NO. 11-20221

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

BLUM'S FURNITURE COMPANY, INC.,
Plaintiff-Appellant

v.

CERTAIN UNDERWRITERS AT LLOYDS LONDON,
Defendant-Appellee

Appealed From the United States District Court
For The Southern District of Texas

BRIEF OF AMICI CURIAE, TEXAS APARTMENT ASSOCIATION, INC., TEXAS AUTOMOBILE DEALERS ASSOCIATION, TEXAS ORGANIZATION OF RURAL & COMMUNITY HOSPITALS, AND TEXAS BUILDING OWNERS AND MANAGERS ASSOCIATION, INC. IN SUPPORT OF REVERSAL

Brendan K. McBride
State Bar No. 24008900
MCBRIDE LAW FIRM
Of Counsel, GRAVELY & PEARSON, LLP
425 Soledad, Suite 600
San Antonio, Texas 78205

Matthew R. Pearson
State Bar No. 00788173
William J. Chriss
State Bar No. 04222100
GRAVELY & PEARSON, LLP
425 Soledad, Suite 600
San Antonio, Texas 78205

NO. 11-20221

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

BLUM'S FURNITURE COMPANY, INC.,
Plaintiff-Appellant

v.

CERTAIN UNDERWRITERS AT LLOYDS LONDON,
Defendant-Appellee

CORPORATE DISCLOSURE STATEMENT

In accordance with FED. R. APP. P. 26.1 and 29(c)(1), the four amici curiae on whose behalf this brief was prepared hereby file this Corporate Disclosure Statement.

Texas Apartment Association, Inc., Texas Automobile Dealers Association, Texas Organization of Rural & Community Hospitals, and Texas Building Owners and Managers Association, Inc. are all Texas domestic non-profit corporations with their principal business offices in Austin, Texas. No parent corporation or publicly-held corporation owns 10% or more of the stock of any of these non-profit corporations.

/S Brendan K. McBride
Brendan K. McBride
Attorney for Amici Curiae

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Page

Cases

Statutes

Rules

IDENTITY OF AMICI CURIAE AND STATEMENT OF INTEREST

Amici curiae believe that the rule relied on by the district court in this case is inconsistent with the jurisprudence of the Supreme Court of Texas regarding the function and purpose of appraisal and, if affirmed, will have a substantial and overwhelmingly negative impact on the security and operations of Texas businesses, particularly those, like hospitals, apartment buildings, or commercial real estate owners whose business could be pushed to financial ruin by a catastrophic event, or would be vulnerable to an insurer using the threat of financial ruin against them to compel the business to take less substantially less insurance coverage than owed if Texas law is construed to provide a financial incentive for insurers to underpay or delay payment of covered insurance claims with no adverse consequences.

Because the outcome of this case substantially affects the rights of all Texas property owners to timely obtain full insurance benefits for covered losses, these amici join together in this brief urging the Court to reverse the district court's summary judgment and to make an *Erie*-guess that the Supreme Court of Texas will adopt a rule on this issue that does not reward unnecessary delay in investigating and paying covered insurance claims, that does not reward underpaying or delaying payment of covered claims, and that protects the public policies embodied in the Texas Legislature's passage of Chapter 542 of the TEXAS INSURANCE CODE, including the Prompt Payment of Claims Act (TEX. INS. CODE §542.051, *et. seq.*) and Texas' statutory and common law rules prohibiting "bad faith" insurance practices.

Pursuant to FED. R. APP. P. 29(c)(5), amici curiae state that no party to this case, nor any party's counsel, has provided payment for preparing or filing this brief. The brief was prepared by the undersigned on a *pro bono* basis at the request of the amici curiae identified herein:

Texas Apartment Association, Inc. ("TAA") is a non-profit trade association that has been serving the rental housing industry in Texas for more than 40 years. In that capacity, TAA represents an association comprised of landlords, managers and allied service representatives of the rental housing industry. TAA has 25 affiliated local chapters and more than 10,500 members. Through its members, TAA represents more than 1.75 million residential dwelling units that provide housing for more than 4 million individuals across the State of Texas, and who pay for and depend on available property insurance benefits in the event of damage and loss to their property. TAA members hold property with a market value in excess of $150 billion, and pay more than $3 billion in annual property taxes.

