

Western Loss 2016 Fall Conference

Estimating the Value of the Appraisal Process in Property Claims

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BOSTON | DALLAS | LONDON | MIAMI | MINNEAPOLIS
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10,000 Foot View of Appraisal

- Contained in Policy Provision
- Required by statute
- Appraisal vs. Arbitration
- Concept of “valuation”



Appraisal “Pop Quiz”



Appraisal “Pop Quiz” #1

What if the policyholder wants to appraise the loss, but the insurer does not?

Too Bad!

Appraisal “Pop Quiz”

#2

Can appraisal resolve disagreements about:

- Whether there is property damage at all,
- The cause or extent of property damage, or
- Whether the loss occurred during the policy period?



YES...BUT IT DEPENDS!

Appraisal “Pop Quiz” #3

Should you go to appraisal if there are disagreements about ...

- Whether there is property damage at all,
- The cause or extent of property damage, or
- Whether the loss occurred during the policy period?

Try to Avoid It

Appraisal “Pop Quiz” #4

What is the standard for selecting the appraisers?

**COMPETENT
AND
IMPARTIAL**

Appraisal “Pop Quiz” #5

Will the Umpire who ultimately decides the amount of loss be familiar with the type of damage at issue?

Good Luck 

What is Appraisal?

- **Majority** = scope is amount of loss only.
- **Minority** = scope includes coverage and/or causation issues.

Appraisal Pros & Cons

PROS

1. Informal and economic alternative
2. Appraisal panels are generally more capable of accurately evaluating damage
3. Juries may award higher damages
4. Timely payment of appraisal award provides protection against extra-contractual claims

Appraisal Pros & Cons

CONS

1. Ill-defined process with very few rules
2. No record or transcript from which to appeal
3. Sometimes looks like informal “litigation”
4. Burden of proof to overturn an appraisal award is high (fraud, accident or mistake)
5. Appraisal award could be greater than the damages claimed by the insured

Common Appraisal Provision- Commercial

2. Appraisal

If we and you disagree on the **amount of loss**, **either may make written demand** for an appraisal of the loss. In this event, each party will select a **competent and impartial appraiser**. The two appraisers will select an umpire. If they cannot agree, **either may request that selection be made by a judge of a court having jurisdiction**. The appraisers will state separately the amount of loss. If they fail to agree, they will submit their differences to the umpire. A decision agreed to by any two will be **binding**. Each party will:

- (a) Pay its chosen appraiser; and
- (b) Bear the other expenses of the appraisal and umpire equally.

If there is an appraisal, we will still retain our right to deny the claim.

Appraisal in a Perfect World

1. The parties agree on the scope of coverage, but disagree on the value of the loss.
2. One party demands appraisal.
3. Both parties promptly name appraisers.
4. The two appraisers each value the loss, and attempt to reach an agreement.
5. If they cannot agree, the appraisers select an umpire to settle the dispute.
6. The parties jointly ask a court to appoint an umpire if the appraisers cannot agree on one.
7. The umpire makes an independent evaluation, and with the agreement of one of the appraisers, sets the value.

The Reality

- Non-judicial dispute resolution process
- No court supervision
- No rules of procedure or ethical guidelines
- Emerging industry of “professional appraisers” / advocates for insured
- Profit of process participants often more important than proper policy application
- Abuse, manipulation, and outright fraud common
- **A process run amok!**

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Possible Issues in Appraisal

1. **“Amount of loss”**
 - Scope of appraisal
 - What issues are appraisable vs. what must be resolved in court
2. **“Either [party] may make written demand”**
 - You might be compelled to appraisal
 - Waiver of right to demand appraisal
3. **“Competent and impartial appraiser”**
 - Incompetent or biased appraisers
4. **“Umpire”**
 - Incompetent or biased umpire
 - Procedure for appointing an umpire when appraisers disagree
5. **“A decision agreed to by any two will be binding”**
 - Grounds for challenging an appraisal award

Issue 1: Scope of Appraisal

- What is the “scope” of appraisal?
 - Actual cash value of the property
 - Cost to repair or replace the property
 - Business income lost as a result of covered property damage
 - “Extra expense” covered by the policy
- Does it include disputes over coverage, causation and liability?

