NATIONAL ASSOCIATION OF PUBLIC INSURANCE ADJUSTERS

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RE : NAPIA's White Paper - Appraisal

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A. INTRODUCTION

Appraisal is a process under an insurance policy to resolve a dispute as to the amount of a covered loss. As an alternative to arbitration, and especially to litigation, appraisal provides insureds a needed avenue for quicker, more cost effective relief. Unfortunately, of late, appraisal has come to the forefront as a result of rare, but serious instances of abuses in the process. This paper explains appraisal, identifies current issues, and proposes a common-sense approach to maintaining appraisal as a fair system for resolving valuation disputes.

B. NAPIA

NAPIA was founded in 1951 to professionalize the then small but growing profession of public adjusting. At that time, the Association enacted a Constitution and By Laws and, importantly, a stringent code of ethics which serve as the model for public adjusting today.[1] For over 60 years since its founding, NAPIA has worked closely with the insurance industry, state

[1] In point of fact, the NAIC Model Bill for Public Adjusters, discussed in Part C of this white paper, codifies NAPIA's Code of Ethics directly within the statute, which has been followed and enacted in many states.

insurance departments, state Governors and legislators, Attorneys General, and others to assure that public adjusters, the only professionals specifically licensed and regulated to prepare first party property claims for a consumer or commercial insured, practice in an ethical and accountable way. We have members in almost every state from Maine to Hawaii, and we have been called to testify and work with state governments in obtaining licensing and assuring that public adjusters properly practice their craft. After Hurricane Katrina, NAPIA was most active in Louisiana and Mississippi to aid their legislative and insurance departments in the drafting and passage of comprehensive public adjusting licensing statutes, as those states previously had none. NAPIA has worked in numerous other states and 45 of the 50 states, plus the District of Columbia, now have comprehensive licensing bills regulating public adjusters.[2]

C. NAPIA AND THE NAIC

It is important to note here that public insurance adjusters are the only professionals licensed and regulated by State Insurance Departments to work for and assist an insured who has sustained a first party property loss.[3] This is due in no small part to the efforts of the National Association of Insurance Commissioners ("NAIC"), with NAPIA's assistance and input, in drafting and passage of the NAIC Model Act, Bill #228, passed on October 28, 2005. For approximately 3 years, from 2002 to 2005, Brian Goodman, on behalf of NAPIA, worked closely with the NAIC Property and Casualty Subcommittee, co-chaired by Gene Reed from Delaware and Treva Wright Donnell from Kentucky, in drafting and passing this Model Bill, whose influence has now become dominant. Of the 45 states plus D.C. that license public adjusters, at least 20 have enacted, in large part, the Model Bill, either as an original or new statute, or to revise a previously existing one.[4]

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[2] *See* Appendix 1 - Public Adjuster Licensing Chart.

[3] Public adjusters are licensed to handle first party claims, that is, to act on behalf of an insured in negotiating for, or effecting the settlement of, a claim for loss or damage covered by an insurance contract. (*See* NAIC Model Act.) Independent adjusters contract with insurers to represent insurers in negotiating claims, but are not employed by the insurance company. Adjusters who are employed by an insurer are known as in-house or company adjusters.

[4] Among those states are (in no particular order): New Hampshire, Mississippi, Louisiana, Tennessee, Illinois, Iowa, Kentucky, Virginia, North Carolina, South Carolina, Idaho, Delaware, Texas, Kansas, and Maryland.

Thus, public adjusters are a well-accepted, licensed profession regulated under the auspices of each state's insurance department and those who are licensed are the only professionals specifically licensed to prepare first party property claims for insureds.[5]

Against this background, NAPIA is working to safeguard the integrity of the appraisal process, which plays an important role in resolving first party claims.

D. APPRAISAL HISTORY AND BACKGROUND

Appraisal is an informal process for property insurance carriers and policy holders to resolve disputes concerning the value of a loss relatively quickly and inexpensively, without resorting to far more expensive and time-consuming litigation. *See, e.g., In re Universal Underwriters of Texas Ins. Co.*, 345 S.W.3d 404, 407 (Tex. 2011). Appraisal clauses are included in most forms of property insurance policies. Johnny C. Parker, *Understanding the Insurance Policy Appraisal Clause: A Four-Step Program*, 37 U. Tol. L. Rev. 931, 931 (2006). Some states have enacted appraisal clauses as part of statutory form property insurance policies. *See, e.g.*, Mich. Comp. Laws § 500.2833(1)(m); N.Y. Ins. Law § 3404(e). Avoiding excessive legal fees and the possibility of bad faith claims benefits both sides in first-party disputes. Courts also have favored appraisal because, in most cases, it minimizes the need for judicial intervention. *CIGNA Ins. Co. v. Didimoi Property Holdings, N.V.*, 110 F. Supp. 2d 259, 269 (D. Del. 2000).