Texas Automobile Dealers Association ("TADA") is comprised of the franchised new motor vehicle dealers in Texas. In 2007, the franchised new motor vehicle dealers in Texas sold over 1,390,000 new vehicles and in 2009, that number was around 853,000. The average franchised dealer has on the dealership lot at any one time, a sixty-five (65) day-supply of new motor vehicles in inventory; thus, if a dealer sells one hundred new vehicles per month, the dealership will have approximately two hundred and ten (210) new motor vehicles available for purchase,

not inclusive of the dealer's used vehicle inventory. In 2011, the total inventory value for the franchised dealers in Texas was in excess of $7 billion. For the franchised motor vehicle dealers in Texas, insurance is a major expense and the timely and proper payment by an insurance company for damage to a dealer's inventory or real property is a major concern, because without inventory and necessary buildings, the dealer's franchise, licenses and livelihood are at risk. This industry is a major component of the economy of both rural and metropolitan areas, providing jobs in sales, service, and financing, and providing transportation for Texas citizens. The security of the dealers' investment in their inventory and property depends on their ability to rely on the prompt and good faith payment of insurance coverage and any rule of law that incentivizes the insurance industry to underpay or delay payment of claims could have disastrous consequences for any given dealership, and will have long-term negative consequences for the industry as a whole.

Texas Organization of Rural & Community Hospitals ("TORCH") is an organization of rural and community hospitals, corporations, and interested individuals working together to address the special needs and issues of rural and community hospitals, staff, and patients they serve. The organization's mission is to be the voice and principal advocate for rural and community hospitals in Texas, and to provide leadership in addressing the special needs and issues of these hospitals. As with other property owners, owners and operators of rural and community hospitals pay for and depend on the availability of insurance coverage in order to continue to

deliver service to patients in the event of damage or loss to hospital property, such as losses caused by fire, hurricanes, tornadoes and other catastrophic losses. The prompt and adequate payment of insurance claims is especially critical to the hospitals represented by TORCH because many of these facilities provide the only accessible hearth care available to medically-underrepresented communities in Texas, and a rule that incentivizes insurers to underpay or delay payment of insurance claims could have disastrous consequences for community health and health-care costs as well as jeopardizing the financial viability of a damaged hospital.

Texas Building Owners and Managers Association, Inc. ("Texas BOMA") represents the interests of owners and managers of commercial real estate in the State of Texas. Texas BOMA is composed of six local federated associations located in Austin, Corpus Christi, Dallas, Fort Worth, Houston, and San Antonio. Texas BOMA members manage 661 million square feet of commercial real estate in Texas, and pay an estimated $1.6 billion in property taxes annually. Texas BOMA represents over 2,000 members state-wide, and approximately 3.3 million people conduct business in Texas BOMA members' buildings. Texas BOMA has a substantial interest in how the Court handles the legal issues involved in this case. Because Texas BOMA members generally carry real property insurance and must depend on the prompt and fair payment of covered claims in the event of a significant or catastrophic loss, Texas BOMA is interested in ensuring that the resolution of claims made on property insurance are properly handled, promptly, and in good faith

consistent with existing Texas common law and statutes. Texas BOMA, joins in this brief to encourage the Court to consider the importance of the matter before it to all parties, particularly those engaged in commercial real estate, and the impact on Texas real estate owners and Texas business operations if Texas law no longer provides any legal incentive for an insurer to adequately or promptly pay for covered losses.

SUMMARY OF THE ARGUMENT

The rule followed and applied by the district court in this case is inconsistent with the purpose and function of insurance appraisals as explained by the Supreme Court of Texas. Moreover, the rule followed and applied by the district court creates a financial incentive for insurers to underpay or delay payment of covered losses owed to insured Texas businesses. By allowing the payment of an appraisal award to negate a claim for breach of contract, attorneys' fees, bad faith and statutory delay penalties, the district court's opinion means that the worst that can happen to an insurer as a result of underpaying a claim (even when done in bad faith or deliberately) is that it may end up paying the amount it owed in the first place – *and nothing more*. Notwithstanding the clear contrary pronouncements the Texas legislature and Texas courts, the rule applied by the district court would extend this judge-made legal immunity to any recalcitrant or even unscrupulous insurer – inviting abuse of insured businesses, especially when they are at their most vulnerable after a catastrophic loss.

