



2-2019

# Insurance Appraisal in Texas and Its Place in Coverage Litigation

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## Recommended Citation

McBride, Brendan K.; Chriss, William J.; and Pearson, Matthew R. (2019) "Insurance Appraisal in Texas and Its Place in Coverage Litigation," *St. Mary's Law Journal*: Vol. 50 : No. 1 , Article 1.

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## ARTICLE

# INSURANCE APPRAISAL IN TEXAS AND ITS PLACE IN COVERAGE LITIGATION\*

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I.	Introduction.....	103
II.	What Is Appraisal? .....	104
III.	Invoking and Avoiding Appraisal and Waiver of Appraisal.....	107
	A. Waiver.....	107
	1. Implied Waiver by Delay .....	109

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\* A prior version of this article was presented as a seminar paper at the Advanced Insurance Law seminar sponsored by the State Bar of Texas. The current article adds analysis of important recent decisions and of jurisprudential and public policy concerns.

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102	ST. MARY'S LAW JOURNAL	[Vol. 50:101
	2. Implied Waiver by Conduct.....	110
	3. Implied Waiver by Failure or Refusal to Participate .....	113
	4. <i>Unilateral</i> Appraisal Clauses—Split of Authority .....	114
	B. Coverage Denials and Disagreement About the Amount of Loss .....	116
	C. Selection of Umpires .....	120
	D. Scope: Which Parts of a Dispute Are Subject to Appraisal and Which Are Not? .....	123
IV.	Challenging an Appraisal Award After Appraisal .....	129
	A. Scope.....	129
	B. Lack of Umpire Authority .....	130
	C. Impartiality and “Disinterestedness” .....	130
	D. Accident or Mistake.....	133
V.	Effect on Claims for Breach of Contract, Bad Faith, and Violations of the Texas Insurance Code.....	133
	A. The <i>Breshears</i> Rule.....	134
	1. Breach of Contract .....	134
	2. Bad Faith .....	135
	3. PPCA.....	135
	B. <i>Franco v. Slavonic</i> .....	136
	C. <i>Breshears</i> & “Independent Injury” .....	137
	D. Isn't This Like What Happens With UM/UIM Claims? .....	139
	E. <i>USAA v. Menchaca</i> and the Near Future.....	141
VI.	Other Procedural Issues.....	146
	A. Abatement.....	146
	B. Mandamus Review .....	147
VII.	Conclusion .....	148

## I. INTRODUCTION

In recent years insurance appraisal has taken a position front and center in Texas property insurance coverage litigation. Understanding the key issues in appraisal is essential to properly handling modern property coverage litigation.

Although appraisal provisions have been a feature of insurance policies in Texas for well over a century, it has only been in the last fifteen years that these policy provisions have become a common and hotly contested part of insurance coverage and bad faith litigation.<sup>1</sup> Indeed, in its 2009 opinion in *State Farm Lloyds v. Johnson*,<sup>2</sup> the Supreme Court of Texas noted that it had only addressed insurance appraisal provisions a total of five times between 1888 and 2002.<sup>3</sup> The old cases were uniform to the effect that appraisal was a method to establish the value of damaged property—i.e., the “amount” of the loss—under circumstances where coverage was not in dispute; for example, when property is damaged or destroyed and the insurance company and policyholder cannot agree on its value or the amount necessary to replace it.<sup>4</sup>

Appraisal-related litigation has grown substantially since, due in large part to an unfortunate holding from the 2004 Corpus Christi Court of Appeals opinion in *Breshears v. State Farm Lloyds*,<sup>5</sup> and opinions from other intermediate appellate courts and federal courts that have followed and expanded upon the “*Breshears* rule.”<sup>6</sup> This recent line of cases has incorrectly construed insurance appraisal in a way that may allow for it to serve as a complete defense to most first-party insurance coverage and bad faith litigation as a matter of law.

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1. See *State Farm Lloyds v. Johnson*, 290 S.W.3d 886, 889 (Tex. 2009) (stating the court has attended to the matter of appraisal clauses only a few times prior to 2010s).

2. *State Farm Lloyds v. Johnson*, 290 S.W.3d 886 (Tex. 2009).

3. See *id.* at 889 (highlighting the regular absence of appraisal-related litigation for over a century).

4. See *Am. Cent. Ins. Co. v. Bass*, 38 S.W. 1119, 1119 (Tex. 1897) (“A policy of insurance may provide that an appraisal shall be made, and that it shall only be conclusive in the event the liability of the insurer is not disputed . . . .”); *Scottish Union & Nat’l Ins. Co. v. Clancy*, 18 S.W. 439, 440 (Tex. 1892) (per curiam) (stating an “agreement to ascertain the amount of the loss . . . has been repeatedly held to be valid as a condition precedent to the right of the plaintiff to sue and recover”).

5. *Breshears v. State Farm Lloyds*, 155 S.W.3d 340 (Tex. App.—Corpus Christi 2004, pet. denied) (mem. op.).

6. See, e.g., *Blum’s Furniture Co. v. Certain Underwriters at Lloyds London*, 459 F. App’x 366, 368–69 (5th Cir. 2012) (per curiam) (citing the *Breshears* rule).

Mistaken reliance by courts on the *Breshears* rule and the “independent injury” rule has allowed insurers to escape liability for breach of contract, attorneys’ fees, statutory and common law “bad faith,” and even liability under the Texas Prompt Payment of Claims Act (PPCA), often irrespective of whether the evidence shows an insurer knowingly undervalued or underpaid the claim by a substantial amount when it originally investigated and adjusted the loss, or even if it could be shown that it did so in bad faith.<sup>7</sup> Not surprisingly, given the scope of the defense now provided by appraisal, issues arising around appraisal have become a large point of focus in first-party coverage litigation in recent years, yielding a number of developing issues that have important effects on the parties’ rights.

## II. WHAT IS APPRAISAL?

The short answer: appraisal is a contractually agreed process for resolving a *disagreement* between the insurance carrier and the policyholder about the *amount* of a loss *under an insurance policy*.<sup>8</sup> A typical appraisal clause is found in the “conditions” portion of a property insurance policy among the other conditions imposed upon the insured, and it will often read something like the following from the homeowners’ property insurance policy in *Johnson*:

**Appraisal.** If you [the policyholder] and we [insurer] fail to agree on the amount of loss, either one can demand that the amount of the loss be set by appraisal. If either makes a written demand for appraisal, each shall select a competent, disinterested appraiser. Each shall notify the other of the appraiser’s identity within 20 days of receipt of the written demand. The two appraisers shall then select a competent, impartial umpire. . . . The appraisers shall then set the amount of the loss. If the appraisers submit a written report of an agreement to us, the amount agreed upon shall be the amount of the loss. If the appraisers fail to agree within a reasonable time, they shall submit their differences to the umpire. Written agreement signed by any two of these three shall set the amount of the loss.<sup>9</sup>

The exact terms can vary from this basic appraisal clause. As discussed further in this paper, some of those variations can be quite substantial and give rise to whole new issues. Conceptually, as a condition of the policy, the

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7. See, e.g., *Garcia v. State Farm Lloyds*, 514 S.W.3d 257, 276–79 (Tex. App.—San Antonio 2016, pet. denied) (precluding bad faith claims).

8. See *Johnson*, 290 S.W.3d at 887–88 (defining appraisal).

9. *Id.* (alteration in original).

provision relates to prerequisites to payment of a covered claim, not to whether the loss or claim is covered or excluded in whole or in part as defined in the “coverage” and “exclusions” portions of the policy.<sup>10</sup>

Thus, appraisal is an “extra-judicial” contractual device for resolving a specific type of disagreement—the *amount* of a covered loss.<sup>11</sup> However, appraisal is not a form of “arbitration,” even though it has some similarities.<sup>12</sup> The key difference, which has several important implications for some of the issues addressed elsewhere in this paper, is that appraisal does not “divest” a Texas court of jurisdiction to decide the legal case, “but 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.*”<sup>13</sup>

Some of the basic requirements for an appraisal issue to arise are self-evident from this stated purpose. The insurer and its policyholder must have (1) a disagreement (2) about the amount of a loss that is (3) apart from disagreement about the question of coverage or liability for such a loss—whatever its amount is ultimately determined to be.<sup>14</sup>

Although this seems simple enough, a number of complicated questions and issues have sprung up with the rapid proliferation of appraisal as a major part of insurance litigation since *Breshears*. These include the following issues to be addressed in this paper:

- When must a party invoke appraisal and how can the right to use the appraisal process be waived?<sup>15</sup>

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10. See *Amine v. Liberty Lloyds of Tex. Ins. Co.*, No. 01-06-00396-CV, 2007 WL 2264477, at \*5 (Tex. App.—Houston [1st Dist.] Aug. 9, 2007, no pet.) (mem. op.) (“Appraisal does not resolve coverage issues.” (citing *Wells v. Am. States Preferred Ins. Co.*, 919 S.W.2d 679, 683 (Tex. App.—Dallas 1996, writ denied))).

11. See *id.* at \*3 (“The purpose of an appraisal clause is to provide a binding, extra-judicial ‘remedy for any disagreement regarding the amount of the loss.’” (quoting *Breshears v. State Farm Lloyds*, 155 S.W.3d 340, 344 (Tex. App.—Corpus Christi 2004, pet. denied) (mem. op.))).

12. See *Johnson*, 290 S.W.3d at 889 (“In *Scottish Union*, we referred to the scope of appraisal in the course of distinguishing it from arbitration[.]” (citing *Scottish Union & Nat’l Ins. Co. v. Clancy*, 8 S.W. 630, 631 (Tex. [Comm’n Op.] 1888))).

13. *Scottish Union*, 8 S.W. at 631 (emphasis added).

14. Cf. *Johnson*, 290 S.W.3d at 890 (“The policy directs the appraisers to decide the ‘amount of loss,’ not to construe the policy or decide whether the insurer should pay.” (citing 15 COUCH ON INS., pt. IX, ch. 210, § 210:42, Westlaw (database updated Dec. 2018))).

15. See discussion *infra* Part III.

- May an insurer include a *unilateral* appraisal clause under which only the insurer may choose to invoke the appraisal process? May an insurer who includes such a unilateral appraisal clause refuse to participate in an appraisal requested by the policyholder prior to a lawsuit, but still compel the policyholder to appraise the loss after the policyholder has had to hire an attorney and incurred the expense and delay to file a lawsuit?<sup>16</sup>
- What is the scope of the appraisal? What distinguishes disagreements about the “amount of the loss” to be determined through the appraisal process from disagreements about the liability for that loss that is supposed to be determined by the courts?<sup>17</sup>
- On what basis may a party challenge the amount of the loss that was determined through the appraisal process or the procedures followed in the appraisal process? And what is the effect of such a challenge, if successful?<sup>18</sup>
- What effect does the determination of the amount of the loss through appraisal have on other policy issues, such as coverage denials based on exclusions, application of deductibles and coverage limits, or other policy conditions about which the parties might disagree?<sup>19</sup>
- Where does the appraisal award fit with the other legal rights and obligations imposed by the terms of the insurance policy, Texas common law rights such as common law bad faith, and provisions of the Texas Insurance Code in Chapters 541 (statutory bad faith) and 542 (PPCA)?<sup>20</sup>
- Is appraisal a part of the claims investigation and adjusting process, or is it a part of the dispute resolution tied into the role of the courts to ultimately determine the parties’ rights and

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16. See discussion *infra* Section III.A.4.

17. See discussion *infra* Section III.D.

18. See discussion *infra* Part IV.

19. See discussion *infra* Part IV.

20. See discussion *infra* Part V.

liabilities that arise only after the claim has already been investigated and adjusted by the insurer?<sup>21</sup>

- What procedural effect does an agreement or order to appraise the amount of a loss have on a pending lawsuit for breach of contract or bad faith? Must or may the lawsuit be abated in whole or in part pending the outcome of the appraisal process?<sup>22</sup>
- What remedies are available in the courts of appeals from orders compelling or refusing to compel the parties to participate in appraisal?<sup>23</sup>

### III. INVOKING AND AVOIDING APPRAISAL AND WAIVER OF APPRAISAL

Invoking the appraisal clause will generally depend on the language of the clause, which may have certain procedural requirements to invoke the process. For instance, in the above quoted clause from *Johnson*, once the policyholder and insurer “fail to agree on the amount of loss” either may make a “written demand for appraisal.”<sup>24</sup> Each side must then select a “competent, disinterested appraiser” and notify the other side of the appraiser’s identity within twenty days of the written demand.<sup>25</sup> Other appraisal clauses may contain differences in this particular procedure, different notice requirements, timelines or deadlines, etc., while some appraisal clauses, as discussed below, purport to be unilateral—allowing only the insurer to decide whether the amount of the loss will be determined through appraisal.<sup>26</sup>

#### A. *Waiver*

As noted above, the determination of the amount of the loss through appraisal is generally considered binding on the parties as to that specific issue, subject to a court then determining the effect of that determination

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21. See discussion *infra* Part V.

22. See discussion *infra* Section VI.A.

23. See discussion *infra* Section VI.B.

24. *State Farm Lloyds v. Johnson*, 290 S.W.3d 886, 887 (Tex. 2009).

25. *Id.* at 887–888.

26. See, e.g., *In re GuideOne Mut. Ins. Co.*, No. 10-16-00404-CV, 2017 WL 1749793, at \*2 (Tex. App.—Waco May 3, 2017, orig. proceeding) (mem. op.) (discussing a policy containing a unilateral appraisal clause).



on the parties' respective rights and liabilities.<sup>27</sup> However, after *Breshears*, insurers increasingly began to rely on appraisal to avoid—as a matter of law—any claim for breach of contract, breach of the statutory and common law duties of good faith and fair dealing, and breach of the PPCA, claiming the *Breshears* rule excuses any late payment or underpayment of the claim during the claims adjusting process so long as the insurer pays the appraised amount of the loss within a reasonable time following the appraisal.<sup>28</sup>

Consequently, one of the biggest issues that emerged with the sudden explosion of appraisal following *Breshears* was the question of when and how the parties to the insurance policy can waive the right to use the appraisal process in lieu of submitting their disagreement about the amount of the loss to the court or ultimately a jury.<sup>29</sup> Given the expansive scope of the defense provided to insurers after *Breshears*, it became important for policyholders to attempt to avoid the appraisal process entirely so as to not lose all of their common law and statutory remedies as a matter of law.<sup>30</sup> To waive rights under an appraisal clause, a party “must intend to relinquish a known right or engage in intentional conduct inconsistent with claiming that right,” and waiver can be either express or implied by conduct.<sup>31</sup> Express waiver is rarely the question when it comes to appraisal.<sup>32</sup> However, there has been considerable case law addressing various situations under which an insurer might waive its right to appraisal by its conduct.

27. See *Johnson*, 290 S.W.3d at 889 (“[The appraisal clause] 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.” (quoting *Scottish Union & Nat'l Ins. Co. v. Clancy*, 8 S.W. 630, 631 (Tex. [Comm'n Op.] 1888))).

28. See, e.g., *Garcia v. State Farm Lloyds*, 514 S.W.3d 257, 275 (Tex. App.—San Antonio 2016, pet. denied) (“[A] long line of cases has held that full and timely payment of an appraisal award under the policy precludes an insured from recovering penalties under the [Prompt Payment of Claims] Act as a matter of law.” (citing *In re Slavonic Mut. Fire Ins. Ass'n*, 308 S.W.3d 556, 563–64 (Tex. App.—Houston [14th Dist.] 2010, orig. proceeding))).