"Although appraisal may be used as another form of alternative dispute resolution, it is not arbitration." *Miller v. USAA Cas. Ins. Co.*, 44 P.3d 663, 673 (Utah 2002). Appraisers' powers are more limited than arbitrators, as "[a]n appraiser's power generally does not 'encompass the disposition of the entire controversy between the parties ... (but) extends merely to the resolution of the specific issues of actual cash value and the amount of loss.'" *St. Paul Fire & Marine Ins. Co. v. Wright*, 629 P.2d 1202, 1203 (Nev. 1981) (quoting *In re Delmar Box Co.*, 127 N.E.2d 808, 811 (N.Y. 1955)). Unlike arbitrators, appraisers determine damages only, not liability. *State Farm Lloyds v. Johnson*, 290 S.W.3d 886, 890 (Tex. 2009).[6]

The appraisal process itself is straightforward. Each side appoints an appraiser of its choosing to determine the loss value. The two appraisers appoint a third individual – a neutral umpire – to resolve any disputes between them or, if they cannot agree on an umpire, a court will appoint one. An award must be agreed to by at least two of the three

[5] Attorneys at law may also perform that function, but are regulated by State bars and separate statutes. Therefore, attorneys are specifically exempted from public adjuster licensing by the NAIC Model Bill and most state statutes.

[6] Unfortunately, some states have decided that appraisal should be treated like arbitration. *See, e.g., Mahnke v. Superior Court*, 180 Cal. App. 4th 565, 573 (Cal. App. 2009) (noting that California law subjects appraisal to Arbitration Act). NAPIA disagrees with this approach.

– whether by the two party-appointed appraisers or, in the case of any disagreement between them, by one party-appointed appraiser and the neutral umpire. Standard policy language provides:

> Appraisal. In case the insured and this Company shall fail to agree as to the actual cash value or the amount of loss, then, on the written demand of either, **each shall select a competent and disinterested appraiser** and notify the other of the appraiser selected within twenty days of such demand. **The appraisers shall first select a competent and disinterested umpire**; and failing for fifteen days to agree upon such umpire, then, on request of the insured or this Company, such umpire shall be selected by a judge of a court of record in the state in which the property covered is located. The appraisers shall then appraise the loss, stating separately actual cash value and loss to each item; and, failing to agree, shall submit their differences, only, to the umpire. An award in writing, so itemized, of any two when filed with this Company shall determine the amount of actual cash value and loss. Each appraiser shall be paid by the party selecting him and the expenses of appraisal and umpire shall be paid by the parties equally.

N.Y. Ins. Law § 3404(e) (emphasis added).[7] This or similar language is included in almost all property insurance policies.

The chief advantage of appraisal is that it is less expensive and faster than litigation. Appraisal omits discovery and other costly features of ordinary litigation. Appraisers, who are often subject matter experts, are focused solely on determining the value of a loss. They do not determine causation or liability. Each party's appraiser uses his own independent judgment to arrive at a loss value and, if the appraisers are unable to agree, any disagreement is submitted to the neutral umpire for a decision.

The chief disadvantage of appraisal from the perspective of the insured is that insurance companies and their appraisers are repeat participants in the appraisal process. An appraiser may feel loyalty to an insurer because of a longstanding business relationship or may even feel dependence on that insurer for a substantial part of his income. And, because of the large number of claims an insurance carrier may handle in a given subject area or geographic area, an insurer likely has a wealth of information in its

[7] This language dates back to the 1943 New York Standard Fire Insurance Policy (known in the industry as "The 165 Lines").

files on which it may conduct statistical analysis regarding loss values or even likely outcomes to be expected from particular umpires. Without discovery, these issues may remain hidden from a policyholder in most claims. Although on the policy holder side appraisers may also be frequently engaged by the same public adjusters or law firms, they generally represent different insureds, as the average insured would be involved in an appraisal only infrequently, after sustaining a major property loss.