The upshot of this rule could and likely will be disastrous for Texas businesses and property owners. If an insured business that depends on its property to generate income and meet expenses – like an apartment complex, auto dealership, or hospital – suffers a catastrophic loss (such as fire or hurricane damage), insurers would have a financial incentive to underpay or delay payment, and to use the vulnerable position in which the business finds itself to force the business owners to accept far less than is contractually owed for the loss. This is precisely the sort of conduct the Texas

legislature has sought to discourage and penalize by passing the statutory bad faith scheme and Texas Prompt Payment of Claims Act ("PPCA"). *See* TEX. INS. CODE §542.001, *et. seq.*

Consistent with these public policies, and with opinions of the Supreme Court of Texas interpreting and explaining the function and effect of appraisal and special duties owed by insurers, the district court's summary judgment must be reversed. The correct rule in Texas is that when a dispute about the amount of the loss is resolved *against* the insurer through appraisal, and the insurer is found to have underpaid the amount of the covered loss, the insured may go forward in the trial court with its claims for breach of contract, bad faith, attorneys' fees and PPCA.

In the alternative, if this Court is not satisfied that the district court's summary judgment should be reversed based on the existing jurisprudence from the Supreme Court of Texas – given the importance of this issue to Texas commerce and its potential impact on Texas business and the existing duties imposed by Texas common law and statute – the Court should certify a question to the Supreme Court of Texas to clarify what effect an appraisal award that is higher than the amount the insurer had agreed to pay has on an insured's claims for breach of contract, bad faith, attorneys' fees, and PPCA penalties.

ARGUMENT AND AUTHORITIES

I. THE SUPREME COURT OF TEXAS WOULD NOT FORECLOSE ACTIONS FOR BREACH OF CONTRACT, BAD FAITH OR PPCA WHEN AN INSURER PAYS AN ADVERSE APPRAISAL AWARD.

In reviewing an issue of substantive state law, federal courts are not bound by the opinions on issues of law from intermediate courts of appeal, but only by those opinions issued from the state court of last resort or, in the absence of an explicit holding, what this Court deems by way of an *Erie*-guess to be the most likely holding of the highest state court were it to reach the legal issue. *Howe ex rel. Howe v. Scottsdale Ins. Co.*, 204 F.3d 624, 627 (5th Cir. 2000) (stating that, when making an *Erie*-guess, this Court is not bound by decisions of intermediate appellate courts if "convinced by other persuasive data that the highest court of the state would decide otherwise").

The district court's opinion in this case ultimately rests on one opinion from an intermediate Texas appellate court that is contrary both to the purpose, function and effect of insurance appraisals as explained by the Supreme Court of Texas and to the clear public policies underlying the Texas legislature's statutory bad faith scheme and PPCA. *Breshears v. State Farm Lloyds*, 155 S.W.3d 340, 344 (Tex. App. – Corpus Christi 2004, pet. denied); *see also Brownlow v. United Services Auto. Assoc.*, No. 13-03-00758-CV, 2005 Tex. App. LEXIS 1987 (Tex. App. – Corpus Christi 2005, pet. denied)(mem. op.)(*citing Breshears*)(hereinafter the *"Breshears* rule"). The *Breshears* court offered little or no explanation for the result it reached, stating that the insurer did not breach its contractual duty to promptly pay the appraisal award once it had been determined, yet

ignoring that the insurer had *already* breached its statutory and contractual duties to promptly pay for the covered loss leading up to the appraisal dispute in the first place. *Breshears* at 344. Courts since, including the district court, have cited *Breshears* while adding little or nothing to the thin and flawed analysis that underlies the *Breshears* rule.

The duty to promptly investigate and pay covered claims in good faith, both as matters public policy and statute, are squarely upon the insurer – as they should be. It is long settled in Texas that because of the "special relationship between an insured and an insurer" the law imposes upon the insurer a "duty to investigate thoroughly and in good faith." *Viles v. Sec. Nat'l Ins. Co.*, 788 S.W.2d 566, 568 (Tex. 1990). As the Supreme Court of Texas explained:

> In the insurance context a special relationship arises out of the parties' unequal bargaining power and the nature of insurance contracts which would allow unscrupulous insurers to take advantage of their insureds' misfortunes in bargaining for settlement or resolution of claims.