Scope of Appraisal

Causation is for the Appraisal Panel

– ***State Farm Lloyds v. Johnson* (Tex. 2009)**

– Covered hail damage

– Issues:

Whether “amount of loss” in an appraisal clause includes the *extent of loss*, and

Whether the insured can compel the insurer to appraisal on such an issue?



Scope of Appraisal



Causation is for the Appraisal Panel

- ***Auto-Owners Ins. Co. v. Summit Park Townhome Assoc.*, 100 F. Supp. 3d 1099 (D. Colo. 2015).**
 - “I agree with the [Colorado state trial court decisions] allowing appraisers to address issues of causation.”
 - Appraisers allowed to decide cause of loss (what damage, if any, was caused by 2013 hail storm, events predating policy period or excluded defective workmanship).
- ***El Toledo, LLC v. Sequoia Ins. Co.*, 2015 WL 3457475 (D. Colo. May 29, 2015).**
 - Panel “also authorized to resolve issues of causation. To the extent that the appraisers might disagree as to whether certain damage was actually caused by the June 6, 2012 hail storm, the umpire is responsible for impartially resolving such disputes.”

Scope of Appraisal



Causation is for the Appraisal Panel

- ***Quade v. Secura Ins.*, 814 N.W.2d 703 (Minn. 2012).**
 - Liability and coverage issues are for the Court, but determining the “amount of loss” includes identifying the cause of the loss, and that is for the appraisal panel. Parties can challenge causation-related coverage issues post-appraisal, with the Court.
- ***Creekwood Rental Townhomes v. Kiln Underwriting*, 11 F.Supp.3d 909 (D. Minn. 2014 (Tunheim)).**
 - Where panel award was for “cause . . . storm – wind and hail,” causation finding was binding on court and insurer’s coverage challenge was rejected.

Scope of Appraisal



Coverage issues are reserved for the Court

- ***Summit Park*, 100 F. Supp. 3d 1099 (D. Colo. 2015)**
 - “[L]egal determinations, including regarding coverage, are clearly outside the scope of the appraisal process” and may be challenged in court proceedings.
 - Causation is not a coverage issue.
- ***Laredo Landing Owners Ass'n, Inc. v. Sequoia Ins. Co.*, 2015 WL 3619205, at *2 (D. Colo. June 10, 2015)**
 - “[W]hile the appraisal process will likely result in a binding determination as to the amount of loss—including any issues as to causation . . . the parties may need to resume this action to resolve issues outside the scope of the appraisal”.

Scope of Appraisal



Matching is Decided by Whom?

- ***Summit Park*, 100 F. Supp. 3d 1099 (D. Colo. 2015)**
 - Can appraisal determine whether the policy requires insurer to pay to replace undamaged property (siding) in order to achieve “matching” or “visual consistency” with the damaged property that was replaced?
 - “This is a clear example of a coverage issue beyond the scope of appraisal.”

Scope of Appraisal



Matching is Decided by Whom?

- It was within the scope of appraisal panel's authority to determine that comparable material and quality required replacement of undamaged siding to make a color match (where panel used the correct legal standard of "reasonable" match, not identical match). *Cedar Bluff Townhome Condo. Ass'n. v. American Family*, 857 N.W.2d 290 (Minn. 2014).

Practical Tips

1. **If possible, avoid appraisal when there are pure liability disputes.**
2. **BEFORE entering into appraisal, seek advice from counsel who understands the process.**
3. **Pay attention throughout appraisal process.**
4. **If unable to avoid appraisal, have the appraisal panel itemize the damages, to better separate damages and causation issues.**
 - *Summit Park*, 100 F. Supp. 3d 1099 (D. Colo. 2015): “The appraisals should separately calculate and identify disputed costs so that the Court can either include or exclude them once it has determined whether the policy provides coverage for them. ... For example, the appraisals should address the cost of replacing undamaged property to achieve matching.”

Practical Tips

- 5. Ask appraisal panel to state whether and to what extent it considered causation issues.**

Examples...

“This appraisal award does not address the cause of loss but only the amount to restore the building to its original condition.”

“This appraisal award does not address whether the hail damage was caused by the 2012 storm or a previous hail event.”

“This appraisal award does not take into consideration any coverage questions but only the amount to repair the damaged property.”