In light of these problems – the disparity of information and loyalty between appraisers engaged by insurance carriers and policy holders – the main safeguard on the integrity of the appraisal system is the ability of each side's appraiser to advocate its respective positions, whether to the opposing appraiser or to the umpire if necessary. The umpire's neutrality or impartiality serves as a final check that ensures a fair and accurate decision. *See, e.g.*, *Brickell Harbour Condo. Ass'n v. Hamilton Specialty Ins. Co.*, 256 So. 3d 245, 248–49 (Fla. Dist. Ct. App. 2018).

1. Appraisers are required to be "competent" and either "disinterested" or "impartial."

Appraisers play a unique role as "disinterested" or "impartial" experts on behalf of the parties who appoint and pay them.[8] As a leading treatise explains: "Appraisers can and should advocate on behalf of the party who appointed them, but must maintain a sufficiently independent mind so as to bring the matter to a conclusion by a reasonable exercise of judgment under the circumstances." Jonathan Wilkofsky, *The Law & Procedure of Insurance Appraisal* 396 (3d ed. 2015). Thus, the hallmark of appraisers is that they are advocates who retain and exercise their independent judgment.

There are two categories of qualifications for appraisers. Appraisal clauses generally require that appraisers be (1) "competent" and (2) either "disinterested" or "impartial."

First, competency ensures the accuracy of the result. "In order to perform competently as an appraiser for this purpose, and to be designated by a party or by other appraisers or the court (as an umpire), logic and common sense require that an appraiser must have experience in the estimation of materials and labor costs for the repair and replacement of damaged property." *Noa v. Fla. Ins. Guar. Ass'n*, 215 So. 3d 141, 143 (Fla. Dist. Ct. App. 2017).

Second, disinterestedness or impartiality ensures the integrity of the process. But, the impartiality required of party-appointed appraisers is not the same as the impartiality required of judges. Indeed, appraisers "are not considered to be quasi-judges." *White v. State Farm Fire & Cas. Co.*, 809 N.W.2d 637, 429 (Mich. Ct. App. 2011). In the context

[8] Professor Parker observes that, "by virtue of both the dictionary definition and judicial construction disinterested and impartial are equivalent terms." Parker, *supra*, 37 U. Tol. L. Rev. at 940 (footnote omitted).

of insurance appraisals, impartiality means that the appraiser may not have a pecuniary interest in the outcome of the dispute, whether by contract, an employment or other longstanding relationship with a party, or otherwise. *See, e.g.*, *Tiger Fibers, LLC v. Aspen Specialty Ins. Co.*, 571 F. Supp. 2d 712, 718–19 (E.D. Va. 2008); *Gebers v. State Farm Gen. Ins. Co.*, 45 Cal. Rptr. 2d 725, 728 (Cal. Ct. App. 1995); *Gen. Star Indem. Co. v. Spring Creek Vill. Apartments Phase V, Inc.*, 152 S.W.3d 733, 737 (Tex. App. 2004). In some states, appraisers have been required to make appropriate disclosures in this regard. *See, e.g.*, Tex. Admin. Code §§ 5.4212, 5.4213.

2. Appraisers play a unique role as advocates within limits.

The Supreme Court of Iowa correctly expressed the current state of the law on appraiser advocacy as follows:

> The intent of the appraisal procedure is not to provide appraisers who possess the total impartiality that is required in a court of law. **The appraisers do not violate their commitment by acting as advocates for their respective selecting parties.** However, appraisers should be in a position to act fairly and be free from suspicion or unknown interest.

Central Life Ins. Co. v. Aetna Cas. & Sur. Co., 466 N.W.2d 257, 261 (Iowa 1991) (emphasis added). Recognizing that "the object and purpose of an appraisal is to secure a fair and just evaluation by an impartial tribunal," *id.* at 260–61, in interpreting a policy calling for "disinterested" appraisers, the court found no problem with an appraiser's advocacy. "Even though advocacy may make an appraiser partial, it does not implicate disqualification as does a pecuniary interest in the outcome of the appraisal." *Id.* at 261.