Arnold v. National County Mutual Fire Ins. Co., 725 S.W. 2d 165, 167 (Tex. 1987)(imposing a duty of good faith and fair dealing on Texas insurers); *see also Aranda v. Ins. Co. of N. Am.*, 748 S.W.2d 210, 212 (Tex. 1988). Because this duty arises out of a relationship recognized at common law, it also gives rise to a common law action in tort that is separate and apart from any cause of action for breach of the underlying contract. *In re Liberty Mut. Ins. Co.*, No. 14-09-00086-CV, 2009 Tex.App.LEXIS 1234, *9 (Tex. App. – Houston [14th Dist.] 2009, orig. proceeding)(mem. op.)(citing *Viles*, 788 S.W.2d at 567).

These duties are not only imposed on an insurer through the common law as a matter of public policy, but are codified by the Texas Legislature. Chapters 541 and 542 of the Texas Insurance Code imposes numerous, specific duties on the insurer to promptly investigate and pay covered claims, including duties to:

- Conduct a reasonable investigation of the claim;
- Effectuate a prompt, fair and equitable settlement of a claim with respect to which the insurer's liability has become reasonably clear;
- Adopt and implement reasonable standards for the prompt investigation of claims;
- Attempt in good faith to effect a prompt, fair and equitable settlement of a claim; and,
- Abstain from compelling a policyholder to institute a suit to recover amounts due under the policy.

TEX. INS. CODE §§ 541.060 & 542.003(b).

In addition, under the PPCA, the legislature has enacted clear timelines for the acknowledgment, investigation, adjusting and payment of claims, making clear its intent to place the duty upon the insurer to promptly investigate claims and pay covered losses. *See* TEX. INS. CODE §542.051, *et. seq.* By legislative mandate, an insurer's failure to meet the clear timelines for the acknowledgement, adjusting and payment of claims provides an additional civil penalty of 18% per year on any claim for which the insurer is liable. *See* TEX. INS. CODE §542.060. The legislature has made the policy behind this statute clear, as well, indicating that it is to be "liberally construed to promote the prompt payment of insurance claims." TEX. INS. CODE §542.054.

The late payment penalties provided by the PPCA apply even if the insurer denies *all* payment and is later judicially determined to owe benefits. *Guideone Lloyds Ins. Co. v. First Baptist Church of Bedford*, 268 S.W.3d 822, 831 (Tex. App. – Fort Worth 2008, no pet.)("the amount of the 'claim' on which a penalty is calculated is the amount ultimately determined to be owed to the claimant, less any partial payments made."). The *reason* the insurer fails to timely pay is *irrelevant*, as the statutory penalties and attorneys' fees remedy apply independent of whether there is a showing of bad faith. *See e.g. Higginbotham v. State Farm Mut. Auto. Ins. Co.*, 103 F.3d 456, 461 (5th Cir. 1997)(by denying the whole claim, insurer "necessarily . . . failed to pay within 60 days of its receipt of all necessary paperwork" violating the PPCA and subjecting itself to penalties and attorneys' fees); *Lusk v. Puryear*, 896 S.W.2d 377, 380 (Tex. App. – Amarillo 1995, orig. proceeding)(explaining PPCA is merely part of the breach of contract action when the claim involves payment under an insurance policy).

Even if the insurer does not deny or underpay the claim in bad faith – and regardless of why it failed to pay within the legislative mandated deadlines under the PPCA – it still owes the delay penalties and attorneys' fees if it is ultimately shown to have not fully paid the claim in a timely manner. Of course, the PPCA has no provision whatever to excuse late payment because the insurer was waiting to resolve a dispute through appraisal. Absent a *statutory* excuse, late payment is late payment, and the insurer owes the penalty to the insured.

The legislature has also made it clear that an insurer who breaches these duties is liable for the insured's attorneys' fees to obtain its coverage benefits. These are provided for both under the insurance code for bad faith and PPCA claims (TEX. INS. CODE §541.152 and §542.060), as well as an additional statutory remedy for breach of contract in general (TEX. CIV. PRAC. & REM. CODE §38.001, *et. seq.*).

A. Appraisal Is Invoked Only Because There Is Already A "Dispute" About Whether The Insurer Breached The Contract By Underpaying The Amount of the Loss.

