carter v. Nationwide Prop. and Cas. Ins. Co.*, No. H–11–561, 2011 WL 2193385, at *1 (S.D. Tex. June 6, 2011) (citing *Berry v. Indianapolis Life Ins. Co.*, 608 F.Supp.2d 785, 789, 800 (N.D. Tex. 2009)). Last month, the United States District Court of Texas Eastern District, Sherman Division held that an insured failed to properly meet the heightened pleading standards not only for **all** of her § 541 violations of the Insurance Code, but also for her allegations of violations of the Texas Prompt Payment of Claims Act (“**TPPCA**”) under Fed. R. Civ. P. 9(b) and 8(a).**[2]**

In **Ruby Elevera v. State Farm Lloyds, No. 4:22-cv-867-SDJ-KPJ (E.D. Tex. August 2, 2023),** the insured originally filed suit in state court for a purported leak caused by freezing and alleged the following causes of action against the insured: breach of contract, violations of §§ 541 and 542 of the Insurance Code, and breach of the common law duty for good faith and fair dealing. Shortly

4. Ensure the letter separately provides an amount of reasonable and necessary attorneys' fees incurred by the insured.

5. Provide a detailed and accurate statement of facts outlining the history of the claim and the payments made, if any.

6. Identify the pertinent policy provisions that impact coverage for the claim.

7. Decide whether to request an inspection of the loss location within 30 days after receiving the 542A Notice Letter.

8. Evaluate whether to accept liability for any agent's acts or omissions related to the investigation and/or adjustment of the claim.

9. Respond to each allegation of a bad act, omission or wrongdoing related to the claim.

10. If plaintiff failed to issue a proper letter or if a lawsuit was filed less than 61 days after sending the letter, consider seeking a Motion to Abate and/or Motion to Preclude Attorneys' Fees within 30 days of filing an Answer to the lawsuit.

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.

thereafter, the insurer removed the case to federal court and filed a Motion to Dismiss for Failure to State a Claim Pursuant to Fed. R. Civ. P. 12(b)(6), 9(b) and 8(a) (the "Motion"). In the Motion, the insurer argued that "Plaintiff's claims for violations of the Insurance Code/DTPA [ ] based on alleged misrepresentations are subject to the heightened pleading requirements for fraud claims set out in [Federal Rule of Civil Procedure] 9(b)" and that the insured failed to provide any factual allegations to support her claims. The insurer also argued that the insured's other claims that are not related to fraud – including the insured's TTPCA claim – are not sufficient under Fed. R. Civ. P. 8(a).

Agreeing with the insured, the Eastern District found that the insured's misrepresentation claims under **§ 541** of the Insurance Code "largely track statutory language and are conclusory assertions" and therefore fail under the heightened standard of Fed. R. Civ. P. 9(b). The Eastern District then went one step further and found that Plaintiff's § 541 allegations that "do not sound in fraud" also fail under Fed. R. Civ. P. 8(a) because these allegations are "threadbare, conclusory allegations without any meaningful support" and the insured failed to allege key facts, such as "how the insurer's liability became reasonably clear, how the affirming or denial of coverage was not within a reasonable time, and how the investigation was not reasonable."

The Eastern District then applied this reasoning to the insured's TPPCA claim and found that the insured failed to meet the pleading standard under Fed. R. Civ. P. 8(a). Specifically, the Eastern District found that conclusory assertions do not show when the insurer acknowledged the claim, when the insured responded to any attempts at contact of submitted any requested information, or when the insured made or did not make any claim payments. As such, the Eastern District found that the insured failed to plead any facts that the insurer agreed to pay part or all of her claim as required by § 542.057(a) to trigger the insurer's obligation under TPPCA, and therefore, the insured failed to plead her TPPCA claim under Fed. R. Civ. P. 8(a).

Notably, the Eastern District also applied Fed. R. Civ. P. 8(a) to determine that the insured failed to state a good faith and fair dealing claim. Once again, the Eastern District found that conclusory assertions that only rely on differences between an insured's estimate and an insurer's estimate does not demonstrate bad faith.

While it remains to be seen how other federal courts will apply this ruling, ***Ruby Elevera*** is a good example of how aggressive litigating can help minimize and ultimately throw out an insured's unsupported bad faith claims.