Iowa's view is consistent with that of other states and with earlier generations of cases. In *Dennis v. Standard Fire Ins. Co.*, 107 A. 161, 162 (N.J. Ch. 1919), the court complimented the appraisers in that case for being "partisans, within bounds, but … nevertheless unbiased and unprejudiced and disinterested within the meaning of the contract of insurance." The court confirmed its earlier view:

> The appraiser chosen by each party is supposed and expected, in a restricted sense, to represent the party appointing him, and within reasonable limits to see to it that no legitimate consideration favorable to the party so appointing him is overlooked by the other appraiser.

Id. (quoting *American Central Ins. Co. v. Landau*, 49 A. 738, 745 (N.J. Ch. 1901)). *See also Mason v. Fire Ass'n of Philadelphia*, 122 N.W. 423, 427 (S.D. 1909) ("[I]n practice each appraiser is apt to be a zealous advocate before the umpire to the end that the interests of the party appointing him may be advanced, and not overlooked; and, within limits, such an attitude seems to be recognized by the courts as legitimate, and indeed unavoidable.") (quoting Richards on Insurance Law 421 (3d ed.)); *See also Bradshaw v. Agric. Ins. Co.*, 32 N.E. 1055, 1058 (N.Y. 1893) ("It is proper, and to be expected, that all

the facts which may be favorable to the party nominating him shall be brought out by the appraiser, so that due weight may be given to them; but the appraiser is in no sense, for the purpose of an appraisal, the agent of the party appointing or nominating him, and he remains at all times under the duty to be fair and unprejudiced, or, in the language of the policy, disinterested.").

This standard remains true today, with Florida recently reiterating "that 'impartiality' means something other than the 'dictionary definition' as it relates to appraisers appointed and paid by the parties," such that a party-appointed appraiser must not be employed by the party and must not have an interest in the outcome of the case, and that "[t]he tie-breaking third appraiser—often referred to as the 'umpire' … or 'neutral'—provides the real impartiality." *Brickell Harbour Condo. Ass'n v. Hamilton Specialty Ins. Co.*, 256 So. 3d 245, 248–49 (Fla. Dist. Ct. App. 2018). Missouri law is in accord, holding that "[a]n appraiser is not required to be entirely impartial. Instead, they may act as advocates for their respective parties without violating their commitments." *Allstate Indemnity Co. v. Gaworski*, 552 S.W.3d 180, 183 (Mo. Ct. App. 2018). There, the court took no issue with an appraiser's "aggressive" communications advocating on behalf of the insurer that appointed him. *See also Harris v. American Modern Home Ins. Co.*, 571 F. Supp. 2d 1066, 1078 (E.D. Mo. 2008).

This view has shifted over time in some states. For example, although older Texas cases suggest appraisers may not be allowed to advocate, *see Delaware Underwriters v. Brock*, 211 S.W. 779, 780–81 (Tex. 1919); *Royal Ins. Co. v. Parlin & Orendorff Co.*, 34 S.W. 401, 403 (Tex. Civ. App. 1896), more recent decisions by Texas courts have permitted limited advocacy, provided the appraiser is not influenced or controlled by the party appointing him and the appraiser does not have a financial interest in the outcome. *See Franco v. Slavonic Mut. Fire Ins. Ass'n*, 154 S.W.3d 777, 786–87 (Tex. App. 2004); *Gen. Star Indem. Co. v. Spring Creek Vill. Apartments Phase V, Inc.*, 152 S.W.3d 733, 737–38 (Tex. App. 2004).

3. States have recognized a distinction between party-appointed appraisers and neutral umpires.

Some states have highlighted the clear, common sense distinction between party-appointed appraisers and neutral or impartial umpires. For example, Michigan law "allows for the likelihood of a party-appointed appraiser's being biased towards the party that retained the appraiser." *White*, 809 N.W.2d at 642 (citing *Auto-Owners Ins. Co. v. Allied Adjusters & Appraisers, Inc.*, 605 N.W.2d 685, 689–90 (Mich. Ct. App. 1999) (per curiam)). Michigan law states expressly the difference between appraisers and umpires that often is implicit in the law of other states: in Michigan, appraisers must be "independent," whereas umpires must be "impartial." *White*, 809 N.W. 2d at 639. This recognizes the reality that appraisers and public adjusters are "more similar to attorneys than to judges and umpires. Attorneys and appraisers are hired by one party to assist in presenting that party's position, while judges and umpires must take the proposals of both parties and decide which one is to prevail." *Id.* at 642. Indeed, "the independent