Issue 2: “Either [Party] May Make Written Demand”

- **Appraisal May Be Compelled**
 - ***Giulietti v. Connecticut Ins. Placement Facility* (Conn. 1987)**
 - Despite denial of coverage, insurance company compelled to proceed with appraisal.
 - ***Carbonneau v. Am. Fam. Mut. Ins. Co.* (D. Ariz. 2006)**
 - What repairs were necessary to repair storm damage, not a coverage question.
 - The court favored appraisal and granted motion to compel.
- **The right to compel appraisal is generally a two-way street.**

“Either [Party] May Make Written Demand”



1. Reasonable Period

- ***Laredo Landing Owners Ass'n, Inc. v. Sequoia Ins. Co., 2015 WL 3619205 (D. Colo. June 10, 2015)***
 - Insurer demanded appraisal on amount of damage caused by hail storm less than 2 months after insured filed suit for breach of contract and bad faith;
 - Insurer continued to assert its right to demand an appraisal;
 - Insurer filed motion to compel appraisal 7 months after insured filed suit;
 - Granted. No unreasonable delay and insurer did not waive its rights under the appraisal provision.

“Either [Party] May Make Written Demand”



2. Denial of liability under the policy

- ***Laredo Landing*, 2015 WL 3619205 (D. Colo. June 10, 2015)**
 - “The denial by an insurer of all liability under a policy is a waiver of the right to an appraisal.”

3. Repairs

- ***Rooftop Roofing, Inc. v. Fire Ins. Exchange*, No. 10CV243 (Elbert County, Colo. Dist. Ct. Apr. 8, 2011)**
 - Insurer compelled to appraisal even after insured had fixed the damage following insurer’s earlier refusal to participate in appraisal.
 - No waiver; not impossible

Practical Tips

1. Know your jurisdiction's scope of appraisal.
2. Seek appraisal early.
3. Think before you deny.

Issue 3: The “Competent and Impartial” Appraiser



Issue 3: The “Competent and Impartial” Appraiser

- Competent – *pretty much anyone*
 - “Competence is not synonymous with neutrality or independence”
 - Public adjusters, contractors, professional appraisers, attorneys, etc. all considered competent
- Impartial – *not entirely clear*
 - Insured’s public adjuster might still be disinterested
 - No financial stake in award
 - Biased in favor of party (frequency of use)

Issue 3: The “Competent and Impartial” Appraiser



COLORADO
Department of
Regulatory Agencies
Division of Insurance

Bulletin No. B-5.26

Requirements Related to Disputed Claims Subject to Appraisal

- Appraisers must be “fair and competent”
 - Not a party to the insurance contract;
 - **No financial interest** in outcome of the appraisal;
 - Not a current employee of the insurer or policyholder; and
 - Not a family member or an individual with whom the insured has a personal relationship that could reasonably suggest bias.

The “Competent and Impartial” Appraiser



COLORADO
Department of
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Division of Insurance

Bulletin No. B-5.26

Requirements Related to Disputed Claims Subject to Appraisal

“An appraiser ... may not have a **direct material interest** in the amounts determined by the appraisal process. The appraiser **must disclose** to all parties any known facts that a reasonable person would consider likely to affect an appraiser’s interest in the amounts determined by the appraisal process, including any contingency arrangement related to payment of the appraiser.”

The “Competent and Impartial” Appraiser

What to look for:

- Financial interest in outcome of appraisal
- Prior employment as appraiser for insurer
- Public adjuster as an appraiser
- Lack of expertise in a specific area

The “Competent and Impartial” Appraiser



Case: 4:10-cv-00891 CDP Doc. #: 151 Filed: 08/21/12 Page: 1 of 31 PageID #: 6371

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MISSOURI
EASTERN DIVISION

TAMKO BUILDING

An appraiser can be “interested” when:

- “frequently or habitually employed by insurers ... and ...by his conduct he is acting in their interests”

INSURANCE COMPANY,

Defendant.

An appraiser can be “interested” when:

- seeks advice from insurer on who should be the umpire
- submits a draft presentation for appraisal hiring insurer to review
- seeks approval from insurer on whether to agree to amount calculated by umpire

insurance policy with defendant Factory Mutual Insurance Company, and it

submitted a claim for the damages it allegedly suffered during the shutdown

An appraiser can be “interested” when:

- works on 26 matters for insurer in one year
- has a 9% interest in accounting firm that gains 7% of its business from the insurer

Based on the undisputed evidence before me, I conclude that the loss here is

covered by the policy, and so TAMKO is entitled to summary judgment on the

The “Competent and Impartial” Appraiser



Appraiser with a financial interest in the outcome of the appraisal is not impartial.