The district court erred because the *Breshears* rule on which it relied is not a correct statement of Texas law. To begin with, the plain language of the clause indicates that the appraisal clause only comes into effect because there is already a "dispute" between the insured and the insurer about whether the insurer has correctly determined the amount of the loss. The duty to investigate and evaluate the amount of the loss falls squarely on the insurer. *See Viles*, 788 S.W.2d 568 (holding an insurer has a "duty to investigate thoroughly and in good faith.").

Thus, regardless of whether an insurer later fulfills the separate obligation to pay the appraisal award, should the dispute about the amount of the loss be decided in favor of the insured (and if the loss is covered) the insurer will already be in breach of the contract by having not adequately and timely paid the amount owed for the covered loss. Put another way, fulfilling a later contractual obligation to abide by the appraisal umpire's award as determinative of the amount of the loss does not excuse

the insurer from its breach of contract when it failed to correctly determine the amount of the loss leading to the coverage "dispute" in the first place.

One of the more perverse results of the *Breshears* rule applied by the district court in this case is that an insured, who is supposed to have a special relationship of trust with its insurer, cannot recover attorneys' fees for its insurer's breach of its contractual and statutory obligations to promptly pay for covered losses, yet any other aggrieved party who prevails in a garden-variety breach of contract dispute resolved through an alternative dispute process (such as arbitration) *would* recover attorneys' fees even in the absence of the type of special relationship specifically created for insurers. *See e.g.* TEX. CIV. PRAC. & REM. CODE § 171.048(c); *Pu Chang Tsai v. Han Kuei Su*, 2010 Tex. App. LEXIS 6838 (Tex. App. – Houston [1st Dist.] Aug. 19, 2010, no pet.)(mem. op.)(allowing award of attorneys' fees by arbitrator since they would have been available under Chapter 38 had the dispute been resolved in district court).

B. Appraisal Only Resolves the Factual Dispute About Whether The Insurer Sufficiently Determined the Amount of Loss When Carrying Out Its Duty to Investigate the Claim.

The Texas Supreme Court has also been very clear that the appraisal process only resolves a discrete *factual* matter and is not determinative of the liability issues such as breach of contract or bad faith. *See e.g. In re Allstate County Mut. Ins. Co.*, 85 S.W.3d 193, 196 (Tex. 2002); *Scottish Union & Nat'l Ins. Co. v. Clancy*, 71 Tex. 5, 8 S.W. 630, 631 (Tex. 1888)(appraisal "only binds the parties to have the extent or amount of the loss determined in a particular way, leaving the question of liability for such loss to

be determined, if necessary, by the courts."); *see also State Farm Lloyds v. Johnson*, 290 S.W.3d 886 (Tex. 2009)(explaining that appraisal resolves a dispute about the amount of the loss, but liability questions are the province of the courts).

Thus, appraisal only arises when the parties already have a "dispute" about whether the insurer adequately investigated and paid the amount of the covered loss, and through the contractual appraisal process, the most that can be resolved by the appraisal process is the discreet factual question of what amount *should* have been determined as the amount of the loss.

C. If The Appraisal Determines That the Insurer Underpaid the Covered Loss, the Trial Court Should Enter Partial Summary Judgment ***For the Insured*** On Its Breach of Contract Claim.

As noted above, an insurer has a contractual, statutory and common law duty under Texas law to investigate a loss in good faith, and promptly pay the amount of a loss. Where a dispute about the amount of the loss has been resolved *against* the insurer, the question of liability then reverts to the courts. The court should determine the effect of the factual finding that the insurer underpaid the loss on the legal causes of action provided by Texas law for failure to timely pay for covered losses.

Though the appraisal process itself is limited to resolving the factual issue of the amount of the loss, the appraisal award may nevertheless become determinative as a matter of law with regard to the insured's cause of action for breach of contract when the parties return to court to resolve the liability issues. Under Texas law, a

contract is breached when a party fails or refuses to comply with a contractual obligation. *Decorative Ctr. of Houston, L.P. v. Direct Response Publ'ns, Inc.*, 264 F. Supp. 2d 535, 547 (S.D. Tex. 2003); *Townewest Homeowners Ass'n, Inc. v. Warner Commc'n Inc.*, 826 S.W.2d 638, 640 (Tex. App.—Houston [14th Dist.] 1992, no writ). Whether a party has breached a contract is a question of law for the court, not a question of fact for the jury. *Garza v. Southland Corp.*, 836 S.W.2d 214, 219 (Tex. App. – Houston [14th Dist.] 1992, no writ). "The court determines what conduct is required by the parties, and, insofar as a dispute exists concerning the failure of a party to perform the contract, the court submits the disputed fact questions to the jury." *Townewest HOA (citing ITT Commercial Fin. Corp. v. Riehn*, 796 S.W.2d 248, 253 n.3 (Tex. App. – Dallas 1990, no writ)).