appraiser may be biased toward the party who hires and pays him, as long as he retains the ability to base his recommendation on his own judgment. The umpire, in contrast, may not favor either party; he must serve only equity, fairness, and justice." *Allied Adjusters & Appraisers, Inc.*, 604 N.W.2d at 689. If appraisers were required to be neutral in the same way arbitrators, jurors, or judges are, then "virtually all party-appointed appraisers would have to be disqualified and the entire appraisal mechanism, which has fairly served all sides for decades, would come to a screeching halt. The result would be more unnecessary litigation." *White*, 809 N.W.2d at 644 (Shapiro, J., concurring).

Colorado similarly provides by regulation that appraisers must be "fair and competent," whereas umpires "must remain neutral." Colorado Department of Regulatory Agencies ("DORA"), Division of Insurance Bulletin B-5.26 (2015). Appraisers must not be a party, must have no financial interest in the outcome of the appraisal, must not be a current employee of a party, and must not have a family or other personal relationship with the insured that could suggest bias. *Id.* at III.A.1. Appraisers have certain disclosure obligations. *Id.* at III.A.2, 3. And, appraisers are permitted to communicate with each other and with their appointing parties, but an appointing party may not communicate with an opposing appraiser. *Id.* at III.A.4. By contrast, "[t]he umpire may not have an existing direct and/or material relationship with any party to the appraisal and must remain neutral." *Id.* at III.B.1. The umpire also has disclosure obligations. *Id.* at III.B.2, 3. And, the umpire is prohibited from having *ex parte* communications with either side or either appraiser. *Id.* at III.B.4.

There are notable exceptions to this rule. In California, for example, not only are party-selected appraisers treated similarly to arbitrators, but California courts have interpreted applicable statutes as requiring that appraisers be held to "a higher [standard] of impartiality than are party arbitrators." *Mahnke v. Superior Court*, 180 Cal. App. 4th 565, 575 (Cal. Ct. App. 2009). NAPIA disagrees with this view, which appears to be against the clear weight of authority among other states.

E. CURRENT ISSUES IN APPRAISAL – APPRAISER BIAS

Despite the long and established history of appraisal, the process has only recently become an area of major focus. In the past, parties invoked appraisal more as a last resort, when coverage was not in dispute but the policyholder and carrier had reached an impasse on the value of the damage. Indeed, when litigation has arisen out of appraisal, courts have sometimes noted the dearth of case law on the topic.

In recent years, however, we have seen appraisal used more and more as an offensive tactic. In Colorado and Texas — where hail and wind damage claims are common — appraisal has particularly increased in frequency over the last decade. Even with increases in the invocation of the appraisal process, most appraisals proceed as intended, toward a speedier, less expensive resolution. However, appraiser bias has become a major issue.

The proliferation of appraisals in major losses has led, in some instances, to appraisers working full time as such, and in some instances with the same law firms and carriers in dozens of losses. When such close business relationships are not disclosed, and appraisers are portrayed to other parties and tribunals as impartial, disinterested or independent, the appraisal process is subverted by crossing the line from advocacy within limits into bias. Although such incidents of abuse are aberrational, they have the potential for very serious effects on the process, and must be promptly put to an end. To illustrate the issue, a current case is discussed below.

1. Developing Case Law – Supreme Court Of Colorado

In a closely watched case now pending before the Colorado Supreme Court, *Owners Insurance Company v. Dakota Station II Condominium Association*, Case No. 2017-SC-583, an insurance carrier seeks to overturn the generally accepted view that party-appointed appraisers are advocates within limits and replace it with an unworkable rule that they must instead remain truly impartial.

The insurance company in *Dakota Station II* seeks to reverse an appraisal award of almost $3 million resulting from hail damage.[9] There was much more at stake in this case than in a run-of-the-mill individual homeowner's claim because it involved several buildings in a large condominium complex and the condominium association had more resources than a typical individual insured. Both the insurer's and the insured's appraisers were repeat players – the insurer's appraiser received 90% of his work from the insurer (50 to 100 cases in the preceding two years), while the insured's appraiser had worked with the insured's public adjusting firm 10 to 12 times before. This disparity is common and expected, with appraisers often earning much of their income by working for the same insurers over and over again.