29. See *In re Universal Underwriters of Tex. Ins. Co.*, 345 S.W.3d 404, 412 (Tex. 2011) (orig. proceeding) (explaining that to establish waiver a party must show an impasse was reached and any failure to demand appraisal within a reasonable time prejudiced the opposing party).

30. See, e.g., *id.* at 406 (showing a policyholder attempting to avoid appraisal by arguing that the insurance company waived its rights to appraisal).

31. *In re State Farm Lloyds*, 514 S.W.3d 789, 793 (Tex. App.—Houston [14th Dist.] 2017, orig. proceeding) (citing *In re Universal Underwriters*, 345 S.W.3d at 407).

32. See *id.* at 794 (“Instead, in deciding whether an insurer waived its right to invoke an appraisal clause, we also must consider the policy’s language and the surrounding circumstances to determine whether the insurer intentionally relinquished its appraisal rights or engaged in intentional conduct inconsistent with claiming these rights.” (citing *In re Universal Underwriters*, 345 S.W.3d at 407; *In re Liberty Ins. Corp.*, 496 S.W.3d 229, 235 (Tex. App.—Houston [1st Dist.] 2016, orig. proceeding))).

### 1. Implied Waiver by Delay

Most of these arguments turn on whether the insurer had waived its right to rely on the appraisal process by delaying invoking the clause until long after the insurer had been sued by the policyholder, or otherwise acting in such a way as to waive appraisal. This sort of waiver has been addressed in two opinions from the Supreme Court of Texas: the 2002 case *In re Allstate County Mutual Insurance Co.*<sup>33</sup> and the 2011 case *In re Universal Underwriters of Texas Insurance Co.*<sup>34</sup> In *In re Universal Underwriters*, an auto dealership, Grubbs Infiniti, sustained covered hail damage to the buildings on its property.<sup>35</sup> After Universal's initial inspection and payment of approximately \$4,000, Grubbs notified Universal that it believed the inspection and payment was not sufficient and requested a reinspection.<sup>36</sup> Universal sent out an engineer who produced an inspection report identifying an additional amount of covered loss for which Universal paid an additional \$3,000.<sup>37</sup> Four months later, Grubbs filed suit for breach of contract, bad faith, and PPCA.<sup>38</sup> After filing suit, Universal moved to compel Grubbs to participate in appraisal, which the trial court denied based on Grubbs's argument that Universal had waived appraisal as a matter of law by an unexplained delay in requesting it.<sup>39</sup> Rejecting Grubbs's argument, the court set out two rules governing waiver of appraisal by delay:

- Any delay is measured from the point at which the parties have an "impasse."<sup>40</sup> However, an impasse required more than just a disagreement.<sup>41</sup> "An impasse is not the same as a disagreement about the amount of loss. Ongoing negotiations, even when the parties disagree, do not trigger a party's obligation to demand appraisal. Nor does an insurer's offer of money to cover damages necessarily indicate a refusal to negotiate further, or to recognize

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33. *In re Allstate Cty. Mut. Ins. Co.*, 85 S.W.3d 193 (Tex. 2002) (orig. proceeding).

34. *In re Universal Underwriters of Tex. Ins. Co.*, 345 S.W.3d 404 (Tex. 2011) (orig. proceeding).

35. *Id.* at 405.

36. *Id.* at 406.

37. *Id.*

38. *Id.*

39. *Id.*

40. *See id.* at 408.

41. *See id.* (clarifying neither disagreements between parties during ongoing negotiations nor offers to cover damages "indicate a refusal to negotiate further").

additional damages upon reinspection.”<sup>42</sup> Rather, an “impasse” was characterized as an “apparent breakdown of good-faith negotiations.”<sup>43</sup>

- Delay alone is not enough—the party avoiding appraisal must also show substantial prejudice.<sup>44</sup> Even if a party unreasonably delays invoking appraisal after there is an “impasse,” waiver will still not occur unless the party seeking to avoid the appraisal process demonstrates that the delay caused some sort of substantial prejudice.<sup>45</sup> Drawing on its legal authorities regarding waiver in other contexts—including waiver of arbitration clauses—the court concluded that implied waiver by delay required both an unexcused delay from the point of impasse and proof that the delay itself resulted in some harm to the policyholder, concluding: “[I]t is difficult to see how prejudice could ever be shown when the policy, like the one here, gives both sides the same opportunity to demand appraisal. If a party senses that impasse has been reached, it can avoid prejudice by demanding an appraisal itself. This could short-circuit potential litigation and should be pursued before resorting to the courts.”<sup>46</sup>

## 2. Implied Waiver by Conduct

Aside from delay, waiver could be found from a party's extensive use of the courts.<sup>47</sup> Generally, to amount to implied waiver of alternative dispute resolution through participation in the ongoing litigation, the party must have taken such acts as to have “substantially invoked the litigation process.”<sup>48</sup> In the specific context of appraisal, acts constituting implied waiver by this sort of conduct are:

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42. *Id.* (citing *Scottish Union & Nat'l Ins. Co. v. Clancy*, 8 S.W. 630, 632 (Tex. [Comm'n Op.] 1888)).

43. *Id.* at 409.

44. *See id.* at 411 (holding a party must show both delay and prejudice to establish waiver).

45. *See id.* at 412 (“In order to establish waiver, therefore, a party must show that an impasse was reached, and that any failure to demand appraisal within a reasonable time prejudiced the opposing party.”).

46. *Id.*

47. *See Perry Homes v. Cull*, 258 S.W.3d 580, 589–90 (Tex. 2008) (recalling occasions where parties waive “an arbitration clause by substantially invoking the judicial process”).

48. *Id.* at 593 (applying to arbitration).

[Acts] reasonably calculated to induce the [insured] to believe that a compliance by him with the terms and requirements of the policy is not desired[] or would be of no effect if performed. . . . [and] relied on must amount to a denial of liability[] or a refusal to pay the loss.<sup>49</sup>

In a recent opinion from the Fort Worth Court of Appeals, the court agreed there was implied waiver by conduct where the insurer, Allstate, made six inspections of the home after being sued, unsuccessfully attempted to remove the case to federal court (it was remanded), agreed to a trial setting, moved for and obtained an order for a seventh inspection of the home, moved for and received extensions of time to designate its experts, and was allowed to designate a new expert.<sup>50</sup> After all of this, Allstate made an offer to settle the lawsuit, which the homeowner rejected.<sup>51</sup> Reviewing all of Allstate’s conduct in the case, the court concluded: “Based on the facts and circumstances outlined above, we hold that it was within the trial court’s discretion to determine that Allstate’s conduct clearly constituted intentional conduct inconsistent with its right to invoke the contractual right of an appraisal to determine the amount of loss . . . .”<sup>52</sup> The court emphasized that in obtaining some of the extensions, new inspections, and additional experts, “Allstate directly verbally expressed to the trial court Allstate’s intent to go to trial despite lack of satisfaction of the appraisal clause condition precedent.”<sup>53</sup>

The court characterized Allstate’s settlement offer as a mere masquerade attempting to establish a new “point of impasse concerning the amount of loss” and emphasized that:

[The offer] was not made until after discovery was closed, after the expert designation deadline had passed, after Jackson had been deposed, after Allstate had agreed to a trial setting, after Allstate had requested and had obtained an extension of the expert designation deadline, and after Allstate

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49. *In re Universal Underwriters*, 345 S.W.3d at 407 (quoting *Scottish Union & Nat’l Ins. Co. v. Clancy*, 8 S.W. 630, 632 (Tex. [Comm’n Op.] 1888)).

50. *In re Allstate Vehicle & Prop. Ins. Co.*, 549 S.W.3d 881, 883–84 (Tex. App.—Fort Worth 2018, orig. proceeding).

51. *Id.* at 885.

52. *Id.* at 890.

53. *Id.* (citing *In re Universal Underwriters*, 345 S.W.3d at 407).

had compelled an opposed seventh inspection of the insured's home for the express purpose of trial preparation.<sup>54</sup>

On the question of prejudice, the court initially noted that it is difficult to show prejudice “simply by a delay in requesting an appraisal after the point of impasse . . . .”<sup>55</sup> The court looked to the whole record and found more than mere delay, concluding, “Prejudice to a party may arise in any number of ways that demonstrate harm to a party’s legal rights or financial position[,]” and that in addition to proving prejudice in the form of incurring expense, “prejudice may arise not only from the delay but also from the requesting party’s intentional conduct in the meantime—like conduct triggering additional expenses, conduct constituting inherent unfairness, conduct constituting purposeful manipulation of the appraisal process, and conduct giving the party requesting appraisal an unfair tactical advantage.”<sup>56</sup> The court detailed some of the facts constituting prejudice, including:

- the insured “could not use her only expert . . . as an appraiser because she had selected him to replace her roof;”<sup>57</sup>
- “the roof damage to her home was over two and a half years old when Allstate demanded an appraisal, and storms during those two and a half years had added to her roof damage, making it impossible for an appraiser to now determine what damage was caused by which storm;”<sup>58</sup>
- “Allstate had compelled a seventh inspection of [the] roof just a few weeks earlier,” obtaining it by “repeatedly representing to the trial court that a seventh inspection was necessary [specifically] for Allstate to use in the upcoming jury trial;”<sup>59</sup>
- “an appraisal [would] take weeks or months to accomplish, further delaying resolution of this matter, which Jackson’s counsel represented could be tried in one or two days;”<sup>60</sup> and

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54. *Id.* at 891 (citing *Jai Bhole, Inc. v. Employers Fire Ins. Co.*, No. G-10-522, 2014 WL 50165, at \*2 (S.D. Tex. Jan. 7, 2014)).

55. *Id.* at 892.

56. *Id.* (quoting *In re Universal Underwriters*, 345 S.W.3d at 411).

57. *Id.*

58. *Id.* at 893.

59. *Id.*

60. *Id.*

- with the proximity of the trial, her counsel had already expended substantial time and expense preparing for the trial Allstate had told the court it intended to go forward with when it obtained an order allowing the seventh inspection and the chance to designate a new expert.<sup>61</sup>

### 3. Implied Waiver by Failure or Refusal to Participate

Cases where a waiver of appraisal by an insurer has been found often involve situations where the policyholder has expressly invoked the appraisal process, but the insurer has refused or failed to participate.<sup>62</sup>

For instance, in the 1895 case *Northern Assurance Co. v. Samuels*,<sup>63</sup> the insurer invoked the appraisal clause, but then refused to appoint its own appraiser and failed to show up for the appraisal.<sup>64</sup> The court held that the insurer had abandoned the demand and could not rely on a subsequent demand for appraisal in which it did finally appoint an appraiser, having already shown that it was not interested in following the policy's appraisal process.<sup>65</sup>

A year later, in *Manchester Fire Insurance Co. v. Simmons*,<sup>66</sup> the court rejected an insurer's argument claiming a district court judgment in favor of the insured should have been overturned because the insured refused to submit the claim to appraisal under the policy.<sup>67</sup> The insurer ignored letters from the insured trying to resolve the dispute about the amount of the loss without suit.<sup>68</sup> The court concluded:

The company, through its agents, met the approaches of the [insured] for settlement with indifference, and exhibited a disinclination to go into any kind

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61. *Id.*

62. There is one notable exception to this regarding unilateral appraisal clauses discussed in the next section. See discussion *infra* Section III.A.4.

63. *Northern Assur. Co. v. Samuels*, 33 S.W. 239 (Tex. App.—San Antonio 1895, no writ).

64. See *id.* at 240–41 (detailing how insurer invoked the appraisal clause and subsequently failed to both appoint an appraiser and attend the appraisal).

65. See *id.* at 242 (“Having made a demand which was abandoned by it, and such abandonment not being caused by [the policyholders], they had a right to consider the appraisement waived. . . . The appraisement being waived, [the insurer] had no right to make the subsequent demand.” (citing *Chapman v. Rockford Ins. Co.*, 62 N.W. 422 (Wis. 1895))).

66. *Manchester Fire Ins. Co. v. Simmons*, 35 S.W. 722 (Tex. App.—Dallas 1896, writ *ref'd*).

67. See *id.* at 724 (holding the insurer's position is not sound because the insurer did not submit the claim pursuant to the appraisal policy).

68. *Id.* at 723.

of investigation and determination of the amount of the loss. . . . [The company] has refrained from such investigation as might have led to an agreement, and by this course has also prevented the occurrence of the contingency in which appraisers are provided for by the contract. It certainly should not be permitted to sit back and take no action until suit is brought to enforce its liability, and then successfully urge as a defense that the amount of the loss has not been agreed upon or fixed by appraisers.<sup>69</sup>

Similarly, in the recent case of *Southland Lloyds Insurance Co. v. Cantu*,<sup>70</sup> the court found waiver by the insurer.<sup>71</sup> The insurer received a letter from the insured expressly invoking the appraisal process, but never responded to this letter.<sup>72</sup> The insured filed suit and the insurer waited another sixteen months to file its motion to compel appraisal, which was almost two and a half years after the insured's letter invoking the appraisal process.<sup>73</sup>

#### 4. *Unilateral Appraisal Clauses—Split of Authority*

Even if the insurer expressly refuses to participate in appraisal when it is requested by the insured, some courts have refused to find this waived appraisal *if* the policy contains a *unilateral* appraisal clause that may only be invoked by the insurance carrier.<sup>74</sup> Thus, an insurer who has such a provision can ignore or refuse any requests by its policyholder to appraise the loss and wait to invoke the appraisal clause only after the insured files a lawsuit.<sup>75</sup> Such an approach was upheld by two courts, who principally relied on “anti-waiver” provisions of the policy to essentially conclude that implied waiver was a near legal impossibility regardless of the insurer's conduct.<sup>76</sup> However, the Dallas Court of Appeals—reviewing the same

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69. *Id.*

70. *Southland Lloyds Ins. Co. v. Cantu*, 399 S.W.3d 558 (Tex. App.—San Antonio 2011, pet. denied).

71. *See id.* at 577–78 (finding the trial court did not err when it denied Southland's motion for an appraisal).

72. *Id.*

73. *Id.* at 578.

74. *See In re GuideOne Nat'l Ins. Co.*, No. 07-15-00281-CV, 2015 WL 5766496, at \*3 (Tex. App.—Amarillo Sept. 29, 2015, orig. proceeding) (mem. op.) (holding unilateral appraisal clauses are generally enforceable).

75. *See, e.g., Biasatti v. GuideOne Nat'l Ins. Co.*, No. 07-17-00044-CV, 2018 WL 3946352, at \*3 n.3 (Tex. App.—Amarillo Aug. 16, 2018, pet. filed) (noting insurer's discretion to refuse requests to appraise prior to insured's filing of suit due to the presence of a unilateral appraisal clause within the policy).