In this context, of course, the appraisal process rather than a jury resolves the factual issue of the amount of the loss. The court then determines the effect of this factual finding on the parties' legal dispute. If the appraisal award determines the amount of loss is more than the insurer agreed to pay prior to the dispute, and if the loss is covered, the trial court would enter judgment as a matter of law for the insured on its claim for breach of contract (and in most cases the PPCA penalties as well), leaving issues of bad faith and attorneys' fees that may or may not need to be resolved by a jury. On the other hand, if the appraisal process shows that the amount of the loss is equal to or less than what the insurer determined leading up to the "dispute" about the amount of the loss, the insurer would then be entitled to judgment as a

matter of law with regard to any breach of contract claim predicated on the failure to adequately pay for a covered loss.[1]

An appraisal of a dispute about the amount of loss does not foreclose a breach of contract, bad faith or PPCA claim. Rather, the Supreme Court of Texas has twice noted that the purpose of appraisal is to determine whether a breach of the insuring agreement has occurred. *In re Universal Underwriters of Tex. Ins. Co.*, No. 10-0238, 2011 Tex. LEXIS 357; 54 Tex. Sup. J. 931 (Tex. May 6, 2011) (designated, but not released, for publication (explaining the appraisal process was "the method by which to determine whether a breach has occurred.")(emphasis added); *In re Allstate*, 85 S.W.3d at 196 (same). Indeed, in *In re Allstate* the court explained that the outcome of the appraisal process goes "to the heart of the plaintiff's breach of contract claim." *Id.*

The *In re Allstate* court reasoned that if the appraisal determined that the property's full value is what the insurance company offered, there would be no breach of contract. *Id.* It is likewise axiomatic that if the appraisal determines that the full value of the loss is *more* than what the insurance company offered, a court can, as a matter of law, determine that the insurer breached the contract by not fully investigating or paying the full amount of the covered loss.

[1] This would usually, though not always, preclude an insured's actions for bad faith or under the PPCA. However, extreme conduct by an insurer causing other damages may still be actionable bad faith even if it did not breach the contract to pay insurance benefits. *See Republic Ins. Co. v. Stoker,* 903 S.W.2d 338 (Tex. 1995). Furthermore, even if it is determined that the insurer paid the full amount of the covered loss, it may still have done so in violation of the deadlines imposed by the PPCA, and still would potentially be liable for the statutory penalties, if any, for failing to promptly investigate and pay the loss, unless it satisfies an exception under the PPCA.

The Houston Court of Appeals has similarly described the purpose and effect of appraisal as determinative of the factual predicate for whether the insurer breached the contract. In *Franco v. Slavonic Mut. Fire Ins. Ass'n*, 154 S.W.3d 777, 786 (Tex. App. – Houston [14th Dist.] 2004, no pet.), the court explained: "The effect of an appraisal provision is to estop one party from contesting the issue of damages in a suit on the insurance contract, leaving only the question of liability for the court." *Id.*; *see also In re State Farm Lloyds, Inc.*, 170 S.W.3d 629 (Tex. App. - El Paso 2005, orig. proceeding), (explaining the function of appraisal is to determine whether there was a breach of contract when the insurer adjusted the claim and offered less than the value of the insured loss).

It would make no sense for only the insured to be bound by the appraisal award. Rather, as indicated by the plain language of the provision and described by several courts, once a *dispute* has already arisen, the appraisal process fixes one discrete, factual issue in that dispute, leaving the effect of the appraisal on the breach of contract and other claims as a question for the court.