The appraisers for each side agreed that a full roof replacement was required and agreed on four out of six categories of damages. They disagreed on the largest category of damages, the cost of the roof replacement. The insurer's appraiser estimated the replacement cost of the roof at $1,865,402.74, whereas the insured's appraiser estimated the cost at $2,553,434.50. The neutral umpire, a retired judge, sided with the insured's appraiser on the disputed roof cost and, together with the other elements of damages, executed a total award of $2,997,709.46.

The insurer moved to vacate the award. In an evidentiary hearing, it became clear that both sides' appraisers advocated for their respected positions, as they are permitted to

[9] In a related case, filed before the insurer's action, the insured sought damages for unfair claims settlement practices and delay. *Dakota Station II Condominium Association, Inc. v. Auto-Owners Insurance Company*, No. 1:14-cv-02839-RMNYW (D. Colo. 2015) (action stayed pending this appeal) ("Related Case").

do. Nevertheless, the insurer found fault with the insured's appraiser's advocacy and communication with the insured, and claimed that the insured's appraiser had a financial interest in the appraisal because of an alleged capped contingent fee agreement. The trial court appropriately upheld the award, and Colorado's intermediate appellate court affirmed, noting that "[s]o long as the selected appraiser acts fairly, without bias, and in good faith, he or she meets the policy requirement of an impartial appraiser." 2017 WL 3184568, slip op. at 4, ¶ 24 (Colo. Ct. App. 2017). One judge disagreed with this standard and dissented from the Court of Appeals' decision.

The Colorado Supreme Court took the case on *certiorari* review and NAPIA filed a brief in that court *amicus curiae*.[10] NAPIA has urged the court to adopt the weight of authority among other states permitting appraiser advocacy within limits. NAPIA took no position in the case regarding the insured's appraiser's capped contingent fee arrangement. The court heard oral argument on January 16, 2019, and the case remains pending.[11]

The result may have far-reaching consequences on the interpretation of impartiality requirements in appraisal provisions. In turn, the way in which policies are written, and the process of appraisal itself under existing policies, may be greatly affected.

2. Additional Current Case Law

State and federal courts in Colorado have dealt with a surge of challenges to appraisal awards in the last few years, mostly linked to one appraiser who is a "repeat player," in that he does a large amount of work for one particular law firm representing policyholders. This appraiser has repeatedly failed to disclose his relationship with this law firm – in at least one case despite a court order to do so – and, courts have found, has engaged in other improper tactics that cast doubt on his independence or disinterestedness as an appraiser.

For example, the Colorado federal court determined that this appraiser had violated the court's disclosure order by not identifying the longstanding business relationship between the appraiser and the retaining lawyer. *Auto-Owners Ins. Co. v. Summit Park Townhome Ass'n*, 2016 WL 1321507, Case No. 14-cv-03417-LTB (D. Colo. April 5, 2016), *aff'd*, 886 F.3d 852 & 886 F.3d 863 (10th Cir. 2018). The court not only disqualified the appraiser for partiality and vacated the appraisal award (which was 47% greater than the policyholder's own adjuster had calculated before suit was filed) but also

[10] Two authors of this white paper, Brian Goodman and Louis Malick appeared on brief for NAPIA in the Colorado Supreme Court. A copy of the brief is available upon request.

[11] As discussed throughout this paper, NAPIA does not believe that contingent appraiser fees, which give an appraiser a direct financial interest in the result, should be allowed.

imposed sanctions. The court had ordered the appraisers for both sides to make certain disclosures concerning any financial or personal interest in the outcome of the appraisal and their relationships with the parties, attorneys, adjusters, or other participants in the case. The policyholder's attorneys and the appraiser they had retained failed to make any detailed disclosures. Evidence presented on the insurer's motion to vacate the award showed their longstanding business relationships; 33 cases in which the appraiser had served as an appraiser or expert on behalf of the policyholder's lawyers' client; the appraiser's past advocacy on behalf of policyholders, including his presentation on how to "harvest the claim money" from an insurer; the website of the appraiser's disaster insurance recovery firm, whose purpose was to "shift the balance of power from the insurer to the policy holder"; and statements by the appraiser that he "has dedicated his professional life to being a voice for policyholders in property insurance claims" and "was taught to always handle a claim as if my momma was the insured." The insurer also pointed to the appraiser's initial fee agreement which, although later amended, had called for a contingent fee capped at 10%.