[1] Fed. R. Civ. P. 9(b) requires that all allegations of fraud or mistake "shall be stated with particularity."

[2] Fed. R. Civ. P. 8(a) requires a short and plain statement of the claim showing that the pleader is entitled to relief.

AI Update

NAIC Releases Highly-Anticipated Draft Bulletin Addressing Insurer Use of Artificial Intelligence Systems

by **Jennifer Gibbs**

On July 17, the National Association of Insurance Commissioners ("NAIC") released the Exposure Draft of the Model Bulletin on the Use of Algorithms, Predictive Models, and Artificial Intelligence Systems ("AIS") by Insurers.

The draft Bulletin encourages insurers to adopt a written AIS program. As part of an AIS program, insurers are asked to address their standards for the acquisition of, use of or reliance on AI systems developed or deployed by third parties. Insurers should ideally include terms in contracts with third parties that: "(i) require third-party data and model vendors and AI system developers to have and maintain an AIS program commensurate with the standards expected of the insurer, (ii) entitle the insurer to audit the

third-party vendor for compliance, (iii) entitle the insurer to receive audit reports by qualified auditing entities confirming the third party's compliance with standards, and (iv) require the third party to cooperate with regulatory inquiries and investigation related to the insurer's use of the third party's product or services and require the third party to cooperate with the insurer's regulators as part of the investigation or examination of the insurer." *See* **https://content.naic.org/sites/default/files/national_meeting/07.17.23%20Exposure%20Draft%20AI%20Model%20Bulletin_0.pdf**

The draft bulletin, however, is not a model law or regulation, but is proposed as a template communication for insurance regulators and is intended to strike a balance between supporting innovative technology while protecting consumers from possible harms related to AIS, such as discrimination and bias.

NAIC is accepting written comments regarding the draft Bulletin through September 5, 2023.

After Appraisal and Interest Payment: Court Finds that Attorneys' Fees & TPPCA Interest Do Not Constitute an Independent Injury

by **Brandt Johnson**, **Ashley Pedigo**, and **Mariana Best**

Most recently, another Texas federal court joined the growing consensus that an insurer's prompt payment of a full appraisal award and accompanying statutory interest precludes the recovery of attorneys' fees from an insurer. In this case, the United States District Court for the Northern District of Texas recently took it one step further, finding that additional interest and attorneys' fees do not constitute an independent injury that entitles an insurer to further recovery. This ruling is consistent with recent decisions from other Texas federal district courts and two Texas appellate courts all holding that attorneys' fees are not recoverable post appraisal when the appraisal award and statutory penalty interest are paid. As discussed in recent editions of *The Lonestar Lowdown*, the Fifth Circuit Court of Appeals has certified this issue for determination by the Texas Supreme Court.

In *McCall v. State Farm Lloyds*, No. 3:22-CV-1712-B, 2023 WL 5311485, at *4 (N.D. Tex. Aug. 17, 2023), the court joined several other federal courts by rejecting an insured's claim for attorney's fees and additional interest under the Texas Prompt Payment of Claims Act ("TPPCA") after the insurer tendered payment of the appraisal award and potential interest under the TPPCA.

The court cited and relied upon the Texas Supreme Court's analysis in **Ortiz v. State Farm Lloyds, 589 S.W.3d 127, 133 (Tex. 2019).** Based on *Ortiz*, the court found that State Farm was entitled to summary judgment on the breach of contract claim after it paid the appraisal award in full. The court reiterated that an appraisal does not determine the rights and liabilities of the parties. Therefore, State Farm's payment of the award did not reflect State Farm's liability under the claim and, in fact, State Farm explicitly denied any liability when issuing the appraisal award payment.