76. *See In re GuideOne Mut. Ins. Co.*, No. 10-16-00404-CV, 2017 WL 1749793, at \*3 (Tex. App.—Waco May 3, 2017, orig. proceeding) (mem. op.) (holding a non-waiver clause valid such

unilateral clause used by the same insurance company—held otherwise, finding the insurer’s pre-suit refusal to participate in appraisal after it was requested by the insured was an express election that it was *not* going to rely on appraisal.<sup>77</sup> In *In re GuideOne National Insurance Co.*,<sup>78</sup> the court held this did not implicate the “anti-waiver” provision because it did not alter the conditions or terms of the policy:

[T]he language of the policy makes appraisal an option available to the insurer and not a condition precedent to suit. Thus, concluding the insurer has evidenced an intention not to exercise its option does not in any way alter the terms of the policy.<sup>79</sup>

Such clauses may implicate public policy concerns as well, as a unilateral appraisal clause can effectively be used to force a policyholder to file a lawsuit in order to get an insurance claim resolved. “[C]ontracts against public policy are void and will not be carried into effect by courts of justice.’ A contract is against public policy if it is illegal or injurious to the public good.”<sup>80</sup> Courts look to state statutes and judicial decisions to determine public policy.<sup>81</sup> Thus, in determining public policy, courts must give special deference to the public policy determinations of the legislature.<sup>82</sup>

Unilateral appraisal clauses that are interpreted to allow the insurer to invoke appraisal after making the policyholder file a lawsuit would seem to contravene the clear public policy stated in the Insurance Code prohibition against “compelling a policyholder to institute a suit to recover an amount due under a policy” by substantially underpaying a covered loss.<sup>83</sup> If the policyholder disagrees that it has been paid what is owed under the policy

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that any issue about a waiver of appraisal clause was immaterial); *In re GuideOne*, 2015 WL 5766496, at \*3 (refusing to address a non-waiver argument after finding the unilateral appraisal clause valid).

77. See *In re GuideOne Nat’l Ins. Co.*, No. 05-15-00981-CV, 2015 WL 5050233, at \*2 (Tex. App.—Dallas Aug. 27, 2015, orig. proceeding) (mem. op.) (affirming trial court’s determination that insurer waived its right to seek appraisal in refusing to participate in appraisal prior to the insured’s filing of suit).

78. *In re GuideOne Nat’l Ins. Co.*, No. 05-15-00981-CV, 2015 WL 5050233 (Tex. App.—Dallas Aug. 27, 2015, orig. proceeding) (mem. op.).

79. *Id.* at \*1 n.2.

80. *Westchester Fire Ins. Co. v. Admiral Ins. Co.*, 152 S.W.3d 172, 182 (Tex. App.—Fort Worth 2004, pet. denied) (en banc) (first quoting *James v. Fulcrod*, 5 Tex. 512, 520 (1851); then citing 14 TEX. JUR. 3D *Contracts* § 143 (1997)).

81. *Stubbs v. Ortega*, 977 S.W.2d 718, 722 (Tex. App.—Fort Worth 1998, pet. denied).

82. *Westchester Fire*, 152 S.W.3d at 182.

83. TEX. INS. CODE ANN. § 542.003(b)(5).



and its attempts to invoke appraisal are refused by the insurer because the clause is unilateral, the policyholder has no means other than a lawsuit to obtain the underpaid or unpaid coverage benefits. This issue was raised by the Amarillo Court of Appeals in one of the three *GuideOne* cases discussed above.<sup>84</sup> However, it was rejected solely on the basis that the court refused to be the first court to invalidate a unilateral appraisal clause on public policy grounds.<sup>85</sup>

#### B. Coverage Denials and Disagreement About the Amount of Loss

Another common issue that arises in the context of initiating appraisal is whether the parties have a “disagreement” about the amount of the loss.<sup>86</sup> This often comes up in the context of outright coverage denials by an insurer. For instance, an insurer might take the position that, regardless of the amount of the loss, no coverage is owed because the loss would fall under an exclusion in the policy or it was caused by an occurrence that pre-dates the coverage period provided by the policy.<sup>87</sup>

It has long been the law in Texas that denying a claim accomplishes a waiver of conditions of the policy that then become superfluous to perform, since the claim has been denied.<sup>88</sup> For instance, this has been held to prevent attempts to avoid payment of denied claims by later claiming a proof of loss has not yet been given.<sup>89</sup> There is no reason to insist on performance of conditions like this after the insurer has already refused to pay the claim on some other basis.<sup>90</sup>

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84. See *In re GuideOne Nat'l Ins. Co.*, No. 07-15-00281-CV, 2015 WL 5766496, at \*3 (Tex. App.—Amarillo Sept. 29, 2015, orig. proceeding) (mem. op.) (implying an insured's sole means of challenging allegedly underpaid benefits is to file suit when the relevant policy contains a unilateral appraisal clause).

85. See *id.* (“Exactly how we should deal with the nonwaiver argument is left unsaid.”).

86. See, e.g., *In re Liberty Ins. Corp.*, 496 S.W.3d 229, 231 (Tex. App.—Houston [1st Dist.] 2016, orig. proceeding) (“[The policyholder] argued that the parties did not disagree over the ‘amount of loss’ because Liberty denied that a ‘loss’ under the Policy occurred at all.”).

87. See, e.g., *Viles v. Sec. Nat'l Ins. Co.*, 788 S.W.2d 566, 567 (Tex. 1990) (discussing insurer's decision to deny coverage after asserting the damage pre-dated the coverage period).

88. See *Ford v. State Farm Mut. Auto. Ins. Co.*, 550 S.W.2d 663, 666 (Tex. 1977) (finding insurer's unconditional claim denial waived policy conditions).

89. See *Viles*, 788 S.W.2d at 567–68 (finding insurer's denial of insured's claim before proof of loss was due waived the policy's proof of loss provision).

90. See *id.* at 568 (Hetch, J., concurring) (“[A]n insurer's denial of a claim before the deadline for presenting the required proof of loss waives that requirement as a matter of law.” (citing *Sanders v. Aetna Life Ins.*, 205 S.W.2d 43, 44–5 (Tex. 1947); *Hazlitt v. Provident Life & Accident Ins. Co.*, 212 S.W.2d 1012, 1013 (Tex. App.—San Antonio, 1948), *aff'd*, 216 S.W.2d 805 (Tex. 1949); *Angelo State Univ. v. Int'l Ins. Co. of N.Y.*, 491 S.W.2d 700, 701–02 (Tex. App.—Austin 1973, no writ));

When the insured files suit after the insurer denies coverage, may the insurer still invoke the appraisal clause to determine the amount of the loss *if* it were covered? Texas courts have generally concluded that the mere denial of a claim does not necessarily constitute a waiver of the right to refer the disagreement to appraisal, but the circumstances of the claim and the nature of the denial must be considered to determine whether the insurer has waived the right to appraisal.<sup>91</sup> “Whether an insurer denied a homeowner’s claim for damages under the governing policy is relevant to the question of waiver of the appraisal clause, but it is not determinative of that question.”<sup>92</sup>

In *In re Liberty Insurance Corp.*,<sup>93</sup> for instance, the insurer denied that any loss had occurred at all, and on that basis denied the claim.<sup>94</sup> The insured argued the parties did not have a disagreement about the “amount of the loss” and that there was thus nothing to determine in appraisal.<sup>95</sup> Discussing Justice Brister’s opinion in *Johnson*, the court noted that a

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*Angelo State Univ.*, 491 S.W.2d at 701 (stating that the policyholder has a “contractual obligation to furnish [the insurer] with a sworn statement of loss[.]” but also acknowledging “the well-established rule of law that insurer will be deemed to have waived this requirement where insurer denies liability within the time allotted by the terms of the policy for proof of loss to be furnished” (citing *Fed. Sur. Co. v. Smith*, 41 S.W.2d 210 (Tex. Comm’n App. 1931, holding approved); *U.S. Fid. & Guar. Co. v. Bimco Iron & Metal Corp.*, 464 S.W.2d 353 (Tex. 1971))); *see also Hazlett*, 212 S.W.2d at 1013 (detailing an insurer’s refusal to permit a policyholder from submitting proof of loss); *Am. Cas. & Life Ins. Co. v. McCuistion*, 202 S.W.2d 474, 478 (Tex. App.—Fort Worth 1947, writ *ref’d n.r.e.*) (“The rule is unquestioned in this state that where the insurance company denies liability under the terms of the policy, that a compliance with the policy to furnish proofs of loss is waived and a recovery may be had thereon without furnishing such proofs.” (quoting *Smith*, 41 S.W.2d at 213)).

91. *See In re Allstate Vehicle & Prop. Ins. Co.*, 542 S.W.3d 815, 820 (Tex. App.—Beaumont 2018, orig. proceeding) (per curiam) (explaining the need to examine the circumstances of a claim and the nature of a denial of benefits when determining whether an insurer has waived appraisal); *see also Pounds v. Liberty Lloyds of Tex. Ins. Co.*, 528 S.W.3d 222, 226 (Tex. App.—Houston [14th Dist.] 2017, no pet.) (“Waiver of a contractual right may be express or implied from conduct.” (citing *G.T. Leach Builders, LLC v. Sapphire V.P., LP*, 458 S.W.3d 502, 511 (Tex. 2015))).

92. *In re Liberty Ins. Corp.*, 496 S.W.3d 229, 235 (Tex. App.—Houston [1st Dist.] 2016, orig. proceeding) (citing *State Farm Lloyds v. Johnson*, 290 S.W.3d 886, 894 (Tex. 2009)); *see also Johnson*, 290 S.W.3d at 894 (“When an insurer denies coverage, appraisers can still set the amount of loss in case the insurer turns out to be wrong.” (citing *Am. Cent. Ins. Co. v. Bass*, 38 S.W. 1119, 1119–20 (Tex. 1897))).

93. *In re Liberty Ins. Corp.*, 496 S.W.3d 229 (Tex. App.—Houston [1st Dist.] 2016, orig. proceeding).

94. *See id.* at 231 (discussing insurer’s denial that a loss under the policy occurred at all).

95. *Id.*

determination that there is no damage is still a determination of the amount of the loss—\$0 would be the value set for that loss by the insurer.<sup>96</sup>

It is a different result if an insurer were to deny a claim based solely on an exclusion without valuing the loss. In an opinion released before the Texas Supreme Court's opinion in *Johnson*, the Amarillo court in *In re Acadia Insurance Co.*<sup>97</sup> concluded there was no abuse of discretion in denying a motion to compel appraisal where the insurer agreed there was tangible damage to the property, but based its denial entirely on the assertion that the damage was completely caused prior to the policy period by non-covered events.<sup>98</sup> Unlike *In re Liberty*, the insurer had not assigned a value to the loss (whether \$0 or otherwise).<sup>99</sup>

This is still a potentially confusing distinction. If an insurer admits there is tangible damage, but claims it was not caused by a peril covered during the relevant policy term—as in *In re Acadia*—and on that basis offers no position as to the amount of the loss, how can there be a “disagreement” between the insured and the insurer about the “amount of loss”? The condition necessary to trigger appraisal arguably does not exist in that scenario, or where the insurer's denial of the claim is based solely on an exclusion and expresses no position on the existence of, or value of, the property damage.<sup>100</sup> Where there is no disagreement, there can be no “impasse,” and the only recourse available to the insured would be to file suit.<sup>101</sup> Moreover, couching the rule about appraisals going forward “without preemptive intervention by the courts” limits its application, since the author of *Johnson* clearly intended it to be more difficult to preempt appraisals than to avoid them once completed.<sup>102</sup>

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96. *Id.* at 234; *see also Pounds*, 528 S.W.3d at 225 (asserting insurer's determination that there was “no storm related damage” was a disagreement about the amount of loss and therefore subject to appraisal).

97. *In re Acadia Ins. Co.*, 279 S.W.3d 777 (Tex. App.—Amarillo 2007, orig. proceeding).

98. *Id.* at 780.

99. *Compare id.* (noting insurer had not assigned a value to the loss due to its belief that the damage was caused by non-covered events), *with In re Liberty*, 496 S.W.3d at 234 (explaining a finding of \$0 by an insurer is still an assignment of value to the loss).

100. *See In re Acadia*, 279 S.W.3d at 780 (noting conditions for appraisal are not present when the insurer does not take a stance as to the loss in question).

101. *See id.* (refusing to grant insurer mandamus relief after insured filed a suit in response to insurer denying their claim).

102. Scott A. Brister & Mark A. Ticer, Panel at the Insurance Law Institute Conference: Appraisal: *State Farm Lloyds v. Johnson*, What Happened? (Oct. 15, 2010), <https://utcle.org/conferences/IN10> [<https://perma.cc/AS9X-CEEU>]. During this CLE panel discussion, Justice Brister explained:

What if the insurer denies the claim based on an exclusion but decides only after a lawsuit is filed that it would now also like to contest the amount of the loss? As noted above, the purpose of appraisal is to permit either party to save the cost and time of litigating a disagreement about the amount of the loss.<sup>103</sup> As the *Johnson* court explained:

[A]ppraisal is intended to take place before suit is filed; this Court and others have held it is a condition precedent to suit. Appraisals require no attorneys, no lawsuits, no pleadings, no subpoenas, and no hearings. It would be a rare case in which appraisal could not be completed with less time and expense than it would take to file motions contesting it.<sup>104</sup>

Creating an additional dispute about the amount of loss only after the parties have gone to the courts would seem to defeat the entire purpose of

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It depends on whether you see these through the glasses of this is like an arbitration which comes up with a binding award that's like engraved in stone and there's nothing you can do about it, or whether this is like a mediation where you come up with an answer and in half or three quarters of the cases, that answer will be what the parties settle on, but then some of them, somebody's not going to like it, so you just disregard it and move on. My view is that it ought to be more like the mediation model.

....

The judges who are going to be deciding this are a lot more comfortable with arbitration now than they were in the 1930s. . . . [J]udges just didn't want arbitration at all. And now it's very common in arbitration to have partisan arbitrators and judges and attorneys are used to that where you pick somebody who you know is going to fight for you. . . . You can find cases, the old cases, some of them say you know it's like an arbitration award . . . you can't undo it unless you show there was . . . a bribe, but [there are] others that just say if you think they were just mistaken, you can undo it, and I think . . . I put a line in the opinion to support [that] I think the latter ones are right, that . . . if it's going to be heavily binding it's never going to be a quick, cheap, no-lawyers-involved process. . . . If it's something you can undo easily, . . . then the process will be quick because you know you can undo it later, and why fight about it until you find out if you need to.

*Id.* at 13:45–14:10, 36:45–38:07.

103. Mark A. Ticer et al., *Appraisal in the New World Order*, 12 J. TEX. INS. L. 1, 7 (2013) (“[T]he purposes of appraisal . . . is a prompt, efficient, and inexpensive method to determine the amount of loss.”).

104. *State Farm Lloyds v. Johnson*, 290 S.W.3d 886, 894 (Tex. 2009) (footnote omitted) (citing *Scottish Union & Nat'l Ins. Co. v. Clancy*, 8 S.W. 630, 631–32 (Tex. [Comm'n Op.] 1888); *Am. Cent. Ins. Co. v. Terry*, 26 S.W.2d 162, 166 (Tex. Comm'n App. 1930, holding approved); *Vanguard Underwriters Ins. Co. v. Smith*, 999 S.W.2d 448, 450 (Tex. App.—Amarillo 1999, no pet.); *Providence Lloyds Ins. Co. v. Crystal City Indep. Sch. Dist.*, 877 S.W.2d 872, 878 (Tex. App.—San Antonio 1994, no writ)).

appraisal.<sup>105</sup> But this question remains open.

### C. *Selection of Umpires*

Most appraisal clauses provide that the appraisers are to appoint a neutral appraisal “umpire” to resolve any disagreements between the parties’ appointed appraisers.<sup>106</sup> This neutral umpire breaks any deadlock and casts the deciding vote on any continuing disagreements about the amount of the loss.<sup>107</sup> Many policies further provide that if the appraisers cannot agree on who should act as the umpire, the parties may ask a judge of a judicial district in the location where the loss occurred, or often “the judge of a court having jurisdiction,” to appoint an umpire for them.<sup>108</sup>

However, courts have held this does not require the filing of any type of pleadings invoking the judicial jurisdiction of the judge asked to appoint the appraiser.<sup>109</sup>

Some counties have local rules that impose restrictions on access to a court unless a suit or proceeding is first filed (and assigned to a particular court or central docketing court) in accordance with the local rules.<sup>110</sup>

105. *See id.* (asserting the goal of appraisal is to determine the amount of loss before suit is filed); *see also Scottish Union*, 8 S.W. at 631–32 (holding appraisal was a condition precedent to litigation).