The same appraiser was disqualified for similar reasons in *Copper Oaks Master Home Owners Ass'n v. American Family Mut. Ins. Co.*, 2018 WL 3536324, Case No. 15-cv-01828-MSK-MJW (D. Colo. July 23, 2018). The court vacated the appraisal award because the appraiser had entered into a contingent fee contract capped at 10% of recovery, had not disclosed other cases where he had been disqualified, and had a close and longstanding referral relationship with the policyholder's attorney, from the same law firm as in *Summit Park*. And, in this case, the appraiser's recommended award was 50% higher than the policyholder's public adjuster had previously estimated. Accordingly, the court found that the appraiser was not "competent and fair" under the Colorado DORA Bulletin and thus not "impartial" under the policy, and, therefore, should be disqualified under principles adopted in the federal courts. The court also found disqualification warranted under a state law approach requiring a showing that the appraiser's partiality distorted the appraisal process or led to a fundamentally unfair award. The non-disclosure of the fee agreements distorted the process by depriving the insurer of critical information. The appraiser also had communicated *ex parte* with the umpire during the appraisal process regarding the *Summit Park* ruling. Finally, the court found the appraiser's testimony to be "evasive, ambiguous, and largely incredible," and his appraisal to be "so bereft of methodology and supporting evidence as to be completely implausible." Slip op. at *14-15.

The same appraiser also was disqualified in the following other cases for the same or similar reasons, not all of which involved the same attorneys for the policyholder. *Great N. Ins. Co. v. 100 Park Ave. Homeowners Ass'n*, No. 16-cv-02009 (D. Colo. March 13, 2017); *Church Mut. Ins. Co. v. Broadmoor Community Church*, No. 2015-cv-32454 (El Paso Cty. Dist. Ct., Colo. July 6, 2016); *Axis Surplus Ins. Co. v. City Center West LP*, No. 2015-cv-30453 (Weld Cty. Dist. Ct., Colo. March 14, 2016).

Close analysis of these cases confirms that, not only are the problems linked to a small group of people and not the entire industry, but that the problems largely can be solved by complying with appropriate disclosure requirements, ensuring that appraisers do not have a financial interest in the outcome of the appraisal, and avoiding excessive "repeat player" relationships between appraisers and public adjusters or law firms, all of which NAPIA supports.[12]

G. NAPIA'S RESPONSE AND ACTION PLAN

NAPIA wishes for insurance departments, legislators, attorneys general, and the industry as a whole to recognize the benefits of appraisal when conducted properly, address the emerging issues, and encourage transparency in the continued development and use of the appraisal process.

First, we as an industry must acknowledge head-on the issues that have recently emerged. It must be made clear that appraisers, under any policy or statutory definition, must not be biased. That means ensuring that appraisers do not have a financial interest in the outcome of a particular loss. In particular, contingent fee arrangements improperly give appraisers the incentive to inflate loss estimates so their percentage fee is also higher. Using an hourly rate that is capped at a percentage of the award, ostensibly to limit the fee an appraiser may earn, can have the paradoxical effect of driving up the appraiser's estimate so that the cap does not negate any of the appraiser's billed hours.[13]

Nor should appraisers have a financial interest by virtue of an extensive relationship with a particular client. The industry should make sure that the "repeat players" are not repeating so often that they are really advocating for the client who keeps hiring them, rather than the client's position on that particular loss. Transparency as to any such relationships is essential to a fair process. To the extent any prior dealings might bear on the appraiser's estimate, the neutral umpire should be able to assess the award in light of all those relevant facts.

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[12] For an in-depth discussion on Texas case law and current appraisal issues, see McBride, Chriss & Pearson, *Insurance Appraisal in Texas and Its Place in Coverage Litigation*, 50 St. Mary's Law Journal 101 (2019).

[13] As an illustration of a contingent-cap fee, an appraiser may charge $400 per hour, with the total fee not to exceed 10% of the total loss. If the appraiser spends 100 hours working on the valuation, explaining the estimate to the opposing appraiser, presenting his estimate to the umpire (and rebutting the other appraiser's estimate), etc., he has incurred $40,000 worth of time. If the appraisal award is $300,000, the appraiser's fee would be reduced to $30,000 pursuant to the 10% cap. Thus, the appraiser has a direct financial interest in ensuring that the award is at least $400,000. Because of the direct financial interest that results under such a contingent-cap fee arrangement, NAPIA opposes the use of such fee structures.