Colorado Hosp. Servs. Inc. v. Owners Ins, Co., 2015 WL 4245821 (D. Colo. July 14, 2015)

- Fee schedule of insured’s appraiser: \$200/hour, with a cap at 5% of the RCV of the final claim if an umpire was involved
- “An expert whose fee might be materially affected by the opinion he expresses cannot be considered to be ‘impartial’ under any reasonable definition of that term.”

The “Competent and Impartial” Appraiser



Appraiser with substantial business relationships with a party and its lawyers is not impartial.

Axis Surplus Ins. Co. v. City Center West LP, No. 2015CV30453 (Weld County, Colo. Dist. Ct. March 14, 2016)

- Insured’s appraiser (George Keys) disqualified because of “known, existing and substantial relationship” with insured and its lawyers.
 - “This information is sufficient to cause a reasonable person to conclude the [appraiser] is predisposed to favor” the insured.
 - “What is even more troubling is that Keys chose not to disclose this information.” The nondisclosure raised suspicions about his impartiality.

The “Competent and Impartial” Appraiser



Appraiser with significant business relationships with party’s lawyers is not impartial.

Auto-Owners Ins. Co. v. Summit Park Townhome Assoc., 2016 WL 1321507 (D. Colo. April 5, 2016) & 2016 WL 4132186 (Aug. 1, 2016)

- Insurer paid appraisal award under a full reservation of rights and moved to recoup appraisal award on grounds that insured’s appraiser (George Keys) was not impartial as required under the policy.
- Merlin and/or Merlin attorneys have served as Keys' personal counsel, served as incorporator and registered agent for Keys' companies, taught with Keys, and donated to a Keys-led group involved in pro-policyholder lobbying.
- Keys’ fee agreement capped his fees and expenses at 10% of insured’s recovery
- Keys “cannot be considered impartial.”
- **Vacated**
- **Insured’s counsel acted in bad faith; attorney’s fees awarded**

Practical Tips

1. Be wary of the other party's appraiser.
2. Make sure appraisers know what is expected of them.
3. Explore potential relationships between the appraisers and the umpire.
4. Avoid frequent retention of the same appraiser.
5. Use "Appraisal Team"
 - Independent adjuster as appraiser
 - Various experts to support appraiser

Issue 4: The Umpire

- The most important aspect of appraisal
- Objective, professional and fair
- Expertise on the particular subject matter involved is generally not required

Issue 4: The Umpire



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Requirements Related to Disputed Claims Subject to Appraisal

Umpire must be “fair, competent and impartial”

- May not have existing direct and/or material relationship with any party and must remain neutral
- Must disclose known facts that would be likely to affect impartiality

The umpire must disclose to all parties in the appraisal process, any known facts that a reasonable person would consider likely to affect the impartiality of the umpire including:

- (a) A financial or personal interest in the outcome of the appraisal; and
- (b) A current or previous relationship with any of the parties to the agreement to appraise or the appraisal proceeding, their counsel or representatives, including licensed public adjusters, a witness, or another appraiser.

Expertise on the particular subject matter involved is generally not required



Issue 4: The Umpire

Possible Umpire Candidates

Mediators/Retired Judges

Pros: fair/impartial/understand legal issues/
won't accept manipulation or abuse

Cons: “split the baby” approach

Construction/Design Experts

Pros: awareness of issues/actual costs

Cons: possibly aligned with one party/position

The Umpire

BEWARE!!!

It is permissible in some jurisdictions to unilaterally seek the appointment of an umpire

Recommendations:

- Get agreement of appraisers to jointly seek appointment
- Advise that represented by counsel and that rules of civil procedure/ethical guidelines require notice to counsel of any court filings

With the Wrong Umpire....

Insurer's Valuation=
\$44,000

Policyholder's
Valuation=
\$414,000

Appraisal Award=
\$592,490



APPRAISAL AWARD

<u>Insured</u>	<u>Insurance Company</u>
Name: _____	Name: _____
Street: _____	Street: _____
City: _____	City: _____
CAUSE OF LOSS: <u>NAIL</u>	DATE OF LOSS: <u>6/21/04</u>
CLAIM NUMBER: <u>348 FL 7894</u>	POLICY NUMBER: _____
PROPERTY DESCRIPTION/ADDRESS: _____	

This acknowledges that Lee Taylor has been appointed to act as umpire in accord with policy provisions.