106. *See Cantu v. S. Ins. Co.*, No. 03-14-00533-CV, 2015 WL 5096858, at \*2 (Tex. App.—Austin Aug. 25, 2015, no pet.) (mem. op.) (discussing the appointment of an umpire called for by many appraisal clauses).

107. *See id.* (“If the appraisers do not agree on the amount of loss, they submit their differences to the umpire, and only two of the three actors need to agree on the amount for the appraisal award to become final.”).

108. *See Floyd Circle Partners, LLC v. Republic Lloyds*, No. 05-16-00224-CV, 2017 WL 3124469, at \*1 (Tex. App.—Dallas July 24, 2017, pet. denied) (mem. op.) (noting “a judge of a court having jurisdiction” may appoint an umpire for the parties); *Cantu*, 2015 WL 5096858, at \*2 (explaining parties may ask a judge to select an umpire if the appraisers cannot agree on one).

109. *See Tex. Mun. League Joint Self-Insurance Fund v. Hous. Auth. of Alice*, No. 04-15-00069-CV, 2015 WL 5964182, at \*2 (Tex. App.—San Antonio Oct. 14, 2015, no pet.) (mem. op.) (“We agree that the selection of an umpire by a judge in accordance with the terms of the Property Coverage Document does not require the filing of a lawsuit of invoking the subject matter jurisdiction of the court.” (citing *Barnes v. W. All. Ins. Co.*, 844 S.W.2d 264, 267 (Tex. App.—Fort Worth 1992, writ dismissed by agr.); *Fire Ass’n of Phila. v. Ballard*, 112 S.W.2d 532, 533 (Tex. App.—Waco 1938, no writ); *In re Roberts Co.*, 128 S.E.2d 137, 138–39 (N.C. 1962) (per curiam))); *see also In re Roberts*, 128 S.E.2d at 138 (“The appointment of the umpire is not the judgment of a court, it is a mere ministerial act pursuant to contract . . .”).

110. *See, e.g., BEXAR (TEX.) CIV. DIST. CT. LOC. R. 3, 6* (“The Presiding Civil District Court hears all nonjury matters, including pretrial matters in cases set for a jury trial, with the exception of issues allocated to the Monitoring Judge under Rule 4. . . . Every request for relief from a civil district court must be presented to the Presiding Court, with the exception of the uncontested matters specified . . .”).

Courts might or might not characterize an umpire appointment as a request for judicial relief that would be subject to these local rules.<sup>111</sup>

Either party can go to a judge who meets the contractual requirement as the selector of the umpire and request an umpire be appointed without being required to invoke the jurisdiction of that judge's court.<sup>112</sup> Moreover, any judge that meets the contractual requirements may generally also appoint a replacement umpire, when necessary, consistent with the language and purpose of appraisal clauses.<sup>113</sup>

May a party or its appraiser go to the judge for appointment of an umpire without notice? Given the lack of any of the ordinary procedural safeguards that would accompany most judicial decisions (like service of citation), not surprisingly, disagreements between appraisers have sometimes sent the parties out seeking secret umpire appointments from a local, friendly judge.<sup>114</sup> Courts in other states have seen this tactic for what it is, and not approved it. As one Kentucky court concluded:

Cahill's counsel, without notice to appellant or its counsel, now applied to the Hon. L. D. Greene, judge of the Jefferson circuit court, Common Pleas branch No. 1, and suggested the appointment of Mr. C. T. Minor, and the court made the appointment. The date of this appointment does not appear, but it was within 48 hours after they were unable to agree . . . .

. . . .

This award was not validly made. A proper tribunal was never set up. The court had no power to act until after the expiration of fifteen days and should not then have acted except after reasonable notice to appellant so that it could be properly represented. True, the contract does not require notice, but the law does.<sup>115</sup>

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111. See, e.g., *Tex. Mun. League*, 2015 WL 5964182, at \*2 (finding the selection of an umpire by a judge did not invoke the subject-matter jurisdiction of the court).

112. See *id.* (holding "the trial court's subject matter jurisdiction was not invoked" after a request for appointment of an umpire).

113. See *Cantu*, 2015 WL 5096858, at \*5 (holding the district court had authority to appoint a replacement umpire pursuant to the contract between the parties).

114. See, e.g., *Ballard*, 112 S.W.2d at 533 (discussing how each party secured a secret umpire appointment from different judges in two different counties).

115. *Camden Fire Ins. Ass'n v. Cahill*, 98 S.W.2d 462, 463 (Ky. 1936); see also *Bos. Ins. Co. v. A.H. Jacobson Co.*, 33 N.W.2d 602, 604 (Minn. 1948) (following *Camden Fire Insurance*).

Similarly, in *Caledonian Insurance Co. v. Superior Court*,<sup>116</sup> a California court concluded that allowing such a tactic would create great confusion as both parties “could simultaneously each procure the designation of an umpire, without notice to the other, by a different person who held the office of judge of some court of record” and obtain different, conflicting umpire awards.<sup>117</sup> However, a Wisconsin court in *Cady Land Co. v. Philadelphia Fire & Marine Insurance Co.*<sup>118</sup> held otherwise and upheld a secret umpire appointment, concluding the contract simply had no provision requiring notice before seeking out a judge to appoint an umpire.<sup>119</sup> The only legal question was whether enough time had passed from the time of the disagreement for an umpire’s appointment to become necessary.<sup>120</sup>

This tactic has not been expressly addressed by a Texas court. It was at issue in a petition for writ of mandamus filed in *In re Amerisure Insurance Co.*,<sup>121</sup> where the policyholder used the tactic to get an umpire appointed without notice to the insurer, but the petition was denied without an opinion by both the court of appeals and the Supreme Court of Texas.<sup>122</sup> In the 1938 *Fire Ass’n of Philadelphia v. Ballard*<sup>123</sup> opinion from the Waco court, both parties secured secret umpire appointments from different judges in different counties.<sup>124</sup> Deciding that only one county was proper under the policy’s terms, the court upheld the appraisal award from the umpire who was appointed by the judge in the county where the property was located.<sup>125</sup> Having noted that both parties had attempted the same gamesmanship, the court passed on the issue of whether such a tactic was appropriate: “Since the parties have apparently waived any consideration of the manner in which the appointment of the respective umpires was procured and the procedure

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116. *Caledonian Ins. Co. v. Superior Court*, 295 P.2d 49 (Cal. Dist. Ct. App. 1956).

117. *Id.* at 50.

118. *Cady Land Co. v. Phila. Fire & Marine Ins. Co.*, 218 N.W. 814 (Wis. 1928).

119. *See id.* at 815 (“This provision does not by its language require that prior notice shall be given of the intention by either party . . .”).

120. *See id.* (holding the umpire appointment valid following the expiration of fifteen days provided for in the contract).

121. *In re Amerisure Ins. Co.*, No. 13-0723, 2014 Tex. LEXIS 1249, at \*1 (Tex. Mar. 21, 2014) (orig. proceeding).

122. *See id.* (denying petition for writ of mandamus).

123. *Fire Ass’n of Phila. v. Ballard*, 112 S.W.2d 532 (Tex. App.—Waco 1938, no writ).

124. *See id.* at 533 (discussing the parties appointment of separate appraisers).

125. *See id.* at 534 (upholding the appraisal award based upon the plaintiff’s residence).

followed after such appointments, we have not considered the regularity or validity of the same.”<sup>126</sup>

D. *Scope: Which Parts of a Dispute Are Subject to Appraisal and Which Are Not?*

Is causation a “liability” issue for the courts or an issue inextricably intertwined with determining the “amount of loss” and subject to appraisal? Is it sometimes one and sometimes the other? Justice Brister attempted to answer this question in his opinion in *Johnson*, but seemingly failed, as different parts of his opinion are still regularly cited by *both* sides in support of “scope” arguments when insurers are moving to compel appraisal.<sup>127</sup>

In *State Farm Lloyds v. Johnson*, Johnson made a claim on her policy after suffering hail damage to her roof.<sup>128</sup> State Farm’s adjuster found the loss was less than Johnson’s \$1,477 deductible.<sup>129</sup> However, a roofer hired by Johnson concluded the damage would cost more than \$13,000 to repair.<sup>130</sup> Johnson requested appraisal under the policy, but State Farm refused to participate, arguing the dispute concerned “causation” rather than the amount of loss.<sup>131</sup> Johnson sued solely to obtain an order compelling State Farm to participate in appraisal.<sup>132</sup> The trial court refused appraisal, but the court of appeals reversed.<sup>133</sup> The Texas Supreme Court took the case to attempt to resolve where “causation” disputes fit into coverage litigation and the scope of appraisal.<sup>134</sup>

The court first noted the key distinction between arbitration and appraisal.<sup>135</sup> Arbitration concerns the parties’ liability and stands in place of the courts’ jurisdiction, while appraisal only resolves the amount of the loss, leaving the question of liability for that loss entirely to the courts.<sup>136</sup> The dispute turned on the number of shingles that were damaged by the

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126. *Id.* (citing *Camden Fire Ins. Ass’n v. Cahill*, 98 S.W.2d 462 (Ky. 1936); *Cady Land Co. v. Phila. Fire & Marine Ins. Co.*, 218 N.W. 814 (Wis. 1928)).

127. *See generally* *State Farm Lloyds v. Johnson*, 290 S.W.3d 886 (Tex. 2009) (affirming the court of appeal’s order granting summary judgment compelling State Farm to participate in the appraisal process).

128. *Id.* at 887.

129. *Id.*

130. *Id.*

131. *Id.* at 887–88.

132. *Id.* at 888.

133. *Id.*

134. *See id.* (“We granted State Farm’s petition to decide whether the dispute here fell within the scope of this appraisal clause.”).

135. *See id.* at 889–90 (noting previous distinctions between arbitration and appraisal).

136. *See id.* at 890 (“[T]he scope of appraisal is damages, not liability.”).



covered hailstorm and needed to be replaced.<sup>137</sup> State Farm's argument that this was a matter of "causation" not subject to appraisal was rejected by the court: "A dispute about how many shingles were damaged and needed replacing is surely a question for the appraisers. . . . What's more, either party could avoid appraisal by simply picking a few extras."<sup>138</sup>

State Farm tried to argue the real dispute was not which shingles were damaged, "but which [shingles] were damaged *by hail*."<sup>139</sup> The court initially seemed to presume this would have been a valid argument, but rejected it on the basis of the specific record in that case, concluding: "But nothing in the summary judgment record establishes Johnson's roof was damaged by anything else. In State Farm's denial letter, its summary judgment motion, and even its briefs in this Court, there is neither evidence nor even a hint about what else caused the damage."<sup>140</sup> Thus, the record did not establish that there was any dispute about causation.<sup>141</sup> That should have resolved the case.

However, the court went on to discuss how it would handle the issue even if it were a matter of "causation."<sup>142</sup> Foreshadowing the rest of the opinion, the court begins by noting: "In the abstract, it is hard to say whether causation is more a question of liability or damages."<sup>143</sup> The court then proceeded to set forth a number of rules that are easy to state in the abstract but often more difficult to apply to any particular dispute:

1. "[W]hen different causes are alleged for a single injury to property, causation is a liability question for the courts."<sup>144</sup> The example given is where appraisers disagreed about the cause of a foundation movement, which the court agreed would be a liability question, not an appraisal question.<sup>145</sup>
2. "[W]hen different types of damage occur to different items of property, appraisers may have to decide the damage caused by

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137. *Id.* at 891.

138. *Id.*

139. *Id.*

140. *Id.*

141. *See id.* ("[T]he trial court could not conclude as a matter of law that the parties' dispute was about causation rather than something else.")

142. *Id.* at 891–93.

143. *Id.* at 892.

144. *Id.*

145. *See id.* (explaining the role of appraisers is to determine the cost of damage while leaving the issue of deciding liability to the courts).

each before the courts can decide liability.”<sup>146</sup> The example concerned water and mold damage under a policy in which the former was covered but the latter excluded, and there was a question as to how much property needed to be replaced because of the excluded mold: “[C]ourts can decide whether water or mold damage is covered, but if they can also decide the amount of damage caused by each, there would be no damage questions left for the appraisers.”<sup>147</sup>

3. “[W]hen the causation question involves separating loss due to a covered event from a property’s [preexisting] condition. Wear and tear is excluded in most property policies (including this one) because it occurs in every case. If State Farm is correct that appraisers can never allocate damages between covered and excluded perils, then appraisals can never assess hail damage unless a roof is brand new.”<sup>148</sup>
4. “[A]ppraisers must always consider causation, at least as an initial matter. An appraisal is for damages caused by a specific occurrence, not every repair a home might need. When asked to assess hail damage, appraisers look only at damage caused by hail; they do not consider leaky faucets or remodeling the kitchen. . . . Any appraisal necessarily includes some causation element, because setting the ‘amount of loss’ requires appraisers to decide between damages for which coverage is claimed from damages caused by everything else.”<sup>149</sup>
5. “[W]hen an indivisible injury to property may have several causes, appraisers can assess the amount of damage and leave causation up to the courts.”<sup>150</sup>
6. “When divisible losses are involved, appraisers can decide the cost to repair each without deciding who must pay for it.”<sup>151</sup>

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146. *Id.*

147. *Id.*

148. *Id.* at 892–93.

149. *Id.* at 893.

150. *Id.* at 894.

151. *Id.* (citing *Lundstrom v. U.S. Auto. Ass’n*, 192 S.W.3d 78, 87–89 (Tex. App.—Houston [14th Dist.] 2006, pet. denied)).

Some of these rules seem to facially contradict one another. For example, the insurer's appraiser decides that he is going to assess the value of a damaged roof at \$0 because he believes the roof was damaged by a prior storm and not the recent hailstorm that occurred during the policy period. The insured's appraiser decides the damage resulted from the recent storm and will cost \$1 million to repair. This is an "indivisible injury to property [that] may have several causes" which would leave the real question as one of causation and not amount, *but* it is also a situation in which the "causation question involves separating loss due to a covered event from a property's [preexisting] condition[.]" which the court considers a question for appraisal and not a liability issue for the courts.<sup>152</sup>

Older cases seemed to be clearer on this distinction. In *Wells v. American States Preferred Insurance Co.*,<sup>153</sup> which is cited in *Jobson*, the appraisal award specified the damages "related to the plumbing leak" were \$0.<sup>154</sup> In the context of the award and the parties' dispute about the loss, the court interpreted this \$0 valuation as turning on whether the plumbing leak was the cause of the loss even though it was expressed in terms of dollar value, and therefore a matter that was beyond the scope of the appraisal clause.<sup>155</sup>

In an opinion released in 2018, another court addressed this issue in the context of a "named perils" policy that provided coverage only if the loss was caused by windstorm or hail.<sup>156</sup> In *Texas Windstorm Insurance Ass'n v. Dickinson Independent School District*,<sup>157</sup> the umpire and the school district's appraiser agreed to an appraisal award of nearly \$10,000,000 for Hurricane Ike-related damage to school properties.<sup>158</sup> The school district was granted summary judgment on "causation" and the amount of damages, and judgment was ultimately entered against the insurer, Texas Windstorm Insurance Association (TWIA), for breach of contract because it had not

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152. *Id.* at 892, 894.