The insured did not necessarily dispute this well-established law, rather the insured argued that she was entitled to her reasonable attorney's fees. The Court found her argument unconvincing. Accordingly, the *McCall* court held that the insured could no longer show that she was entitled to actual damages, preventing the insured from prevailing on her breach-of-contract claim

Next, the court determined that by paying the appraisal award plus interest, State Farm foreclosed any argument that the insured was entitled to additional damages over and above what had been paid. It is well established that attorney's fees, although compensatory, are not damages. *Ortiz*, 589 S.W.3d at 134. Relying again on the analysis in *Ortiz*, the *McCall* court recognized that without actual damages, the insured cannot prevail on a breach of contract claim and, therefore, recover attorney's fees.
In reaching this conclusion, the court presented the following hypothetical: even if the insured could show she prevailed on her claim—which she cannot— and was entitled to attorney's fees under Texas Civil Practices and Remedies Code Section 38.001 and Texas Insurance Code Sections 541 and 542, she would nonetheless be entitled to nothing in this case. Section 542A.007 of the Texas Insurance Code allows the insured to recover the lesser of either: (1) the amount of attorney's fees supported at trial; (2) the amount of attorney's fees that may be awarded under the law; or (3) the amount calculated by dividing the amount to be awarded in the judgment to the insured by the amount alleged to be owed for that claim and then multiply this number by the amount of fees supported at trial. In this scenario, the insured is not entitled to any judgment award, as State Farm has already paid the full amount of benefits owed. Therefore, because zero will always be "the lesser of", the insured is not entitled to fees under section 542A of the Texas Insurance Code.

The *McCall* court next turned to the insured's extra-contractual claims based on alleged violations of Chapters 541 and 542 of the Texas Insurance Code, violations of the Texas Deceptive Trade Practices Act, bad faith insurance practices, and fraud. For these extra-contractual claims, the insured maintained that she was owed attorneys' fees and additional TPPCA interest. In addressing these claims, the *McCall* court went a step further than previous cases addressing the recoverability of attorneys' fees.

The court addressed the insured's argument that she was legally entitled to the recovery of attorney's fees, not under the Texas Insurance Code, but **as actual damages**. The court rejected this argument, finding that the insured failed to show that she suffered an

injury independent of the benefits owed under her insurance policy. Citing *USAA Texas Lloyds Co. v. Menchaca*, 545 S.W.3d 479, 490 (Tex. 2018), the court found that the insured provided no evidence that she sustained damages other than the amount identified by the appraisal award and the insured's extra-contractual claims, which were based solely on State Farm's alleged mishandling of the claim.

The general rule is that an insured cannot recover policy benefits as extra-contractual damages if no additional benefits are owed under the policy. Because the amount of loss had been determined by appraisal and paid by State Farm, the insured did not sustain any damages that could allow her to maintain any of her pleaded extra-contractual causes of action. The court found that the insured did not seek (and had no evidence of) any injury independent of her claim for policy benefits. In doing so, the Court confirmed that attorney's fees are not an independent injury. What's more, State Farm's payment of the appraisal award, plus any potential statutory penalty interest under the Texas Prompt Payment of Claims Act which was paid the same day as the award, bars the insured's claim for any additional interest.
Accordingly, because (1) the insured failed to establish an independent injury to sustain her extra-contractual claims, and (2) the insurer had paid above the interest that could be owed, the Court granted the insurer's motion for summary judgment on the insured's extra-contractual claims.

The *McCall* decision reaffirms that growing consensus that an insurer's payment of an appraisal award, coupled with a preemptive payment of all TPPCA statutory interest potentially owed, absolves an insurer's liability and precludes an insured from additional recovery. But more importantly, the *McCall* serves to remove another legal avenue of recovery for a policyholder after an appraisal award and potential interest has been paid. This same analysis is likely to similarly apply to public adjuster fees that an insured claims are recoverable. To date, Texas courts have "yet to encounter" an instance of a truly independent injury in this type of dispute. *Id.* at 499.
This case affirms that attorneys' fees and interest are not independent injuries and arguments to the contrary ignore well-settled Texas case law. Nevertheless, as noted in our last issue of *The Lonestar Lowdown*, the Texas Supreme Court will soon be confronted with answering the following:

> In an action under Chapter 542A of the Texas Prompt Payment of Claims Act, does an insurer's payment of the full appraisal award plus any possible statutory interest preclude recovery of attorney's fees?

Although it is uncertain if the Court will explicitly address whether an independent injury claim remains a viable option for an insured to seek additional recovery after an appraisal award and potential interest has been paid, the growing consensus among courts provides a great weight of authority for the Court to review, and in the interim, serves to deter the commencement or continuation of frivolous suits after appraisal has been invoked.