Moreover, if *Breshears* were a correct statement of Texas law, it would be nonsensical for the Supreme Court of Texas to repeatedly refuse to abate the litigation of insurance coverage disputes pending appraisal – yet it has. *See In re Universal Underwriters*, 2011 Tex. 357 at *24, n.5; *In re Allstate*, 85 S.W.3d at 196 ("in any event, the proceedings need not be abated while the appraisal goes forward"). If the payment of an appraisal award negates or excuses a prior breach of contract or bad

faith by the insurer as a matter of law, it would be a waste of time and judicial resources to continue with discovery and litigation in the case while the appraisal is ongoing. Under the *Breshears* rule, there could be no breach of duty unless and until the insurer fails to promptly pay the coverage it owes, which cannot occur until after the appraisal fixes the amount of the loss. Thus, there would be nothing to litigate if *Breshears* were correct and it would be pointless for the Supreme Court of Texas to allow the cases to proceed without abatement pending appraisal.

To the contrary, the Texas Supreme Court's refusal to abate litigation pending appraisal further demonstrates that – far from absolving the insurer from liability for having underpaid the loss and breached the contract – the highest civil court in Texas considers the appraisal process as a means to determine *whether* the insurer breached the contract by underpaying a covered loss.

II. RELIEVING INSURERS OF THE CONSEQUENCES OF FAILING TO ADEQUATELY OR TIMELY PAY FOR COVERED LOSSES WOULD UNDERMINE TEXAS'S COMMON LAW AND STATUTORY BAD FAITH SCHEMES, AND WOULD CREATE HAVOC AND UNCERTAINTY FOR TEXAS BUSINESSES.

If misconstrued and misapplied as it was in *Breshears* and by the district court, the contractual appraisal process undermines the policy of placing the duty on insurers to investigate and promptly pay covered losses in good faith. It provides a perverse financial incentive to insurers to underpay and delay payment of claims because it would negate any potential remedies an insured has for this conduct under

Texas common law (breach of contract/attorneys' fees, bad faith) and under the Texas Insurance Code (bad faith and PPCA).

Under *Breshears*, if an insurer does not adequately investigate and pay for a covered loss, it can rely on the appraisal clause to avoid any responsibility for the delay and expense it would otherwise be liable for in the civil justice system and by statute. The insured would have to perform its own investigation – at its own expense – and navigate through the appraisal process (with its attendant costs and delays) in order to get the coverage it was owed. Under the mistaken reasoning of *Breshears* and its progeny, the insurer would not pay anything more than it would have paid had it properly adjusted and agreed to pay the claim promptly.

Misconstrued to absolve an insurer of contractual and bad faith liability, appraisal also provides an insurer an incentive to undervalue the loss or delay adjusting or paying the claim. At best, an insured that has suffered a catastrophic loss and cannot afford any delay or expense in proving up its covered loss may have to accept substantially less than it is owed under its policy. At worst, the insured proves up the actual value of the loss at its own expense and the insurer simply invokes the appraisal clause only after it has been sued causing the insured to incur additional expenses and delay for which it has no remedy. The most the insurer would ever pay under the *Breshears* rule would be the amount it would have had to pay had it properly evaluated the amount of the loss in the first place. In the meantime, the insurer has been able to retain all or part of the amount owed for the covered loss until such time

as the appraisal process is complete, both placing pressure on the insured to accept less than it is owed and collecting interest on policy benefits that rightfully belong to the policyholder.

In other words, under *Breshears*, an insurer has everything to gain and nothing to lose by underpaying or delaying payment of a covered loss – turning the "special relationship" meant to be protected by Texas statute and common law on its head. Indeed, as noted above, an insured would have less remedy available for an insurer's breach of its statutory duties than does a claimant who prevails in a garden-variety breach of contract claim.

Insurers would also have an incentive to force their policyholders to retain counsel or initiate suit to collect insurance benefits by delaying investigating or even deliberately underpaying the loss to force a dispute – again placing the insured in the position of either accepting less than is owed or incurring substantial expenses to dispute the claim that it will never be able to recover under the *Breshears* rule.

If the appraisal process is construed as merely an additional part of the claims adjusting process, rather than a mechanism for resolving what has already become a "dispute," an insurer will have a financial incentive to underpay a claim and force the insured to try to navigate through the appraisal process or initiate litigation at the insured's expense in order to get amounts owed for the covered loss. When the appraisal award fixes the amount of the loss, the insurer simply pays the covered loss,

and then argues that it bears no responsibility for having breached the contract when it investigated and adjusted the claim as a matter of law.