153. *Wells v. Am. States Preferred Ins. Co.*, 919 S.W.2d 679 (Tex. App.—Dallas 1996, writ denied).

154. *Id.* at 682.

155. *Id.* at 683.

156. *See* *Tex. Windstorm Ins. Ass'n v. Dickinson Indep. Sch. Dist.*, No. 14-16-00474-CV, 2018 WL 4781526, at \*10 (Tex. App.—Houston [14th Dist.] Oct. 4, 2018, no pet. h.) ("[The policy at issue] explicitly excluded loss or damage caused by or resulting from 'rain, whether driven by wind or not unless wind or hail first makes an opening in the walls or roof of the described building.'").

157. *Tex. Windstorm Ins. Ass'n v. Dickinson Indep. Sch. Dist.*, No. 14-16-00474-CV, 2018 WL 4781526 (Tex. App.—Houston [14th Dist.] Oct. 4, 2018, no pet. h.).

158. *Id.* at \*3.

paid the appraisal award.<sup>159</sup> TWIA argued the appraisal award by itself was insufficient evidence to support the judgment because it only contained the valuation of the damages and no causation analysis or other explanation identifying any of that damage as having been caused by the two named perils—windstorms or hail.<sup>160</sup> TWIA also produced evidence that wind and hail were not the only causes of damage they found to the school properties.<sup>161</sup> The “critical issue” therefore was whether the appraisal award alone could establish the amount of *covered* loss suffered by the school district.<sup>162</sup> The court concluded that it could not establish liability as a matter of law in the face of evidence raising a genuine issue of material fact as to how much of the damage found by the appraisers was caused by the named perils covered under the policy.<sup>163</sup> The case was reversed and remanded.<sup>164</sup>

Ultimately, the question of “whether the appraisers have gone beyond the damage questions entrusted to them will depend on the nature of the damage, the possible causes, the parties’ dispute, and the structure of the appraisal award.”<sup>165</sup> This issue will likely continue to be regularly litigated, both in the context of compelling cases to appraisal or avoiding appraisal *and* enforcing or setting aside appraisal awards where one side or the other claims the appraisers exceeded the scope of the appraisal clause, as occurred in *Garcia v. State Farm Lloyds*,<sup>166</sup> a 2016 San Antonio Court of Appeals case.<sup>167</sup>

There may also be situations where it is completely ambiguous whether the insurer’s refusal to pay any amount for a claim is based on a disagreement about the amount of the loss, or a disagreement about causation or the interpretation and application of the policy. For example, if the carrier’s claim denial simply states the claim was denied because “we found no evidence of any covered damages in an amount more than your applicable deductible” but provides no further details, that “denial” of the claim could be because (a) the insurer found some damage but not enough

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159. *Id.* at \*4.

160. *See id.* at \*8 (asserting that appraisal awards establish damages but not liability).

161. *Id.*

162. *Id.* at \*9.

163. *See id.* at \*11 (“Under the specific facts of this case, causation is a liability question for the court.”).

164. *Id.* at \*13.

165. *State Farm Lloyds v. Johnson*, 290 S.W.3d 886, 893 (Tex. 2009).

166. *Garcia v. State Farm Lloyds*, 514 S.W.3d 257 (Tex. App.—San Antonio 2016, pet. denied).

167. *Id.* at 267.

to exceed the deductible (which would be a disagreement about the amount of the loss), *or* (b) it could be that the insurer found plenty of damage, but considered all or most of it to be caused by non-covered losses (which would be potentially a disagreement about causation or policy interpretation). The Texas Insurance Code imposes a duty on carriers to state the reasons for a rejection of a claim, but there is not much guidance for what constitutes sufficiently detailed reasons.<sup>168</sup>

Justice Brister's rules get even more complicated when the insurer's position on the amount it will pay for the claim combines *both* disagreements about causation and disagreements about the amount of the loss. For example, the insurer determines there are substantial amounts of hail damage to a property. However, the insurer determines that most of the repairs are due to hail damage caused prior to the policy period by a non-covered hailstorm, but then also concludes that the remaining damages that *are* covered are less than the deductible, and on the basis of both of these conclusions it pays nothing on the claim. Is that disagreement only *partially* subject to appraisal? Would the umpire determine the amount of the loss as to the portion of damages the insurer acknowledges is covered, leaving the question of whether the remainder of the damage was caused by a covered hailstorm for the courts?

In a seminar presentation sponsored by the Insurance Section of the State Bar of Texas shortly after the *Johnson* opinion was published and its author's departure from the bench, Justice Brister explained his belief that the *Johnson* opinion would be relatively uncontroversial because appraisals would operate much like mediations, resolving only those simple cases not hotly contested, while parties to more serious disputes would still get to litigate liability for the loss, as well as to attack the validity or relevance of the result of the appraisal in a jury trial.<sup>169</sup> Of course, the court had not been tasked with reviewing the *Breshears* rule or the "independent injury" rule at that point.<sup>170</sup>

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168. See TEX. INS. CODE ANN. § 542.056(c) ("If the insurer rejects the claim, the notice required . . . must state the reasons for the rejection.").

169. See Brister & Ticer, *supra* note 102, at 13:45–14:10 ("[Y]ou come up with an answer and in half or three quarters of the cases, that answer will be what the parties settle on, but then some of them, somebody's not going to like it, so you just disregard it and move on.").

170. See Republic Ins. Co. v. Stoker, 903 S.W.2d 338, 341 (Tex. 1995) (acknowledging "a general rule [that] there can be no claim for bad faith when an insurer has promptly denied a claim that is in fact not covered[,] but nevertheless recognizing "the possibility that in denying the claim, the insurer may commit some act, so extreme, that would cause injury independent of the policy claim"); *Breshears v. State Farm Lloyds*, 155 S.W.3d 340, 344 (Tex. App.—Corpus Christi 2004, pet. denied) (mem. op)

## IV. CHALLENGING AN APPRAISAL AWARD AFTER APPRAISAL

Once the appraisal process is complete and at least two of the three appraisers (the two parties' appointed appraisers and the "umpire") have agreed to the amount of the loss, that determination is binding on the parties unless it can be legally set aside.<sup>171</sup> There are several ways that appraisal awards have been challenged after the fact, including accident, mistake, fraud, the appraisal was outside the scope of or not in compliance with the policy, and lack of authority.<sup>172</sup> These arguments are often grouped together into three categories: "(1) when the award was made without authority; (2) when the award was made as a result of fraud, accident, or mistake; or (3) when the award was not in compliance with the requirements of the policy."<sup>173</sup> Whatever the basis, the party attempting to avoid the award bears the burden of setting it aside and "every reasonable presumption" will be indulged in favor of the appraisal award.<sup>174</sup>

A. *Scope*

"Scope" of the award is dealt with in the previous section of this paper on invoking and avoiding appraisal, as it turns on the same issues often used to try to avoid appraisal in the first place.<sup>175</sup> Frequently, the central question that arises in attempting to set aside an appraisal award is whether the appraisers and umpire exceeded their authority in the sense that they went beyond the limitations of the process and attempted to adjudicate coverage or liability instead of merely the amount of the loss.<sup>176</sup> As stated

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(finding the insurers were entitled to summary judgment against the insureds' breach of contract claim because the insurers established proof of their participation and full compliance with the appraisal process).

171. See *Bresbears*, 155 S.W.3d at 342 n.1 (discussing the terms of the appraisal provision present in the insurance contract which states appraisal awards shall be binding on both parties if the process of appraisal was followed properly).

172. See *id.* at 346 ("[A]n appraisal award is binding and enforceable unless the insured proves that the award was unauthorized or the result of fraud, accident, or mistake." (citing *Barnes v. W. All. Ins. Co.*, 844 S.W.2d 264, 267 (Tex. App.—Fort Worth 1992, writ dismissed by agr.))).

173. See *Garcia v. State Farm Lloyds*, 514 S.W.3d 257, 265 (Tex. App.—San Antonio 2016, pet. denied) (citing *Wells v. Am. States Preferred Ins. Co.*, 919 S.W.2d 679, 683 (Tex. App.—Dallas 1996, writ denied); *Providence Lloyds Ins. Co. v. Crystal City Indep. Sch. Dist.*, 877 S.W.2d 872, 875–76 (Tex. App.—San Antonio 1994, no writ)).

174. *Providence Lloyds*, 877 S.W.2d at 875 (citing *Continental Ins. Co. v. Guerson*, 93 S.W.2d 591, 594 (Tex. App.—San Antonio 1936, writ dismissed)).

175. See discussion *supra* Section III.D.

176. See, e.g., *Garcia*, 514 S.W.3d at 265–69 (discussing whether appraisers acted outside the scope of their authority); see also *Wells*, 919 S.W.2d at 683 (answering "whether the appraisal section of

above, this is a thorny question as to which the existing case law leaves few definitive answers.

### B. *Lack of Umpire Authority*

The umpire is not necessarily limited to siding with one appraiser or the other.<sup>177</sup> Rather, the umpire is supposed to exercise his or her own independent judgment in determining the value of the loss.<sup>178</sup> Thus, the umpire is not constrained to the values the parties' appointed appraisers placed on the loss, but may determine the loss value at more or less than the amounts determined by either of them.<sup>179</sup>

### C. *Impartiality and "Disinterestedness"*

A second argument often raised in this context is a challenge that either one party's appointed appraiser or the umpire was not unbiased, competent, disinterested, or otherwise independent.<sup>180</sup> The burden of proof is significant. "The showing of a [preexisting] relationship, without more, does not support a finding of bias."<sup>181</sup> Cases finding a disqualifying interest or bias tend to revolve around facts showing the appraiser had a particular pecuniary interest in setting the value of the loss at a certain amount. For example, in *General Star Indemnity Co. v. Spring Creek Village Apartments Phase*

the policy . . . authorized and empowered the appraisers to determine what caused or did not cause the loss claimed").

177. See *Providence Lloyds*, 877 S.W.2d at 877–78 (establishing an umpire is under no duty to constrain his estimates to meet those of the appraisers).

178. See *id.* at 878 ("[It is] the duty of the umpire under the terms of the contract of insurance to ascertain and determine, in the exercise of his own judgment and as the result of his own investigation, the cost values of the disputed items, independent of the findings of the appraisers, or either of them.").

179. See *id.* at 876 ("The function of an umpire who is to act in matters of difference only is not to coincide with one or the other of the appraisers, but he is to make his award independently of such estimates." (quoting *Fisch v. Transcon. Ins. Co.*, 356 S.W.2d 186, 190 (Tex. App.—Houston 1962, writ re'fd n.r.e.)); *Garcia*, 514 S.W.3d at 268 (relying on *Providence Lloyds*).

180. See *Franco v. Slavonic Mut. Fire Ins. Ass'n*, 154 S.W.3d 777, 786–87 (Tex. App.—Houston [14th Dist.] 2004, no pet.) (challenging the validity of an appraisal award based on an appraiser's alleged bias, prejudice, and interest due to a preexisting relationship).

181. *Id.* at 786 (citing *Allison v. Fire Ins. Exch.*, 98 S.W.3d 227, 255 (Tex. App.—Austin 2002, pet. granted, judgment vacated w.r.m.); *Gardner v. State Farm Lloyds*, 76 S.W.3d 140, 143–44 (Tex. App.—Houston [1st Dist.] 2002, no pet.); see also *Gardner*, 76 S.W.3d at 143–44 (explaining how the evidence failed to establish a preexisting relationship between the insurer and the insurer's appraiser).

*V, Inc.*,<sup>182</sup> the insured's appraiser was a contractor who had an agreement under which his percentage of compensation would go up if the cost of repair were over \$2 million.<sup>183</sup> The court found that, as an appraiser, he had a direct pecuniary interest in assuring the loss was high enough to trigger a bigger profit for his contracting business.<sup>184</sup>

However, other evidence that an appraiser was biased or prejudiced might suffice. In an older opinion, the Texas Supreme Court, quoting from an Alabama Supreme Court opinion, suggested a pecuniary interest was not essential to show the appraiser was not disinterested.<sup>185</sup> However, distinguishing that case, a more recent opinion concluded the appraisers need only meet whatever requirements are imposed by the policy and need not be "disinterested" if all the policy required was that they be "competent."<sup>186</sup>

If there is room for arguments about bias aside from showing a direct pecuniary interest, it appears to be construed narrowly. For instance, in *Gardner v. State Farm Lloyds*,<sup>187</sup> the insured argued the carrier's appraiser—Boudreaux—was not "independent" as required under their insurance policy because of a preexisting business relationship between State Farm and his employer, Haag Engineering.<sup>188</sup> The record showed "(1) Haag wrote a training program used by State Farm, about hail damage claims; (2) Haag wrote numerous publications about hailstorm evaluations, and served as a 'consultant' for State Farm on those matters; and (3) Haag was

182. *Gen. Star Indem. Co. v. Spring Creek Vill. Apartments Phase V, Inc.*, 152 S.W.3d 733 (Tex. App.—Houston [14th Dist.] 2004, no pet.).

183. *Id.* at 738.

184. *See id.* at 737 ("An appraiser with a financial interest in the outcome of the appraisal is not impartial." (citing *Del. Underwriters v. Brock*, 211 S.W. 779, 780–81 (Tex. 1919)); *see also* *Cent. Life Ins. Co. v. Aetna Cas. & Sur. Co.*, 466 N.W.2d 257, 262 (Iowa 1991) ("The appointment of an appraiser with a concealed pecuniary interest in the outcome is a sufficient ground for voiding the award as a matter of law without a showing of prejudice." (citing *Edwards v. Emp'rs Mut. Liab. Ins. Co. of Wis.*, 132 S.E.2d 39, 42 (Ga. 1963); *Produce Refrigerator Co. v. Norwich Union Fire Soc'y*, 97 N.W. 875, 876 (Minn. 1904); *Orr v. Farmers Mut. Hail Ins. Co.*, 201 S.W.2d 952, 954–57 (Mo. 1947))).

185. *See Brock*, 211 S.W. at 780–81 ("For the term 'disinterested' 'does not mean simply lack of pecuniary interest, but requires the appraiser to be not biased or prejudiced.'" (quoting *Hall Bros. v. W. Assur. Co.*, 32 So. 257, 258 (Ala. 1902))).

186. *See* *Tex. Farm Bureau Cas. Ins. Co. v. Sampley*, No. 07-13-00151-CV, 2015 WL 3463028, at \*3 (Tex. App.—Amarillo May 16, 2015, no pet.) (mem. op) (finding no legal requirement that "every appraiser appointed under a Texas insurance policy have the attribute of disinterestedness, regardless of the policy's language" and distinguishing competence from "disinterestedness").

187. *Gardner v. State Farm Lloyds*, 76 S.W.3d 140 (Tex. App.—Houston [1st Dist.] 2002, no pet.).