Correcting the bias-related problems that have arisen, however, does not require any fundamental changes to appraisal. Rather, preventing this rather isolated problem from spreading merely requires that appraisal be practices as it was intended, and for the most part has and does. What the industry needs to avoid is an over-correction based on an unrealistic definition of appraiser impartiality, disinterest, or independence. An appraiser advocates for his client's measure of the damages in a loss. In doing so, the appraiser naturally must, within the proper limits, advocate for the party who hired him. This is how it is supposed to work. Thus, NAPIA seeks to reinforce the role of the appraiser as an advocate within limits, based on established criteria and robust disclosure requirements.

J. NAPIA AND NATIONAL ACTIVITY

NAPIA continues its national work on appraisal issues. We frequently address commissioners through the NAIC and monitor pending legislation all over the nation.

For example, NAPIA alerted Puerto Rico's insurance commissioner to the barriers to appraisal in their jurisdiction, recognizing that appraisal could benefit policyholders and ease the burden on the court system. On June 12, 2018, the Puerto Rico Office of the Commissioner of Insurance issued Ruling Letter CN-2018-241-D, adopting the appraisal process for commercial claims related to Hurricane Maria. Under that guidance, each party may select an appraiser to represent each of them, and in turn select a neutral umpire. The Puerto Rico Commissioner's statement recognizes the proper appraisal system and safeguards, including disclosure of an appraiser's or umpire's past relationship with a policyholder or carrier, which recognizes that an impartiality challenge should be reserved for situations where bias or financial interest in the outcome is at issue, not merely advocacy for the appraiser's loss estimate from his client's perspective.

There are opportunities for legislative solutions as well. In 2017, Colorado House Bill 1319 was introduced as a measure to set standards for fairness and impartiality for appraisers, and neutrality for umpires. As to appraisers, the bill focused on preventing financial interest and *ex parte* contact, not on advocacy of lack thereof for one side or another. The bill was postponed indefinitely by the Colorado House Committee on the Judiciary, but is worth further study because the proposed legislation had the correct focus to address bias without upheaval of the benefits of the appraisal system.

K. ENFORCEMENT OPPORTUNITIES

It is NAPIA's position that for an appraiser to present himself as independent, disinterested, or impartial (depending on the statutory or policy language that applies), when the appraiser actually has a significant past relationship with a party to an insurance contract, is not consistent with the purpose and intent of appraisal. Such conduct is improper, whether by the appraiser or umpire, as well as by the party hiring that individual. Similarly, failure to disclose a fee arrangement that is contingent in any form on the amount of the appraisal award should be considered wrong.

Only full disclosure can allay this problem — so the other party can challenge the appraiser's impartiality, so the neutral umpire can consider the past relationship or contingent-fee interest, and if necessary, so a court can evaluate the bias, vel non, of an appraiser or umpire.

Reporting requirements dovetail with the need for such disclosure. Basically, if an appraiser makes a living off of appraising losses for a particular client, or a particular side of the insurer/insured relationship, then the others involved in adjusting and evaluating the loss have a right to know.

L. CONCLUSION

In sum, NAPIA hopes to work cooperatively with all industry stakeholders to preserve appraisal as a fair, speedy form of alternative method to resolve disputes as to the value of a covered loss.

RESOURCES – AVAILABLE UPON REQUEST

1. Master Public Adjuster Licensing and Legal Chart

2. *Auto-Owners Ins. Co. v. Summit Park Townhome Ass'n,* 886 F.3d 852 & 886 F.3d 863 (10th Cir. 2018).

3. *Copper Oaks Master Home Owners Ass'n v. American Family Mut. Ins. Co.*, 2018 WL 3536324, Case No. 15-cv-01828-MSK-MJW (D. Colo. July 23, 2018).

4. Amicus Brief, Owners v. Dakota Station, (Colo. 2018).

5. Puerto Rico Office of the Commissioner of Insurance, Ruling Letter CN-2018-241-D (June 12, 2018).

6. Bill Summary, Colorado

7. McBride, Chriss & Pearson, *Insurance Appraisal in Texas and Its Place in Coverage Litigation*, 50 St. Mary's Law Journal 101 (2019).