Fortunately, this is not Texas law. In order to give effect to the public policy underlying insurers' common law and statutory duties, an appraisal award does not preclude an action against the insurer for breaching the contract, for bad faith, or for violation of the PPCA if the award establishes that the insurer undervalued the amount of the loss as occurred in this case. As the Supreme Court of Texas has already explained, the litigation should proceed pending the appraisal, which will decide only a particular factual dispute that will, in turn, typically determine *whether* the insurer breached its contractual duty to pay the full amount of the coverage. *See In re Universal Underwriters*, 2011 Tex. 357 at *24.

Here, the appraisal process resolved the factual question of the amount of the loss overwhelmingly in favor of Blum's Furniture and against the insurer. Consistent with the duties imposed on an insurer by Texas law, and the vital public policies that underlie those duties, this Court should reverse the district court's summary judgment. Rather than grant summary judgment for the insurer on all claims, the facts of this case are such that the trial court ultimately will probably have to grant partial summary judgment *for the insured* on its breach of contract and PPCA claims, leaving the question of bad faith for a jury - but that should be addressed on remand.

In the alternative, if the Court is not satisfied that the Supreme Court of Texas has sufficiently explained the effect of an appraisal award on a claim for breach of

contract or bad faith – and given the potential impact this rule has on Texas business and the rights of property owners across Texas – the Court should certify the question to the Supreme Court of Texas rather than interpret and determine Texas law on an issue of broad and great importance to Texas business and commerce based ultimately on the flawed and incomplete reasoning in an opinion from an intermediate court of appeals.

CONCLUSION

The district court relied on a flawed opinion from an intermediate Texas court of appeals that is contrary to the understanding of appraisal and its effect on insurance coverage litigation expressed by the state's highest civil court. It is also contrary to and undermines the vital public policies sought to be accomplished by the Texas legislature through the passage of the bad faith insurance statute and Prompt Payment of Claims Act as well as Texas common law regarding an insurer's duties to its insured. The Court should reverse the district court's summary judgment and remand this case.

Respectfully submitted,

/S Brendan K. McBride
Brendan K. McBride
State Bar No. 24008900
THE MCBRIDE LAW FIRM
Of counsel to GRAVELY & PEARSON, LLP
425 Soledad, Ste. 620

San Antonio, Texas 78205
(210) 227-1200 (Telephone)
(210) 881-6752 (Facsimile)

Matthew R. Pearson
State Bar No. 00788173
William J. Chriss
State Bar No. 04222100
GRAVELY & PEARSON, LLP
425 Soledad, Suite 600
San Antonio, Texas 78205
(210) 472-1111 (Telephone)
(210) 472-1110 (Facsimile)

Attorneys for Amici Curiae, Texas Apartment Association, Inc., Texas Automobile Dealers Association, Texas Organization of Rural & Community Hospitals, and Texas Building Owners and Managers Association, Inc.

CERTIFICATE OF SERVICE

Pursuant FIFTH CIRCUIT LOCAL RULE 25.2.5, this Brief of Amici Curiae has been served on all counsel of record, all of whom are filing users of the Court's EM/ECF electronic filing system, by electronic copy sent through the Court's EM/ECF electronic filing system and with a bound, paper copy via first class U.S. Mail this 27th day of July, 2011.

/S Brendan K. McBride
Brendan K. McBride

Attorneys for Amici Curiae, Texas Apartment Association, Inc., Texas Automobile Dealers Association, Texas Organization of Rural & Community Hospitals, and Texas Building Owners and Managers Association, Inc.

CERTIFICATE OF COMPLIANCE RULE WITH RULE 32(a)

1. This brief complies with the type-volume limitation of FED. R. APP. P. 32(a) (7) (B) because:

√ **this brief contains 5,790 words, excluding the parts of the brief exempted by FED. R. APP. P. 32(a) (7) (B) (iii)**, or

□ this brief uses a monospaced typeface and contains _____ lines of text, excluding the parts of the brief exempted by FED. R. APP. P. 32(a) (7) (B) (iii).

2. This brief complies with the typeface requirements of FED. R. APP. P. 32(a)(5) and the type style requirements of FED. R. APP. P. 32(a) (6) because:

√ **this brief has been prepared in a proportionally spaced typeface using Microsoft Word 2010 in Garamond 14-pt. font**, or

□ this brief has been prepared in a monospaced typeface using [state name and version of word processing program] with [state number of characters per inch and name of type style].

/S Brendan K. McBride
Brendan K. McBride

Dated: July 27, 2011