Move it On Back - Court Enforces New York Forum Selection Clause

by **Bella Arciba**

Many carriers include forum selection clauses in their policies. Despite these clauses, policyholders continue to file lawsuits in different courts in attempt to escape the contractually chosen forum. Their efforts have mixed results with courts more often siding with the venue the parties chose when the policy was written.

Recently, the United States District Court of Texas Southern District, Houston Division enforced a forum selection clause that chose New York as the venue, holding that a forum selection clause will be enforced if public-interest factors do not rise to the level of making it an "exceptional case" to render the clause unenforceable.

In **US Rubber Corporation v. Mt. Hawley Insurance Co., No. H-23-2104 (S.D. Tex. August 25, 2023)**, the insurer and the policyholder executed a renewal policy, which included a "Legal Action Conditions Endorsement." This endorsement was identical to the previous policy's Legal Action Conditions Endorsement. The endorsement stated that any litigation commenced against the insurer shall be initiated in New York. The policyholder's property was damaged by a storm, and the insurer paid for part of the damage but denied coverage for the rest. Despite the forum selection clause, the policyholder filed suit for breach of contract in Texas.

The insurer filed a Motion to Transfer Venue pursuant to the forum selection clause. The policyholder argued that the forum selection clause was invalid and unenforceable, asserting the clause was included after the parties executed the renewal policy and the clause weighed against public-interest.

The court determined that the forum selection clause in the renewal policy was referenced by the same title as the prior policy and the policyholder specifically recognized any changed endorsements during the negotiations. Further, the renewal

Spotlight:

On August 30, 2023 **Brandt Johnson** presented **"How Golf Can Teach Adjusters Stronger Good-Faith Claim Handling Skills"** with co-presenters Annette Tarquinio (Engle Martin) and Jeromy Fielder (JS Held) to Engle Martin.

On September 11, 2023 **Steve Badger**

quote stated the clause was available upon request, giving the policyholder access to verify the clause. The court determined that the clause was valid because the insurer gave the policyholder notice that the clause was unchanged, indicating the policyholder knew about the forum selection clause since it was in the previous policy. And the policyholder could have easily verified the clause upon request.

The policyholder further argued the forum selection clause should not be enforced because the public-interest factors weighed against enforcement. The court disagreed, holding that a valid forum selection clause will be enforced “in all but the most exceptional cases.”

The policyholder argued the “court congestion factor” weighed against the transfer because the Southern District of New York had five thousand more civil cases than this district. But the court determined that the court congestion factor did not weigh against the transfer because the Southern District of New York has more district judges, and more civil cases per judge.

Further, the policyholder argued that the “local interest factor” weighed against the transfer since Texas courts have an interest in resolving disputes over Texas property. The policyholder also argued the “jury duty burden factor” weighed against the transfer since the case lacked a connection to the Southern District of New York or its citizens. The court agreed that both factors weighed against the transfer; however, the court determined that the factors did not rise to the level of an exceptional case, holding the forum selection clause enforceable.

Going forward, carriers should continue to seek enforcement of their forum selection clauses by Texas courts. Forum selection clauses provide carriers with predictability by allowing the carrier to choose a forum that is convenient and appropriate for its business. Ultimately, a valid forum selection clause will be enforced “in all but the most exceptional cases,” and factors weighing against a transfer do not automatically rise to the level of “exceptional cases.” Above all, this opinion clarifies that policyholders must meet a heavy burden to avoid enforcement of a forum selection clause.

presented **"Insurance and Public Policy Issues Arising From The 911 Terrorist Attack"** for DFW Women in Property Insurance Group.

Reach out to Zelle LLP if your organization would benefit from a presentation, class, discussion, or seminar from one of our attorneys.

Contact Us!

Thank you for reading this issue of The Zelle Lonestar Lowdown!

Visit our website to view all previous issues of The Zelle Lonestar Lowdown!

The Lonestar Lowdown All Issues

For more information on any of the topics covered in this issue, or for any questions in general, feel free to reach out to any of our attorneys. Visit our website for contact information for all Zelle attorneys at zellelaw.com/attorneys.

Follow us on social media to keep up with all Zelle updates!

Visit our Website

Join The Zelle Lonestar Lowdown mailing list!

Sign me up!

ZELLE LLP

If you would like to be taken off this distribution list without unsubscribing from all Zelle emails and updates, please click here.