188. *Id.* at 143–44.



paid by various State Farm companies for assignments across the United States over seven years.”<sup>189</sup> This was insufficient to raise a fact issue about whether the appraiser lacked independence.<sup>190</sup> The court explained:

[The insured] presented no evidence that State Farm influenced or exercised control over Boudreaux. There [was] no evidence that Boudreaux ever was an employee of State Farm or had a financial interest in the claim. None of their evidence relate[d] to Boudreaux, the [insureds'] claim, or the particular hailstorm. Instead, their evidence involve[d] an arm's length business relationship, which [was] unrelated to [their] specific claim, between various State Farm companies and Haag.<sup>191</sup>

Similarly, in *Franco v. Slavonic Mutual Fire Insurance Ass'n*,<sup>192</sup> the insured argued the appraisal award should be set aside because the insurer's appraiser was an “interested, prejudiced, and biased appraiser, due to his status as an investigating engineer” on the same claim but for another insurer, “and the fact that he already had issued a report containing his opinions regarding the scope of [the] damages and coverage prior to his appointment as appraiser.”<sup>193</sup> The court found this was insufficient to raise a fact issue regarding disqualifying bias, reasoning the appraiser was not an employee of the insurer and his “report and conclusions regarding the cause of the plumbing leak were his own.”<sup>194</sup> Because the insured presented “no evidence suggesting that [the insurer] influenced or exercised control” over the appraiser, or that he “had a financial interest in Franco's claim[,]” there was no fact issue sufficient to challenge the award.<sup>195</sup>

Other courts have suggested the standard might be met merely by showing an “error resulting in the award is so great as to be indicative of gross partiality, undue influence, or corruption.”<sup>196</sup> Where there is some evidence to support a claim that an appraiser or umpire was not qualified to meet the policy's requirements, however, it has often been treated as a fact

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189. *Id.* at 143.

190. *Id.* at 144.

191. *Id.* at 143.

192. *Franco v. Slavonic Mut. Fire Ins. Ass'n*, 154 S.W.3d 777 (Tex. App.—Houston [14th Dist.] 2004, no pet.).

193. *Id.* at 785.

194. *Id.* at 787.

195. *Id.*

196. *García v. State Farm Lloyds*, 514 S.W.3d 257, 269–70 (Tex. App.—San Antonio 2016, pet. denied) (quoting *Barnes v. W. All. Ins. Co.*, 844 S.W.2d 264, 268 (Tex. App.—Fort Worth 1992, writ dism'd by agr.)).

issue for a jury.<sup>197</sup> Importantly, once it is established that the party relying on the appraisal award appointed a biased appraiser, Texas courts have generally held that the party has waived the right to appraisal.<sup>198</sup>

#### D. *Accident or Mistake*

In the appraisal context, a “mistake” is often described as “a situation where the appraisers and umpire were laboring under a mistake of fact by which their appraisal award was made to operate in a way they did not intend, such that the award does not speak the intention of the appraisers and umpire[.]”<sup>199</sup> The main question is not whether the appraisal award was correct or incorrect in amount, but whether the amount stated in the award is what the appraisers *intended* it to be.<sup>200</sup>

### V. EFFECT ON CLAIMS FOR BREACH OF CONTRACT, BAD FAITH, AND VIOLATIONS OF THE TEXAS INSURANCE CODE

One of the biggest issues in Texas insurance coverage litigation is the question of what the relationship is between the appraisal process and the claims adjusting process, and what effect appraisal has on claims for breach of contract, common law and statutory bad faith, and violation of the Texas Prompt Payment of Claims Act (PPCA). Is appraisal a dispute resolution mechanism that comes into play only after the claim has been investigated and adjusted by the insurer, or is it a device that is itself part of the claims adjusting process that values the claim rather than resolves a disagreement?

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197. See *Gen. Star Indem. Co. v. Spring Creek Vill. Apartments Phase V, Inc.*, 152 S.W.3d 733, 735 (Tex. App.—Houston [14th Dist.] 2004, no pet.) (“Because we find fact issues with regard to whether Spring Creek’s appraiser was impartial, we reverse the judgment and remand for proceedings consistent with this opinion.”); *Providence Lloyds Ins. Co. v. Crystal City Indep. Sch. Dist.*, 877 S.W.2d 872, 876 n.5 (Tex. App.—San Antonio 1994, no writ) (“The jury was asked whether it found from a preponderance of the evidence that the [appraisal] award should be set aside because of fraud, accident, or mistake.” (alteration in original) (citing *Barnes*, 844 S.W.2d at 268)); *Pa. Fire Ins. Co. v. W.T. Waggoner Estate*, 39 S.W.2d 593, 595 (Tex. Comm’n App. 1931, judgment affirmed) (“This issue being properly raised, the question as to the competency or disinterestedness of an appraiser is primarily for the jury.”).

198. See *Del. Underwriters v. Brock*, 211 S.W. 779, 782 (Tex. 1919) (holding insurer’s appointment of a biased appraiser constituted a waiver).

199. *Garcia*, 514 S.W.3d at 269 (quoting *Barnes*, 844 S.W.2d at 268).

200. See *id.* at 269–70 (stating that the issue was the intention of the appraisers); *MLCSV10 v. Stateside Enters.*, 866 F. Supp. 2d 691, 702 (S.D. Tex. 2012) (“A court may set aside an award on the ground of mistake [or accident] only ‘upon a showing that the award does not speak the intention of the appraisers.’” (alteration in original) (quoting *JM Walker LLC v. Acadia Ins. Co.*, 356 F. App’x 744, 746 (5th Cir. 2009))).

Confusion about this fundamental question underlies the central issue that has brought appraisal to the forefront of Texas coverage litigation.

#### A. *The Breshears Rule*

In *Breshears v. State Farm Lloyds*,<sup>201</sup> homeowners gave notice of a loss for plumbing leaks under their policy with State Farm.<sup>202</sup> State Farm valued the loss at \$18,742, and the homeowners disagreed with whether the amount was enough for the repairs.<sup>203</sup> Suit was filed but abated while the disagreement went through appraisal where the appraisers and umpire agreed the amount of the loss was actually \$21,484.<sup>204</sup> State Farm paid the difference within thirty days of the appraisal award.<sup>205</sup> Both sides moved for summary judgment, with State Farm taking the position that the amount of the loss was determined by the appraisal and therefore there was no breach of the contract and by extension no possible breach of the Insurance Code.<sup>206</sup> The Breshears argued the appraisal award established as a matter of law that State Farm had breached the contract when it undervalued the claim when the claim was handled.<sup>207</sup> The trial court granted State Farm's motion and the court of appeals affirmed.<sup>208</sup>

##### 1. Breach of Contract

In support of their position that payment of an appraisal award did not foreclose a claim for breach of contract, the Breshears relied on the following language from *In re Allstate County Mutual Insurance*,<sup>209</sup> wherein the court was justifying mandamus relief from the denial of appraisal:

[I]f the appraisal determines that the vehicle's full value is what the insurance company offered, there would be no breach of contract. Accordingly, at a minimum, denying the appraisals will vitiate the defendants' ability to defend the breach of contract claim. Because the appraisals go to the heart of the

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201. *Breshears v. State Farm Lloyds*, 155 S.W.3d 340 (Tex. App.—Corpus Christi 2004, pet. denied) (mem. op).

202. *Id.* at 342.

203. *Id.*

204. *Id.*

205. *Id.*

206. *Id.* at 342–43.

207. *Id.* at 343.

208. *Id.* at 341.

209. *In re Allstate Cty. Mut. Ins. Co.*, 85 S.W.3d 193 (Tex. 2002) (orig. proceeding).

plaintiffs' breach of contract claim, we need not decide here the significance of the appraisals to each of the remaining claims.<sup>210</sup>

The *Breshears* court characterized this as dicta from the *Allstate* court and concluded that because the Breshears' policy with State Farm specified the "appraisal process was the remedy for any disagreement regarding the amount of loss," there simply could be no breach of contract where the insurer timely paid the appraisal award.<sup>211</sup>

## 2. Bad Faith

The *Breshears* court also affirmed summary judgment denying the homeowners' bad faith claims under then Article 21.21 of the Texas Insurance Code (now codified in Chapter 541).<sup>212</sup> In so doing, the court found there was evidence that the amount originally paid by the insurer was reasonable and based on average repair costs from local contractors' estimates obtained at the time of the payment.<sup>213</sup> The Breshears presented no evidence that State Farm's method of using average costs was unreasonable, "or that the average cost State Farm calculated in their case was itself unreasonable."<sup>214</sup> Thus, the court concluded there was no evidence to support a statutory bad faith claim.<sup>215</sup>

## 3. PPCA

The *Breshears* court also affirmed summary judgment in favor of State Farm on the homeowners' claim for violations of the Prompt Payment of Claims Act, then Article 21.55 of the Texas Insurance Code (now codified in Chapter 542 Subchapter B).<sup>216</sup> Without specifically addressing the statutory language, the court concluded:

The Breshears argue that because of the appraisal process, they were not actually paid until after State Farm paid them the difference between the first

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210. *In re Allstate Cty. Mut. Ins. Co.*, 85 S.W.3d at 196.

211. *Breshears*, 155 S.W.3d at 344.

212. *See id.* at 346 ("Therefore, denial of the Breshears' motion for summary judgment was proper as they have failed to establish an article 21.21 violation against State Farm."); *see generally* TEX. INS. CODE ANN. § 541 (dealing with unfair methods of competition and unfair or deceptive acts or practice).

213. *Breshears*, 155 S.W.3d at 345–46.

214. *Id.* at 346.

215. *Id.*

216. *Id.* at 345; *see generally* INS. § 542.051–.061 (dealing with the prompt payment of claims).

payment and the appraisal award, which occurred long after the sixty-day statutory limit. . . . We disagree. . . . The fact that the appraisal process was later invoked does not alter the fact that State Farm complied with the insurance code, and provided a reasonable payment within a reasonable time.<sup>217</sup>

#### B. Franco v. Slavonic

Two months after the opinion in *Breshears*, another court issued a similar opinion precluding any further recovery following appraisal. In *Franco v. Slavonic Mutual Fire Insurance Ass'n*, the homeowner received a coverage payment from her insurer in the amount of \$3,680 actual cash value for damages from a covered plumbing leak.<sup>218</sup> The homeowner invoked the appraisal process, which resulted in an appraisal umpire's actual cash value award in the amount of \$6,902.<sup>219</sup> The insurer paid the balance of the award to the homeowner, who proceeded with a breach of contract action.<sup>220</sup> The court held that since the appraisal award was agreed to be "binding" regarding disagreements about the amount of the loss, the homeowner was "estopped" from claiming there had been any breach of the contract when the insurer timely paid the appraisal award.<sup>221</sup> As in *Breshears*, the court did not affirm summary judgment on the statutory bad faith claim merely on the basis that the appraisal award was paid, but because there was no evidence of any bad faith at the time of the original, deficient

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217. *Breshears*, 155 S.W.3d at 345; see also *Nat'l Sec. Fire & Cas. Co. v. Hurst*, 523 S.W.3d 840, 847 (Tex. App.—Houston [14th Dist.] 2017, pet. filed) ("As this court has recognized, full and timely payment of an appraisal award under the policy precludes an award of penalties under the Insurance Code's prompt payment provisions as a matter of law."); *In re Slavonic Mut. Fire Ins. Ass'n*, 308 S.W.3d 556 (Tex. App.—Houston [14th Dist.] 2010, orig. proceeding), *overruled on other grounds*, *In re Universal Underwriters of Tex. Ins. Co.*, 345 S.W.3d 404, 405–07 (Tex. 2011) (orig. proceeding) ("Texas courts considering the issue have concluded that full and timely payment of an appraisal award under the policy precludes an award of penalties under the Insurance Code's prompt payment provisions as a matter of law." (citing *Amine v. Liberty Lloyds of Tex. Ins. Co.*, No. 01-06-00396-CV, 2007 WL 2264477, \* 4 (Tex. App.—Houston, [1st Dist.] Aug. 9, 2007, no pet.) (mem. op.); *De La Garza v. State Farm Mut. Auto. Ins. Co.*, 175 S.W.3d 29, 32–33 (Tex. App.—Dallas 2005), *supp. op. on reh'g*, 181 S.W.3d 755, 756 (Tex. App.—Dallas 2005, pet. denied); *Breshears*, 155 S.W.3d at 344–45)).

218. *Franco v. Slavonic Mut. Fire Ins. Ass'n*, 154 S.W.3d 777, 780 (Tex. App.—Houston [14th Dist.] 2004, no pet.).

219. *Id.* at 780–81.

220. *Id.* at 781.

221. *Id.* at 787.

payment.<sup>222</sup> The homeowner apparently raised no complaint on appeal regarding their PPCA claims.<sup>223</sup>

### C. *Breshears* & “Independent Injury”

Since *Breshears* and *Franco*, the timely payment of an appraisal award has generally been construed to preclude *any* liability for breach of contract, statutory bad faith, or violation of the PPCA as a matter of law, regardless of whether there is evidence of bad faith in the original handling of the claim prior to appraisal.<sup>224</sup> However, the reasons for precluding claims for bad faith have been expanded from the “no evidence” rationale applied in *Breshears* and *Franco*, combining the rule from *Breshears* with the “independent injury” rule and thereby making the timely payment of an appraisal award a complete defense as a matter of law to all claims against an insurer based on the insurer’s conduct investigating or paying the claim prior to appraisal.<sup>225</sup>

For instance, in the Fifth Circuit case *Blum’s Furniture Co. v. Certain Underwriters at Lloyds London*,<sup>226</sup> a furniture store sustained damage from Hurricane Ike in September 2008, and over the next year received two payments totaling \$350,000 from its insurer.<sup>227</sup> Blum’s requested appraisal and filed suit.<sup>228</sup> The appraisal resulted in an umpire’s award exceeding \$1 million.<sup>229</sup> Following *Breshears* and *Franco*, the Fifth Circuit upheld

222. *See id.* at 788 (“[T]here is no evidence raising a fact issue about [insurer’s] compliance with the time deadlines imposed by article 21.55.”).

223. *Id.*

224. *See generally* Nat’l Sec. Fire & Cas. Co. v. Hurst, 523 S.W.3d 840 (Tex. App.—Houston [14th Dist.] 2017, pet. filed) (finding that an insurer’s full and timely payment of appraisal award precludes as a matter of law any award for breach of contract, penalty interest, or any statutory or common-law bad faith violations).

225. *See* Floyd Circle Partners, LLC v. Republic Lloyds, No. 05-16-00224-CV, 2017 WL 3124469, at \*9 (Tex. App.—Dallas July 24, 2017, pet. denied) (mem. op.) (“Where a plaintiff’s claim for breach of an insurance contract fails, to prevail on an action for violations of chapter 541 of the insurance code, the plaintiff must show either that the insured failed to timely investigate the claim or that the insurer committed an extreme act that caused an injury independent of the policy claim.” (citing *Bernstien v. Safeco Ins. Co. of Ill.*, No. 05-13-01533-CV, 2015 WL 3958282, at \*2 (Tex. App.—Dallas June 30, 2015, no pet.) (mem. op.); *USAA Tex. Lloyds Co. v. Menchaca*, No. 14-0721, 2017 WL 1311752, at \*11–12 (Tex. Apr. 7, 2017), *superseded by* *USAA Tex. Lloyds Co. v. Menchaca*, 545 S.W.3d 479 (Tex. 2018))).

226. *Blum’s Furniture Co. v. Certain Underwriters at Lloyds London*, 459 F. App’x 366 (5th Cir. 2012) (per curiam).

227. *Id.* at 367.