DATE: 12-13-2005 APPRAISER: Joe Sanders
 DATE: 12/13/05 ~~APPRaiser~~ Judge

ITEM	LOSS (R/C)	LOSS (ACT)
1) INSTALL FRANK OVER EXISTING ROOF FOR LEAKAGE	\$ 131,252 ⁰⁰	\$ N/A
2) INSTALL INSULATION BETWEEN OLD ROOF & NEW ROOF	\$ 182,085 ⁰⁰	\$ N/A
3) INSTALL NEW METAL ROOFING AND RELATED COMPONENTS	\$ 270,705 ⁰⁰	\$ N/A
4) REMOVE TWO WIRE SYSTEMS AND REPAIR STEAKS	\$ 25,200 ⁰⁰	\$ N/A
5) REPLACE POLY CARBONATE PANELS (PREPARED BY INSURANCE)	\$ 00	\$ N/A
6) INTERIOR DEMOLISH (CRANE TILES)	\$ 542 ⁰⁰	\$ N/A
TOTAL:	\$ 592,490⁰⁰	\$ N/A

Replacement cost of building(s), if requested: \$ N/A

CLARIFICATION, IF ANY: THIS IS A REPAIR ESTIMATE/PROPOSAL. REPLACEMENT OF THE ROOF WOULD REMOVE THE OCCUPANTS TO RELOCATE AND RE-TOO COOLING. REPAIR IS THE BEST INTEREST OF ALL PARTIES.

We certify that we have conscientiously and impartially performed the duties assigned to us in accord with the appraisal provisions of the policy and do hereby award the amounts established above for the described loss.

WITNESS OUR HAND:
(Two signatures required)

DATE: 11-28-2006 APPRAISER: Joe Sanders
 DATE: 11/28/2006 APPRAISER: _____
 DATE: 11/28/2006 UMPIRE: _____

Practical Tips

1. Make sure the umpire is properly educated as to scope of appraisal and issues
2. Explore potential relationships between the appraisers and the umpire
3. Explore potential relationships between the umpire and the judge
4. Be the first to file for the appointment of an umpire

Issue 5: “A Decision Agreed to By Any Two Will Be Binding”

- As a general rule, appraisal awards are binding but may be challenged in three circumstances:
 - (1) when made without authority
 - (2) fraud, accident or mistake
 - (3) not in substantial compliance with the policy
- Legal standards extremely high = courts confirm the award most of the time

“A Decision Agreed to By Any Two Will Be Binding”

- Is there evidence that the umpire was unfair, biased, impartial, or unethical?
- Is there evidence that the opposing appraiser was unfair, biased or interested?
 - Court may allow time to take depositions and gather evidence

“A Decision Agreed to By Any Two Will Be Binding”



Auto-Owners Ins. Co. v. Summit Park Townhome Assoc.,
2016 WL 1321507 (D. Colo. April 5, 2016).

Colorado Hosp. Servs. Inc. v. Owners Ins, Co., 2015 WL
4245821 (D. Colo. July 14, 2015)

- Policy required that each party select a “competent and impartial” appraiser
- Insured’s appraiser was not impartial due to his fee schedule
- “The Court holds that the appraisal award was not conducted in accordance with the policy, and it vacates the award.”

Practical Tips

1. Do not expect to vacate an appraisal award
2. Watch carefully for bias, bad faith, mistake, etc.
3. Know your jurisdiction

Appraisal Protocol

- **Defines the scope of appraisal**
 - Specifically requires the panel to identify the scope of the damage it considered
 - Establishes process for appraisal (example: parameters for discovery, witnesses and briefing)
- **Prescribes the form of the award**
- **Defines ACV and RCV**
- **Agreement on cost.**
- **Agreement that award is binding absent fraud, mistake, etc.**
- **Whatever else you believe is appropriate**

Appraisal Protocol

- **Primary Benefits:**
 - Provides guidance to the panel
 - Minimizes the risk of collateral attacks
 - Greater overall clarity in the process
 - Enforceable (It is an agreement between two parties to be used instead of the appraisal provision in the policy)

Questions ?

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