228. *Id.*

229. *Id.*

summary judgment on the breach of contract claim.<sup>230</sup> However, rather than focus on the evidence supporting a bad faith claim, the *Blum's* court relied on the Texas Supreme Court's decisions in *Republic Insurance Co. v. Stoker*<sup>231</sup> and *Liberty National Fire Insurance Co. v. Akin*<sup>232</sup> to conclude that because there was no breach of contract, there could not be any bad faith.<sup>233</sup>

Thus, while both *Bresbears* and *Franco* left open the possibility that an insured could produce evidence that an underpayment was made in bad faith violation of the Insurance Code, even in the absence of a breach of contract, the Fifth Circuit combined the *Bresbears* rule with what is often called the "independent injury" rule based on *Stoker* to effectively eliminate any bad faith claim as a matter of law, regardless of whether there was evidence that the claim was underpaid in bad faith.<sup>234</sup> This modified rule has been followed by several cases since—applying the *Bresbears* rule to preclude any claim for breach of contract as a matter of law, and combining that rule with the "independent injury" rule to preclude any bad faith claim as a matter of law.<sup>235</sup>

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230. *Id.* at 369.

231. *Republic Ins. Co. v. Stoker*, 903 S.W.2d 338 (Tex. 1995).

232. *Liberty Nat'l Fire Ins. Co. v. Akin*, 927 S.W.2d 627 (Tex. 1996).

233. *Blum's Furniture*, 459 F. App'x at 369.

234. *See id.* at 368 ("The only recognized exceptions to this rule are if the insurer 'commit[s] some act, so extreme, that would cause injury independent of the policy claim,' or fails 'to timely investigate the insured's claim.'" (alteration in original) (quoting *Stoker*, 903 S.W.2d at 341)).

235. *See, e.g., Garcia v. State Farm Lloyds*, 514 S.W.3d 257, 277 (Tex. App.—San Antonio 2016, pet. denied) ("[I]n order to avoid summary judgment on her common law bad faith claim, Garcia had the burden to raise a genuine issue of material fact that appellees 'commit[ed] some act, so extreme, that would cause injury independent of the policy claim' or failed to timely investigate her claim." (alteration in original) (quoting *Stoker*, 903 S.W.2d at 341)). *See also Biasatti v. GuideOne Nat'l Ins. Co.*, No. 07-17-00044-CV, 2018 WL 3946352, at \*3 n.3 (Tex. App.—Amarillo Aug. 16, 2018, pet. filed) (finding the insured "has not demonstrated that any policy benefits were withheld, nor has it shown damages from any injury independent of its policy claim" (footnote omitted)); *Nat'l Sec. Fire & Cas. Co. v. Hurst*, 523 S.W.3d 840, 847–848 (Tex. App.—Houston [14th Dist.] 2017, pet. filed) (determining the insured was "precluded from maintaining his prompt payment claim as a matter of law" and "has not alleged any act so extreme as to cause independent injury" (citing *USAA Tex. Lloyds Co. v. Menchaca*, No. 14-0721, 2017 WL 1311752, at \*11–12 (Tex. Apr. 7, 2017), *superseded by* *USAA Tex. Lloyds Co. v. Menchaca*, 545 S.W.3d 479 (Tex. 2018); *Progressive Cty. Mut. Ins. v. Boyd*, 177 S.W.3d 919, 922 (Tex. 2005); *Cantu v. State Farm Lloyds*, No. 7:14-CV-456, 2016 WL 5372542, at \*8 (S.D. Tex. Sept. 26, 2016); *Alvarado v. State Farm Lloyds*, No. 7:14-CV-166, 2016 WL 6905865, at \*4–5 (S.D. Tex. June 15, 2016)); *Floyd Circle Partners, LLC v. Republic Lloyds*, No. 05-16-00224-CV, 2017 WL 3124469, at \*9 (Tex. App.—Dallas July 24, 2017, pet. denied) (mem. op.) (reasoning that there must be an independent injury for a bad faith claim); *Anderson v. Am. Risk Ins. Co.*, No. 01-15-00257-CV, 2016 WL 3438243, at \*6 (Tex. App.—Houston [1st Dist.] June 21, 2016, no pet.) (mem.

#### D. *Isn't This Like What Happens With UM/UIM Claims?*

Underlying these opinions—particularly *Breshears* and *Franco*—is the idea that the appraisal process is not a dispute resolution procedure but rather the contractually agreed process for actually determining the value of the claim. In that sense, one would expect it to be treated the same way that claims are treated for purposes of Uninsured/Underinsured Motorist (UM/UIM) coverage. If so, one would expect the Supreme Court of Texas to treat appraisal the same way it treats UM/UIM claims. But it has not done so.

Had the Texas Supreme Court believed that a property insurance claim could be adjusted through appraisal instead of the insurer's existing common law and statutory duty to investigate and promptly pay covered losses, the court would have reached a very different result in both *In re Allstate* and *In re Universal Underwriters*. Indeed, if appraisal were just part of the claims adjusting process as the *Breshears* rule presumes, the Supreme Court of Texas would have dismissed all of the breach of contract and bad faith claims in both *In re Allstate* and *In re Universal Underwriters* just like it did in *Brainard v. Trinity Universal Insurance Co.*<sup>236</sup> Instead, the court has explained—twice—that appraisal determines “whether” the contract has been breached, and that the outcome of an appraisal will go to the “heart” of the plaintiffs’ breach of contract claim; both times the court also acknowledged that the “bad faith” claims need not even be abated pending appraisal.<sup>237</sup>

In a UM/UIM case, the “insurer is obligated to pay damages which the insured is ‘legally entitled to recover’ from the underinsured motorist.”<sup>238</sup> The court explained the unique attribute of UIM coverage that exempted it from the general contractual duty to investigate losses and pay coverage benefits:

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op.) (stating that an insured cannot maintain a bad faith claim unless there is a breach of contract or an independent injury).

236. See *Brainard v. Trinity Universal Ins. Co.*, 216 S.W.3d 809, 819 (Tex. 2006) (dismissing the breach of contract and bad faith claims).

237. See *In re Universal Underwriters of Tex. Ins. Co.*, 345 S.W.3d 404, 412 (Tex. 2011) (orig. proceeding) (stating the appraisal clause determines whether the contract has been breached and thus “if the appraisal determined that the full value was what the insurer offered, there would be no breach of contract”); *In re Allstate Cty. Mut. Ins. Co.*, 85 S.W.3d 193, 196 (Tex. 2002) (orig. proceeding) (“As to the plaintiffs’ breach of contract claim, the parties have agreed in the contracts’ appraisal clause to the method by which to determine whether a breach has occurred.”).

238. *Brainard*, 216 S.W.3d at 818 (quoting TEX. INS. CODE art. 5.06–1(5)).



The UIM contract is unique because, according to its terms, benefits are conditioned upon the insured's legal entitlement to receive damages from a third party. Unlike many first-party insurance contracts, in which the policy alone dictates coverage, UIM insurance utilizes tort law to determine coverage. Consequently, the insurer's contractual obligation to pay benefits does not arise until liability and damages are determined.<sup>239</sup>

From this, it logically follows that a "UIM insurer is under no contractual duty to pay benefits until the insured obtains a judgment establishing the liability and underinsured status of the other motorist. Neither requesting UIM benefits nor filing suit against the insurer triggers a contractual duty to pay."<sup>240</sup> Thus, after *Brainard* there could be no breach of contract without a judicial determination of the tortfeasors' liability, which was the only way for the UIM carrier to determine how much it owed under the policy.<sup>241</sup>

Contrast this with what the court said and did in *In re Allstate* and *In re Universal Underwriters*, where the Supreme Court of Texas not only explained that the outcome of the appraisal went to the "heart" of the breach of contract case and determined "whether" the contract had been breached, but also refused to abate the bad faith claims against the insurer pending the outcome of the appraisal.<sup>242</sup> If the court had understood appraisal to be the means by which an insurer determines the amount of coverage obligation rather than a dispute resolution mechanism, it would have reached a similar result as it had in *Brainard*, where the court found there simply could be no breach of contract claim regardless of how much the coverage obligation turned out to be after an adversarial proceeding.<sup>243</sup> An adversarial proceeding was the only means by which the amount of the loss could be determined where the coverage amount depended on the "liability" of the underinsured motorist.<sup>244</sup> The Texas Supreme Court also would likely have found error in the trial court's refusal to abate the bad faith

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239. *Id.* (citing *Henson v. S. Farm Bureau Cas. Ins. Co.*, 17 S.W.3d 652, 654 (Tex. 2000)).

240. *Id.* (citation omitted) (citing *Henson*, 17 S.W.3d at 653–54).

241. *Id.* (affirming there is no claim for UIM benefits until a judgment establishing negligence of an uninsured motorist).

242. *See In re Universal Underwriters*, 345 S.W.3d at 412 n.5 (stating that the failure "to abate is not subject to mandamus"); *In re Allstate Cty.*, 85 S.W.3d at 196 ("[I]he proceedings need not be abated while the appraisal goes forward.").

243. *See Brainard*, 216 S.W.3d at 818 ("Where there is no contractual duty to pay, there is no just amount owed.").

244. *See id.* ("[N]either a settlement nor an admission of liability from the tortfeasor establishes UIM coverage, because a jury could find that the other motorist was not at fault or award damages that do not exceed the tortfeasor's liability insurance." (citing *Henson*, 17 S.W.3d at 654)).

litigation against Allstate and Universal Underwriters pending appraisal, as courts have done in UIM cases in light of *Brainard*.<sup>245</sup>

It would seem that—at least in the Supreme Court of Texas, and consistent with the language of typical appraisal clauses and the long history of the purpose of these clauses—appraisal is not the device by which an insurer values the claim as adversarial trials are in the UM/UIM context, but rather an extra-judicial alternative dispute resolution mechanism that applies only *after* the insurer has already determined the amount of the loss in the claims adjusting process, and the parties now disagree about that determination.

#### E. USAA v. Menchaca and the Near Future

The Texas Supreme Court has not directly addressed the *Bresbears* rule, though it has recently requested full briefing on the merits in the petition for review proceeding arising from *Barbara Technologies Corp. v. State Farm Lloyds*,<sup>246</sup> which appears to be limited solely to the issue of whether a PPCA claim survives after the payment of an appraisal award.<sup>247</sup> The court has also requested merits briefing in *Ortiz v. State Farm Lloyds*,<sup>248</sup> where the issue is limited to the “independent injury” question of whether a statutory bad faith claim can survive the payment of an appraisal award.<sup>249</sup> A petition was also filed in *National Security Fire & Casualty Co. v. Hurst*,<sup>250</sup> and the court has recently requested briefing on the merits in that case as well, which raises

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245. See, e.g., *In re United Fire Lloyds*, 327 S.W.3d 250, 256 (Tex. App.—San Antonio 2010, orig. proceeding) (finding error in the trial court’s refusal to abate bad faith claims against UIM carrier pending a trial to determine underinsured motorists’ liability).

246. *Barbara Techs. Corp. v. State Farm Lloyds*, No. 04-16-00420-CV, 2017 WL 1423714 (Tex. App.—San Antonio Apr. 19, 2017, pet. filed) (mem. op.).

247. See *id.* at \*2 (considering the legal question of whether a PPCA claim can be sustained when the insurer has paid an appraisal award).

248. *Ortiz v. State Farm Lloyds*, No. 04-17-00252-CV, 2017 WL 5162315 (Tex. App.—San Antonio Nov. 8, 2017, pet. filed) (mem. op.).

249. *Id.* Similar petitions for review in two other State Farm cases were filed. *Lazos v. State Farm Lloyds*, No. 04-17-00286-CV, 2018 WL 521585 (Tex. App.—San Antonio Jan. 24, 2018, pet. filed) (mem. op.); *Alvarez v. State Farm Lloyds*, No. 04-17-00251-CV, 2018 WL 340135 (Tex. App.—San Antonio Jan. 10, 2018, pet. filed) (mem. op.). At the time of this writing the Supreme Court of Texas has requested a response to the petitions in *Lazos* and *Alvarez*, but has not requested briefing on the merits.

250. *Nat’l Sec. Fire & Cas. Co. v. Hurst*, 523 S.W.3d 840 (Tex. App.—Houston [14th Dist.] 2017, pet. filed).

all three claims: breach of contract, PPCA, and bad faith.<sup>251</sup>

However, the Texas Supreme Court *has* recently addressed the language from *Akin* and *Stoker*, often relied on as the basis for the “independent injury” rule, and narrowed the application of the rule in *USAA Texas Lloyds Co. v. Menchaca*.<sup>252</sup> The issue was not addressed with reference to appraisal, but with regard to the more general question of whether underpaid policy benefits can be “actual damages” for purposes of a statutory bad faith claim even in the absence of some separate independent injury—the court concluded they can.<sup>253</sup> The *Menchaca* court also described a number of scenarios in which a claim for bad faith insurance handling might go forward even if there was not technically any breach of the contract.<sup>254</sup>

*Menchaca* casts serious doubt on the independent injury rule as it was applied in cases like *Blum's*, *Garcia*, *Ortiz*, and *Hurst*, and opens the possibility of a bad faith claim where there is sufficient evidence of bad faith underpayment during the claims handling process, even if the insurer eventually paid what it owed after an appraisal award.<sup>255</sup>

251. See generally *id.* at 849 (holding “that an insured cannot defeat an otherwise valid and binding appraisal award simply by refusing to accept the insurer’s payment of the award or by asserting extra-contractual claims that are derivative of the policy claim”).

252. See *USAA Tex. Lloyds Co. v. Menchaca*, 545 S.W.3d 479, 489–500, 521 (Tex. 2018) (analyzing *Akin* and *Stoker* and clarifying “that a plaintiff does not have to prevail on a separate breach-of-contract claim to recover policy benefits for a statutory violation”).

253. See *id.* at 494 (permitting the insured to recover actual damages for an insurer’s statutory violation if the insured has a right to benefits under the policy).

254. See *id.* at 491 (“[S]ome acts of bad faith, such as *failure to properly investigate a claim* or an unjustifiable delay in processing a claim, do not *necessarily* relate to the insurer’s breach of its contractual duties to pay covered claims, and may give rise to different damages.” (quoting *Twin City Fire Ins. Co. v. Davis*, 904 S.W.2d 663, 666 n.3 (Tex. 1995))).

255. Compare *id.* at 499 (“[I]f an insurer’s statutory violation causes an injury independent of the insured’s right to recover policy benefits, the insured may recover damages for that injury even if the policy does not entitle the insured to receive benefits.” (citing *Republic Ins. Co. v. Stoker*, 903 S.W.2d 338, 341 (Tex. 1995))), with *Hurst*, 523 S.W.3d at 848 (“In order to recover any damages beyond policy benefits, the statutory violation or bad faith must cause an injury that is independent from the loss of benefits.” (citing *USAA Tex. Lloyds Co. v. Menchaca*, No. 14-0721, 2017 WL 1311752, at \*11–12 (Tex. Apr. 7, 2017), *superseded by Menchaca*, 545 S.W.3d 479)), *Garcia v. State Farm Lloyds*, 514 S.W.3d 257, 277 (Tex. App.—San Antonio 2016, pet. denied) (“[G]arcia had the burden to raise a genuine issue of material fact that appellees ‘commit[ed] some act, so extreme, that would cause injury independent of the policy claim’ . . . .” (alteration in original) (quoting *Republic Ins. Co. v. Stoker*, 903 S.W.2d 338, 341 (Tex. 1995))), and *Blum’s Furniture Co. v. Certain Underwriters at Lloyds London*, 459 F. App’x 366, 369 (5th Cir. 2012) (per curiam) (“[I]n most circumstances, an insured may not prevail on a bad faith claim without first showing that the insurer breached the contract.” (quoting *Liberty Nat’l Fire Ins. Co. v. Akin*, 927 S.W.2d 627, 629 (Tex. 1996))).

If or when the Texas Supreme Court writes directly about this issue, there are several possible outcomes, though only one of these would be consistent with the court's current jurisprudence describing the function and role of appraisal, the court's recent opinions in *Menchaca*, and the language of the Insurance Code.

1. The court could treat the timely payment of appraisal awards as a complete defense as a matter of law to *all* statutory and common law claims against the insurer, even if the evidence demonstrates bad faith at the time the claim was investigated and adjusted. This is essentially the *Bresbears* plus “independent injury” rule.<sup>256</sup> This would preclude any recovery of interest or attorneys' fees, regardless of how or why the insurer underpaid the amount of the loss when the claim was originally investigated and paid.<sup>257</sup> It also would provide a direct financial incentive for insurers to deliberately underpay claims *and* to shift the cost of investigating the amount of the loss onto the insured, since the insurer will never have to pay more than it should have paid when the claim was originally handled, even if evidence shows the insurer deliberately refused to investigate or pay a covered claim in reliance on its appraisal clause.<sup>258</sup> This incentive could be particularly problematic in the future as some Texas courts have also allowed unilateral appraisal clauses that can only be invoked by the insurer—effectively forcing the insured to file a lawsuit solely to get to the appraisal.<sup>259</sup> This result would also be difficult to reconcile with the court's opinions in *Menchaca* placing limitations on the “independent injury” rule, or with the plain language of the PPCA, which provides no exceptions to its statutory deadlines for appraisal.<sup>260</sup>

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256. See generally *Blum's Furniture*, 459 F. App'x 366 (applying *Bresbears* and *Stoker*).

257. See, e.g., *Hurst*, 523 S.W.3d at 843, 849 (reversing trial court's judgment awarding, among other things, interest and attorney's fees).

258. Cf. *Menchaca*, 545 S.W.3d at 495 (“[A]n insurer's statutory violation permits an insured to receive only those ‘actual damages’ that are ‘caused by’ the violation . . .”).

259. See *In re GuideOne Nat'l Ins. Co.*, No. 07-15-00281-CV, 2015 WL 5766496, at \*3 (Tex. App.—Amarillo Sept. 29, 2015, orig. proceeding) (mem. op.) (“[W]e note that there is not a case cited by [insured] where the Texas Supreme Court or any intermediate appellate court has held an appraisal clause that can only be instituted by the insurance company to be against public policy.”).

260. See generally TEX. INS. CODE ANN. § 542.053 (listing exceptions to the PPCA); *Menchaca*, 545 S.W.3d at 494 (finding “the insured does not *also* have to prevail on a separate breach-of-contract

2. The court could treat the timely payment of appraisal awards as a defense as a matter of law to a claim for breach of contract but permit a statutory or common law claim to proceed against the insurer where the policyholder can produce sufficient evidence to support a claim for bad faith. This is how the issue was implicitly addressed in *Breshears* and *Franco*, and would be consistent with how the court wrote about the “independent injury” rule in *Menchaca*.<sup>261</sup> This would allow additional recovery to an insured who demonstrates the insurer effectively used the appraisal process in bad faith to delay paying the claim or shifting the cost of the investigation onto the policyholder, including the statutory remedies available under Chapter 541 of the Insurance Code, and at least partially take away the incentive created by the rule discussed in point 1, above.<sup>262</sup> It would not be consistent with the court’s prior description of appraisal as going to the “heart” of a breach of contract action<sup>263</sup> or with the court’s long history of characterizing appraisal as “leaving the question of liability for such loss to be determined, if necessary, by the courts.”<sup>264</sup>
3. The court could preclude any claim for breach of contract or bad faith as a matter of law but permit the recovery of attorneys’ fees

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claim based on the insurer’s failure to pay those benefits” if it is found that the insured had a right to benefits under the policy).

261. See *Menchaca*, 545 S.W.3d at 499 (recognizing exceptions to the timely payment of appraisal awards defense for insurers); see also *Breshears v. State Farm Lloyds*, 155 S.W.3d 340, 346 (Tex. App.—Corpus Christi 2004, pet. denied) (mem. op) (discussing how the insurer “acted in good faith and conducted a reasonable investigation in response to their claim”); *Franco v. Slavonic Mut. Fire Ins. Ass’n*, 154 S.W.3d 777, 790 (Tex. App.—Houston [14th Dist.] 2004, no pet.) (affirming summary judgment in favor of the insurer because there was no evidence to show the insurer acted in bad faith).

262. See generally TEX. INS. CODE ANN. § 541 (defining and prohibiting unfair methods of competition and deceptive acts within the business of insurance); see also *Menchaca*, 545 S.W.3d at 499 (allowing insured to recover damages for bad faith claim if damages are independent from the insurer’s statutory violation).

263. See *In re Universal Underwriters of Tex. Ins. Co.*, 345 S.W.3d 404, 412 (Tex. 2011) (orig. proceeding) (“[D]enying the appraisal would vitiate the insurer’s right to defend its breach of contract claim.” (citing *In re Allstate Cty. Mut. Ins. Co.*, 85 S.W.3d 193, 196 (Tex. 2002) (orig. proceeding))); *In re Allstate Cty.*, 85 S.W.3d at 196 (“Because the appraisals go to the heart of the plaintiffs’ breach of contract claim, we need not decide here the significance of the appraisals to each of the remaining claims.”).

264. *State Farm Lloyds v. Johnson*, 290 S.W.3d 886, 889 (Tex. 2009) (quoting *Scottish Union & Nat’l Ins. Co. v. Clancy*, 8 S.W. 630, 631 (Tex. [Comm’n Op.] 1888)).

and penalties under the PPCA, calculating the penalty to run from the time the claim was originally supposed to be paid under the PPCA deadlines up through the date the insurer paid the appraisal award. This is a statutory interpretation question and is essentially the issue raised in the *Barbara Technologies* case that is currently pending in the Supreme Court of Texas.<sup>265</sup> This result would somehow have to be harmonized with the court's opinions in *Menchaca* and its prior characterizations of the limited scope and role of appraisal in coverage litigation.<sup>266</sup>

4. The court could preclude claims for breach of contract but permit a claim for violation of the PPCA as in point 3, above, *and* leave open the possibility of a statutory or common law bad faith claim as in point 2, where the evidence supports such a claim.<sup>267</sup>
5. Finally, the court could confirm that the only effect of an appraisal award is to determine the specific factual issue of the amount of the loss, leaving all of the *legal effects* of that factual determination for the court to resolve. For instance, where the amount of the loss is determined to be more than the insurer paid when it investigated and adjusted the loss, a trial court could find the insurer breached the contract as a matter of law by failing to pay the amounts owed under the policy. By contrast, where the appraisal award is equal to or less than the amount the insurer paid, absent unusual circumstances, a court could find there was no breach of contract as a matter of law. This would be consistent with the court's characterization of appraisal from its 1892 opinion in *Scottish Union* through its 2011 opinion in *In re Universal Underwriters*.<sup>268</sup> It would also be consistent with the

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265. See *Barbara Techs. Corp. v. State Farm Lloyds*, No. 04-16-00420-CV, 2017 WL 1423714, at \*2 (Tex. App.—San Antonio Apr. 19, 2017, pet. filed) (mem. op.) (“Barbara Technologies argues that the trial court erred in granting State Farm’s summary judgment motion because its TPPCA claim survived State Farm’s invocation of the appraisal process and its payment of the appraisal award.”).

266. Cf. *id.* (“In reaching this holding, we relied on a long line of cases holding that a full and timely payment of an appraisal award under the policy precludes an insured from recovering penalties under the TPPCA as a matter of law.” (citing *Garcia v. State Farm Lloyds*, 514 S.W.3d 257 (Tex. App.—San Antonio 2016, pet. denied))).

267. Cf. *Menchaca*, 545 S.W.3d at 499 (finding an insured may recover damages truly independent from a breach of contract claim).

268. See *In re Universal Underwriters*, 345 S.W.3d at 412 (“[I]f the appraisal determined that the full value was what the insurer offered, there would be no breach of contract.” (citing *In re Allstate Cty.*,

court's holdings in *Menchaca*, substantially limiting the "independent injury" rule by permitting a bad faith claim to proceed in those cases where the evidence supports such a cause of action for one of the types of actual damages outlined in *Menchaca*.<sup>269</sup> Finally, it would be consistent with the plain language setting forth the statutory deadlines to investigate and pay covered claims under the PPCA, and consistent with that statute's express requirement that it be construed liberally to "promote the prompt payment of insurance claims."<sup>270</sup>

## VI. OTHER PROCEDURAL ISSUES

### A. Abatement

One commonly litigated procedural issue concerns the effect of a pending appraisal on an ongoing lawsuit where the policyholder has already filed suit prior to appraisal. This was a secondary issue addressed by the court in both *In re Allstate*<sup>271</sup> and *In re Universal Underwriters*.<sup>272</sup>

In its first opinion on the subject, the court concluded that the denial of an abatement was not subject to mandamus, but the timing of the case and the appraisal were matters entrusted to the discretion of the trial court.<sup>273</sup> Nevertheless, the court further concluded a case "need not be abated" pending appraisal.<sup>274</sup> In its second opinion, the issue was relegated to a footnote, where the court simply cited *In re Allstate*.<sup>275</sup>

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85 S.W.3d at 196)); *Scottish Union & Nat'l Ins. Co. v. Clancy*, 18 S.W. 439, 441 (Tex. 1892) (per curiam) (finding the insurer was "endeavoring to ascertain the amount of damage, while the [insured] declined to comply with the conditions in the policy on which alone his right to recover depends").

269. See *Menchaca*, 545 S.W.3d at 521 ("[A] plaintiff does not have to prevail on a separate breach-of-contract claim to recover policy benefits for a statutory violation . . .").

270. TEX. INS. CODE ANN. § 542.054.

271. See *In re Allstate Cty.*, 85 S.W.3d at 195 ("After plaintiffs filed suit, the insurance companies answered and then filed a plea in abatement and motion to invoke appraisal.").

272. See *In re Universal Underwriters*, 345 S.W.3d at 406 ("Grubbs sued Universal . . . . In response, Universal invoked the policy's appraisal clause . . .").

273. See *In re Allstate Cty.*, 85 S.W.3d at 196 ("While the trial court's denial of the motion to invoke appraisal was error, the failure to grant the motion to abate is not subject to mandamus." (citing *Abor v. Black*, 695 S.W.2d 564, 567 (Tex. 1985))).

274. *Id.*

275. See *In re Universal Underwriters*, 345 S.W.3d at 412 n.5 ("The trial court's failure to grant the motion to abate is not subject to mandamus, and the proceedings need not be abated while the appraisal goes forward." (citing *In re Allstate Cty.*, 85 S.W.3d at 196)).

Prior to *In re Universal Underwriters*, one court held it was an abuse of discretion not to abate the case where the appraisal clause was a “condition precedent” to suit.<sup>276</sup> While the *In re Universal Underwriters* court overruled *In re Slavonic* as to the latter’s discussion of what constitutes a waiver, it said nothing about the lower court’s opinion that abatement was mandatory where the appraisal was a condition precedent.<sup>277</sup> Still, the Houston Court of Appeals read *In re Universal Underwriters* as effectively nullifying the abatement holding of *In re Slavonic*.<sup>278</sup> Thus, for now it would appear that a trial court has unreviewable discretion to abate or not to abate the lawsuit pending the outcome of an appraisal. However, one recent opinion from the San Antonio Court of Appeals has bucked this trend. In *In re Acceptance Indem. Ins.*,<sup>279</sup> the court conditionally granted a writ of mandamus directing the trial court to compel the dispute to appraisal *and* to abate the case pending appraisal.<sup>280</sup> The court’s majority opinion contains no discussion of the question raised by *In re Universal Underwriters* or *In re Allstate* as to whether the court has mandamus jurisdiction to address the abatement issue. The court seems to have simply overlooked that this is a separate issue from whether it could issue a writ of mandamus compelling the case to appraisal.

#### B. *Mandamus Review*

As the foregoing discussion and case citations clearly indicate, the denial of a request for appraisal is subject to interlocutory review through

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276. See *In re Slavonic Mut. Fire Ins. Ass’n*, 308 S.W.3d 556, 564 (Tex. App.—Houston [14th Dist.] 2010, orig. proceeding).

277. Compare *In re Universal Underwriters*, 345 S.W.3d at 411 (“Delay alone is not enough; a party must also show prejudice.”), with *In re Slavonic*, 308 S.W.3d at 562 (“We acknowledge that silence or inaction for an unreasonable period of time may show an intention to yield a known right.” (citing *Tenneco Inc. v. Enterprise Prods. Co.*, 925 S.W.2d 640, 643 (Tex. 1996))).

278. See *In re Cypress Tex. Lloyds*, No. 14-11-00713-CV, 2011 WL 4366984, at \*1 (Tex. App.—Houston [14th Dist.] Sept. 20, 2011, orig. proceeding) (mem. op.) (“[T]he parts of our two prior opinions in which this court granted mandamus relief as to the trial court’s failure to abate during the appraisal process are no longer good law.”); see also *In re Cypress Tex. Lloyds*, 425 S.W.3d 444, 448 (Tex. App.—Houston [1st Dist.] 2011, orig. proceeding) (“We agree with the Fourteenth Court of Appeals’ more recent opinion recognizing that, pursuant to controlling authority from our supreme court, the trial court’s denial of CIL’s motion to abate pending the appraisal is not subject to mandamus.” (citing *In re Cypress Tex. Lloyds*, 2011 WL 4366984, at \*1)).

279. *In re Acceptance Indem. Ins. Co.*, No. 04-18-00231-CV, 2018 WL 4608261 (Tex. App.—San Antonio Sept. 26, 2018, orig. proceeding).

280. *Id.* at \*6.



mandamus because there is “no adequate remedy by appeal.”<sup>281</sup> However, it is not clear whether a party seeking to avoid a wrongfully compelled appraisal would be able to avail itself of mandamus relief. Given that similar language used to describe the public policy encouraging the use of appraisal has been used for arbitration, the Supreme Court of Texas may follow a similar double standard for mandamus review of appraisal as it did for arbitration—though the latter turned on arbitration being a matter of “statutory imperative.”<sup>282</sup>

## VII. CONCLUSION

There continues to be substantial confusion among Texas courts as to how the appraisal process posited by many property insurance policies is supposed to work, and what the timing and extent of court intervention into the process should be.<sup>283</sup> Taking into account the purposes of the appraisal clause, the intent behind the most recent Texas Supreme Court pronouncements on the subject, and the purpose of various consumer protection provisions of the Texas Insurance Code, courts should construe the process so as not to distort the claims process or vitiate the protections afforded to insureds by statute and over a century of common law.

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281. *In re Allstate Cty. Mut. Ins. Co.*, 85 S.W.3d 193, 196 (Tex. 2002) (orig. proceeding); *see also In re Universal Underwriters*, 345 S.W.3d at 412 (“We have held that mandamus relief is appropriate to enforce an appraisal clause because denying the appraisal would vitiate the insurer’s right to defend its breach of contract claim.” (citing *In re Allstate Cty.*, 85 S.W.3d at 196)).

282. *See, e.g., In re Gulf Expl., LLC*, 289 S.W.3d 836, 843 (Tex. 2009) (contending that when there are competing statutory imperatives “the balance will generally tilt toward reviewing orders compelling arbitration only on final appeal”).

283. *Cf. USAA Tex. Lloyds Co. v. Menchaca*, 545 S.W.3d 479, 521 (Tex. 2018) (“[T]he confusing nature of our precedent precludes us from faulting USAA for the position it has maintained throughout this litigation.”).